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**609 – Crossing the Cultural Divide:
Succeeding in International Business
Negotiations**

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Mr. Connor was also previously senior attorney at the U.S. Federal Communications Commission and practiced at largest independent law firm in the Middle East. Mr. Connor was the recipient of a U.S. Fulbright fellowship in 2004 to teach law in the Middle East. Mr. Connor began his legal practice career as an associate at the Washington office of Heller Ehrman.

Rodolfo Rivera

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Prior to joining Fidelity National Title Group, Mr. Rivera was in private practice representing clients throughout Latin America and the Caribbean. Mr. Rivera is a graduate of Ohio Northern University and St. Louis University School of Law. At St. Louis University, he served as assistant managing editor of the *St. Louis University Law Review*. Mr. Rivera also studied international law at The Hague.

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He first joined Eastman as a senior attorney in the legal department. During his career at Eastman, he has worked in several areas of the legal division, including assistant general

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International Expansion: How to Handle Conflicting Laws and the Regulators

presented by

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Frustrated Lawyer

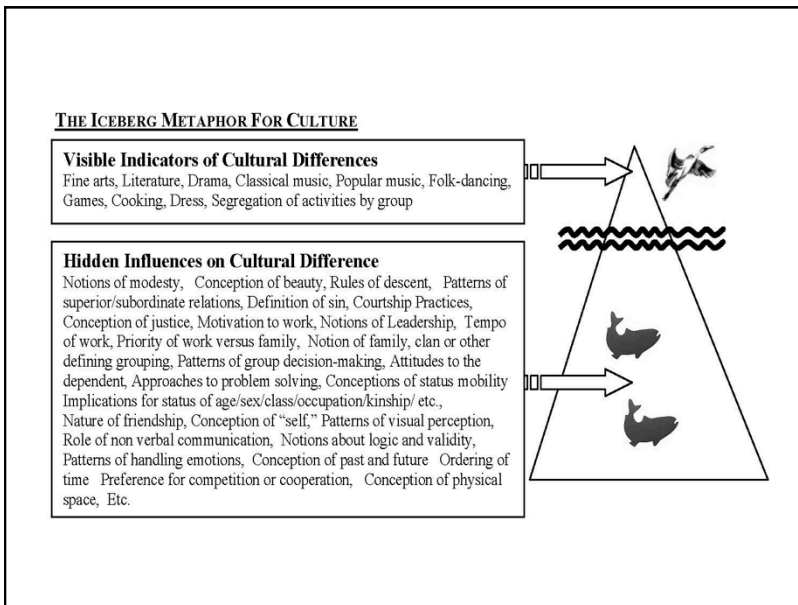


Cultural differences have fundamental impacts

- Our culture shapes the way we see the world.
- How we see the world shapes what is important to individuals, to corporations and, in turn, how we view risks, and why we form and break business arrangements.
- Attitudes and values are not universal.

Obvious cultural faux pas (the tip of the iceberg)

- Multiple types of potential blunder:
- Some examples:
 - Linguistic
 - Non-Verbal
 - Status & Etiquette
 - Local Taboos



Different perspectives prompt different approaches
Traditional American Style

- American negotiators frequently assume that their counterparts have the power to conclude a deal.
- Get straight to the point.
- Break down the issues into “logical” categories sequentially until all aspects are resolved.
- Adhere to stringent deadlines: positioning requires the possibility of withdrawal.
- Emotional outbursts are a sign of weakness.

Different perspectives prompt different approaches

- Negotiators from different cultures may be very confused:
 - Lack power to sign the deal without confirmation from his superiors.
 - No chance to establish any kind of personal rapport with the Americans.
 - Lack of emotion signifies disinterest while confrontational approach is disrespectful or worse.
 - Big picture lost in focus on detail.
 - Agitation over an arbitrary deadline suggests opportunities to leverage concessions.

A tool of general applicability

- **Cross-cultural competency is not culture-specific**
 - It is the ability to perceive how the dynamics of other societies differ, and to find ways to adapt such differences to produce workable outcomes.
 1. Recognize that there are fundamental differences between cultures.
 2. Question how these differences may affect business relationship building and maintenance, legal documents, risk appetite, dispute avoidance, effective communication and management methods.
 3. Identify solutions and adapt process and expectations to bridge the cultural divides.
 4. Identify cross-cultural synergies (win-wins using both cultures)

Conflicts: Which Rules Apply

- Often more a problem of conflicting business practices than conflicting laws.
- Risk management issue on liabilities.
- Can set up separate structures to mitigate conflicting laws in some cases.
- Usually safer if you follow the more restrictive law or operating model.

Local Regulators

- Capabilities and training can vary from country to country.
- Regulators can range from highly skilled and educated to incompetent.
- Regulators in emerging markets may need more background on business structure and objectives.
- No substitute for good local representation.
- Former regulators can be an effective tool

Legal Support

- Should have representatives at each site:
- Direct employee
- Trusted law firm/accountant
- Have several sources and do not rely on just one
- Constantly re-evaluate performance
- Beware of promises and guarantees

Emerging Markets

- More costly.
- Plan on things taking longer than usual.
- Understand political drivers.
- Cultural understanding is more critical.
- Be prepared for unexpected changes in the law/policy and implementation.

European Cultural Comparisons

- American cultural roots have many European origins (then blended and adapted)
- Despite EU and Euro, European culture retains distinct country cultural differences—omnipresent and not easily changed
- Europeans typically consider history relevant, travel extensively abroad and are multi-lingual
- Europeans stay abreast of American business trends and politics

European Legal Differences Impacting Business Negotiations

- Typically Civil Code Orientation v. Common Law
- Major differences in substantive law between countries (even as to adoption of EU directives by member states)
- Civil Law Notaries: Substantive Comments
- Legal Privilege: Not for European In-house Lawyers
- Burden of Proof: Through Party's own Documents (affects records management and discovery)
- Class Actions: Not Common
- Contingency Fee Arrangements: Not Common
- Dispute Resolution—court systems typically very slow

Total Harmony



Thank You

Negotiating in Asia

- A mix of extremely varied civilisations/culture.
- Varied legal regimes – both civil and common law.
- Critical to heed the macro cultural context
 - Society over individual.
 - Emphasis on relationships (harmony/cooperation) and long-term objectives.
 - Premium placed on compromise; patience and re-negotiation is required.

Negotiating in Asia

- Fine details (seating arrangements, manner of exchanging cards and level of eye contact) need to be managed.
- Trust building / social interface is key.
- Indirect / implicit, vague and non-verbal communication.
- The concept of 'face'.
- An expectation of gift giving.
- More rigid gender roles.
- Respect for the elder.
- Tiered approval of seniors.
- Family dominated business structures.

The Ability to Bridge Cultural Differences: A Prerequisite for Good Counsel in International Transactions

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Introduction

Our culture shapes the way we see the world.¹ How we see the world shapes what we regard as proper, or important, and, hence, how we organize our society and evaluate the propriety of actions, in everyday life, in business and at law. Where cultural values differ, the same comment, concept, text or act may be understood completely differently. For this reason, the ability to appreciate cultural differences is essential to successful international commerce, and to the provision of legal services that support it.²

Culture is the "set of distinctive spiritual, material, intellectual and emotional features of society or a social group and ... encompasses, in addition to art and literature, lifestyles, ways of living together, value systems, traditions and beliefs."³ Unfortunately, visible manifestations of cultural differences—such as fine arts, literature, drama, music, pastimes, cuisine and dress—are of little practical help in predicting how cultural differences will affect notions of how business should be conducted and the enforcement mechanisms that underpin business certainty.⁴ The visible manifestations of cultural difference have been compared to the tip of an iceberg, since they represent only a tiny fraction of the whole and are visible only because of the existence of the much larger body of unseen influences.⁵

¹ Cultures are not coterminous with nationality, but tend to be ethnically, and sometimes religiously, defined. Cultures may co-exist, with the dominant one largely shaping the society, or the predominant culture may vary by region. See, Convention on the Protection and Promotion of the Diversity of Cultural Expressions (2005) Article 2(3), available at http://portal.unesco.org/en/ev.php-URL_ID=31038&URL_DO=DO_TOPIC&URL_SECTION=201.html. Culture evolves over time and from outside contact, though generally on a generational time scale. See, John Hewko, "Foreign Direct Investment in Transitional Economies: Does the Rule of Law Matter?" East European Constitutional Review, Fall 2002/Winter 2003, p. 78. Individuals within a culture will vary in the degree to which they reflect cultural generalizations due to differing exposure to divergent cultural traditions and that exist in all societies and differences in the personality of individual members of societies and cultures.

² This paper addresses the impact of cultural differences on business negotiation. The purpose is to illustrate how cross-culturally adept legal representation is essential, both to the successful conclusion of sustainable, economically viable and enforceable business agreements and to the maintenance of these going forward. For an in-depth examination of why and how cross-cultural competence in legal representatives can be especially influential on the outcome of international arbitration and other forms of alternative commercial dispute resolution, see the authors' previous article, in "Cross-Cultural Understanding: An Essential Skill in International Advocacy," in INTERNATIONAL MEDIATION & ARBITRATION FROM THE PROFESSIONAL'S PERSPECTIVE, Anita Alibekova & Robert Carrow eds., Yorkhill Law Publishing (2007) ISBN: 978-1-4303-2526-0, pp. 55-83.

³ UNESCO definition (2002). Source: http://www.unesco.org/education/imld_2002/universal_decla.shtml#1.

⁴ See, the authors, in Alibekova et al, eds., supra, n.2.

⁵ See, e.g., Intercultural Learning T-Kit, Silvio Marinelli, ed., Council of Europe Publishing (2000). ISBN 92-871-5364-7, p. 21, attributed to "AFS Orientation Handbook," Vol. 4, p 14, New York: AFS Intercultural Programs Inc., 1984.

Culture goes to the heart of whether a party will view a business opportunity as worthy of investigation, the terms on which it will do so, and the likelihood that the relationship will be lasting and mutually beneficial. It shapes the conception of what has been entered into and perceptions of why each party has done so, and hence can legitimately expect as a result. Not surprisingly, therefore, it also plays a role in the emergence of disagreements and misunderstandings, whether these escalate into disputes, and whether and how such disputes can be resolved.

To appreciate the perspective of another culture, one must understand that even the most fundamental tenets of our own culture may not be recognized, let alone understood, in another. Such appreciation entails not only an ability to appraise the fundamental values of others, but to realize that such cherished concepts as freedom, democracy, transparency and individual rights may not be shared, and that this difference critically impacts business transactions and notions of law.

For example, if the written law of a jurisdiction is not what determines behavior, it is likely that instruments that draw their force from written law will be of limited or questionable value as well. There will almost always be an indigenous means of achieving certainty in business and resolution of disputes, but this means may not be legalistic in the Western sense. Cultural rules may be unwritten and may operate by changing the meanings of written law in ways that reflect the traditional values of the importing culture. Dispute resolution may be based on the application of moral codes or interpretations of religious teachings. In such circumstances, transactional undertakings or litigation conducted on the basis of written law alone are unlikely to produce the desired outcome.

Failure to appreciate cultural differences can be fatal to any international negotiation. Americans have acknowledged such failings in the past: “America has never lost a war and never won a conference.”⁶ Failure to understand foreign cultures can be disastrous at the governmental level; it can be equally so in business and in litigation. “Cultural differences are the most significant and troublesome variables ... the failure of managers to fully comprehend these disparities has led to most international business blunders.”⁷ Differences in approaches

⁶ Will Rogers, a 20th Century U.S. wit, purportedly reacting to the Versailles Peace Conference after World War One.

⁷ DAVID A. RICKS, “BLUNDERS IN INTERNATIONAL BUSINESS,” *quoted in* Margaret Kammeyer, *The Other Customs Barrier: Cultural Research Avoids Business Blunders*, Export America, April 2001, p. 32.

to the completion of tasks, to timeliness, and to conflict, decision-making and management are frequent causes of problems with transnational business dealings.⁸ The scale of the problem for lawyers is increasing dramatically as the amount of cross-border transactions increases. Phenomena such as outsourcing of production or functions, as well as the Internet, have dramatically increased the number of businesses that conduct international transactions. Furthermore, the changing balance of economic power may signal the increasing importance of cultural factors in transnational business and legal practice, contrary to the long-held general Western assumption that economic progress will inevitably usher in universal Western legalism.

The increase in international transactions can be expected to result in more disputes. Cross-cultural skills can be the difference between smooth resolution of a problem and escalation of that problem into a dispute, at which point the same skills can critically impact the potential for a satisfactory outcome in any form of dispute resolution process. The increasing number of smaller businesses involved in international transactions has already led to advice on such matters being no longer solely the domain of the biggest international firms, able to access their own lawyers admitted in most foreign jurisdictions. The combination of a wave of novice clients and advisors suggests that the consequences of legal advice and litigation bereft of cultural acuity could become a source of major client dissatisfaction and litigation in the near future.

Advice by American lawyers regarding legal matters in a foreign jurisdiction requires compliance with the minimal standards of professional competence. *Black's Law Dictionary* defines competence as “[a] basic or minimal ability to do something.”⁹ There are two elements to this basic competence: knowledge and legal skills. “A competent lawyer possesses sufficient information about law and legal institutions to be able to deal effectively with many common legal problems, to recognize legal problems that require legal research, and to assess the lawyer’s own ability to deal with a legal problem.”¹⁰ The American Bar Association (ABA) defines competent representation as requiring “the legal knowledge, skill,

⁸ Andy McCue, “*Cultural Differences Cause Offshoring Problems*,” Silicon.com, June 17, 2006, available at <http://services.silicon.com/offshoring/0,3800004877,39160348,00.htm>.

⁹ BLACK’S LAW DICTIONARY 278 (7th ed. 1999).

¹⁰ CHARLES W. WOLFRAM, MODERN LEGAL ETHICS, West Publishing Co. (1986) ISBN 0-314-92639-9, p. 185.

thoroughness and preparation reasonably necessary for the representation.”¹¹ Such minimal capabilities require “a fair modicum of knowledge and skill”; a newly-trained lawyer should not have an overdeveloped sense of his or her ability as a practicing lawyer.¹² Significantly, failure to achieve such standards flirts with malpractice, defined by *Black’s* as a “failure to render professional services with the skill, prudence, and diligence that an ordinary and reasonable lawyer would use under similar circumstances.”¹³

Tools exist to assist in predicting salient sources of cultural difference and illustrate that, even in established legal systems, different underlying values have a fundamental impact on the operation of commercial law, in transactions and litigation. However, in emerging economies, such effects may become even more profound. In such jurisdictions, law (in the Western sense) may be only marginally involved in either the development of a transactional relationship or dispute resolution, such that cultural awareness and adroitness become perhaps the most critical elements of advice.

Businesses seem to have realized that cross-cultural skills are essential to successful international commerce. There is plenty of evidence that many companies are investing heavily in training their personnel, yet there are also disturbing suggestions that law firms and practitioners are lagging behind their clients with regard to the significance of cross-cultural issues and the investment required to ensure culturally adept legal services. If true, this cannot be good for the profession or for clients, and the proliferation of international transactions and associated legal advice may become a significant source of liability for attorneys who venture to advise their clients without an appropriate understanding of foreseeable cultural issues. As such, appreciation of cultural differences is increasingly an indispensable skill for business counsel.

Has Economic Power Confused Western Cultural Values With Universal Certainties?

The basis of modern international business is the concept of contracts and a legal system (whether civil or common law in nature) that provides a basis for contract interpretation and enforcement. It is easy to fall into the trap of regarding one’s own legal structure as a kind of platonic form, an expression of the rational way of ordering things. It is

¹¹ ABA Model Rules of Professional Conduct (2004), Rule 1.1.

¹² WOLFRAM, *supra*, n.10. p. 187.

¹³ BLACK’S LAW DICTIONARY 971 (7th ed. 1999).

even more tempting to believe that individualistic legalism is a prerequisite of an effective commercial system. Yet such assumptions are open to being challenged as culturally blinkered. Legal systems that have developed organically within a culture are the reflection, not the source, of that culture's values.¹⁴ The current global commercial system is arguably a construct of two similar, sequentially-dominant cultures: British and American. It is based on assumptions that contracts are binding and recourse to law is properly an early option. In short, it is a product of an individualistic, legalistic and short-term oriented culture.¹⁵ In other cultures, these values are dissonant, and the result is a different attitude to the conduct of commerce, and to dispute resolution.¹⁶

Business practices reflect cultural sensitivities and objectives, and, hence, are not universal. For example, in the United States, profit is seen as a legitimate goal, success in business can be measured empirically, and the work ethic is highly developed.¹⁷ For the Japanese, the focus may not be on the pursuit of bottom line profit alone, but also include considerations of human efficiency; the group is superior to the individual. In France, an emphasis on moderating one's own freedom of action in order to avoid harming the interests of others is common, often expressed as a social compact.¹⁸ This is not to say that a French or Japanese person does not seek to make a profit. It is simply that business people from these and other cultures may not necessarily view true return on investment as measurable solely by bottom-line financial gain, but rather as an amalgam of profit, long-term market position, and the welfare of all stakeholders in the venture, including the workforce, and perhaps even the local community.

As commerce is shaped by culture, so is law. Commercial law is designed chiefly to perform two functions: the creation of certainty in business transactions, and the resolution of

¹⁴ William K. Slate II, "Paying Attention to 'CULTURE' in International Commercial Arbitration," 59 Disp. Resol. J. 96 (Aug.-Oct. 2004), available at http://www.findarticles.com/p/articles/mi_qa3923/is_200408/ai_n9430961. Mr. Slate is the former Chief Executive Officer and President of the American Arbitration Association.

¹⁵ In this context, short-term means a focus on an individual transaction rather than a long-term, evolving business relationship.

¹⁶ In the modern world, many formerly authoritarian nations and developing economies have adopted entire legal codes, or copied large tracts of western commercial law. Such imports inherently reflect the values of the originating culture and are unlikely to accord with those of the importing nation.

¹⁷ P. Poirson, "Personnel Policies and the Management of Men," *Ecole Supérieure de Commerce de Lyon*, Trans. Thierry Devisse. (1989), cited in TORRINGTON, DEREK TORRINGTON & LAURA HALL, PERSONNEL MANAGEMENT: HRM IN ACTION," Prentice Hall, 3rd ed. (1995), ISBN 0-13-149543-7, p. 117.

¹⁸ TORRINGTON, et al., *supra*, n.17, p. 117.

disputes.¹⁹ Dispute resolution and commercial regulation are based on conceptions of what is important to an individual, and in society. In a culture where a contract is absolute, interpretation on the basis of the language is not only logical, but also essential to establishing certainty in the marketplace. However, in many cultures, commercial accommodation requires trust, which can be created only by the gradual building of a relationship.²⁰ In such societies, a written contract is not always seen as a rational final embodiment of the accommodation.²¹ The idea that words on paper could replace trust built through mutual understanding may appear ludicrous. In such cultures, a breach of an obligation under a relationship duly grounded in trust may carry infinitely more severe consequences than a breach of contract.

From many Westerners, the attitude that Western values are somehow “more advanced” or “inherently superior” is arguably deeply ingrained. Two particularly unabashed examples, three quarters of a century apart, ably illustrate the kind of thinking that tempts us to assume that, for example, Western-style contract law is a prerequisite of a stable business environment capable of supporting a developed economy. Perhaps the classic enunciation of the Victorian imperialism is contained in Rudyard Kipling’s 1899 poem “*The White Man’s Burden*,”²² a call for the United States to assume the task of developing the Philippines, acquired during the Spanish-American War. Kipling’s message is clear: America had a moral obligation to intervene and bring the “benefits” of their cultural achievements to less fortunate

¹⁹ “The very first need of the business community is legal predictability. An unpredictable legal climate is unacceptable to business, forcing traders into necessary legal advice and insurance cover to secure against the risk of their deals being defeated.” Lord Irvine of Lairg, “*The Law, an Engine for Trade*” (2001) 64 MLR 333, p. 334.

²⁰ “*Seven Disciplines for Venturing in China*,” Deloitte Research (2005), p. 4 col. 1.

²¹ The Japanese have sometimes been characterized as averse to written contracts. Rather, certainty comes from “*giri*,” a system of intertwining social and moral obligations. “In the event that parties under *giri* should fall into a dispute, then they will adopt a conciliatory and flexible concessionaire approach. The presence of *giri* might be incompatible with the nature of litigation and operate to inhibit a resort to legal resolution of disputes.”

Masayuki Yoshida, “*The Reluctant Japanese Litigant: A New Assessment*,” available at: <http://www.japanesestudies.org.uk/discussionpapers/Yoshida.html>.

²² Rudyard Kipling, “*The White Man’s Burden: The United States and the Philippine Islands*,” McClure’s Magazine 12 (Feb. 1899), available at: <http://www.fordham.edu/halsall/mod/Kipling.html>. Verses 2, 3 and 5 read: (1) *Take up the White Man’s burden / Send forth the best ye breed / Go bind your sons to exile / To serve your captives’ need / To wait in heavy harness / On fluttered folk and wild— / Your new-caught, sullen peoples, / Half devil and half child.* (2) *Take up the White Man’s burden / In patience to abide / To veil the threat of terror / And check the show of pride; / By open speech and simple / An hundred times made plain / To seek another’s profit / And work another’s gain.* (5) *Take up the White Man’s burden— / And reap his old reward: / The blame of those ye better / The hate of those ye guard— / The cry of hosts ye humour / (Ah slowly) to the light: / “Why brought ye us from bondage, / “Our loved Egyptian night?”*

peoples.—whether the recipients desired this or not. The unambiguous underlying belief is that Anglo-American culture is morally superior. Indeed, the beneficiaries of intervention were expected to resist, until raised up to a more enlightened position that enabled them to appreciate the benefits.

It is tempting to dismiss such sentiments as relics of a bygone age. But, consider the statements of U.S. Congressmen leading up to the passage of the Foreign Corrupt Practices Act (FCPA) in 1977.²³ During Watergate hearings, it emerged that American companies had been making “unethical” payments to secure business and favor overseas.²⁴ The revelations caused public outrage. Congress reacted with the Foreign Corrupt Practices Act, unilaterally prohibiting bribery of foreign officials.²⁵ The legislative history of the FCPA contains plenty of insight into the moral objectives and certainty of its supporters. “From a social perspective, business transactions that generate the payment of questionable or illegal payments are morally repugnant.”²⁶ Such acts are “counter to the moral expectations of the American public”²⁷ and “interference with democratic ideals with corporate gifts undermines everything we are trying to do as leader of the free world.”²⁸ In short, American legislators believed that such behavior, whether or not proper in the country in which it took place, was beneath the standard of morality that Americans expect of themselves. The parallels with Kipling are obvious: America must shoulder the burden of raising the standards of morality elsewhere to the level achieved domestically, despite any economic cost. In other words, the FCPA signaled America’s unilateral assumption of a moral duty to, as it saw it, raise the rest of the world up to its standards of propriety.

This is not a critique of the FCPA, which is simply a salient example of thinking predicated on an assumption of the superiority of Western values, extending from morality

²³ 15 U.S.C § 78dd-2.

²⁴ Department of Justice (DOJ), “*Foreign Corrupt Practices Act: Anti Bribery Provisions*,” briefing, available at: <http://www.usdoj.gov/criminal/fraud/docs/dojdocb.html>. Over 400 companies took advantage of a moratorium to admit to the Securities and Exchange Commission (SEC) “questionable or illegal” payments amounting to some \$300 million.

²⁵ The FCPA prohibits any offer, promise or gift of “anything of value” to a foreign official for the purposes of influencing any act or decision in violation of the lawful duty of such official, or securing an improper advantage or inducing the official to use his or her influence with a foreign government to influence any act or decision of that government or any instrumentality thereof. The prohibition covers anything designed to assist “in obtaining or retaining business for, or with, or directing business to any person.” 15 U.S.C § 78dd-2(a).

²⁶ H.R. Rep. No. 640, at 1-5 (1977).

²⁷ *Id.*

²⁸ The Activities of American Multinational Corporations Abroad, Hearings before the Subcommittee on International Economic Policy, 94th Congress, 1 (1975).

into political, legal and economic structures and practices. Other manifestations of Western cultural assumptions are commonplace and Americans are by no means the only source. Western academic and professional thought is often felt by outsiders to be colored in this way. For example, many Western commentators have assumed that full economic development in a country inherently requires the development of liberal democracy and rule of (Western-style) law.²⁹ While events may yet prove this to be true, the evidence—from Asia at least—is inconclusive at best.³⁰ This assumption is significant to lawyers because it often forms a major plank in predictions regarding the future enforceability of civil and commercial rights in emerging economies. If this assumption is really the inappropriate juxtaposition of an alien cultural conclusion, then lawyers that do not at least question it may be misled as to the significance of developments in statutes or judicial process in other parts of the globe.

Acquiring Cross-Cultural Competence is Not an Easy Process

Once one accepts that different cultures operate differently and are grounded on different assumptions, it becomes clear that the form of any business or legal undertaking must accommodate the different objectives and needs of those involved.³¹ However, the journey to understanding that this is the case may be neither easy nor, for many, comfortable.

Acquiring the ability to operate effectively across different cultures is a process requiring an individual to question fundamental personal and professional assumptions. Such personal reappraisal is a necessary precursor to the development of the ability to assess the differences in terms of practical consequences and, hence, identify a viable approach to a particular legal or business objective. This is a skill that takes time to hone. It may also require a significant catalyst to create sufficient awareness of the problem—the natural

²⁹ For an erudite example of a work that appears predicated on this assumption, *see, e.g.*, RANDALL PEERENBOOM, "CHINA'S LONG MARCH TOWARD RULE OF LAW," Cambridge University Press, 2002 ISBN 0-521-01674-6. This is merely one among many academic and professional pieces that appear to make this supposition.

³⁰ *See, e.g.*, Jane Kaufman Winn, "Relational Practices and the Marginalization of Law: Informal Financial Practices of Small Businesses in Taiwan," originally published in *Law and Society Review* 28/2 (1994), reprinted in full in *CONTRACT, GUANXI AND DISPUTE RESOLUTION IN CHINA*, Tanhirih V. Lee, ed., Garland Publishing Inc. (1997), 223-24 ISBN 0-8153-2483-9, pp. 235.

³¹ Mitchell R. Hammer & Milton J. Bennett. *The Intercultural Development Inventory (IDI) Manual*. Intercultural Communication Institute (1998). An introduction to the IDI concept is available at: http://www.aucp.org/sous_pages/aix/IDI%20Explained.pdf.

inclination, of lawyers and businesspeople alike, may initially be, first, to deny the existence of real differences and, when this becomes untenable, to dismiss them as insignificant.³²

Cross-cultural competency is not culture-specific, but is a general ability to combine observed and reported behavior with an understanding of common cultural differences and their manifestations. It is the ability to perceive how the dynamics of other societies differ, and to find ways to surmount such differences to produce workable outcomes that meet the requirements and expectations of all parties. Thus, while a cross-culturally adept lawyer may have a greater learning curve with a culture that he or she has not addressed previously, he or she will possess the tools to acquire the necessary knowledge.

Cross-cultural competence is not the same as assuming the *Weltanschauung*³³ of another culture. To truly understand a foreign culture as does a native may be a (long) life's work. Anecdotes, many certainly apocryphal, abound concerning the foreigner who came to believe that he or she was fluent in a culture after many years, only to come to tragicomic grief. The critical element is to be able to identify potential problems and find ways to bridge the cultures involved to ensure that the parties share an understanding, that an agreement can be meaningfully enforced, that an argument is in a form that appeals to a tribunal, and so on. Often a key element will be the ability to find local counterparts with similar skills, to enable the effective exchange of information and issues. Finding the right counterpart is part of the cross-cultural skill-set and is not the same as, for example, finding a local lawyer. Even within the same firm and office, cultural communication may fail—many cultural business disasters have been attributed to the failure to communicate effectively across such internal corporate cultural divides.³⁴

According to Bennett and Hammer, the first step is to realize that there are fundamental differences between cultures.³⁵ Once this has occurred, most people go through phases where they deny the real significance of the differences or become defensive—this

³² *Id.*

³³ *Weltanschauung* is a German noun signifying the “overall perspective from which one sees and interprets the world”. The American Heritage® Dictionary, 4th ed., Houghton Mifflin Company (2006). The term has no true English equivalent, but is often inadequately rendered into English as “world view.”

³⁴ See, e.g., Daniel Altman, “*Managing Globalization: Crossing borders? Then expect culture clashes.*” International Herald Tribune, June 27, 2006. Available at:

<http://www.iht.com/articles/2006/06/27/business/glob28.php> .

³⁵ Bennett et al., *supra*, n.31

generally manifests as hostility to the practices and principles of the different culture.³⁶ The next phase is to accept that legitimate cultural differences exist and that these differences have significant impact on the way societies operate.³⁷ At this point, respect and curiosity are often exhibited, but there is no acceptance that a cross-cultural solution is necessary.³⁸ To gain such acceptance—the final stage—the ability to get inside the mindset of the other culture must have developed to a point where legal advice can be adapted to produce solutions that meet the needs of both parties.³⁹ Achieving such cross-cultural adroitness requires significant time and experience.⁴⁰

Law firms have, for the most part, been slow to follow the increasing trend in business circles to train employees in cross-cultural skills.⁴¹ Some international firms are on record as believing that cross-cultural awareness is unnecessary, because they have so many offices in so many nations, or because such issues can be adequately addressed informally, or as an adjunct to domestic sensitivity training.⁴² This appears to confuse international diversity and cross-cultural understanding, and contrasts with the approach of many major businesses that retain such firms. Others may be more candid: “Some lawyers said law firms don't invest in cross-cultural training because it can't be linked to billable hours.”⁴³ For others the issue seems to equate to business etiquette—surely the very tip of the cultural iceberg. “[I]t's not terribly effective to have a workshop or a course that will tell you how to receive business cards,” notes the head of one multinational law firm,⁴⁴ suggesting that some law firms have yet to become appreciative of the impact of culture.

The increasing globalization of commerce is expected to continue for the foreseeable future. If that is the case, and if the process of becoming adept in advising across cultural boundaries is as involved and difficult as Bennett and Hammer suggest, then how likely is it

³⁶ *Id.*

³⁷ *Id.*

³⁸ *Id.*

³⁹ *Se, id.*

⁴⁰ *Id.*

⁴¹ As one business performance consultancy to law firms notes: “North American lawyers, in particular, may be surprised to learn that styles and behaviors that work well at home may produce unintended negative effects among lawyers and staff in other countries.” Source: <http://www.walkerclark.com/articles.html>.

⁴² *See, e.g.,* Vesna Jaksic, “*The Culture Gap: Firms going global study client customs,*” *The National Law Journal*, May 11, 2007, available at:

<http://www.law.com/jsp/llf/PubArticleLLF.jsp?id=1178787890511&rss=newswire>.

⁴³ *Id.*

⁴⁴ *Id.* (quoting the managing partner of one of the world's largest law firms).

that clients will regard cross-cultural skills as marginal or optional elements in their requirements of legal counsel? If the legal profession fails to keep pace with client expectations and internal capabilities on this issue, the consequences for lawyers, firms, and the reputation of the profession as a whole may be unpleasant.

Domestic Legal Training and Practice Neither Fosters Cross-Cultural Skills Nor Exposes Attorneys to International Cultural Issues

Lawyers are trained to acquire information, to analyze materials and draw conclusions according to certain rules, to document transactions, and present argument in certain ways. Essentially, this learning is the source of our expertise as domestic counsel. However, this training arguably creates an added layer of programming that must be transcended in order to achieve cross-cultural competence. While applicable to any national legal training regime, the American example is illustrative, and perhaps especially pertinent given America's status as the largest economy.

The nature of American legal training and practice rests on the premise that law school and bar examinations are not required to produce an expert legal practitioner, but rather one with a basic competence in the American legal system, on which professional experience can build.⁴⁵ Inculcation of a process of critical thought has been the guiding principle of American legal education since 1870.⁴⁶ A competent lawyer must be equipped with the skills to “effectively represent and sensitively communicate with a client in one or more of the common lawyer roles: analyzing a client's problem in the light of available facts and law, investigating, researching, planning, advising, negotiating, mediating and litigating.”⁴⁷ All graduates of U.S. law schools are supposed to have the basic tools, including the ability to locate legal sources to acquire particularized knowledge, or to realize that additional or special assistance from another lawyer is required. The American legal educational establishment has grounds for its belief that, in terms of domestic law, it is reasonably adept at providing a tool kit, such that “incompetence ... caused by serious deficiencies in an individual lawyer's ... formal training ... [is] probably quite rare.”⁴⁸ Once in practice, a lawyer will learn both

⁴⁵ While other systems also train students in equivalent techniques, most also require a practical element of training, and thus arguably place less emphasis on thought process as a basis of practice.

⁴⁶ WOLFRAM, *supra*, n.10, p. 195.

⁴⁷ *Id.* at 185.

⁴⁸ *Id.* at 186.

techniques and special knowledge associated with his or her field of activity; however, this will be within the philosophies and practices of the American legal system.

Yet “[t]he practices and philosophies of lawyers practicing in other legal cultures very often bear little resemblance to those of lawyers in the U.S.”⁴⁹ Thus, the premise on which the competence of American lawyers is based is removed when those lawyers must deal with other cultures. For example, *stare decisis*—literally “standing by what has been decided”—is not only a principle, but defines how an American lawyer determines what the law is. What if the principle is not recognized, and the relevant statute is a mere two lines of text? Further, what if the rule is unwritten, decisions are unpublished, and the ability to appeal is non-existent? Alternatively, written law may simply be interpreted in the light of local values, producing very different meanings from those an American might deduce from the text. Lawyers are trained to think in a certain way, and to appraise situations via methods that work domestically, but that may result a totally misleading appraisal of issues and opportunities in a system that does not operate upon the same principles. Furthermore, the more one is conditioned to rely on a given thought process, the more confusion may result when traditional signs and signals are absent.⁵⁰

From the earliest days of nationhood, U.S. courts have recognized that overseas law is fundamentally different. In 1796, Justice Iredell stated that “[e]very man is bound to know the laws of his own country; but no man is bound to know the laws of foreign countries.”⁵¹ The reasons for this were well summarized by another court some 170 years later: “Access to the laws of foreign countries is . . . difficult. Even if the laws were readily available, language barriers, problems of interpretation and unfamiliar legal systems compound the difficulties involved in a search of the law.”⁵²

If legal qualifications in one country were truly sufficient to support competence in another, then one would expect interchangeability to be allowed between at least some national jurisdictions. In reality, there is no such arrangement between any developed legal jurisdictions. The convention is to restrict the ability of foreign lawyers to practice domestic law completely, or to require some element of additional training, evidenced by examinations,

⁴⁹ *Id.* at 4-5.

⁵⁰ Kalvero Oberg, “*Culture Shock: Adjustment To New Cultural Environments*,” 7 *Practical Anthropology* (1960), pp. 177-82.

⁵¹ *Searight v. Calbraith*, 21 F. Cas. 927, 928, 4 U.S. 325 (U.S. Ct. App. 1796).

⁵² *Milwaukee Cheese Co. v. Olafsson*, 162 N.W.2d 609, 613, 40 Wis. 2d 575, 581 (Wis. 1968).

in some cases no less than that required for non-lawyers. This is a more complex, but no less revealing, expression of the differences between legal systems and what constitutes adequate skill and knowledge to provide competent representation. Both American and EU jurisdictions consistently require lawyers from overseas nations to pass examinations if they are to provide advice beyond that a layperson would be entitled to offer.

In America, at least the full state bar examination is required, and possibly more. New York allows overseas lawyers to sit for its bar exam subject to prior completion of 20 semester hours of study in a U.S. law school, or proof of three years practice in a common law jurisdiction.⁵³ At the other end of the scale, Texas has adopted a purely discretionary approach to overseas training and experience, which places the burden on the applicant to prove relevance, and often leads to applicants from civil law jurisdictions receiving no credit for past experience.⁵⁴ In practice, lawyers qualified in civil law jurisdictions are more or less constrained to complete an L.L.M. from an American law school before being permitted to take bar exams.⁵⁵ In the EU, there is a similar range of attitudes to admittance of foreign counsel to practice. In some countries, a foreign practitioners test, such as the Qualified Lawyers Transfer Test (QLLT) required by the Solicitors Regulation Authority of England and Wales, will be necessary.⁵⁶ Other nations are as yet unready to provide any means to admission other than completion of full domestic training. For example, an American lawyer based in Belgium cannot advise on Belgian law without locally qualified lead counsel named

⁵³ Sydney M. Cone III, "Cross-Border Legal Practice In International Legal Centers as Viewed from New York," presented at ABA Section of International Law and Practice Conference on Regulation of Cross-Border Legal Practice: Transactional Dialogues on Law and Practice, Brussels, October 12, 2003. Available at <http://www.abanet.org/intlaw/hubs/programs/Fall0311.01-11.04.pdf>

⁵⁴ Wayne J. Carroll, "Innocents Abroad: Opportunities and Challenges for the International Legal Adviser," 34 Vand. J. Transnat'l L. 1097, 1109 (2001).

⁵⁵ Carole Silver, "Lawyers on Foreign Ground", p. 13, available at http://www.law.northwestern.edu/faculty/fulltime/silver/documents/chapter_foreign_lawyer.pdf. (originally published in MARK JANIS AND SALLI SCHWARZ, EDS., CAREERS IN INTERNATIONAL LAW (ABA 2001), pp. 1-21).

⁵⁶ Solicitors Regulation Authority, "Qualified Lawyers Transfer Test: Test Specification," (2007) p. 2. The QLLT is a conversion test, not an equivalent of an American bar exam. "The purpose of the test is to identify candidates who have a sound knowledge of the principles of common law and the distinctive features of practice in England and Wales relating to the major actions or transactions in common areas of practice." *Id.* at 3. U.S. lawyers are excused from the Principles of Common Law element. Lawyers from most Commonwealth common law jurisdictions need only take the Professional Conduct & Accounts paper. Lawyers for other EU (civil law) jurisdictions must take the full test. *See*: http://www.college-of-law.co.uk/uploadedFiles/core/Brochures/qltt_brochure.pdf.

as the source of advice on any communication unless the American lawyer has undergone the full standard process of qualification as a *tableau* lawyer required of Belgian nationals.⁵⁷

Both the professional bodies and judiciary on both sides of the Atlantic seem to feel that foreign-trained lawyers are not, as a general rule, equipped to understand domestic law despite their legal qualifications and experience in their country of training. There is a general acceptance that neither legal skills nor knowledge is readily transferable, and this, in part, appears to be due not to substantive differences, but to cultural notions of interpretation and application. Lawyers embarking on transnational practice may lack awareness of the critical role of culture in the actual operation of law in other nations. Without such awareness, there is a real danger of culturally inapplicable analysis and consequently of providing flawed advice to the detriment of one's client. It is hard to overemphasize the potential for disaster posed by cultural ineptitude in the provision of legal services in support of transnational commerce.

Of course, there are at least two cultures involved in any cross-cultural misunderstanding. As it is easy for members of one culture to perceive "strangeness" in the ways of another, so it is tempting to fall back on a purely outward-looking perspective. However, to do so should be recognized as embodiment of the ethnocentric assumption that one's own culture does things in the only "natural" or "rational" way. In fact, what is considered "natural" behavior by Americans often seems perplexing, irrational and even rude to much of the rest of the world. Just as business can be pointlessly undermined or lost in foreign lands as a result of cultural ineptitude, so it can be lost in the United States as a result of failing to bridge the gap to American culture.

Negotiators from societies where relationship is the determinant of confidence are often baffled by the short-term, transaction-based, focus of Americans. To them, building a relationship is a major investment that is nonsensical if only one transaction is contemplated.

⁵⁷ Laurel S. Terry, "A Case Study of the Hybrid Model For Facilitating Cross-Border Legal Practice: The Agreement Between The American Bar Association and The Brussels Bars" 21 *Fordham Int'l L. J.* 1382, 1430 (1998). Lawyers qualified in EU member countries may provide temporary cross-border services without prior representation. This is rather similar to the ability of American lawyers to advise on the law of other states concomitant to their on-going in-state representation, and to apply for admission before a court *pro hac vice*. Although there is a requirement in the EU for introduction to the court by local counsel, the European Court of Justice has rendered this a mere formality, with no requirement for involvement in the proceedings by the introducer similar to that expected of co-counsel in US actions involving other US jurisdictions. "Multi Jurisdictional Practice: The Experience of the Law Society of England and Wales" *supra*, n.32, at (2).

Furthermore, the American confidence in a contract may appear to be both pointless and akin to preparing to divorce before marriage. Contracts are often perceived as a means to prepare the ground for resort to court in the event of differences arising. Litigation carries the inherent risk of public “loss of face” that the careful forging of a relationship is meant to protect against. Furthermore, Americans divorce social and business relationships to a degree that baffles many cultures. Americans can be extremely forthright in a business meeting and yet depart as friends. To many cultures, such overt disagreement would kill a relationship.⁵⁸ In hierarchical cultures, a subordinate’s role is to put into effect the decisions of his or her superiors by diligent application of accepted processes. To see colleagues at different levels arguing can completely undermine confidence in the order of things, and in the seeming ability of the participants to cooperate in the future.⁵⁹

For counsel to participants in cross-cultural undertakings, the task must surely be to help the client. This requires an ability to anticipate and forestall such misunderstandings, which necessitates an ability to identify and explain the idiosyncrasies of the domestic and the foreign parties’ cultural notions of negotiations and dispute resolution in a manner that clients can comprehend. The law of physics, holding that for every action there is an equal and opposite reaction, is apposite: each parties’ domestic conception is likely equally incongruous from the cultural perspective of the other.

Such issues arise even between closely-related cultures. For example, British business people commonly spend considerable time seeking “agreement in principle.” This involves establishing that the parties share a mutual business interest in doing business of the kind envisaged and have similar conceptions of the broad parameters. Britons are often frustrated by Americans’ impatience with such discussions (which appear to them to be a necessary precursor to entering into detailed exchanges of information, and the expenditure of time and resources that these entail). Conversely, Americans wonder why the British are wasting time discussing ephemerals when they could get down to real facts and figures.⁶⁰ Interestingly, both see their approach as logical from an efficiency perspective. Other differences also arise. Americans often appear too “full of themselves” to Britons, who tend to self-depreciate and

⁵⁸ See, e.g., George B Whitfield, III, “*The View Across Cultures: Meetings and Expectations*,” available at www.expat.or.id/business/meetings/html.

⁵⁹ *Id.*

⁶⁰ Robert Day, “*Export Country Profiles – North America*,” Farnham Castle International Briefing (2002), available at www.link2exports.co.uk/regions.asp?1sid=658&pid=1208.

understate their case. The American is often merely showing enthusiasm and commitment for his or her company and the project, yet Britons can take it as suspicious over-confidence or as reflecting an attitude of superiority.⁶¹ Americans are similarly often baffled by the British reluctance to state a final rejection of a proposal. This may be linked to the concept of agreeing in principle (the time may not be right but the idea is valid), although a greater British reluctance to reject the other party outright can be a factor. The result can be that Americans regularly “get back on that,” creating discomfort and a feeling on the part of the British that Americans are insensitive to the obvious.⁶²

If such differences can exist between Americans and the foreign culture perhaps most closely linked to American law and business, it is hardly surprising that the potential for misunderstandings grows with the degree of separation between the cultures. As the degree of separation increases, so the number of differences in fundamental concepts increases and deepens. Legal systems reflect the culture that created them, and therefore that culture’s perception of the world. Not surprisingly, therefore, such systems differ in core precepts and the relative importance even of shared elements.

Differences in Culture Profoundly Impact Legal Analysis and Practice

The United States has a common law system, a characteristic basically restricted to former British possessions. Other long-standing developed economies generally have systems based upon civil law. Illinois law differs from that of New York, California, and all the other U.S. states, but for the most part the difference is substantive. The law of other nations also has substantive differences, but underpinning these is something perhaps harder to understand, a different appreciation of the proper values on which a legal system should be based, which is reflected in notions of origin of rights, the duties of individuals and proper conduct of investigation and the determination of truth.

Even in established legal systems with long histories of commercial interaction with common law parties and lawyers, these differences can have profound effects. One of the

⁶¹ *See, e.g., id.*

⁶² Such Anglo-American differences can result in a potential trading partnership eroding to a point where each business in fact resolves to avoid trading with the other for the foreseeable future, not simply the cancelation of the proposed transaction. Yet such differences can readily be avoided if each side understands the differences at the outset and tailors its actions and expectations accordingly. That such disconnects occur as often as they do suggests that cross-cultural understanding can have a significance even in dealings between parties from two closely-related cultures.

then most senior English Law Lords, Lord Templeman, acknowledged the practical difficulties posed by trans-system practice in commending an English text for “grappl[ing] manfully with the different problems of construing English and [European] Community legislation.”⁶³ In addition, there are other distinct types of legal systems more distant in cultural origin from U.S. common law. These include Sharia law, Hindu law and various forms of cultural “law,” such as the *guanxi* system of relationships in China, or *giri* in Japan. To make this class more complex, there are often overlays of adopted systems, such as Egypt, which has elements of civil, common and Sharia law, and South Africa, where common law is blended with uncodified civil law.⁶⁴ Many emerging nations have imported statute law, or more often civil law code, yet this written law often seems not to be determinative of courtroom practice. Indigenous lawyers know these systems and apply rules and practices developed from an understanding of the values of both judges and society in order to navigate them.

As has been observed, the law is a reflection of societal values; thus, a true understanding of divergent legal cultures requires an ability to identify the differing influences and to adapt accordingly. Consider contract law--a commonly faced, and representative, example of the difference in the conceptual approach underpinning the operation of civil law in European jurisdictions—as illustrative of the effects of such differences on business concepts and associated effective legal advice.

Variant Concepts in Contract Law

Under common law, a contract is not binding unless consideration of at least nominal value is exchanged. In civil law, the critical element is cause, which does not necessarily require any flow of consideration.⁶⁵ Thus, gratuitous promises may form the basis of a binding arrangement, and, as a result, contracts in favor of a third party can be recognized without any obstacle to enforcement by the third party stemming from the fact that they have not tendered

⁶³ The Rt. Hon. Lord Templeman MBE, Lord of Appeal in Ordinary (1982 to 1994), Foreword to JAMES A. HOLLAND & JULIAN S. WEBB, *LEARNING LEGAL RULES*, Blackstone Press, 4th ed. (2001), ISBN 1-85431-889-6, at vii.

⁶⁴ William Tetley, Q.C., “*Mixed Jurisdictions: Common Law vs. Civil Law (Codified and Uncodified)*,” 60 *La. L. Rev.* 677, 683 (2000), originally published in 1999 in two parts by *Unif. L. Rev.* (N.S.).

⁶⁵ Ceslav Pejovic, “*Civil Law and Common Law: Two Different Paths Leading To The Same Goal*,” [2001] *VUWL Rev* 42, III. A., available at <http://www.austlii.edu.au/nz/journals/VUWLRev/2001/42.html>.

consideration for the benefit.⁶⁶ “With regard to bilateral contracts, the [cause] of one party is the correlative obligation. In the case of gratuitous contracts, the [cause] amounts to the spirit of liberality of the donor.”⁶⁷ Consequently, there is no equivalent to the concept of privity (under which only a party to a contract can sue, except under certain statutory and judicial exceptions to the general rule).

In common law, an offer can be revoked until acceptance, even if the language suggests otherwise (unless consideration has been exchanged in return for what is perceived as a separate contract to keep the offer open for a given period). This is far from the case in civil law, where once made, an offer is binding for any period specified, or for a reasonable time beyond its making, if accepted within that period.⁶⁸ If breach occurs, the concepts applied to determine damages also diverge. Common law holds breach of contract to be a strict liability issue, and consequently, it is enough that a breach has occurred: no intent or fault is necessary to enable the aggrieved party to recover damages. However, an award of damages under civil law requires a finding of fault. Even if performance is not timely, at civil law, notice must be given to the potential defaulter, who must also be given a reasonable time to remedy the situation.⁶⁹ At common law, the contract is deemed to provide adequate notice of conditions and duties, and generally no notice is required to enable damages to be sought.

In “most legal systems outside of the common law world, the law of obligations recognizes and enforces an overriding principle of good faith” as applied to the making and application of contract.⁷⁰ Common law applies no such rule, rather allowing equitable principles to address unconscionable dealings.⁷¹ The civil law duty of good faith applies to pre-contractual negotiations as well as performance: good faith is presumed and the party alleging otherwise bears the burden of proof.⁷² The potential implications of the civil law approach are illustrated by the determination that good faith required debt revaluation by courts in periods of hyper-inflation because it was contrary to good faith for the creditor to be

⁶⁶ *Id.* citing articles 328 of the German Civil Code, 1121 of the French Civil Code, 1411 of the Italian Civil Code, 112(2) of the Swiss Code of Obligations, and 537 of the Japanese Civil Code.

⁶⁷ Dr. Aron Mifsud-Bonnici, “*The requirement of a lawful consideration in the law of obligations (section 987 [of the Italian Civil Code])*,” available at: <http://www.mifsudbonnici.com/lexnet/articles/causa.html>.

⁶⁸ Pejovic *supra*, n. 65. at III. C, citing articles 145 of the German Civil Code, 1328 of the Italian Civil Code, article 3 of the Swiss Code of Obligations, and article 521 of the Japanese Civil Code

⁶⁹ *Id.* at III. G.

⁷⁰ *Interfoto Picture Library Ltd v. Stiletto Visual Programmes Ltd* [1988] 1 All ER 348, 352-53, Bingham L.J.

⁷¹ *Id.*

⁷² HOLLAND, et al., *supra*, n.63, pp. 308-09.

deprived of actual value by the debtor.⁷³ What would the attitude of civil law courts be regarding a commodities contract where there was a severe price dislocation subsequent to the price being agreed?

The timing of passing of title is another area of conceptual difference that can cause significant problems. Under common law, the contract, as representative of the desire of the parties, determines when title to goods transfers. However, traditionally, under French law, title passes the moment the nature of the goods and the price to be paid are agreed: delivery and payment are inconsequential.⁷⁴ German concepts evolved differently from the French: not only must there be agreement, but the goods must also be delivered.⁷⁵ This, in combination with the lack of a privity requirement, means that a secondary buyer can acquire the contractual rights of the first buyer for goods not yet delivered, without the need to consult the original seller.

Cumulatively, these and other differences significantly alter the considerations required to draft contractual arrangements, and the potential sources of liability and requirements for enforcement. Such concepts are directly contrary to the common law precept that parties can contract for risk unless wholly unforeseeable and that if parties fail to do so there is no basis for the courts, absent duress, to step in and apply a higher principle of good faith. More fundamentally, this demonstrates a conceptual divide, between common law pragmatism and equity and civil law concept and doctrine. In reality, the lines are blurred by equity, by statutes such as the Uniform Commercial Code and by exceptions and sub-doctrine in civil law, yet the starting rationale and burdens placed on the parties are fundamentally different conceptually, resulting in a “difficulty finding even a common starting point for lawyers in the two systems.”⁷⁶

Contract law is frequently discussed in legal and commercial materials because trade between civil and common law jurisdictions occurs constantly. Consequently, bare awareness of different concepts is unusually accessible. However, competent advice would appear to require knowledge of the law as applied, and how some effects may be ameliorated through

⁷³ *Id.* at 309.

⁷⁴ Pejovic, *supra*, n.60, at III H, *citing* Article 1583 of the French Civil Code.

⁷⁵ *Id.* at III H, *citing* Article 929 of the German Civil Code.

⁷⁶ HOLLAND, et al., *supra*, n.63 p. 311.

contractual devices such as choice of law, forum, arbitration and other clauses.⁷⁷ Such problems are well illustrated by the following:

Because of different training, of a different legal method ... the Anglo-American lawyer [tends] to evaluate the importance of code provisions, of decisions of higher courts ... and underestimate treatises or commentaries The continental lawyer in contrast will usually find himself at a loss among the innumerable precedents which are binding, but yet can be distinguished out of existence ... and will vaguely look for precise concepts among the legal synonyms, loosely phrased decisions and unsystematic text books.⁷⁸

Furthermore, “the legal knowledge, skill, thoroughness and preparation reasonably necessary for the representation”⁷⁹ likely demands an ability to explain the legal and conceptual differences between the two systems, and their implications, to clients in a manner sufficiently comprehensible to support informed decision-making. Such comparative analysis is likely to require a significantly greater understanding of both the overseas system as applied, and the effect of differences, than would mere identification of civil law contract principles.

European Civil Law and Common Law Decision Makers Draw from Different Sources

The approach to codification of laws in common law and civil law systems is different, as is the related concept of precedent. A common law attorney’s reaction to a lack of knowledge is to look to statute and case law. In civil law systems, this may be a frustratingly unhelpful exercise from the statutory perspective, and dangerously misleading from a precedential viewpoint. “Civil law is highly systematized and structured and relies on declarations of broad, general principles, often ignoring the details.”⁸⁰ Civil Code is “a ‘style’: a particular mode of conception, expression and application of the law and transcends legislative policies that change with the times.”⁸¹ If so, a key basis of the belief that a common law lawyer has the tools to identify issues and to be self-educating concerning the law that determines them is removed.

⁷⁷ For more detail on the essential importance of cross-cultural skills to management and advocacy in international commercial arbitration, see Alibekova *et al*, eds., *supra*, n.2.

⁷⁸ C. SZLADITZ & C. GERMAIN, GUIDE TO FOREIGN LEGAL MATERIALS: FRENCH, 2nd Ed. Oceana (1985) at ix.

⁷⁹ ABA Model Rules of Professional Conduct (2004), Rule 1.1.

⁸⁰ William Tetley Q.C., *supra*, n.64, at 683.

⁸¹ *Id.* at 683 n.21, quoting René David.

Generally, civil law is codified in one body of text designed to be comprehensible to the lay reader.⁸² The archetypal *Code Napoleon/Code Civil* expresses key principles in a short statement in plain language. For example, the central provisions of the French *Code Civil* equivalent to the law of torts are as follows:

- § 1382: Every action of man whatsoever which occasions injury to another, binds him through whose fault it happened to reparation thereof.
- § 1383: Everyone is responsible for damage of which he is the cause, not only by his own act, but also by his own negligence or imprudence.

Since enacted in 1804, the text has never changed, yet France has gone from empire to republic to monarchy, and through other social and political upheavals over two centuries. The law as practiced in France has not remained static during this time. While not seeking to confuse the Code with the French Constitution, the nature of the tort sections is perhaps closer to the clauses found in the U.S. Constitution than an American statute. Civil law practitioners often find the fragmentary, scattered nature of common law across multiple statutes and precedent baffling.

Civil law codes are generally interpreted by reference to their purpose rather than through textual parsing.⁸³ Indeed, civil code almost always lacks definitions, often rendering textual analysis effectively impossible. “The purpose of the law is to identify, from a broad perspective, the general principles of the law, to establish the principles that have the most profound impact, and not to descend into the details of questions raised by application.”⁸⁴ The result is analysis based upon the broad purpose attributed to the legislation, as determined by academic interpretations, such that often a judgment is, in common law terms, more legislative than interpretive.⁸⁵ A civil law judge, however, would see this as pure application of the law, as explained by academics, to the facts presented. English courts have traditionally applied a resolutely textualist methodology. Yet when addressing EU statutes, and even British ones derived from EU legislation, English courts have felt constrained to drop textualism for “a very wide purposive approach in line with European judges.”⁸⁶

⁸² HOLLAND, et al., *supra*, n. 63, p. 184.

⁸³ *Id.* at 226.

⁸⁴ Portalis, one of the drafters of the Code Napoleon, *quoted in French in Tetley, supra*, n.64 at 703 n. 119 (translation by the authors).

⁸⁵ HOLLAND, et al., *supra*, n. 63, p. 226.

⁸⁶ *Id.* at 227, *citing Lister v. Forth Dry Dock* [1990] AC 546, [1889] 1 All ER 1134.

Common law opinions generally explain in some detail the law relating to the issues, how the facts and the law combine, and how this may differ from other combinations. The reason for this is the doctrine of *stare decisis*.⁸⁷ In civil law, no such doctrine exists. Classically, courts are not bound by prior judgments, regardless of how exalted their origin, how recent, or how effectively identical the facts.⁸⁸ This would, in itself, remove a critical common law analytical tool. However, civil law decisions also seldom elucidate upon the analysis, but rather tend, to a greater or lesser extent, to produce either conclusory statements of the outcome, or sparse, brief synopses equivalent to common law opinions of the 18th century.⁸⁹

Civil law has a means to predict, but it does not primarily originate from case or statute law; it instead is built upon legal academia. The concept of academic writing is on a different plane in civil law.⁹⁰ Academics strive to understand the ethos of the law and to distill the socio-philosophical purpose thereof as applied to various legal issues.⁹¹ The function of such writings is “to draw from this disorganized mass [cases, books and legal dictionaries] the rules and principles which will clarify and purge the subject of impure elements, and thus provide both the practice and the courts with a guide for the solution of particular cases in the future.”⁹² The focus is upon the history and purpose of principles, the proper scope of their application and explaining their effect “in terms of rights and obligations.”⁹³

Critically, once accepted, the academic doctrine of how principles should be applied in an area of law becomes effectively part of the principle embodied in the Code which, under the civil law separation of powers, judges apply, and do not reinterpret.⁹⁴ Indeed, the starting point for judicial analysis will be to identify the appropriate doctrine, then to ascertain whether facts exist to support application, rather than to consider the facts and which causes

⁸⁷ OXFORD TALKING DICTIONARY, The Learning Company, Inc. (1998).

⁸⁸ Pejovic, *supra*, n.65, at C.

⁸⁹ Gillian K. Hadfield, “*The Quality of Law in Civil Code and Common Law Regimes: Judicial Incentives, Legal Human Capital and the Evolution of Law*” (2006), p. 2, available at www.law.yale.edu/documents/pdf/Hadfield.pdf.

⁹⁰ A standard and only somewhat apocryphal piece of advice to English legal writers seeking influence is that it is best to be both ancient and dead.

⁹¹ HOLLAND, et al., *supra*, n. 63, p. 307.

⁹² RENÉ DAVID & J.E.C. BRIERLEY, MAJOR LEGAL SYSTEMS IN THE WORLD TODAY, 3rd Ed., Stevens & Sons (1985) p. 94, *quoted in* William Tetley Q.C., *supra*, n.64 at 701.

⁹³ *Id.* at 702.

⁹⁴ *Id.*

of action they may support.⁹⁵ In contrast, the common lawyer distinguishes cases, which would appear hopelessly incompatible to a civil lawyer, to determine the bounds of a rule or principle.⁹⁶ The focus of common law analysis is the application of precedent to variant fact patterns, producing rules tailored often to very narrow applications.⁹⁷

Thus, both the substantive law and the process of self-education require very different skills and techniques from those found in the portfolio of an average newly-admitted member to a U.S. Bar, or acquired through experience of domestic practice. American lawyers are, of course, not alone; lawyers trained in civil law nations are typically no better equipped to navigate U.S. statute and case law.⁹⁸

Cross-Cultural Issues Influence Negotiation

Although no two legal systems are exactly similar in the established world, in the developing world the differences are magnified greatly. Generally, in established civil law jurisdictions the law is codified, the equivalent of precedent is publicly available, and procedure is both open and openly prescribed. While the tools may be different, the system appears transparent and navigable if the differing concepts of propriety, justice and fairness are also understood and applied to the correct public materials. This is not necessarily the case in many newer or emerging economies, even those that seemingly possess a body of written law, constitutional and procedural guarantees, and other symbols of Western legalism. In other emerging economies, the laws and structures may be relatively transparent, but the results of their application differ from that one would expect in a Western society applying the same law and procedure.

As the former Senior Vice-President, General Counsel, and Secretary of General Electric Company, Benjamin Heineman, has observed: “[s]o much of practicing law these days outside of the United States is understanding the economic and political system, not just the legal system. I think we should not confine ourselves to a narrow view of the law. You simply can’t practice law in a country unless you have people there who understand the

⁹⁵ *Id.* In some mixed jurisdictions, such as Quebec, common law fact-driven analysis is applied to civil law.

⁹⁶ *Id.* at 701.

⁹⁷ *Id.*

⁹⁸ A few jurisdictions, such as Quebec, South Africa, Scotland and Egypt, combine civil and common law elements for historical reasons, potentially giving practitioners some advantages in relation to transition.

history and the culture.”⁹⁹ Differences in fundamental points of reference can profoundly impact notions of commerce and justice. America and China, for example, have a very different traditional concept of the place of the individual in society. Although this is but one aspect of their different concept of the world, arguably it can be directly traced to the different concepts of how commerce should be conducted.

The American Concept of Negotiation: Rooted in Individualism

“[C]ultural context significantly influences the way U.S. negotiators plan and conduct negotiations.”¹⁰⁰ Legal systems are reflections of the cultural norms of the society that created them. Thus, the same concepts that have affected legal thinking also affect other aspects of our interaction with others. In America the fundamental unit of the legal system is the individual. As the Declaration of Independence puts it, “[w]e hold these truths to be self-evident, that all men are created equal, that they are endowed by their Creator with certain unalienable Rights, that among these are Life, Liberty and the pursuit of Happiness.--That to secure these rights, Governments are instituted among Men, deriving their just powers from the consent of the governed.”¹⁰¹ The Constitution opens with the words: “WE THE PEOPLE of the United States, in order to form a more perfect union ...”¹⁰² Government is “of the people, by the people, for the people.”¹⁰³ There is little doubt that the political and legal culture of the United States is based upon the precept that individuals possess the rights, and that government is a result of the delegation of only some of those rights to a central authority.

The mechanism by which the interests of individuals are balanced is the law, as interpreted by the courts. “Since the Second World War most of the action in [American] constitutional law has been concerned with defining individual rights.”¹⁰⁴ Law must be a public commodity such that anyone can access it; it must be relatively stable and predictable; it cannot be arbitrary.¹⁰⁵ Law applies equally to all regardless of their personal status: as such

⁹⁹ Quoted in Silver, *supra* n.55, p. 16.

¹⁰⁰ Nigel Quinney, “U.S. Negotiating Behavior” U.S. Institute of Peace, Special Report No. 94, October 2002, p. 5.

¹⁰¹ *The Unanimous Declaration of the thirteen united States of America, in Congress, July 4, 1776.*

¹⁰² Preamble, *The Constitution of the United States.*

¹⁰³ Abraham Lincoln, “*The Gettysburg Address*,” November 1863.

¹⁰⁴ JAY M. FEINMAN, “LAW 101: EVERYTHING YOU NEED TO KNOW ABOUT THE AMERICAN LEGAL SYSTEM,” Oxford University Press (2000), ISBN 0-19-513265-3.

¹⁰⁵ Patricia Pattison and Daniel Herron, “*The Mountains Are High and the Emperor Is Far Away: Sanctity of Contract in China*,” 40 *American Business Law Journal* (Spring 2003), at 491-92.

it must bind rulers as it does ordinary citizens.¹⁰⁶ The law and judicial decisions are in the public domain, and, through doctrines such as *stare decisis*, provide a reasonably predictable basis for anticipating how disputes will be adjudicated. In a common law system, consistent interpretation on the basis of the text is not only logical, but essential to establishing certainty in dealings with others.

The American Heritage Dictionary defines negotiation as “[t]he act or process of negotiating: successful negotiation of a contract.”¹⁰⁷ This succinctly highlights the quintessential transaction-specific focus of American negotiators. Because a contract must be comprehensive to protect against even anticipated future eventualities, negotiation tends to be a linear progression through the elements required, until a detailed agreement defining rights and obligations for each party is concluded.¹⁰⁸

Perhaps as a result, Americans favor straight talking and textual interpretation, rather than nuance, and make relatively little use of gestures and other non-spoken cues. Americans are comfortable saying what they mean overtly and directly: to be called a straight-talker is a compliment. Emotion and custom are given little weight: objective and empirical evidence are what counts. It is not necessary to be friendly, if the facts support the contemplated action.¹⁰⁹ Americans negotiate principally to secure a finalized, enforceable contract, not to build something as intangible as rapport.¹¹⁰ As such, negotiators tend to get to the point very quickly, and to aim for a quick resolution. The longer it takes, the more it costs: delay costs money.

Contracts are primarily interpreted by the plain meaning of the text of the contract document, in isolation where possible. Thus, negotiation requires agreement upon all material elements of the transaction and then generally concludes with recording the terms in a detailed writing. One word may alter the interpretation of the whole contract, rendering precision essential. The result is a sequential approach designed to address all aspects of concern regarding a transaction. Relationships are largely unimportant, for the contract is governed by

¹⁰⁶ *Id.*

¹⁰⁷ THE AMERICAN HERITAGE® DICTIONARY OF THE ENGLISH LANGUAGE, 4th Ed., 2000, Houghton Mifflin Company. Available online at <http://www.bartleby.com/61/17/N0051700.html>.

¹⁰⁸ Nigel Quinney, *supra*, n.100, at 5.

¹⁰⁹ *Id.*

¹¹⁰ *Id.* at 5-6.

its content, statute and precedent. The focus tends to be short-term; future deals will require future contracts, and are outside the scope of current negotiations.

The concept of the individual as the fundamental unit of society is reflected in the way Americans do business: generally, people are individuals first and employees second. This also affects notions of success and how individuals advance. “In the Western workplace, an individual is recognized as a leader, encouraged, and even rewarded, for being assertive, for being a self-starter” and for individual accomplishment.¹¹¹ Negotiators seek to obtain the best possible outcome, in the form of a legally enforceable document defining the intended transaction, and the terms under which it will be carried out. Enforcement is by the courts under the established rules of contract law, and traditionally the person with the right to enforce are the parties, under the doctrine of privity of contract. Resort to, or the threat of, litigation is commonplace, and an accepted part of commercial activity.

The American Concept of Individualism is Not Universally Accepted

If the fundamental concept of the individual as the source of rights is removed, the basis on which the American paradigm is constructed is undermined. In Europe, the rights of the individual are more commonly seen as being balanced with those of wider society. This notion is often described as a “social contract,” under which citizens surrender all individual rights to the state in order to achieve a higher degree of protection from others than full individual assertion of those rights could achieve.¹¹² The German Basic Law illustrates the state-determined balance of constitutional rights, for example, “favoring dignity over freedom of speech, and favoring the preservation of democracy over the exercise of free speech.”¹¹³ In the U.S., constitutional rights are seen as never having been ceded by citizens to the government, and thus to exist independently of it.¹¹⁴ In Germany, as in most civil law

¹¹¹ Dianne Y. Fermin, “Face Value,” SunStar Newspapers, August 11, 2003, available at <http://www.sunstar.com.ph/static/ceb/2003/08/11/life/face.value.html>.

¹¹² See generally, JEAN-JACQUES ROUSSEAU, “THE SOCIAL CONTRACT AND DISCOURSES”, G.D.H Cole trans., Dent (1973) ISBN 0 460 11660 6.

¹¹³ Ronald J. Krotoszynski, Jr. “A Comparative Perspective on The First Amendment: Free Speech, Militant Democracy, and the Primacy of Dignity as a Preferred Constitutional Value in Germany,” 78 Tul. L. Rev. 1549, 1556 (2004).

¹¹⁴ See, e.g., William Tetley Q.C., *supra*, n.64, at 705. Tetley suggests that this is a Hobbesian conception, wherein society ceded only that required to achieve security; however, the natural rights theory of rights possessed by virtue of existence and hence incapable of delegation, as argued by Thomas Paine in “*The Rights of Man*”, may be an equally valid origin.

constitutional democracies, even if one successfully invokes a provision of the Basic Law, this may prove ineffectual because conflicting public policy is given greater weight.¹¹⁵

If European conceptions of the source of rights diverge from that of America, they are probably closer than those held in other cultures. One culture increasingly at the forefront of international commerce is that of the Chinese. China is a major location for international investment. It is the second largest trade partner of the U.S.,¹¹⁶ and, as of the end of 2005, U.S. enterprises had invested \$51 billion in China, setting up 49,000 businesses.¹¹⁷ Chinese culture also extends beyond its borders. For example, Taiwan¹¹⁸ is ethnically Chinese and other countries, such as Singapore, have been heavily influenced by ethnic Chinese populations. Also, for historical reasons, many other major trading countries in the region also possess relationship cultures much closer to the Chinese than to those of the West.

China Has a Tradition of Non-Legalistic Civil Regulation of Society

China governed itself without recourse to legalism for almost 1,800 years—after a brief experiment with a legalistic system based on concepts of equal justice for all ended around 220 A.D.¹¹⁹ China has recently promulgated a considerable, and increasing, amount of civil law code. However, China has not yet become a transparent, legalistic jurisdiction to a degree comparable with established legal systems in the West. Although advances have been made in recent years, the availability of legal information in China is limited in comparison with Western civil law jurisdictions, such that it can often be difficult to find the applicable law and even harder to be certain of correct interpretation.¹²⁰ There is also no systematic

¹¹⁵ Krotoszynski, *supra*, n.113, at 1556.

¹¹⁶ Zhou Shijian & Wang Lijun. “China, US complementary in trade,” China Daily, April 18, 2006, available at http://www.chinadaily.com.cn/china/2006-04/18/content_570030.htm.

¹¹⁷ *Id.*

¹¹⁸ Formerly the Chinese province of Formosa, Taiwan’s de facto independence from mainland China since the communist triumph of 1949 is a subject of significant contention. The name Taiwan is here used to avoid confusion.

¹¹⁹ Sunny Z. Hou, “Negotiation in China – Stereotypes and Fallacies,” Australian Dispute Resolution Journal, Vol. 11, No. 3, August 2000, p. 2. Significantly, law in the approximate Western sense, when it existed, traditionally applied only to those unable to live within the standards set by Confucianism; as such, it applied only to social outcasts. Duran Bell and Christine Avenarius, “Guanxi, Bribery and Ideological Hegemony” (1999), p. 8, available at: orion.oac.uci.edu/~dbell/bribery.pdf.

¹²⁰ Charles McClain & Hang-Sheng Cheng, “China’s Foreign Trade And Foreign Investment Law” (1995), available at: <http://1990institute.org/files/public/1990/ipaper/ForeignInvestmentLaw-ip11.pdf>.

compilation of civil law doctrine to aid in the interpretation of statutes and regulations.¹²¹ Furthermore, there are “*Neibu*” or secret internal agency regulations,¹²² which are inaccessible to the public, and yet are often the real rules under which an agency operates.¹²³ The Chinese Constitution provides for an independent judiciary, in theory; however, the courts are, in practice, responsible to government.¹²⁴ Chinese judges are loathe to second-guess agency interpretations of complex laws,¹²⁵ and most local judges are former local government officials, paid by local government. Thus, it is very difficult to win cases brought against local government officials, and even when litigants win, they often find it impossible to enforce the judgments.¹²⁶ Interpretation and enforcement is more a function of context—the industry, locale, the affected parties, and their political sponsors—than of the literal law.

Many in the West have seen the adoption of civil code in China as a significant and necessary step in an inevitable migration towards a “modern” legal system essential to full participation in global commerce. For adherents of such views, the problems summarized in the preceding paragraphs are simply obstacles of the sort that inevitably face a nation in the midst of such a transformation. Yet, there is an alternative explanation rooted in the traditional method of policing civil interactions in China. It is therefore possible that China is not participating in an inevitable evolution to a system based upon Western models. There are other jurisdictions with historical and cultural similarities with China that imported Western-style code or statute law much earlier than China. Before considering whether these suggest that China is indeed likely to be moving towards a legalist system and diminishing the effect of cultural business on law and commerce, it is necessary to review the nature of the traditional, culturally indigenous, system of civil regulation in China.

¹²¹ Wei Luo & Joan Liu, “*A Complete Research Guide to the Laws of the People’s Republic of China*”, available at <http://www.lawinfochina.com/Article/Article1.html>.

¹²² David Cowhig, “*China’s Internal Publication System*” in *International Journal of Civil Society Law*, Vol. IV, 1 (Jan. 2006), 81-83.

¹²³ See generally Luo et al., *supra*, n.121.

¹²⁴ The Supreme People’s Court is constitutionally responsible to the National People’s Congress, which is itself required to be under the control of the Communist Party. Locally, the President of the Court controls appointments, and the local government, which is controlled by the regional Party, appoints this position. See, Organic Law of Peoples Courts of The People’s Republic of China, Art. 35.

¹²⁵ Nathan Bush, “*Chinese Competition Policy: It takes more than a law,*” (2005). Source: <http://www.globalcompetitionforum.org/asia.htm#china>.

¹²⁶ U.S. Department of State, Bureau of Democracy, Human Rights, and Labor, “*Country Reports on Human Rights Practices - 2006*” (2007), available at: www.state.gov/g/drl/rls/hrrpt/2006/78771.htm.

In China, society is made up of family and other groups bound together and regulated by mutual obligation. Such interconnected networks are called *guanxi wang*. *Guanxi* is a web of mutual obligations and favors binding each member of a group, controlling each member's freedom of action, and so creating certainty. It also enables the power of members of the group to be lent in support of the external objectives of individual members.¹²⁷ Such networks include members from social, business, political and other aspects of life, and, of course, overlap.¹²⁸ A fundamental principle of *guanxi* is that each member benefits from the good of another.¹²⁹ *Guanxi* requires that wealth or other advantages be shared, not with an amorphous public, but with members of the group. In a society historically devoid of civil law, these supportive networks provided the means by which individuals could gain some measure of protection and security.¹³⁰ In the West, "relationships help the individual; to the Chinese they also define the individual."¹³¹

Confucianism is based upon a system of standards of conduct that define the parameters of acceptable behavior.¹³² Under Confucianism, society is hierarchical with civilized people combining via *guanxi* groups to form the building blocks of society.¹³³ The central tenets are an unquestioning acceptance of the authority of superiors, and loyalty to them.¹³⁴ A Chinese person is expected to spare no effort in pursuit of a positive outcome for his or her network, and the enforcement mechanism is the network itself.¹³⁵ Thus, certainty in any aspect of Chinese life depends not on law in the Western sense, but upon a complex system of social norms.

The significance of *guanxi* is all-pervasive, but three themes are of particular significance. There is no higher obligation than to not bring opprobrium or misfortune on

¹²⁷ Hou, *supra*, n.119, p. 3.

¹²⁸ These networks suggest corruption or nepotism to westerners for whom gifts to officials are bribes. In China, it is an accepted practice required to build relationships. *Id.* at 4-5. *Guanxi* is not transactional, but relationship based, and cannot be bought. A gift is a proportional show of respect, which may go some way to create a reciprocal obligation; it is not determined by the value of the immediate objective. *See*, "An in-depth look at *Guanxi*" *infra* n.131. Disproportionate gifts invite loss of status. Acceptance of gifts for specific actions or out of all proportion to status approaches the Chinese conception of graft or bribery.

¹²⁹ Bell, et al., *supra*, n.119, p. 7.

¹³⁰ *Id.*

¹³¹ "An in-depth look at *Guanxi*", available at <http://resources.alibaba.com/topic/infoDetail.htm?topic=154&printFlag=true>.

¹³² Henry C. K. Liu, "Rule of law vs Confucianism," Asia Times, July 24th 2003, available at <http://www.atimes.com/atimes/China/EG24Ad01.html>.

¹³³ *Id.*

¹³⁴ *Id.*

¹³⁵ *Id.*

those to whom one is obligated, either directly or by the actions of others to whom one is connected. Therefore, all relationships must be based on trust, rather than on a legal document such as a contract. Furthermore, the rights of individual parties are only as significant as their *guanxi* ties dictate. If *guanxi* suggests that the greatest benefit lies in a result favoring the other party, even though literal interpretation of the statute suggests otherwise, no injustice is done.¹³⁶ Finally, the decision of superiors is not to be challenged, because wisdom and position are equated. Consequently, judges are naturally inclined to follow codes of legal interpretations issued by the government, or to seek guidance from the government,¹³⁷ and would be likely to do so even without fiscal reliance on such bodies. Furthermore, it is not seen as peculiar that court decisions are not reported, or that there is no real equivalent to the abundant academic or judicial interpretation found in established common and civil law jurisdictions respectively: the only source of interpretive guidance are Party instructions, which are secret. The Standing Committee of the National People's Congress has the final authority over legislative interpretation, not a court.¹³⁸ Hence, the ability of members of the public to predict the outcome of a given case is very low. Nor is it felt particularly odd that *neibu* decisions, which form a great deal of what would be legal decision-making in the West, are even less available or explained.

The reason is, simplistically, twofold. Firstly, because superiors are seen as being in a better position to make informed decisions, it is logical that they should be afforded the greatest discretion possible to take the best long-term decision. Secondly, such decisions reflect *guanxi* obligations to protect the group good, and thus will be predictable to insiders. Conversely, the ability of foreigners to predict the outcome of a given case may be very low, compounded by the fact that the rules that determine decision-making are complex; inherently understood by locals, but unwritten, and foreigners are typically without the connections that give force to the merits of their interests.

¹³⁶ The Chinese word for citizen, "*huaren*," does not distinguish between singular and plural, rather like the English word for sheep. Library of Congress, "*Country Profile: China*," February 2005. This is a simple but powerful comment on the status of the individual.

¹³⁷ Bruce M. Owen, Su San & Wentong Zheng, "*Antitrust in China: The Problem of Incentive Compatibility*," AEI Brookings Joint Center for Regulatory Studies (2003, revised 2006), p.16.

¹³⁸ The Chief Judge of the People's Supreme Court is not a member of the Politburo -- the body that controls the Communist Party, which in turn controls the People's Congress -- so the Court has no direct link to the supreme seat of power (in fact the Standing Committee of the Politburo).

The difficulty of achieving the level of understanding required to provide competent representation relating to such systems is considerably greater than that of established and accurately documented systems. Not only must the written civil law divide be bridged, but one must also master a vastly complex system of rules and practices that are both unwritten and defined by local interpersonal ties and cultural norms that are not easily accessible to an outsider.

Taiwanese Observations Suggest That Imported Written Law Does Not Guarantee Western-Style Legalism

The notion that development will inherently require the abandonment of relationship practices in favor of Western legalism is widespread among Western scholars, and urged by Asian advocates for Western-style democracy. Essentially, the argument is an evolutionary one, based upon the principle that only Western legalism can ensure the stable, predictable, and relatively equal commercial environment required to support a developed economy, and that as an economy emerges, such a system is enabled by increased resources that support key requirements, such as financially independent police and judiciary, often lacking in less developed more traditional systems.¹³⁹

Such evolutionist theories are seldom put forward based upon empirical evidence of such a transformation occurring in South East Asia, beyond the importation of foreign legal code. Yet there are prior examples of relationship cultures that have legalized in response to the demands of the international community and trade pressures. Japan is a classic example; however, Taiwan is perhaps the best source of comparison for China, because, as in mainland China, most Taiwanese are from the Han ethnic group (although there are reasons why the official percentages in both jurisdictions may be inflated). Thus, despite having been under Japanese rule for 50 years (1895-1945),¹⁴⁰ and normal regional differences in culture, Taiwan represents perhaps the closest cultural comparative to mainland China.

If the “evolutionists” are correct, Taiwan should provide a very good example of the erosion of cultural mechanisms in favor of written law. Such an example would speak strongly in support of the “evolutionist” notion that Western legalism is, if not inevitable, a

¹³⁹ See, e.g., RANDALL PEERENBOOM, “CHINA’S LONG MARCH TOWARD RULE OF LAW,” Cambridge University Press, 2002. ISBN 0-521-01674-6.

¹⁴⁰ Mainland Chinese first came to Taiwan in large numbers in the 1600s. Over a million mainlanders came as refugees at the end of the Chinese Civil War in 1949. Japanese nationals had been repatriated in 1945.

logical conclusion to of any process of supplanting cultural systems with written law. This would in turn suggest the potential for cultural divides to narrow accordingly, rendering the need to bridge cultural divisions a transitory issue of decreasing importance.

Taiwan did not revoke the prior mainland civil law on declaring independence as did the People's Republic, but built upon it. Further, Taiwan has achieved significant economic growth since the 1950s, developing from an almost purely agrarian economy to having the 24th largest national GDP.¹⁴¹ Thus, Taiwan has a civil law tradition that began with the adoption of civil and criminal codes in 1929, modeled on those of Imperial Germany.¹⁴² From 1949, the ruling regime (*Kuomintang*) has enforced the law in Taiwan in a determined and authoritarian manner.¹⁴³ Five decades of industrialization have had a profound impact on Taiwan's social fabric, not least the transition from an agrarian economy to an urbanized industrial one.¹⁴⁴ Over this period, an institutionalized system of code enactment and revision developed, along with a court structure now staffed by a "technically proficient cadre of lawyers and judges."¹⁴⁵ However, Confucian ideas, while not unchanged, are "still visible under the veneer of modern legality": even legal professionals "steeped in modern western traditions of legality" evidence traditional conceptions of law in practice.¹⁴⁶ "Many elements of the modern ... legal system have been drawn into relational structures to compensate for the loss of more traditional techniques of maintaining relationships."¹⁴⁷ "While culture is not necessarily able to explain 'big things,' it does frequently shape the form many things take."¹⁴⁸

¹⁴¹ ECONOMIST, POCKET WORLD IN FIGURES, 2010 Ed. Profile Books Ltd. in association with The Economist Newspaper Ltd., ISBN 978 1 84668 358 9, pp. 26, 28. Taiwan has the 49th highest GDP per capita, approaching double that of the Peoples Republic of China. *Id.*

¹⁴² *Id.* at 227, noting that for reasons of lack of control, Japanese occupation, war with Japan and finally civil war, enforcement was uneven prior to 1949.

¹⁴³ *Id.*

¹⁴⁴ Jane Kaufman Winn, "Relational Practices and the Marginalization of Law: Informal Financial Practices of Small Businesses in Taiwan" originally published in *Law and Society Review* 28/2 (1994), reprinted in full in CONTRACT, *GUANXI AND DISPUTE RESOLUTION IN CHINA*, Tanhirih V. Lee ed., Garland Publishing Inc. (1997), pp. 223-24. ISBN 0-8153-2483-9, pp. 235.

¹⁴⁵ Pitman B. Potter, "Doctrinal Norms and Popular Attitudes Concerning Civil Law Relationships in Taiwan," 13 *UCLA Pac. Basin L.J.* 265 (1995).

¹⁴⁶ Winn, in Lee ed., *supra* n.144, p. 231.

¹⁴⁷ *Id.* at 235.

¹⁴⁸ Michael Mattlin, "Campaigning without issues: networks, face and service politics," paper presented to the Nordic Association for China Studies Conference, June 2003, p. 2. Mattlin studied the practice of electoral politics, finding that use of *guanxi* techniques by candidates was seen as essential by both the candidates and the electorate, and effectively produced campaign practice very different from that in an equivalent Western election.

One method to accommodate tradition has been to exercise a form of discretion in enforcement: in Taiwan, the practice is unspoken, but observable.¹⁴⁹ One illustration of such discretion comes from the mode of decision described by Chinese economic court judges in 1989: *Heqing, heli, hefa* (according to relationship, propriety and the law).¹⁵⁰ This may mean only that all three must be satisfied in any judgment, and that the letter of any law (of which China had relatively little in 1989) might need to be softened to accommodate the others.¹⁵¹ Alternatively, it may signify that an issue is decided on relationship-derived obligations first, perceptions of more general society second, and only if necessary would the court resort to law.¹⁵² The situations where written law would be applied typically appear to accord with classic traditional breaches of *guanxi* obligations that placed the perpetrator beyond Confucian bounds of acceptability sufficiently to warrant application of law, such as actions contrary to state interests or criminal infractions.¹⁵³ Under either interpretation of *Heqing, heli, hefa*, the law, if it is to be applied at all, must accord with traditional rules. Some commentators see this as “marginalization of the law in Taiwan.”¹⁵⁴ Whether marginalized or melded, the significance is the same: *guanxi* still plays a very significant role in the operation of society.

In Taiwan, who one is remains a function of the relationships one possesses, not something defined by one’s existence,¹⁵⁵ unlike the notions of rights by virtue of citizenship that underpin U.S. jurisprudence. Relationships still depend, not on contract, but on personally developed trust reinforced by mutual obligation. There is a “clear consensus emphasizing informality and personal relations in the regulation of business conduct. Mutual supervisory and enforcement powers between and among members of particular business fields were ... more powerful than the law in encouraging performance of obligations.”¹⁵⁶ This is despite the increasing necessity of dealing with strangers resulting from the flow of the population to urban areas during industrialization.¹⁵⁷ Such changes have led to traditional and

¹⁴⁹ Winn, in Lee ed., *supra* n.144, p. 233.

¹⁵⁰ Lucie Cheng and Arthur Rosett “*Contract with a Chinese Face: Socially Embedded Factors In The Transformation from Hierarchy to Market 1978-1989*” in Lee ed., *supra*, n.144, p. 201.

¹⁵¹ *Id.* at 202.

¹⁵² *Id.*

¹⁵³ *Id.*

¹⁵⁴ Shin-yi Peng, “*The WTO Legalistic Approach and East Asia: From the Legal Cultural Perspective*,” 1 *Asian-Pacific L. & Pol’y J.* 13, 20 (2000), p. 19.

¹⁵⁵ Winn in Lee ed., *supra* n.144, at 236.

¹⁵⁶ Potter, *supra*, n.145, at 279-80 (discussing results of interviews and survey research in Taiwan).

¹⁵⁷ Winn, in Lee ed., *supra*, n. 144, pp. 237-38.

legal mechanisms being used in tandem to reinforce each other. The reason is conceivably that courts are seen as requiring too high a standard of proof, probably because much, if not all, of the agreement was oral.¹⁵⁸ Contracts are not seen as the basis for a relationship, and while frequently signed, it has been suggested that attention to the contents is rare.¹⁵⁹ The incentive to comply with agreements is not the threat of litigation, but of being “sanctioned by the local business community through denial of future business.”¹⁶⁰ Indeed, an oral agreement is often performed according to its terms “despite subsequent and contrary written terms” that should theoretically be enforced under the Civil Code.¹⁶¹ The result has been that industrialization, and political liberalization since 1987, has had “much less impact on the principles of social organization.”¹⁶² A 2006 study found that Taiwanese over 30 years of age are likely to see *guanxi* as less important than their younger counterparts.¹⁶³ In fact, far from being inimical to modern society, *guanxi* appears to have accommodated the societal changes of the digital era—for example, by the recognition of digital networking tools as viable fora for building and maintaining *guanxi* ties.¹⁶⁴

It is clear that five decades of economic transformation under the auspices of legal codes have not undermined the importance of *guanxi*; rather, law has melded with it. Thus, law as applied in Taiwan is neither purely legalist nor traditional; however, the result is likely to accord with traditional concepts of obligation and propriety. It is often claimed that “[t]he legal system will eventually come to play the central, universal role generally associated with [established Western] legal systems ... [yet such an] outcome is far from clear.”¹⁶⁵ Indeed, the lesson seems to be that the result of any accepted practice will be what society feels is just, which is inherently a product of cultural notions of fairness and justice.

¹⁵⁸ *Id.*

¹⁵⁹ Potter, *supra*, n. 145, at 280.

¹⁶⁰ *Id.*

¹⁶¹ *Id.* at 281.

¹⁶² Dung-Sheng Chen, “*Taiwan’s Social Changes in the Patterns of Social Solidarity in the 20th Century*,” *The China Quarterly* (2001) (despite arguing an “evolutionist” interpretation, and still concluding that rule of law will supplant traditional relationship structures at some point).

¹⁶³ Dennis B. Hwang, Patricia L. Golemon, Yan Chen, Teng-Shih Wang & Wen Shai Hung, “*Guanxi and Business Ethics in Confucian Society Today: An Empirical Case Study*” *Journal of Business Ethics*, Spring 2008, Commentary to Table IV, available at <http://74.6.239.67/search/cache?ei=UTF-8&p=taiwan%2C+guanxi&fr=yf...u.cn/article/cy.pdf&w=taiwan+guanxi&d=bzFb8UxISsN6&icp=1&.intl=us> (10 of 28) [4/30/2009 1:10:20 PM]

¹⁶⁴ *Id.*, Commentary to Table II.

¹⁶⁵ Winn in Lee ed., *supra* n.144, pp. 255-56 (responding to an archetypal “evolutionist” assumption).

It is unsurprising that long-held cultural means to achieve such ends are not simply relinquished overnight in favor of a culturally alien body of law, such as the European-influenced written codes of Taiwan,¹⁶⁶ which were at odds with local tradition.¹⁶⁷ Foreign lawyers must therefore accomplish the difficult task of acquiring a sufficient understanding of traditional cultural practices to enable them to determine if, and to what degree, such written law will actually govern in a given situation. Furthermore, they must be able to comprehend how such law will be construed and applied when viewed through the lens of local cultural norms if they are to advise a client competently during a negotiation or regarding potential litigation.

Negotiation in Chinese Cultures: Confidence Through Trust

As Taiwanese experience suggests that cultural factors have not simply receded into history, but rather continue to significantly impact how business is done, the likelihood is that similar drivers not only exist in mainland China, but will continue to influence business practice and perceptions there in the future.

“Chinese culture determines the style of Chinese negotiation. ... [it is] important for foreigners to understand China-style negotiation.”¹⁶⁸ Without an understanding of the pivotal role of *guanxi* and “face”, many Chinese practices will appear incomprehensible.¹⁶⁹ The process of negotiation in China is divided into three phases: pre-negotiation, negotiation and post-negotiation.

While pre-negotiation occurs in America, it is usually limited to brief and superficial ice-breaking. However, in China, this phase takes the longest and often incurs the most cost, and unless trust emerges from it, actual negotiation will not occur.¹⁷⁰ Pre-negotiation is the relationship-building phase, during which each party determines whether it has confidence in

¹⁶⁶ The rules of globalization are often seen as the imposition of Western economic and cultural interests. See, e.g., Shin-yi Peng, *supra*, n.154 p. 24.

¹⁶⁷ Winn in Lee ed., *supra* n.144, p. 225.

¹⁶⁸ Hou, *supra*, n.119, p. 2.

¹⁶⁹ Just how frustrating this can be is perhaps underlined by the public acknowledgment that the U.S. Executive was delighted when Wu Yi was appointed to lead a top-level dialogue on economic issues. During China's WTO negotiations “[S]he got right to the point, and dispensed with any formalities.” Richard McGregor, “*US takes Shine to China's 'iron lady'*,” *Financial Times*, September 23/24, 2006.

¹⁷⁰ Pervez N. Ghauri & Tony Fang, “*The Chinese Business Negotiation Process: A Socio-Cultural Analysis*,” University of Groningen, (1999), p. 6. Available at: <http://som.eldoc.ub.rug.nl/FILES/reports/1995-1999/themeB/1999/99B15/99b15.pdf>, at 6.

the trustworthy nature of the other. Discussions are informal, often unrelated to work, akin to exploratory soundings and presentations. During this phase, small talk is critically important, allowing time to decide whether there is the requisite trust to justify moving on. Negotiation itself comprises intense task-related specific exchanges of information and positions. This closely approximates to negotiation as a whole as understood in the West, concluding with an agreement. After agreement is reached, Chinese parties seek to re-negotiate continually as the relationship develops and circumstances evolve.

“Chinese people do not believe in contract: they believe in people.”¹⁷¹ Thus, success requires the investment of time and money in building relationships before negotiations begin. The Chinese do not form relationships with companies, but with individuals.¹⁷² Creating obligations can foster relationships; for example, inviting a Chinese person to spend time overseas grants “face” to them. Inviting a Chinese visitor into your home is also a significant gesture of respect requiring a return gesture. These are not bribes as understood in Chinese culture, although the Foreign Corrupt Practices Act¹⁷³ as interpreted by the U.S. Department of Justice may suggest otherwise.¹⁷⁴ Although reciprocation may lead to improved final terms, there is no explicit *quid pro quo*. The main impact is to increase mutual knowledge and understanding at the individual level and begin the ritual exchange that underpins the formation of a *guanxi* tie. Until complete, the Chinese party is likely to feel uncertainty, similar to that experienced by an American who is operating under a contract he or she fears is unenforceable. Further, the strength of a *guanxi* bond grows with time: “long roads test the horse, but long dealings test the friend.”¹⁷⁵ It is through *guanxi* ties that any eventual relationship will be maintained.¹⁷⁶

¹⁷¹ *Id.* at 21.

¹⁷² “An in-depth look at Guanxi,” *supra*, n.131.

¹⁷³ The Foreign Corrupt Practices Act of 1977 (FCPA) (15 U.S.C. §§ 78dd-1, *et seq.*).

¹⁷⁴ While gift giving and other forms of relationship building are expected in China, and practiced by many foreign corporations in that country, any American citizen, corporate or individual, should carefully determine the scope of its ability to undertake such practices in light of the FCPA. It should be noted that practices seemingly condoned with regard to their citizens by other signatories of the OECD and UN conventions on corruption may not be tolerated under the current American interpretation of the FCPA. The U.S. remains uniquely enthusiastic in its definition and enforcement of corruption. *See, e.g.,* Fritz Heimann & Gillian Dell, “2006 TI Progress Report: Enforcement of the OECD Convention on Combating Bribery of Foreign Public Officials,” Transparency International (2006), p. 4.

¹⁷⁵ T.C. LAI & Y.T. KWONG, “CHINESE PROVERBS,” Kelly & Walsh Ltd, Hong Kong, (1970).

¹⁷⁶ “Seven Disciplines for Venturing in China,” *supra*, n.20, p. 4 col. 1.

The Chinese approach is to assume untrustworthiness until the opposite is demonstrated.¹⁷⁷ Chinese domestic commercial contacts ordinarily, perhaps necessarily, start with an introduction.¹⁷⁸ The Chinese tend to be suspicious of even Chinese strangers, and are even more so of foreigners.¹⁷⁹ Westerners tend to forget that the Chinese have, for most of their history, regarded the “Middle Kingdom” as the center of civilization.¹⁸⁰ Foreigners are still seen as unversed in the ways of civilization: the very Confucian norms through which *guanxi* enables the creation of trust.¹⁸¹

One experience frequently encountered by non-Chinese negotiators causes much confusion, yet in fact indicates the essential influence of *guanxi* on commercial activity. This is the ferocious price focus and tenacious bargaining often experienced by Western negotiators in China. Indeed, Chinese price-haggling is a highly developed art. How does this fit with the notion of a relationship-based system? The answer is fundamental and illuminating.

In the course of life and commerce there are myriad occasions where transactions need to be made with a stranger. For example, “[c]onfrontational bargaining is prevalent in street markets precisely because the parties typically do not have a working relationship.”¹⁸² Since there is no relationship on which to base trust, the parties bargain keenly, each seeking to maximize advantage based upon assessed value and quality of the good or service at issue. The focus is on that transaction alone, and success is determined by whether any deal is on terms favorable under the circumstances. There is no obligation to consider the other party’s

¹⁷⁷ Ghauri et al, *supra*, n.170, p. 12.

¹⁷⁸ Peter Hanneforth “*Doing Business in China: The Next Imperative.*” SpaCom LLC, undated, p. 2, available at http://www.spacom.com/DoingBusinessInChinaArticle10_04.pdf.

¹⁷⁹ Gerard J. Brandon, “*Chinese Negotiation – Balancing your Yin to Their Yang.*” American Chronicle, May 19, 2006, available at <http://www.americanchronicle.com/articles/view/9829>.

¹⁸⁰ The domestic name for China is *Zhongguo*, which means “Central Country” or “Middle Kingdom.” Underlying this was a historical tendency to regard those outside of its borders as uncivilized. The following is a strident modern example of traditional sentiments: “Many Chinese people believe that China is the center of the civilized world, and there is no need for further advancement. Surrounding the Middle Kingdom on all sides are uncivilized barbarians ... The Chinese have always cared little about the people who live beyond their borders.” Tan Mei Yun “*Varying Chinese Views of the British.*” available at <http://www.angelfire.com/ny5/h3gproj/barbarians.htm>.

¹⁸¹ Jeanette W. Gilsdorf “*Metacommunication Effects on International Business Negotiating in China.*” Business Communication Quarterly, Vol. 60, No. 2, June 1997, p. 22, available at <http://www.esulb.edu/~gilsdorf/chinamet.html>.

¹⁸² John Hooker, “*Corruption from a Cross-Cultural Perspective*” Carnegie Mellon University (2008), p. 6, available at: ba.gsia.cmu.edu/jnh/corruption08s.pdf.

interest: value for money is the sole arbiter.¹⁸³ If a contract is involved, it will typically be relatively simple and clear. These are precisely the type of contracts that are most likely to be taken to court in the event of a dispute, and which the Chinese legal system is most effective in enforcing.¹⁸⁴ Although public enforcement may risk “face” if the plaintiff was seen to be naive, there is no consequence for wider relationships or commercial expectations, because none existed.

This distinction between transactions with strangers and the development of lasting commercial relationships profoundly affects the approach of the Chinese to negotiation.¹⁸⁵ Critically, the pivotal factor is not the nature of the business envisaged, but the presence, or absence, of an adequate *guanxi* tie. In simple terms, until one has developed *guanxi* ties, one is a stranger, and will be negotiated with as such. This is one reason why introductions are such a valuable tool in China: an introduction does not create a lasting relationship, but it does create an obligation not to disoblige a mutual connection, and thus lays a foundation for the outsider beyond the status of stranger.

The effect on the approach of negotiators is significant. Faced with a stranger, the Chinese will employ an approach based on tactics culled from traditional sources such as Sun Tzu’s “*Art of War*” and the “*Thirty-Six Stratagems*.”¹⁸⁶ The negotiation is a battle, and the aim is to win as crushingly as possible.¹⁸⁷ This differs markedly from the type of win-win approach calculated to preserve trust and the kind of flexibility necessary to establish the type of flexible long-term working relationship that is the objective of negotiation between parties where *guanxi* ties exist.¹⁸⁸ This distinction is a major explanation for the markedly different experiences of different business negotiating in China,¹⁸⁹ and underlines the folly of

¹⁸³ Tony Fang, “*Negotiation, the Chinese style*”, *Journal of Business & Industrial Marketing*, Vol. 21, No. 1 (2006) pp. 50-60, at 54.

¹⁸⁴ See p. 40 for related discussion.

¹⁸⁵ *Id.*

¹⁸⁶ *Id.* at 55. For brief real-world illustrations, see Daily Telegraph, “*Westerners Struggle to Scale the Wall*” (2004), available at <http://www.telegraph.co.uk/finance/2898668/Westerners-struggle-to-scale-the-wall.html>.

¹⁸⁷ *Id.* at 54

¹⁸⁸ Price-bargaining will still occur and it is usually wise to build in scope for concession on this as a source of face for one’s Chinese counterpart. However, when seeking to establish or expand a commercial relationship, such price considerations are only part of the equation, not the defining factor.

¹⁸⁹ See, e.g., Fang, *supra*, n.183 at 51.

neglecting to adapt timelines and approaches to reflect the Chinese cultural landscape.¹⁹⁰ *Guanxi* remains “one of the essential elements” of doing business in China.¹⁹¹

Introducers are sources of information and trust to both parties via *guanxi* obligations and connections.¹⁹² Typically, they will not be directly interested in the transaction. Initial presentations are an opportunity to emphasize the value of one’s company, and the reasons the other party would benefit from associating with it. This is a positioning tool: if the foreign company is old, large, growing rapidly, or there is third-party testimony to an aspect of its expertise, this should be emphasized. Doing business with a leading company gains individual and corporate “face” while connections with a failing company risk a loss of “face.”

One of the key differences in practice is the method and timing of due diligence. In China, this is done at the outset, largely during the pre-negotiation phase, which is a protracted exercise in developing understanding and confidence. The Chinese will research the other party in great depth.¹⁹³ They will also use connections to acquire insights and inside information: the concept of confidentiality is not understood in China as it is in America; rather, information is seen as a commodity within the *guanxi* obligation chain.¹⁹⁴ For this reason, it is hard to get away from past mistakes.

During the pre-negotiation phase, factual information is exchanged, but more time is spent in entertaining and small talk. In a sense, it is a kind of courtship ritual. It is essential to remember that this phase is extremely important to the Chinese decision-making process. Due diligence may be best conducted during this phase, rather than later as is often the case in Western transactions: asking for documentation and probing after the relationship is formed can be interpreted as indicating a lack of trust, which requires a broader, more comprehensive understanding of the other party.

¹⁹⁰ *Id.* at 54.

¹⁹¹ Meiling Wong, “*Guanxi* Management in View of Complex Adaptive System: A Case Study of Taiwanese ODI in China,” Department of Industrial Engineering & Management, National Chinyi University of Technology, Taiwan (2008), presented at the International Colloquium on Asian Business (ICAB), Bangkok, July 1, 2008, p. 14. Available at icbm.bangkok.googlepages.com/1.ICAB.Meiling.Wong.RP.pdf.

¹⁹² “*Seven Disciplines for Venturing in China*,” *supra*, n.20, p. 4, col. 1-2.

¹⁹³ Gilsdorf, *supra*, n.181 at 16.

¹⁹⁴ “*Negotiating in China*” Global Skills Update, Issue 9, July 2002, available at <http://admin01.meridianglobal.com/home.cfm?id=65-12>.

Chinese negotiators tend to start actual negotiations by announcing that certain points cannot be negotiated, perhaps because of instructions from superiors, or because they are unaware of acceptable alternatives.¹⁹⁵ Often, this is explained as being “required by Chinese law,”¹⁹⁶ when, in fact, the purpose is frequently to secure concessions on key issues early on, without giving up anything in return. Additional tactics, such as circular questioning, are often employed, many of which are not common, or condoned, in American negotiating. “[U]nstructured meetings, inadequate facilities,” are common examples in China.¹⁹⁷ The Chinese may open discussions with more than one potential partner in order to strengthen their positioning by playing one against the other.¹⁹⁸ Flattery is used to convince certain opposing negotiators that they have particular insight or trust because, where accepted, this can increase the Chinese ability to manipulate that person.¹⁹⁹ Aspersion may be cast on an individual’s character, or complaints made against them, in an attempt to create dissension and to isolate perceived opponents.²⁰⁰

Patience is an essential virtue. The process of developing trust requires time and understanding beyond the facts of a particular commercial opportunity. Time allows an opponent to be properly assessed and tactics honed accordingly. The Chinese have many proverbs along the lines of “error is a part of haste,” or “a little impatience spoils great plans.”²⁰¹ Price is aggressively negotiated, however, and must be seen to be so.²⁰² The Chinese generally will not conclude a deal until they are certain that they have achieved the best possible terms.²⁰³ The perception of the bargaining ability and performance is a component of “face,” similar to the idea of relentless negotiation. Chinese negotiators lose “face” if they make mistakes, including entering into poor commercial agreements.²⁰⁴ Conversely, they are seldom rewarded for exceptional performance, resulting in a tendency to

¹⁹⁵ Fabrizio Soda, “*Successful Negotiation in China: Notes for Managers of an equity joint venture*”, Universita Commerciale Luigi Bocconi, 1999, p. 5.

¹⁹⁶ *Id.*

¹⁹⁷ *Id.* at 2.

¹⁹⁸ I. Made Astawa, “*Chinese Behavior*” MRIupdate, July 2003, issue 2. Available at: <http://www.moore-rowland.com/publications/MRI%20Update%200703.pdf>.

¹⁹⁹ Hou, *supra*, n.119, at 3.

²⁰⁰ Soda, *supra*, n.195, at 6.

²⁰¹ LAI, et al., *supra*, n.175.

²⁰² Brandon, *supra*, n.179..

²⁰³ Soda, *supra*, n. 195, at 2.

²⁰⁴ Pervez N. Ghauri & Tony Fang, “*The Chinese Business Negotiation Process: A Socio-Cultural Analysis*,” University of Groningen, (1999), p. 16. Available at: <http://som.eldoc.ub.rug.nl/FILES/reports/1995-1999/themeB/1999/99B15/99b15.pdf>.

prefer not to commit unless absolutely certain. A recent poll by *China Youth Daily* found 87% of Chinese people found saving “face” an essential preoccupation.²⁰⁵ In general, the use of the most concise terms possible, combined with removal of non-essential elements (especially standard provisions not actually pertinent to the matter at hand) may assist in successfully concluding negotiations.²⁰⁶ Similarly, it is advisable to specify in clear and simple language the truly critical benchmarks, dates and terms that must be adhered to if the contract is to meet your needs.²⁰⁷

If successful, from the Chinese perspective, the contract merely suggests one aspect of commercial cooperation based upon the relationship forged in the preceding encounters. The contract is a by-product, not an end. Generally speaking, the Chinese will honor a contract,²⁰⁸ and courts will enforce them—the World Bank Group Doing Business project actually rates contract enforcement in China as being easier than in the United Kingdom.²⁰⁹ However, this applies best to clear, written contracts. Typically, these often stem from one-off, *guanxi*-free transactions, which tend to be more clear-cut. This also explains a fact which those who belittle the importance of *guanxi* often cite in their support: Chinese courts actually enforce a significant number of contacts between Chinese parties each year.

Significantly, however, Chinese courts are less comfortable reforming contracts or determining their existence and meaning from extrinsic evidence.²¹⁰ It is worth remembering that Chinese parties are well-positioned to determine the enforceability of the document being negotiated, and, when *guanxi* is present, may be less concerned about operating without a binding legal basis for the arrangement. The establishment of relationships remains at least an equal, and probably the primary, objective and source of business confidence. The absence of a legally enforceable contract may be seen as a negotiated position of advantage, but will

²⁰⁵ Source: www.worldlink-china.net/news_CWL.htm.

²⁰⁶ See, e.g., Steve Dickinson “*Enforcing Contracts In China. Way, Way Better Than You Think*”, available at <http://www.chinalyst.net/node/73143>.

²⁰⁷ *Id.*

²⁰⁸ Ghauri, *et al.*, *supra*, n.204, p. 18.

²⁰⁹ World Bank Group, “*Doing Business 2009 Report*”, data available at <http://www.doingbusiness.org/EconomyRankings/>. This addresses contracts written in Chinese, that are subject to Chinese law and do not specify enforcement in another jurisdiction. The information is based upon the Shanghai District People’s Court, and thus on data from one of the most cosmopolitan jurisdictions in China. It should be noted that the comparative cost of legal enforcement is a significant weighting factor in this ranking.

²¹⁰ Dickinson, *supra*, n.206.

almost certainly also be seen as aiding the evolution of the relationship that enabled the parties to enter into business with each other.

From the traditional Chinese perspective, since the true “glue” is the relationship, as events unfold it is natural to seek to adapt accordingly.²¹¹ Trust is more important than specifics. Where trust exists, it should be possible to work out solutions, and to vary the terms of a commercial relationship to reflect changing conditions. “The Westerner ... is expected to ask for something in return for what he is asked to yield.”²¹² Thus, the language of the contract is probably determinative of neither the basis of the relationship nor the terms of trade between the parties, from the Chinese perspective. If litigated or arbitrated, it is conceivable that tribunals would sympathize with such a view, as suggested by Taiwanese experience.²¹³

It is critical to maintain the *guanxi* tie that underpins the relationship. This requires continuity of personnel, as *guanxi* is between individuals not organizations, and is not transferable. One classic Western error is to rotate negotiators during discussions, or to replace a successful negotiator with a different person as project manager upon conclusion of negotiations. *Guanxi* ties need to be actively maintained, which requires that time be spent face-to-face with Chinese counterparts on a reasonably frequent basis, regardless of whether any deal is currently pending. Further, one is expected to actively look out for the interests of one’s wider network, which can be difficult ethically for many Westerners, and sometimes compromising in legal or public relations terms.

Thus, both the key parties and the source of the relationship are different: individuals and trust in China, contract and organizations in America. Advising a client that is attempting to secure such agreements is likely to be as much related to managing *guanxi* etiquette as to traditional contract drafting and negotiation.

²¹¹ See, e.g., James K. Sebenius & Cheng Qian, “*Cultural Notes on Chinese Negotiating Behavior*,” Harvard Business School, Working Paper 09-076 p. 5, available at <http://www.hbs.edu/research/pdf/09-076.pdf>.

²¹² Jeanette W. Gilsdorf “*Metacommunication Effects on International Business Negotiating in China*,” Business Communication Quarterly, Vol. 60, No. 2, June 1997 p. 24, available at <http://www.csulb.edu/~gilsdorf/chinamet.html>.

²¹³ A cynic might observe that having two systems of “law,” written and cultural, allows selective enforcement. Thus, if a foreigner is involved, and written law unfavorable to the foreigner, then conspicuous enforcement of written law adds an appearance of legitimacy in the West. Alternatively, the *Heqing, heli, hefa* (according to relationship, propriety and the law) could allow an unpopular party favored by written law to be ruled against on moral or relationship grounds.

The nature of the end result is also very differently perceived. For the Chinese, it is the establishment of trust that forms the basis for long-term collaboration. Thus, management of disputes is seen in a different light. Resort to public dissension goes directly to the “face” of the Chinese company and its senior personnel. Chinese traditional attitudes to litigation are illustrated by Chinese proverbial wisdom: “it is better to die of starvation than to become a thief; it is better to be vexed to death than to bring a lawsuit” and “it is better to keep a friend than to win a victory.”²¹⁴ Even a threat of litigation may undermine trust, and once instigated it is likely that any relationship is beyond repair. What is often overlooked is that any potential contacts linked to the Chinese litigation opponent may also be foreclosed, and related existing contacts undermined. The effect of a loss of “face” ripples throughout a *guanxi* chain. Litigation is thus a practice to be reserved for the very last resort. Arbitration, particularly if *in camera*, may be a more fruitful option; it is best to follow Chinese practice and mediate informally in private first, if possible.

Both contracts and litigation are likely to be less significant to the practice of business in China than in the U.S. Without an understanding of the pivotal role of *guanxi*, many Chinese practices will continue to perplex many Westerners, despite an increasing body of written law regulating commerce in China.²¹⁵ The nature of advice required from lawyers is consequently different in nature and focus: the mere transplantation of American approaches by counsel is simply inadequate, with all that entails for the client and professional liability. “Good counsel” inherently requires significantly more profound cross-cultural understanding and aptitude.

Negotiators from different cultures often start out with different objectives, seek to build understanding between the parties in very different ways, and seek to define agreement differently in terms of expression and confidence in the nature of the obligations and interests created. Furthermore, the Chinese and American examples show that the drivers of these differences are deeply rooted. Significantly, each culture has developed expectations and processes that are rational and predictable in their domestic cultures, but are often counterintuitive from the perspective of the other culture. Recognizing that such differences between cultures impact virtually every transnational commercial and legal undertaking is a

²¹⁴ See, e.g., Deborah Chow, “Development of China's Legal System Will Strengthen Its Mediation Programs,” source: <http://www.asialawreport.com/development-china.htm>.

²¹⁵ See, e.g., Uniform Contract Law, enacted 1999; Anti-Monopoly law, effective August 2008.

first step, and one that itself is not always made; however, it is far from the achievement of cross-cultural competence.

The key is to be able to craft strategies capable of producing favorable results in the real world. Doing so requires understanding the objectives and expectations of your counterparts. Further, techniques and methodology need to be tailored accordingly. This is equally true when forging a business arrangement, or when seeking positive resolution of difficulties in a commercial relationship. Critically for lawyers, it is as true for counsel as it is for clients—perhaps more so, because the client is paying for the lawyer's expertise in framing or enforcing obligations. As it appears that written law has not, and may never, remove cultural differences, it is surely essential to success for counsel to be able to assist their clients in bridging these divides and to reflect this ability in appropriate documentation, policies and dispute avoidance and resolution.

Cross-Cultural Competency Will Likely Become More Crucial in Future

Chinese cultural factors may become even more significant. The principle argument for this lies in the increasing weight of the Chinese economy and the accompanying political influence, coupled with a reassertion of confidence in Chinese values.

Over the last century and a half, Western political and economic dominance has encouraged or obliged the adoption of Western legal structures and law in many countries across the globe. Indeed, few Asian countries have a purely indigenous system of law. In most cases in Asia, the impetus was Western control over investment capital or market access, if not direct political control. For example, Japan adopted civil law codes at the end of the 1800s, but a more far-reaching body of legislation stemmed from the U.S. occupation after World War II. Taiwan also has a civil code system that was in large part a result of the desire to secure U.S. market access, diplomatic support and weapons access after the 1949 separation from mainland China.²¹⁶ However, the economic and political ascension of nations such as China presages a fundamental shift in the balance of economic and potentially political power. The rise of a non-Western culture to economic and political power may also

²¹⁶ Dorothy Solinger, "The Nexus of Democratization: Guanxi and Governance in Taiwan and the PRC," Center for the Study of Democracy, University of California, Irvine, (2006) pp. 5-6, available at <http://repositories.cdlib.org/csd/06-13>.

dramatically alter other nations' willingness to adopt law and legal practices alien to their domestic cultural values.

China has a population of over 1.3 billion, as opposed to approximately 300 million in the U.S., and less than half that in Japan.²¹⁷ China is also approximately the same size as the U.S. geographically. China is potentially a larger internal market and global economic power than the U.S. Potential is one thing, reality is another: during the twentieth century, it never looked like China would achieve its potential. However, China has achieved impressive rates of growth, averaging around 15% per annum from 1997-2007.²¹⁸ In 2006, China recorded a GDP approximately 23% of that of the U.S. (GDP of \$3,206, compared with \$13,751bn for the U.S.).²¹⁹ This proportion has virtually doubled in three years.²²⁰ Furthermore, it exported approximately 10% of world exports, while the U.S. was responsible for 11½%.²²¹ Such figures may be more reassuring than the reality. For example, almost all the export differential is due to invisible trade; China's percentage of visible exports was more than three quarters of that of the U.S. in 2007.²²² Typically, an economy develops visible strength before invisible trade, such as banking and services (a tendency seemingly borne out by the dominance of the E.U. and U.S. in such areas).²²³ Indeed, the growth of Chinese trade has been staggering. China's exports to the U.S. grew 212% to \$163 billion between 2000 and 2005; an annualized rate of over 40%, making it the second largest trade partner of the U.S.²²⁴ Trade volume between the U.S. and China has increased more than eighty-fold between 1979 and 2006.²²⁵ China is already the EU's second biggest trading partner.²²⁶

Furthermore, China has the same internal advantage that originally propelled the U.S. to economic supremacy: a huge internal market, potentially almost four times the size of that

²¹⁷ ECONOMIST, *supra*, n.141, at 16.

²¹⁸ *Id.* at 32. In comparison, the U.S. economy grew at 3.2% over the same period. *Id.*

²¹⁹ *Id.* at 132, 236.

²²⁰ Compare ECONOMIST, POCKET WORLD IN FIGURES, 2007 Ed., Profile Books Ltd., in association with The Economist Newspaper Ltd., ISBN 978 1 86197 863 9, pp. 130, 234.

²²¹ *Id.* at 35

²²² *Id.*

²²³ *See Id.*

²²⁴ Zhou Shijian & Wang Lijun, "China, US Complementary in Trade", *supra*, n.116.

²²⁵ Eben Kaplan, "The Uneasy U.S.-Chinese Trade Relationship" Council on Foreign Relations, April 19, 2006, available <http://www.cfr.org/publication/10482/>. 1979 was the year that the U.S. established normal trade relations with China.

²²⁶ Richard Carter, "EU becomes China's Biggest Trading Partner," EU Observer.com, January 10, 2005.

of the U.S. based upon population.²²⁷ Chinese imports are expected to almost double between 2006 and 2010, to around \$4 trillion.²²⁸ By 2010, it is estimated that there will be 83 million middle-class households in China, and half that again in India, together outnumbering those in the U.S.²²⁹ An internal market is important as a source of economies of scale and potential volumes of sales and profit, but it also has a powerful strategic aspect. A large internal market provides some insulation from the world economy as well as from the impact of economic and trade barriers imposed by other nations. Thus, China is less exposed to the ability of the U.S. to use exclusively economic measures to impact the Chinese domestic economy than is Japan, or any other Asian economy ever was.²³⁰

China is also achieving milestones giving it political as well as economic leverage as a superpower. China recently superseded the U.S. as Japan's biggest trading partner.²³¹ Chinese ownership of U.S. Treasury securities has reached levels where it is now a significant financier of the U.S. current account deficit.²³² China is estimated to have foreign exchange reserves of more than \$1 trillion, and to be looking to invest increasing amounts overseas as its reserves continue to grow.²³³ Another use of such reserves is as a diplomatic "carrot" among less developed nations: China is also becoming not only a major trading partner with Africa—China's trade with Africa quadrupled to nearly \$40bn per annum between 2000 and 2006²³⁴—but also a major source of finance for the continent. Sino-African trade has been growing at around 40% per annum in the last few years.²³⁵ During the Beijing Summit of the Forum on China-African Cooperation in November 2006, China promised \$5bn in loans and credits to African nations, seemingly on soft terms, and committed to a doubling of aid to the

²²⁷ See, Catherine Bolger "Corporations Need a Global Mindset to Succeed In Today's Multipolar Business World," Accenture, published as a special advertising section in The Wall Street Journal, June 18, 2007, p. A6.

²²⁸ Shijian, et al., *supra*, n.116.

²²⁹ Bolger, *supra*, n.227.

²³⁰ There is no doubt that China is susceptible, as indicated by its massive trade surplus; however, the potential for internally driven growth is also spectacular, although slower rates would be likely due to lack of foreign capital flows to Chinese companies currently generating development capital at a rate beyond the reach of the domestic market alone.

²³¹ Michyo Nakamoto, "China Overtakes US in Trade with Japan," Financial Times, April 26, 2007, p. 5.

²³² Jonathan R. Laing, "What Could Go Wrong With China," Barron's, July 31, 2006, p. 23.

²³³ Florian Gimbel, "Overseas Markets Prepare for an Inflow as China Turns on the Tap," comment, Financial Times, February 13, 2007, p. 11.

²³⁴ "China Pledges Aid to Africa" The Sydney Morning Herald, November, 5, 2006, available at <http://www.smh.com.au/news/World/China-pledges-aid-to-Africa/2006/11/05/1162661540873.html>.

²³⁵ Andrew Yeh and Richard McGregor, "China's Path Through Africa Not All Smooth," Financial Times, January 27, 2007, p. 2.

continent by the end of 2009.²³⁶ One motivation for this is thought to be the drive to secure access to commodities required to fuel Chinese industrial production.²³⁷ The EU has shown signs of concern regarding China's broader foreign policy objectives in Africa, but China's confidence is illustrated by the purported reaction of a Chinese diplomat: "Europeans have their foreign policy and China has hers."²³⁸

"The United States should be under no illusion that China will be content with the status quo should its relative power increase (*vis-à-vis* the U.S. in the Pacific Rim)."²³⁹ China is replacing Japan as the political and economic focus of Asia.²⁴⁰ By 2016, it has been predicted that China will be the world's top trading nation, and that it will have the largest GDP by 2021.²⁴¹ The OECD estimates that China will be the world's largest exporter as soon as 2010.²⁴² China is already the largest consumer of commodities such as copper, nickel and zinc, and is approaching U.S. levels of crude oil consumption.²⁴³ The scale and significance of the shift in economic power is dramatic. It is not an evolutionary change but a revolutionary one. "It defies the economic law of gravity that had been in existence before."²⁴⁴

China is approaching parity in terms of economic power with the EU and the U.S. (taken individually). As this point nears, the ability of the U.S. to impose its values on China, by force of economic or political realities, diminishes. At the same time, China is likely to feel less inclined to accept that its traditional practices are somehow less meritorious than those of the West.²⁴⁵ No prior Asian economy has had the scale that China's has today, nor has developed in a world where a leading economic power offered an alternative to the Western legalist model.²⁴⁶ Approximate parity of influence with the U.S. would suggest that China will no longer need to adopt Western law to gain international commercial access, as it

²³⁶ *Id.*

²³⁷ Gideon Rachman, "As America Looks the Other Way, China's Ride Accelerates," comment, *Financial Times*, February 13, 2007, p. 13.

²³⁸ "Union Calls for Free Flowing Discussions on Africa," *Europe Information Service*, July 28, 2006.

²³⁹ Robert S. Ross, "Assessing the China Threat," *National Interest*, October 1, 2005, 2005 WLNR 16021027.

²⁴⁰ *Id.*

²⁴¹ Kaplan, *supra*, n.225.

²⁴² Honor Mahony "China Expected to be World's Biggest Exporter by 2010," *EU Observer.com*, Sept. 19, 2005.

²⁴³ Laing, *supra*, n.232 at 23.

²⁴⁴ Jean-Pierre Lehman, Professor of International Political Economy at IMD Business School, *quoted in* Catherine Bolger "Corporations Need a Global Mindset to Succeed In Today's Multipolar Business World," *Accenture*, published as a special advertising section in *The Wall Street Journal*, June 18, 2007, p. A6.

²⁴⁵ *See, e.g.*, Peng, *supra*, n.154 at 20.

²⁴⁶ *Id.*

did to secure WTO accession. Thus, China is likely to be sufficiently essential to the global economy that it will no longer need to suppress or reject traditional means of resolving disputes and creating business certainty, unless it suits Chinese interests to do so. Indeed, it may be in China's self-interest to reinforce its traditional practices, rather than dilute them. Relationship systems inherently place the indigenous at an advantage against the rest of the world. China could decide that its economic interests would benefit from continuing to require foreigners to learn to navigate its system, just as Chinese businesspeople have had to learn to function within the alien legalistic frameworks of Western countries in order to do business abroad.

China is a natural magnet for other economies with similar cultural attributes, which, in turn, may feel emboldened regarding overt application of their own traditional values. Chinese culture may be seen by other nations as an alternative to Western legalism that is less removed from their domestic values. Many Western businesses have accepted that operations in Asia require a "different way of thinking" that goes beyond cultural sensitivity to developing operational methodologies and approaches consistent with the domestic culture.²⁴⁷ If such views are correct, it would appear that legal advice and representation will similarly need to adapt.²⁴⁸

The current shift in political and economic power suggests that the ability of Western nations to impose Western-style legalism on other cultures may be coming to an end, emphasizing an increasing need for businesses and their advisers to become adept at playing by the rules of other cultures. If so, no U.S. lawyer engaged in advising clients in relation to business activities involving parties from different cultural backgrounds can rest on the assumption that the rest of the world is approaching a consensus on the "proper" form of law

²⁴⁷ Clyde D. Stoltenberg, "Globalization, 'Asian Values,' and Economic Reform: The Impact of Tradition and Change on Ethical Values in Chinese Business," 35 *Cornell Int'l L.J.* 711, 728 (2000).

²⁴⁸ Although China is currently the most visible emerging economic power, it should not be forgotten that the second most populous country in the world, India, has also been growing significantly. India has a population of approximately 1.16 billion and India and China together comprise more than one-third of the entire world population according to the CIA World Factbook 2009 (available at <https://www.cia.gov/library/publications/the-world-factbook/geos/in.html>). In India, too, there is cultural resistance to the idea that "American business culture will eventually be adopted by osmosis because of its inherent superiority." Dr Karine Schomer, "American Business Culture: What Offshore Teams Need To Know" (available at http://www.cmct.net/articles_business_culture.html). Other significant nations, such as Russia (fortified by mineral wealth), Indonesia and Brazil, also add to the potential for cultural influences which are alien to American legalism in world trade. However, China is currently the vanguard in terms of both economic growth and current size of economy.

and its application. International practitioners will require additional skills, as compared to domestic colleagues, over the coming decades. Certainly, the need to question parochial assumptions when advising on matters crossing cultural boundaries can no longer be an academic luxury.

Conclusion

Culture is already a powerful influence on notions of justice and the proper priorities of society, and will continue to be so for the foreseeable future. China's rise, in particular, appears to challenge Western conventional wisdom that the West's legal and economic structures are prerequisites for significant economic development.

Experience seems to suggest that *guanxi* remains a powerful influence over both deal-making and dispute resolution in China. Furthermore, observations from Taiwan suggests that there is little basis for concluding that the advent of civil code will change this reality. Moreover, economic power is likely to continue to flow towards countries that do not share Western cultural norms or practices. Some claim that Western economies have already lost the ability to impose their legal and commercial practices upon world trade, for the first time since the Industrial Revolution.

An increase in cultural diversity between legal and commercial systems may exacerbate what is already a potential source of discomfort for international legal counsel. Clients who are increasingly aware of the problem—and investing considerable resources to build cross-cultural capabilities internally—may also be increasingly less forgiving of law firms which fail to follow suit. Lawyers need to accept that the true determinants of success or failure in international business negotiations or dispute resolution may be significantly removed from Western legal conventions.

Competent advice on cross-cultural transactions demands both awareness of cross-cultural differences and the means to overcome them. To practice in these areas without such abilities is to invite disaster, for both the counselor and the client. Cross-cultural skills should be an essential a part of the business lawyer's tool kit. The growing volume of transnational transactions compels such a new and vital talent.

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Cross-Cultural Competency: A Non-Negotiable Skill for Lawyers Involved in International Commerce

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Businesses of all sizes are selling more to foreign buyers, sourcing from foreign suppliers, entering into ventures with foreign partners and investing directly in foreign businesses or infrastructure. Since businesses rely on legal advice, documentation and advocacy throughout the lifecycle of a business undertaking, lawyers are increasingly being asked to provide counsel relating to transnational business transactions and disputes. Such advice is frequently critical to the successful outcome of a client's initiative. Legal input shapes risk assessments and strategic choices, influences the direction of negotiations and the form of joint ventures, and provides management with the groundwork for moving forward.

Yet transnational commerce inherently crosses cultural boundaries, raising the question of whether domestic assumptions that underpin traditional legal reasoning travel effectively. The answer is that, more often than not, such assumptions do not translate well, and the result is that sound advice in one culture may be far from beneficial in another. To be effective, legal counsel must be able to develop legal support for negotiations, transactions and operational management that is accepted by the counterparty and enforceable in the relevant localities. The absence of such capabilities in counsel can be disastrous. At the outset, flawed risk assessments may result and strategic decisions may be based upon erroneous assumptions. Cultural miscomprehension can alienate or confuse employees, partners, suppliers, customers, and key local constituencies. Needless misunderstandings or minor disagreements may be created or existing ones escalated into major crises resulting in significant costs and, sometimes, more lasting damage to future prospects.

The scale of this challenge is significant. Differences in business culture may represent a greater obstacle to successful outcomes than even language differences.¹ "Cultural differences are the most significant and troublesome variables ... the failure of managers to fully comprehend these disparities has led to most international business blunders."² General Motors has stated in court briefs that "cross-cultural competence is the most important new attribute for future effective performance in a global marketplace."³ Microsoft has acknowledged past losses resulting from an inability to identify and bridge international cultural divides. Microsoft's response, in common with large sections of the business community, has been to invest heavily to establish and broaden cross-cultural skills. The amount of attention devoted by the business media to cross-cultural management tools and techniques reflects the international business

¹ Horwitz, F. M., Anderssen, K., Bezuidenhout, A., Cohen, S., Kirsten, F., Mosoeunyane, K., Smith, N., Thole, K. & Van Heerden, A, "Due diligence neglected: managing human resources and organizational culture in mergers and acquisitions." South African Journal of Business Management, Vol. 33(1), pp 1-10 (2002).

² David A. Ricks, BLUNDERS IN INTERNATIONAL BUSINESS, 3rd Ed. Blackwell (2000) ISBN: 0631217762.

³ *Amicus Curiae* Brief in *Gratz v. Bollinger*, 122 F. Supp. 2d 811 (E.D. Mich. 2000).

community's recognition that developing cross-cultural competence internally is essential to international business success. It should be no less important to ensure that both in-house and outside counsel possess the same cross-cultural capabilities. This is particularly so given the economic and political rise of areas of the world that do not share European-derived commercial or legal traditions or the cultural characteristics from which these developed.

Why are Cultural Differences So Significant?

Our culture shapes the way we see the world.⁴ How we see the world shapes what we regard as proper, or important, and, hence, how we organize our society and evaluate the propriety of actions, in everyday life, in business and at law. Where cultural values differ, the same comment, concept, text or act may be understood completely differently. For this reason, the ability to appreciate cultural differences is essential to successful international commerce, and to the provision of legal services that support it.⁵

Culture is the "set of distinctive spiritual, material, intellectual and emotional features of society or a social group and ... encompasses, in addition to art and literature, lifestyles, ways of living together, value systems, traditions and beliefs."⁶ Unfortunately, visible manifestations of cultural differences—such as fine arts, literature, drama, music, pastimes, cuisine and dress—are of little practical help in predicting how cultural differences will affect notions of proper business conduct and the enforcement mechanisms that underpin business certainty.⁷ The visible manifestations of cultural difference have been compared to the tip of an iceberg, since they represent only a tiny fraction of the whole and are noticeable only because of the existence of the much larger body of unseen influences, as illustrated by the following diagram.⁸

⁴ Cultures are not coterminous with nationality, but tend to be ethnically, and sometimes religiously, defined. See, Convention on the Protection and Promotion of the Diversity of Cultural Expressions (2005) Art. 2(3), available at http://portal.unesco.org/en/ev.php-URL_ID=31038&URL_DO=DO_TOPIC&URL_SECTION=201.html.

⁵ Culture evolves over time and as a result of outside contact, but significant change generally occurs on a generational time scale. See, John Hewko, "Foreign Direct Investment in Transitional Economies: Does the Rule of Law Matter?" East European Constitutional Review, Fall 2002/Winter 2003, p. 78.

⁶ UNESCO definition (2002). Source: http://www.unesco.org/education/imld_2002/universal_decla.shtml#1. Individuals within a culture will vary in the degree to which they reflect cultural generalizations due to differing exposure to divergent cultural traditions and differences in the personality of individual members of societies and cultures.

⁷ See, Robert L. Gegios & Stephen D. R. Taylor, "Cross-Cultural Understanding: An Essential Skill in International Advocacy," in INTERNATIONAL MEDIATION & ARBITRATION FROM THE PROFESSIONAL'S PERSPECTIVE, Anita Alibekova & Robert Carrow eds., Yorkhill Law Publishing (2007) ISBN: 978-1-4303-2526-0.

⁸ Adapted from INTERCULTURAL LEARNING T-KIT, Silvio Marinelli, ed., Council of Europe Publishing (2000). ISBN 92-871-5364-7, p. 21, attributed to "AFS Orientation Handbook," Vol. 4 p. 14, New York: AFS Intercultural Programs Inc. (1984).

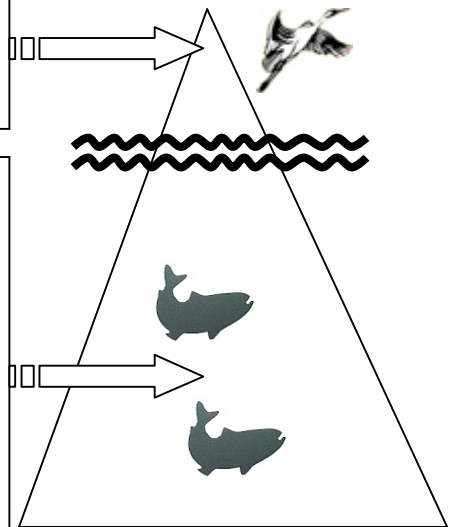
THE ICEBERG METAPHOR FOR CULTURE

Visible Indicators of Cultural Differences

Fine arts, Literature, Drama, Classical music, Popular music, Folk-dancing, Games, Cooking, Dress, Segregation of activities by group

Hidden Influences on Cultural Difference

Notions of modesty, Conception of beauty, Rules of descent, Patterns of superior/subordinate relations, Definition of sin, Courtship Practices, Conception of justice, Motivation to work, Notions of Leadership, Tempo of work, Priority of work versus family, Notion of family, clan or other defining grouping, Patterns of group decision-making, Attitudes to the dependent, Approaches to problem solving, Conceptions of status mobility Implications for status of age/sex/class/occupation/kinship/ etc., Nature of friendship, Conception of "self," Patterns of visual perception, Role of non verbal communication, Notions about logic and validity, Patterns of handling emotions, Conception of past and future Ordering of time Preference for competition or cooperation, Conception of physical space, Etc.



Business practices reflect cultural sensitivities and objectives, and hence are not universal. For example, in the United States, profit is seen as a legitimate goal, success in business can be measured empirically, and the work ethic is highly developed.⁹ For the Japanese, the focus may not be on the pursuit of profit alone, but on human efficiency; the group is superior to the individual. In France, there may be more of an emphasis on moderating one's own freedom of action in order to avoid harming the interests of others, often expressed as a social compact.¹⁰ This is not to say that a French or Japanese person does not seek to make profit. It is simply that as they may not necessarily see true return on investment as measurable solely by bottom-line financial gain, but rather as an amalgam of profit, long-term market position, and the welfare of all stakeholders in the venture, including the workforce, and even the local community.

As commerce is shaped by culture, so is law. Legal systems that have developed organically over time fundamentally reflect the belief system that spawned and upholds them. Indeed, "the rule of law is the very bedrock of our civilization."¹¹ It is not surprising, therefore, that cultural divergence is, if anything, more pronounced in law than in commerce. As Professor Charles W. Wolfram observed in his treatise *Modern Legal Ethics*, "the practices and philosophies of lawyers practicing in other legal cultures very often bear little resemblance to those of lawyers in the U.S."¹² This goes to the heart of legal reasoning and practice:

⁹ P. Poirson, "Personnel Policies and the Management of Men," École Supérieure de Commerce de Lyon, Trans. Thierry Devisse. (1989), p. 6. cited in DEREK TORRINGTON & LAURA HALL, PERSONNEL MANAGEMENT: HRM IN ACTION," Prentice Hall," 3rd Ed. (1995), ISBN 0-13-149543-7, p. 117.

¹⁰ See Torrington, et al., *supra* n. 9, p.117.

¹¹ Margaret Thatcher, "Follow the Leader", American Outlook, Hudson Institute, Spring 2000, at 23.

¹² West Publishing Co. (1986), ISBN 0-314-92639-9.

[T]he Anglo-American lawyer [tends] to evaluate the importance of code provisions, of decisions of higher courts ... and underestimate treatises or commentaries The continental lawyer in contrast will usually find himself at a loss among the innumerable precedents which are binding, but yet can be distinguished out of existence ... and will vaguely look for precise concepts among the legal synonyms, loosely phrased decisions and unsystematic text books.¹³

One of the then most senior English Law Lords, Lord Templeman, acknowledged the practical difficulties posed by trans-system practice in commending an English text for “grappl[ing] manfully with the different problems of construing English and [European] Community legislation.”¹⁴

However, the conceptual divide between established European civil and common law systems is far narrower than that between the traditional systems of many major trading nations.¹⁵ Both legal paradigms are primarily the product of Christian Western European peoples. For all the differences between them they have far more in common than regulatory mechanisms developed in other parts of the world. Other distinct legal traditions include Sharia law, Hindu law and various forms of cultural “law,” such as the *guanxi* system of relationships in China, or *giri* in Japan. To complicate matters, many modern societies operate a fusion of systems, such as Egypt, which has elements of civil, common, and Sharia law, and South Africa, where common law is blended with uncodified civil law. Many emerging nations have imported statute law or civil law code, yet this written law alone often seems not to be predictive of legal outcomes, at least as interpreted without overlaying an understanding of local values and practices inherent to indigenous practitioners.

Contract Law as an Illustration of Divergent Cultural Priorities

Generally, commercial law, or its equivalent in a given culture, performs two functions: the creation of certainty in business transactions, and the resolution of disputes.¹⁶ Where there is trade, some mechanism will have developed to foster certainty in transactions and disputes resolution. However, this may not be legalistic. Cultural rules may be unwritten or may operate by changing the meanings of written law in ways that reflect the traditional values of the culture. Sometimes, the mechanism operates in the absence of enforced law, or outside of its structures. Dispute resolution may be based on the application of moral codes or interpretations of religious

¹³ C. SZLADITZ & C. GERMAIN, GUIDE TO FOREIGN LEGAL MATERIALS: FRENCH, 2nd Ed. Oceana (1985) at ix.

¹⁴ The Rt. Hon. Lord Templeman MBE, Lord of Appeal in Ordinary (1982 to 1994), Foreword to JAMES A. HOLLAND & JULIAN S. WEBB, LEARNING LEGAL RULES, Blackstone Press, 4th ed. (2001), ISBN 1-85431-889-6, at vii.

¹⁵ For more on these divides, see Stephen D. R. Taylor & Robert L. Gegios, “*The Ability to Bridge Cultural Differences: A Prerequisite for Good Counsel in International Transactions*,” COMPARATIVE LAW YEARBOOK OF INTERNATIONAL BUSINESS, VOL. 32, Kluwer Law International (2010) ISBN: 90-411-3361-5.

¹⁶ The fundamental purpose of commercial law is “to maintain the commercial harmony, integrity, and continuity of society.” Source: <http://www.commonlawvenue.com/Glossary/GlossaryA-D.htm>.

teachings. In such circumstances, transactional undertakings or litigation conducted on the basis of written law alone are unlikely to produce the desired outcome.

Dispute resolution and commercial regulation are outgrowths of what is important to a society. In a culture where an agreement is defined by the language in which it is expressed, interpretation on the basis of the language is not only logical, but also essential to establishing certainty in the marketplace. Yet, in many cultures, commercial accommodation requires trust, which can be created only by the gradual building of a relationship.¹⁷ In such societies, a written contract is not always seen as a final embodiment of the accommodation.¹⁸ The idea that words on paper could replace trust built through mutual understanding may appear ludicrous. Breach of obligations under a relationship duly grounded in trust may carry infinitely more severe consequences than a breach of contract. For the same reasons, culture goes to the heart of whether a party will view a business opportunity as worthy of investigation, the terms on which it will do so, and the likelihood that the relationship will be lasting and mutually beneficial. It shapes the conception of what has been entered into and perceptions of why each party has done so, and hence can legitimately expect as a result. Not surprisingly, therefore, it also plays a role in the emergence of disagreements and misunderstandings, whether these escalate into disputes, and whether and how such disputes can be resolved.

The profound impact of such cultural differences is illustrated by considering the differences in the concept of operation of contract between the relatively closely-related Western European civil and common law traditions. Under common law, a contract is not binding unless consideration of at least nominal value is exchanged. Consideration is “an inducement given to enter into a contract that is sufficient to render the promise enforceable in the courts.”¹⁹ In civil law, the critical element is cause, which does not necessarily require any flow of consideration. Thus, gratuitous promises may form the basis of a binding arrangement, and, as a result, contracts in favor of a third party can be recognized and enforced despite no consideration having been tendered for the benefit. “With regard to bilateral contracts, the [cause] of one party is the correlative obligation. In the case of gratuitous contracts, the [cause] amounts to

¹⁷ “Seven Disciplines for Venturing in China,” Deloitte Research (2005), p. 4 col. 1.

¹⁸ The Japanese have sometimes been characterized as averse to all-controlling written contracts. Rather, certainty comes from “*giri*,” a system of intertwining social and moral obligations. “In the event that parties under *giri* should fall into a dispute, then they will adopt a conciliatory and flexible concessionaire approach. The presence of *giri* might be incompatible with the nature of litigation and operate to inhibit a resort to legal resolution of disputes.” Masayuki Yoshida, “*The Reluctant Japanese Litigant: A New Assessment*,” available at: <http://www.japanesestudies.org.uk/discussionpapers/Yoshida.html>.

¹⁹ Encyclopædia Britannica online, available at <http://www.britannica.com/EBchecked/topic/133519/consideration>.

the spirit of liberality of the donor.”²⁰ Consequently, there is no equivalent to the common law concept of privity (under which, as a general rule, only a party to a contract can sue to enforce).²¹

The notions of when a contract can be revoked or is breached differ equally markedly. In common law, an offer can be revoked until acceptance, even if the language suggests otherwise (unless consideration has been exchanged in return for what is perceived as a separate contract to keep the offer open for a given period). This is far from the case in civil law, where once made, an offer is binding for any period specified, or for a reasonable time beyond its making, if accepted within that period. If breach occurs, the concepts applied to determine damages also diverge. Common law holds breach of contract to be a strict liability issue, and consequently, it is enough that a material breach has occurred: no intent or fault is necessary to enable the aggrieved party to recover damages. However, an award of damages under civil law requires a finding of fault. Even if performance is not timely, at civil law, notice must be given to the potential defaulter, who must also be given a reasonable time to remedy the situation. At common law, the contract is deemed to provide adequate notice of conditions and duties, and generally no notice is required to enable damages to be sought.

In “most legal systems outside of the common law world, the law of obligations recognizes and enforces an overriding principle of good faith” as applied to the making and application of contract.²² Common law applies no such rule, rather allowing equitable principles to address unconscionable dealings.²³ However, “only where the contract is unconscionable as might arise from situations of unequal bargaining power between the parties, should the courts interfere with agreements that parties have freely concluded.”²⁴ In other words, the common law acknowledges the potential for abuse of power at creation of a contract. In contrast, the civil law duty of good faith applies to pre-contractual negotiations as well as performance: good faith is presumed and the party alleging otherwise bears the burden of proof.²⁵ The different philosophy of the civil law approach is illustrated by the determination that good faith required debt revaluation by courts in periods of hyper-inflation because it was contrary to good faith for the creditor to be deprived of actual value by the debtor.²⁶ A similar principle is at play in Quebec civil law, under which a party who exercises a contractual right in a manner that would not be expected of a “prudent and

²⁰ Dr. Aron Mifsud-Bonnici, “*The requirement of a lawful consideration in the law of obligations (section 987 [of the Italian Civil Code])*,” available at: <http://www.mifsudbonnici.com/lexnet/articles/causa.html>.

²¹ See, Australian Contract Law website available at <http://www.australiancontractlaw.com/law/scope-privity.html>. As a general rule, under common law, a contract cannot confer rights or impose obligations on persons who did not assent to the agreement that the contract records.

²² *Interfoto Picture Library Ltd v. Stiletto Visual Programmes Ltd* [1988] 1 All ER 348, 352-53, Bingham L.J.

²³ *Id.*

²⁴ *Hunter Engineering Company Inc. et al v. Syncrude Canada Ltd. et al* [1989] S.C.R. 425, 426

²⁵ HOLLAND, et al., *supra*, n. 14, pp. 308-09.

²⁶ *Id.* at 309.

reasonable individual” may be subject to an action to recover damages incurred as a result, even if there was no malicious intent.²⁷

The timing of passing of title is another area of conceptual difference that can cause significant problems. Under common law, the contract, as representative of the desire of the parties, determines when title to goods transfers. However, traditionally, under French law, title passes the moment the nature of the goods and the price to be paid are agreed: delivery and payment are of no consequence.²⁸ German concepts evolved differently from the French: not only must there be agreement, but the goods must also be delivered.²⁹ Taken together, the result is that a secondary buyer may, in certain jurisdictions, acquire the contractual rights of the first buyer for goods not yet delivered, without the need to consult the original seller. Such concepts are directly contrary to the common law precept that parties can contract for risk (unless utterly unforeseeable) and that if parties fail to do so there is no basis for the courts, absent duress, to step in and apply a higher principle of good faith.

Different Cultural Priorities Result in Dramatically Different Approaches to Disputes

Cultural differences affect every aspect of commercial activities, not merely the process of entering into an arrangement. The concept of dispute resolution differs just as profoundly. Consider the approach to evidence in European-derived civil and common law traditions. The principal characteristic of civil law systems is “full exchange before hearings of documents on which each party intends to rely.”³⁰ Judges in civil law countries bear the bulk of the responsibility for bringing out the facts of the case. Pre-trial is not distinguished from trial, or clearly understood as a concept.³¹ The whole American discovery process is frequently viewed as fishing for cause, and as distasteful in the extreme, and often as contradicting fundamental rights of privacy and confidentiality.³² “Never underestimate foreign fear and loathing of American Discovery Practices.”³³ This is so even in common law England, where disclosure (discovery) is generally only available from parties, and then only of identified documents for which relevance can be justified in advance. Depositions, essential to the American process, are regarded as little more than exercises in intimidation and entrapment, to the point that they are

²⁷ *Banque Nationale du Canada v. Houle et al* ([1990] 3 S.C.R. 122, 155; Article 7, Civil Code of Quebec (“No right may be exercised with the intent of injuring another or in an excessive and unreasonable manner which is contrary to the requirements of good faith”).

²⁸ Ceslav Pejovic, “*Civil Law and Common Law: Two Different Paths Leading To The Same Goal*,” [2001] VUWL Rev 42, III. A. at III H, *citing* Article 1583 of the French Civil Code. Available at .

²⁹ *Id.* at III H, *citing* Article 929 of the German Civil Code.

³⁰ W. LAWRENCE CRAIG, WILLIAM W. PARK & JAN PAULSSON, “INTERNATIONAL CHAMBER OF COMMERCE ARBITRATION,” 3rd Ed. Oceana Publications, Inc. (2000), ISBN: 0-379-21392-3, p. 418.

³¹ Glen P. Hendrix, in “*Ten Rules for Obtaining Evidence from Abroad*,” in “INTERNATIONAL LITIGATION STRATEGIES AND PRACTICE,” Barton Legum, ed., ABA Section of International Law (2005), ISBN 1-5903-544-8, p. 105, cites examples for emphasis, including a declaration of a staff attorney at the Russian High Commercial Court that pre-trial discovery enables a party to obtain documents even before a complaint is filed, to facilitate the filing.

³² Javier H. Rubinstein, “*International Commercial Arbitration: Reflections at the Crossroads of the Common Law and Civil Law Traditions*” CJIL, Vol. 5 No. 1, (2004), p. 2.

³³ Glen P. Hendrix, in Legum ed., *supra*, n. 31, p. 105, Rule 1.

almost unheard of in international arbitration. Notions of privilege also vary greatly, in large part because the privilege is the result of a different policy concern. In the United States the aim is to foster full and frank communication, generally safe from discovery. In civil law, the object is to protect professional confidences as a right of the lawyer, who determines what constitutes such a confidence.³⁴ On the other hand, American privilege extends to employees consulted by in-house counsel, whereas civil law privilege generally will not.³⁵ Together these differences over evidentiary rights provide excellent examples of a potentially determinative differences arising directly from different cultural perceptions of privacy.

Such contracts reflect fundamental differences in the rights of the participants, the objective of the judicial process and the manner in which it is conducted. Arguably, the difference goes to the very core of the concept of the position of the individual. The common law focus on these rights of an individual as the basic unit of law is not the same as the civil law concept of an individual as a member of a wider society. Put another way, compare the state-determined balance of constitutional rights expressed in the German Basic Law: “favoring dignity over freedom of speech, and favoring the preservation of democracy over the exercise of free speech”³⁶ with the statement that “all men are created equal, that they are endowed by their Creator with certain unalienable Rights” from the United States’ Declaration of Independence. Just as in conceptions of contract, there are many “largely unbridgeable conceptual chasms between common and civil law” in the areas of pleading, testimony, discovery and the proper time for production of written argument.³⁷ “Counsel should be wary of their own – and their colleague’s culturally conditioned conceptions” and the behavior that springs from these.³⁸

The above differences demonstrate fundamental conceptual divergences between these systems. The starting rationale and burdens placed on the parties are fundamentally different conceptually, resulting in a “difficulty finding even a common starting point for lawyers in the two systems.”³⁹ Cumulatively, these and other differences shed some light on the different notions of the role of contracts in society, on the approach to resolving disputes and the proper limitations on a person’s ability to establish and enforce rights and obligations through a contract. Obviously, the optimal language and structure of any documentation reflecting a given, hypothetical agreement to transact will look very different depending on whether a civil or a common law legal system applies. What is often overlooked is that the ability to enforce agreements and the impact of external events may also differ significantly.

³⁴ Javier H Rubinstein & Britton R Guerrina, “*The Attorney Client Privilege in International Arbitration*,” 18 J. Intl Arb. 587 (2001), p. 591-99.

³⁵ *Id.*

³⁶ *The Unanimous Declaration of the thirteen united States of America, in Congress, July 4, 1776.*

³⁷ Cliff Hendel, “*Transnational Litigation and International Arbitration: Cross-Cultural Reflections*,” International Law News, Winter 2006, p. 8.

³⁸ *Id.*

³⁹ HOLLAND, et al., *supra*, n. 14. p. 311.

Cultural differences deeply impact the concept of an acceptable contract document. For example, the prototypical American conception of contract is an all-encompassing document that is the exclusive record of the respective rights of the parties expressed in a detailed writing. One word may alter the interpretation of the whole contract, rendering precision essential. Therefore language is necessarily specific and direct regarding obligations. The result is a detailed, sequential document intended to address all potential eventualities that may arise over the term of a contract in explicit language. In contrast, in European civil law jurisdictions, contracts are traditionally “relatively straightforward and brief” since major contractual principles are implied as a result of their being enumerated in applicable civil code.⁴⁰ In other parts of the world, the divergence in the conception of contract is often greater. In such circumstances, practical considerations are paramount. The length, breadth and subject matter appropriate for a contract should both facilitate the intended commercial activity and provide certainty in the event of a dispute arising. In many cultures, an American-style detailed exposition may alone be sufficient to prevent the other party ratifying an otherwise acceptable agreement. Alternatively, signature may be effectively valueless, since contracts in such form are either unenforceable under local law, or at best only offer the potential for a pyrrhic victory. As a result, very careful consideration should be given to whether to include and how to fashion dispute resolution clauses, and the manner that these can be beneficially invoked in a cross-cultural setting.

To Achieve Cross-Cultural Competence, One Must First Comprehend the Problem

To appreciate the perspective of another culture, one must understand that even the most fundamental tenets of one’s own culture may not be recognized, let alone understood, in another. Such appreciation entails not only an ability to appraise the fundamental values of others, but to realize that such fundamental concepts as freedom, transparency and individual rights may not be shared, and that this difference critically impacts business transactions and notions of law.

Acquiring the ability to operate effectively across different cultures is a process that requires an individual to question fundamental personal and professional assumptions before he or she can acquire the skills to assess the differences in terms of practical consequences. Only then can a viable approach to a particular legal or business objective be identified and pursued. This is not a sudden process, but a skill that requires time to acquire. For most people it also requires a catalyst to create awareness of the existence of the problem.

Businesspeople with experience in international commerce have often learned all too well that simply being part of the same company does not ensure efficient cross-cultural cooperation. If a corporate connection was sufficient to promote cross-cultural competence, most international cultural problems would disappear or have been solved long ago. In contrast, international businesses increasingly encourage, and often require, senior appointees to have had extensive

⁴⁰ Sara McLaughlin Mitchell and Emilia Justyna Powell, “*Legal Systems and Variance in the Design of Commitments to the International Court of Justice*,” Shambaugh Conference, University of Iowa, October 12-14, 2006. Available at: saramitchell.org/mitchellpowellcmps.doc.

experience of working not just with people from different parts of the globe, but as leaders of business units and teams physically located in different cultures—staffed by and transacting with people and businesses that are part of that culture. In addition, many industries are investing heavily to develop cross-cultural awareness and competency among their personnel.

Lawyers appear to be more insulated from exposure, perhaps in part because lawyers typically focus on their domestic environment. This is supported by the fact that international law firms have, for the most part, been slow to acknowledge the need to invest in such skills.⁴¹ Some international firms are on record as believing that cross-cultural awareness is unnecessary, because they have so many offices in so many nations, or because such issues can be adequately addressed informally, or as an adjunct to domestic sensitivity training.⁴² This appears to confuse international diversity with cross-cultural understanding, and contrasts with the approach of many major businesses that retain such firms. Others may be more candid: “Some lawyers said law firms don't invest in cross-cultural training because it can't be linked to billable hours.”⁴³ For others the issue seems to equate to business etiquette—surely the very tip of the cultural iceberg. “[I]t's not terribly effective to have a workshop or a course that will tell you how to receive business cards,” notes the head of one multinational law firm,⁴⁴ suggesting that some law firms have yet to become appreciative of the impact of culture. Perhaps the reason is the lack of direct exposure of most attorneys to a catalyst.

Some writers, such as Milton Bennett and Mitchell Hammer, believe that without such exposure, the natural inclination, of lawyers and businesspeople alike, is to refuse to recognize that differences exist, and when forced to do so, dismiss their significance or insist on American practice.⁴⁵ One of the most fertile sources of cultural blunders occurs when businesses from developed countries assume their strong belief in the correctness of their domestic operational principles and practices upon operating units located in emerging economies.⁴⁶ According to Bennett and Hammer, even when it becomes apparent that different peoples possess divergent but nevertheless valid and complex world views, there may be problems in coming to terms with the validity of the practices that reflect the underlying cultural differences. The inescapable conclusion is that true cross-cultural competence requires significant time and experience to develop to a point where an individual can grasp different cultural realities and identify means to achieve objectives in a manner that finds support within all the cultures involved.

⁴¹ As one business performance consultancy to law firms notes: “North American lawyers, in particular, may be surprised to learn that styles and behaviors that work well at home may produce unintended negative effects among lawyers and staff in other countries.” Source: <http://www.walkerclark.com/articles.html>.

⁴² See, e.g., Vesna Jaksic, “*The Culture Gap: Firms going global study client customs*,” *The National Law Journal*, May 11, 2007, available at: <http://www.law.com/jsp/llf/PubArticleLLF.jsp?id=1178787890511&rss=newswire>.

⁴³ *Id.*

⁴⁴ *Id.* (quoting the managing partner of one of the world's largest law firms).

⁴⁵ See “The Development Model of Intercultural Sensitivity,” Milton Bennett and Mitchell Hammer (1998), available at <http://www.intercultural.org/pdf/dmis.pdf>.

⁴⁶ Ahlstrom, D. & Bruton, G., *INTERNATIONAL MANAGEMENT: STRATEGY AND CULTURE IN THE EMERGING WORLD*, Cengage Learning, ISBN-10: 0324406312 (2010)

Identifying Cross-Culturally Competent Counsel

The risk of false cultural confidence is genuine, as are the potential consequences. As a result, prudent business decision-makers give cross-cultural expertise significant weight in evaluating potential legal counsel for transnational matters, even where they have had a long and productive relationship with prospective counsel in domestic activities.

There is no miracle test. If available, the assessment should involve individuals within the client organization who have real experience verifying and implementing transactions and operations in other cultures, ideally in close geographic proximity. Whether such resources are available or not, asking the right questions of potential legal counsel at the outset is critical. The following are a few suggestions for developing questions to evaluate prospective counsel. If he or she can address the client's potential impact in relation to a business or project, then one has, at a minimum, established awareness and some potential to develop appropriate solutions. If such responses are lacking, the client may wish to look elsewhere. While far from comprehensive, these suggestions may shed light on whether counsel has an awareness of obstacles and will be able to address how such issues can be accommodated in practice.

In General Dealings

1. Is the individual the rightful focus, or the community, or other group, and to what degree?
2. Is communication direct, or is nuance preferred?
3. Is deference to superiors expected, and to what extent?
4. What are the sources of superiority?
5. Is linear negotiation favored?
6. What is the attitude to devolved decision-making?
7. What is the real source of business certainty?
8. Is there great focus on the past, or is past practice viewed as something to be continuously improved upon?
9. How important is decisiveness (or the public appearance thereof)?
10. What are local attitudes to gender, age or overt sexuality?

In Relation to Resolving Disputes

1. Is the dispute as expressed likely to be the true source of contention?
2. What is the attitude to public conflict?
3. Is "face" a significant concern?
4. Which is most valued: visible affluence or demonstrable contribution to the community?
5. Is there a black or white view of conflict or one of shades of gray?
6. Is conciliation a tenet of the society, or is there a win-lose approach?
7. Is the proper scope of consideration limited to parties or properly inclusive of all stakeholders?
8. Are contracts viewed as final expressions, loose guides, or agreements to agree, etc.?
9. Is profit motive accepted as the prime purpose of business?
10. Can disputes impact prospects beyond the scope of the parties to the dispute?

In relation to Successful Advocacy

1. What are the attitudes to, and bounds of, privilege?
2. Is lawyer contact with witnesses viewed as tainting?
3. What is the concept of privacy? Does this conflict with domestic evidentiary principles?
4. In a deferential society, which sources of evidence attract particular deference?
5. Is the goal to punish wrongdoing or to find the solution offering the least harm to interested parties?
6. Is truth validated by rational, dispassionate investigation, or by live test under cross-examination?
7. Is cross-examination seen as ineffably hostile?
8. Is oral testimony or written evidence seen as more dispositive?
9. Is aggression in advocacy indicative of conviction and right, or improper intimidation?
10. Is precedent seen as an inhibition on the ability of a decision-maker's scope of action?

The above provides a starting point for further research into linguistic abilities, political issues and, most critically, individual background and experience. Detailed knowledge of the laws of a particular nation is not a pre-requisite. Rather, the search is for evidence of a lawyer's awareness and knowledge of the nature and scale of the cultural difference issue, combined with insight into how differences can be identified and addressed to secure effective business and legal advantage.

Businesses with cross-cultural business understanding and experience should expect as much from their counsel. For those companies less experienced in international dealings, advice from peers in the business community on the realities and pitfalls of transnational commerce can help in creating a basis for evaluating potential counsel. The stakes are high: cross-cultural competence can mean the difference between success and failure in matters crucial to a client's long-term business prospects as well as short-term profits.



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Bob Gegios chairs the Litigation Department of the Milwaukee law firm of Kohner, Mann & Kailas, S.C. He has nearly 30 years of experience representing public and private companies and individuals in a wide range of legal matters, including general business and commercial litigation and counseling, securities, antitrust and trade regulation, dealership and franchise law, intellectual property, RICO, employment disputes, insurance coverage, and international controversies. His clients have spanned a broad array of industries and occupations, and he has represented their interests in disputes across the United States as well as in foreign settings.

Bob's many accomplishments include: winning one of the largest jury verdicts in a business case in the State of Wisconsin in recent years; securing dismissals of numerous multi-million dollar class and individual actions brought against both public and private companies, and successfully handling multi-jurisdictional and international litigation, arbitration and mediation matters for both domestic and foreign clients. Bob has been selected for leadership positions in many professional organizations, including the American Bar Association, the Fellows of the American Bar Foundation, and the American Inns of Court. He recently served as President of the Eastern District of Wisconsin Bar Association. Bob is a frequent speaker on mastering cross-cultural differences in business and dispute resolution.

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Prior to becoming an attorney with Kohner, Mann & Kailas, S.C., Stephen Taylor was a businessman and venture capitalist who focused on business development and development of international markets, latterly within the high technology sector. Stephen advises businesses on how to manage electronic information to protect their interests in the event of litigation, and on the conduct of electronic discovery. He also provides transactional and strategic support to businesses involved in trading across international and cultural boundaries and in identifying effective dispute resolution strategies arising out of such activities. An alumni of Marquette University Law School (*cum laude*), Stephen also holds an MBA and degrees in international trade and relations.

Mr. Gegios and Mr. Taylor are the co-authors of internationally published papers on successful navigation of cultural differences in international business and dispute resolution, including:

- *"The Ability to Bridge Cultural Differences: A Prerequisite for Good Counsel in International Transactions,"* Comparative Law Yearbook of International Business, Vol. 32, Kluwer Law International (2010).
- *"Cross-Cultural Understanding: An Essential Skill in International Advocacy,"* International Arbitration and Mediation—From the Professional's Perspective, Yorkhill Law Publishing (2007).

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Founded in 1937, KMKSC is a business and commercial law firm. KMKSC provides quality legal expertise across the areas of law encountered by businesses in the normal course of their operations and growth. Our services range from high-profile appellate representation and international business issues to ensuring that critical everyday needs, such as debt recovery, are fulfilled efficiently and expertly. Our purpose is to deliver excellent results for our clients, whether the issue is advice on the avoidance of legal disputes, closing a deal, protecting assets or winning in court. KMKSC is continually advancing the interests of its clients in negotiations, transactions, litigation and alternative dispute forums across North American and beyond. We help U.S. companies address the legal issues raised by trading across international borders and provide legal support and advice to foreign companies operating in American markets.

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- ▶ General counsel should have strong relationship with PR group
- ▶ Strategies should reduce risks and provide clear, simple and safe messages
- ▶ Foreign subsidiaries should be mindful of cultural and language differences

By Aarti Maharaj

The general counsel's role in PR strategy

Let's face it: a major corporate crisis can happen anywhere, at any time. Whether it's employee misconduct, a hostile takeover or an environmental disaster, companies frequently encounter issues that wreak havoc with their corporate reputation and have a negative impact on their bottom line.

Having a well-thought-out PR strategy can help a firm contain such a crisis, communicate its message to stakeholders and duly emerge with limited damage and perhaps even an enhanced reputation. And one person who can help drive a successful PR strategy is the general counsel.

'Showing that you are adding value to other functions of the company is one of the critical roles of a good legal department,' says Christopher Reynolds, group vice president, general counsel and secretary for legal services at Toyota Motor Sales (TMS). 'The general counsel or corporate secretary should have a well-nourished relationship with the PR group.'

Reaching a large audience with the right message during or after a crisis can be challenging for companies. Reynolds points out that an effective PR strategist should involve the legal function to avoid issuing a message that carries risks - for instance, by contradicting the company's overall mission.

'A representative from the legal function can identify and point out a securities issue and review the PR strategy when necessary, particularly when you are

dealing with highly regulated products,' Reynolds says.

Often, when companies are unprepared and are caught in a crisis, they resort to providing inaccurate information just to protect their image. But this can easily cause more harm than good.



Take Massey Energy, which was cited for more than 1,300 safety violations in the years leading up to the explosion at its Upper Big Branch Mine that killed 29 miners in 2010. A West Virginia state investigation issued earlier this year blamed the mining giant, asserting that it 'knowingly violated the law' and 'blatantly disregarded known safety practices'. The Richmond, VA-based firm lost control of the incident and allowed the situation to escalate, resulting in a series of federal investigations that eventually led to the sale of the company.

Another example of a poorly handled incident was the BP oil disaster. When the spill was first reported, the company's CEO, Tony Hayward, was quoted as saying, 'I think the environmental impact of this disaster is likely to have been very, very modest.' In fact, it caused catastrophic and permanent ecological damage.

'PR strategies need to be accurate, truthful and consistent so your customers and employees can feel comfortable relying on your products,' stresses Reynolds, who is also corporate secretary and chief environmental officer at TMS. 'The problem with PR strategies built around falsehoods is that they have an inherent weakness at their

core, so they tend not to resonate as well.' He advises general counsel and corporate secretaries to become actively involved in formulating a PR plan by considering the following points.

- ▶ **Be a facilitator.** As the company's lawyer, you should have a track record of being a facilitator rather than an obstructor. Remember that your job is to say 'yes' in a smart way that protects the company. Provide alternatives if a suggestion does not seem to be fruitful.
- ▶ **Allow the PR group to do its job.** General counsel with a litigation background are pretty confident in communicating in a cogent way and, as lawyers, they tend to pride themselves on being good wordsmiths. The problem is that their skills are geared for legal purposes and don't always translate well to the general media. There are people with a unique skill for responding to old and new media: they're called PR professionals. Use them to your advantage.
- ▶ **Identify risks.** Scrutinize the message to make sure there are no risks associated with what is being conveyed to the public. If you push the message 'we fired an executive', that can create the risk of employment litigation. Better to provide a simple, clear and safe message.

Handling a crisis overseas

A major crisis at a foreign subsidiary can happen more often than one may think. Many US companies have expanded into emerging markets by establishing subsidiaries, but they are not always equipped with the necessary resources and skills to immediately deal with a corporate crisis overseas. Once a problem surfaces in a foreign country, it can take a significant amount of time to put out the fire. Without an effective strategy in place, it can take even longer.

'When a crisis spins out of control overseas, a simple press release is not enough to handle the issue,' says Rodolfo Rivera, regional counsel at a New York-based Fortune 500 company. 'An action plan should be included in any communication with the public and, when creating a PR strategy in a foreign country, companies should factor in the cultural aspects of those affected by the crisis.'

For example, if regulators overseas are attempting to

shut down a foreign subsidiary, this can morph into a bigger problem if there's no communication strategy in place. A key executive should be designated as the point of contact when a crisis occurs, and that individual should have a team of well-qualified employees to advise him or her on all aspects of the crisis.

As the world's seventh-largest economy, Brazil

'PR strategies built around falsehoods have a weakness at their core, so they tend not to resonate as well'

Christopher Reynolds



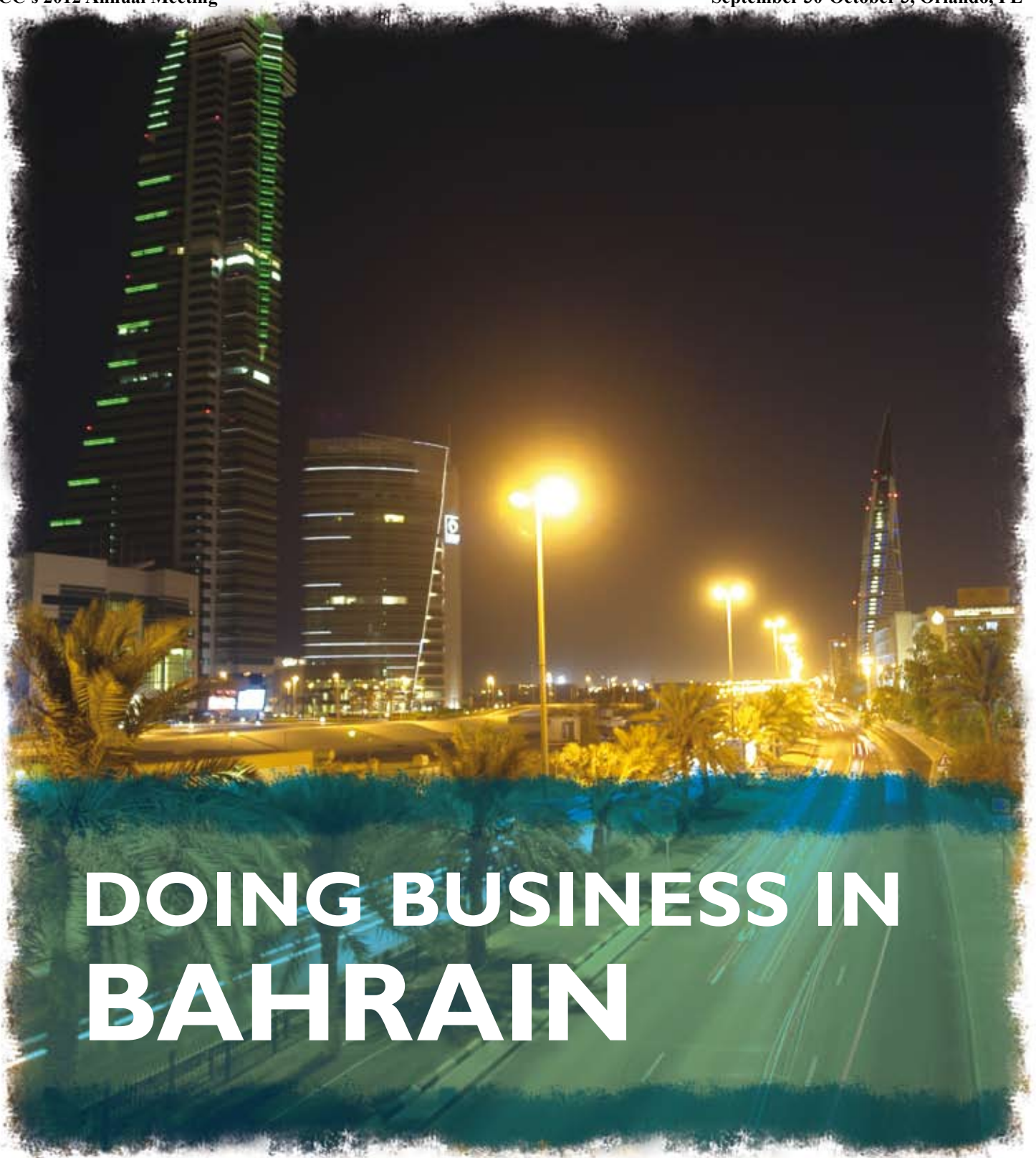
continues to be an attractive destination for international investors. It is rich in natural resources and many US companies are investing heavily in its real estate. In emerging nations, complying with local sustainability efforts has become a common problem for foreign subsidiaries. Environmental issues and climate change often plague Rio Grande do Sul, the southernmost state in Brazil, which is home to many local and international businesses.

In the event that a sustainability issue occurs, Rivera advises that 'the key strategy here is to have a crisis team designated to handle the matter.' One person alone will not have the necessary knowledge base and skills to handle all the issues that surface. Companies must understand that communication is a core business strategy, especially in a foreign country.

'The team must take into account not only what is being said, but also *how* it's being said,' Rivera points out. If the target audience is Brazilian, it is important that the information be accurately translated in that country's language.

'How you communicate ideas is as important as the message itself,' Rivera concludes. 'The most significant problem is that companies don't necessarily understand that communication with stakeholders in a foreign country should be carried out by someone who is familiar with the country's native language.'

▶ **Aarti Maharaj is deputy editor of *Corporate Secretary***



DOING BUSINESS IN BAHRAIN



EVERYTHING MATTERS

OVERVIEW

This guide has been prepared by DLA Piper for foreign clients considering investing in the Middle East and is intended to provide a brief overview of some of the key legal issues in relation to establishing a business in the Kingdom of Bahrain (“**Bahrain**”).

BAHRAIN BACKGROUND

Bahrain is located in the heart of the Arabian Gulf and is an archipelago made up of approximately 36 islands. Bahrain was the first of the Gulf states to discover oil in 1932. However its oil resources are very limited compared to that of its neighbours. As a result of government policy implemented during the 1970’s designed to encourage new investment, Bahrain is now recognised as being a major financial and banking centre within the region.

The Bahraini government is keen to promote Bahrain as “business-friendly” and as such, it has adopted economic policy designed to encourage inward and foreign investment. Companies in Bahrain are permitted to be 100% foreign owned. Foreign owned companies must meet the same requirements and comply with the same regulations as Bahraini-owned companies. The Bahraini government specifically encourages investment in sectors which are export orientated and do not compete with locally owned businesses.

LEGAL BACKGROUND

Bahrain is a sovereign independent Arab Islamic State. A new constitution was implemented on 14 February 2002, which provides that Islamic Shari’a law is the guiding principle behind the country’s legislation. General matters and private transactions are, in principle, governed partially by laws derived from the English common law system, such as the Contract Law and Civil Wrongs Ordinance, and all laws follow a civil law format similar to those of Egypt and France.

Almost all business entities operating in Bahrain are governed by the Commercial Companies Law – Decree 21 of 2001 and the Implementing Regulations of the Commercial Companies Law – Ministerial Order No.6 of 2002 (the “**Companies Law**”). Foreign investment and 100% foreign ownership is generally permitted in Bahrain for service based companies (i.e. non-retail, importing and exporting). There are however, a limited number of business activities which are reserved by law for Bahraini and/or GCC citizens and companies.

As a general note, Bahraini legislation is published in Arabic. Most legislation has been translated however, in the event of

a conflict between the Arabic and English translation, the Arabic version will always prevail.

STRUCTURES FOR DOING BUSINESS IN BAHRAIN

If entities wish to conduct business in Bahrain, they must establish a presence in Bahrain. The two most common types of private companies in Bahrain are limited liability companies (“**W.L.L.**”) and closed joint stock companies (“**B.S.C.(c)**”). All types of company will permit 100% foreign ownership under certain circumstances. An alternative is a single person company.

A foreign company which is incorporated and registered outside Bahrain can establish a branch, office or agency within Bahrain. A local sponsor is required unless otherwise exempted by the Minister of Industry and Commerce.

A foreign investor looking to conduct business in Bahrain will need to ascertain whether foreign ownership of its business activity is in fact permitted. In the case of a proposed acquisition, even if the target Bahraini company is currently owned by a foreign company, it should not automatically be assumed that foreign ownership is permitted in respect of a foreign incoming purchaser, as certain non-transferable exemptions may exist.

LIMITED LIABILITY COMPANY

A W.L.L. in Bahrain is a private company with no less than two and no more than 50 partners. As the name suggests, each partner is only liable to the extent of their respective shareholding in the company. There are certain activities that W.L.L’s cannot engage in, such as banking and insurance activities. A limited liability company must not issue any shares, negotiable warrants or debentures to the public.

The main prerequisites for a W.L.L. are:

- The minimum capital of the company is 20,000 Bahraini dinars;
- The capital of the company must be divided into shares of equal value of not less than 50 Bahraini dinars each. All shares are indivisible and non-negotiable; and
- The company must set up a local office.

It is important to note that in accordance with the Companies Law, a percentage of the profits of the W.L.L. must be set aside each year for depreciation, and 10% of the profits thereafter must be set aside to build up a compulsory reserve until the amount of the reserve equals 50% of the capital of the company.

JOINT STOCK COMPANY (CLOSED)

A B.S.C.(c) is a company that can be incorporated with no less than two shareholders and may be 100% foreign owned, however, the shares of a B.S.C.(c) cannot be offered to the public. Banking and insurance activities are allowed with this type of company and a legal sponsor is not required.

The main characteristics of a B.S.C.(c) are:

- There is a minimum capital requirement of 250,000 Bahraini dinars;
- The value of each share must be at least 100 fils and not more than 100 Bahraini dinars;
- 100% foreign ownership is permitted;
- A local sponsor is not required; and
- The company must set up a local office.

The requirement with regard to the build up of compulsory reserves is similar to that of a W.L.L.

BRANCHES, OFFICES OR AGENCIES OF FOREIGN COMPANIES

Foreign companies incorporated abroad may establish a branch, office or agency in Bahrain if it:

- Obtains a licence to do so from the Minister of Commerce and Industry;
- Has a Bahraini sponsor, who may be a businessman or company. The Minister of Industry and Commerce however, can exempt the foreign company from this requirement if the company's branch or office shall use Bahrain as a regional centre or representative office for the company's activities; and
- Provides a guarantee to ensure the performance of its obligations. The guarantee shall either be a sponsorship by the head office or by a Bahraini sponsor or a bank deposit. The Minister of Industry and Commerce shall define the guarantee required in respect of each branch, office or agency and, if the guarantee is a deposit, the Minister shall designate the bank with which the money shall be deposited.

COMMERCIAL AGENCIES

In Bahrain, a commercial agent can be appointed by a foreign party to represent the foreign party's product or service in Bahrain. The Commercial Agency Law of 1992 ("Agency Law") is the law that governs these relationships in Bahrain. The Agency Law allows foreign parties to distribute or sell their products and commodities in Bahrain through agents, alleviating the need to establish a local presence. Agents must be either Bahraini nationals or majority-owned Bahraini companies.

An agency contract must contain the names, nationalities, and assets of the parties, along with a description of the types of products handled. The law requires that agents assume responsibility for providing all customers the spare parts and tools necessary to maintain and to repair any machinery and equipment sold by the agency. It is important to note that when a contract is being drawn up, the use of the term "agent" can create difficulties due to definitional differences. The Ministry of Industry and Commerce ("MIC") allows for substitution of the term "agent" with the term "distributor", which can more accurately describe the function intended.

All commercial agency agreements must be registered with the Commercial Agencies Register maintained for this purpose at the Directorate of Commerce and Companies Affairs, MIC. An unregistered agency will not be recognised and cannot be the subject of court proceedings.

A foreign principal may appoint more than one agent, as well as being able to enter fixed-term agency agreements. Further, a principal may terminate an unproductive agreement through the MIC.

EMPLOYMENT IN BAHRAIN

Under Bahrain law, if a company wants to hire a foreign employee, it must first obtain a work permit and a residence permit for each such expatriate employee. The Ministry of Labour's Employment Directorate is responsible for issuing work permits to expatriate employees and numerical restrictions for work permits set by the Ministry may apply from time to time.

It is important to note that Bahrainisation requirements apply to companies which hire 10 or more expatriates, and the specific requirements which must be met vary from sector to sector. There is currently no written legislation setting numerical Bahrainisation requirements, and enquiries must be made at the Ministry of Labour as to the Bahrainisation rules set for that particular sector.

An end of service benefit may be payable to an employee whose employment is terminated and who is not covered by the Social Insurance Law.

REAL PROPERTY IN BAHRAIN

The Bahraini government has introduced a number of initiatives to help increase overseas investment, such as allowing foreign ownership of land in selected areas especially developed or designated for foreigners. Foreigners who buy real property in Bahrain are automatically granted residency, which extends to the owner's family, for the whole duration of the ownership.

TAX IN BAHRAIN

Except for a single corporate tax of 46% imposed on oil, gas and related companies, Bahrain levies no taxes on capital gains, sales, estates, interest, dividends, royalties or fees.

It is also worth noting that there are no exchange control restrictions on converting or transferring funds. In addition to having no corporate tax, Bahrain has no restrictions with regard to the repatriation or remittance of profits, capital or on the convertibility of currency.

The regulatory system in Bahrain is dynamic and subject to frequent changes in application and interpretation. This guide is based on material available to DLA Piper as at April 2011 and will require amendment from time to time as legislation is amended or new policies or interpretations are adopted by government authorities, courts and/or regulators. We therefore recommend that you obtain legal advice and liaise with the relevant government authorities on how the law applies to foreign investors in respect of a particular investment or business activity at the relevant time.

We hope you find this guide to be a useful overview of the high level legal issues regarding doing business in Bahrain. Please do not hesitate to contact us if you have any queries in relation to the material set out in this guide or if you require specific legal advice in respect of an establishment.

GENERAL

This guide only highlights material legal issues which DLA Piper believes are relevant to a potential foreign investor in Bahrain. It does not constitute legal advice nor does it purport to address every legal issue or summarise all current rules, structures or regulatory frameworks.

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DOING BUSINESS IN EGYPT



OVERVIEW

This guide has been prepared by DLA Piper for foreign clients considering investing in Egypt and is intended to provide a brief overview of some of the key legal issues in relation to establishing a business in Egypt.

EGYPT

Egypt is located in North Africa and is the second most populous country on the African continent, with an estimated population of 78 million. The majority of the population is Muslim with a Christian minority and the official language of Egypt is Arabic, though English is widely used.

Following the decision of the former President Hosni Mubarak to step down on 11 February 2011, the Supreme Council of Armed Forces is officially in charge of managing the country's affairs, together with a civil government.

The Supreme Council of Armed Forces has suspended the 1971 Constitution and issued a new Constitutional Declaration to serve as an interim Constitution for the transitional period. Key changes in the Constitutional Declaration include the shortening of the presidential term, the creation of a two-term limit, significant expansions to the pool of eligible presidential candidates and restored judicial supervision.

Certain temporary restrictions may be imposed on offshore transfers of funds by foreign investors in the Egyptian market for investment purposes e.g. for financing their businesses and transferring revenues.

LEGAL BACKGROUND

The Egyptian legal system is based on the civil law system. It mirrors principles of the Napoleonic code while adopting Islamic law in specific areas. Egypt accepts the compulsory jurisdiction of the International Court of Justice with reservations. Judicial review is by the Supreme Court and Council of State, which oversees the validity of administrative decisions. Egypt is a signatory to the 1958 Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

STRUCTURES FOR DOING BUSINESS IN EGYPT

Foreign companies or individuals wishing to establish a business presence in Egypt have various options available to them, the most common of which are outlined below.

Joint Stock Company ("JSC")

An Egyptian JSC is a regulated company of which its capital is divided into shares and the liability of each shareholder is limited to the paid up value of their shares. The minimum number of shareholders of a JSC is three (3) and a JSC may be wholly owned by non-Egyptians.

The minimum share capital for a JSC whose shares are not offered to public subscription is EGP 250,000. If shares are offered to the public, the minimum capital is EGP 1,000,000 and each share must have the same nominal value. While preferential shares may be issued, these are less commonly used.

The shares of a publicly listed JSC can be traded on the Egyptian Stock Exchange. The annual net profit of a JSC must be appropriated in accordance with the provisions of Companies Law No. 159 of 1981 ("Companies Law").

A JSC is managed by a board of directors and there are no nationality requirements for directors. Provided it does not conflict with public order or morality in Egypt, there are no restrictions on the purposes of a JSC.

According to the Companies Law, shares of the JSC are freely transferable. The articles of incorporation of the JSC may regulate the process of the transfer of shares without depriving any of the shareholders of the right to transfer shares within the provisions of the applicable laws.

Limited Liability Company ("LLC")

An LLC is a company with limited liability, where the number of shareholders may not exceed fifty and should not be less than two. An LLC may be wholly owned by foreigners.

The articles of incorporation of an LLC determine the minimum capital to be paid in full upon incorporation and the value of the quotas. All quotas must have the same face value of no less than EGP 100. The shareholders' liability is limited to the extent of capital contributions.

An LLC cannot raise funds through public offerings. An LLC may conduct a variety of business activities, with the exception of insurance, banking, savings, receiving deposits or investing funds on behalf of others, each of which must be conducted by a JSC.

The day to day management of an LLC is vested in one or more managers and the shareholders have the right to appoint managers, at least one of whom must be Egyptian.

Branch Office

Foreign companies are allowed to open branches in Egypt to carry out construction works, hotel management, commercial, financial and industrial activities or generally to execute works of a contractual nature. A branch does not have a separate legal existence from its parent company. Accordingly, the establishing foreign company is fully liable for all the obligations and liabilities of the branch.

The equivalent of a minimum of EGP 5,000 must be transferred in foreign currency to a bank account in Egypt in the name of the branch.

A manager must be appointed to manage the branch and to legally represent it in all matters related to its activity and existence. The manager may be a foreign national.

Representative Office

Foreign companies can establish representation, liaison or scientific offices. The object of such offices is limited to studying and exploring the Egyptian market without actually performing any kind of commercial or income generating activity.

The equivalent of a minimum of EGP 5,000 must be transferred in foreign currency to a bank account in Egypt in the name of the representative office.

The manager of the representation, liaison or scientific office can be a foreigner. There is no minimum capital applicable but the funds required to establish such an office and operate it should be transferred from abroad in foreign convertible currency and deposited in one of the accredited banks in Egypt.

INVESTMENT GUARANTEES AND INCENTIVES LAW NO. 8 OF 1997 ("IGIL")

Companies can incorporate an entity in Egypt under the IGIL. The rules and regulations are virtually identical to the Companies Law. However companies incorporated under the IGIL are licensed by the General Authority for Investment and Free Zones and may be entitled to tax and capital investment incentives.

The benefits given under the IGIL depend on the activity to be conducted. The activities covered by the IGIL include infrastructure, manufacturing and mining, transport, software and computer systems development and production, medical services, certain financial services, oil fields services, agriculture, reclamation of desert land, hotels and tourism.

The IGIL provides for the establishment of Free Trade Zones including privately run free zones. Products exported outside of Egypt and products imported for the purpose of the PFZs (private free zone) activity are not subject to the applicable general laws governing exportation or importation. PFZs generally are not subject to Egyptian tax laws, including in respect of distribution of dividends.

Machinery and equipment imported by the PFZ for the purposes of practice of the company's activities are exempt from applicable Egyptian Customs Law and procedure as well as from the Egyptian Sales Tax law.

The previous tax exemptions applicable under the IGIL have now largely been repealed, and we would welcome your further inquiries regarding this important matter.

COMMERCIAL AGENCIES

Agencies are principally regulated by Law 120 of 1982 (as amended), and the subsequent Commercial Code of 1999. In addition, a number of provisions of the Civil Code apply more generally to the relationship between a principal and his agent, unless specifically regulated by the provisions of the Commercial Code.

Egyptian laws recognize several types of agents. The main distinction lies between commission agents, who undertake dealings in their own name but for the account of third parties and commercial or contract agents who conclude contracts in the name, and for the account of, the principal.

Commercial agents must be either a person of Egyptian nationality or an Egyptian legal entity. Agents must be registered at the Registry of Commercial Agents.

While agencies are widely used by foreigners as a vehicle for undertaking business in Egypt, the termination of unlimited period agencies has proved to be challenging if the termination is made without prior notice or at an inconvenient time. If no choice of law is expressly agreed in the contract, the principal and the agent will be deemed to have chosen Egyptian Law. Moreover, a number of Egyptian law provisions are mandatory and may not be derogated from.

EMPLOYMENT IN EGYPT

Egyptian Law 12 of 2003 (the "Labour Law") governs the relationship between employer and any employee working in Egypt regardless of their nationality.

The provisions of the Labour Law cannot be contracted out to the detriment of the employee. In general, the provisions of the Labour Law benefit and protect employees more than their employers. For example, the events of termination of an employment relationship under the Labour Law are very limited. Furthermore, an employee's accrued rights under an employment relationship may not be diminished in a manner that is unfavorable to the employee.

Employee benefits extend to the compulsory national social insurance coverage as well as an annual salary increase of a minimum of seven percent. In addition, the Labour Law addresses and regulates employee rights to strike peacefully in relation to their economic, social and professional interests through their labour unions.

REAL PROPERTY IN EGYPT

Real Estate in Egypt is mainly regulated under the Egyptian Civil Law, the Real Estate Registration Law and Law No. 230 of 1996 on the foreigners' acquisition of real estate and related legislations.

Companies and other entities doing business in Egypt are entitled to acquire ownership of Egyptian real estate without any restriction or limitation as to the nationality of the shareholders of such companies or entities as long as the acquired real estate is necessary for doing business. However, a recent decree provides that certain limited areas may not be acquired by foreigners.

TAX IN EGYPT

With the exception of companies incorporated in a free zone, all locally registered companies are subject to corporate tax at the standard rate of 20 percent. A higher rate of 40.55 percent applies to companies engaging in specific oil and gas activities. Personal income tax is also payable in Egypt, on a sliding scale. There are no restrictions within Egypt regarding currency accounts or repatriation of capital and profits.

The annual profit of a branch is taxed at a rate of 20 percent in the same way as for Egyptian companies. However, taxable profits are determined on the activities exercised by the branch in Egypt, not on the whole value of the contract(s).

GENERAL

This guide only highlights material legal issues which DLA Piper believes are relevant to a potential foreign investor in Egypt. It does not constitute legal advice nor does it purport to address every legal issue or summarize the current rules, structures or regulatory frameworks.

The regulatory system in Egypt is dynamic and subject to frequent changes in application and interpretation. This guide is based on material available to DLA Piper as at May 2011 and will obviously require amendment from time to time as legislation is amended or new policies or interpretations are adopted by government authorities, courts and/or regulators. We recommend that you obtain legal advice and liaise with the relevant government authorities on how the law applies to foreign investors in respect of a particular investment or business activity at the relevant time.

We hope that you find this guide to be a useful overview of the high level legal issues in relation to doing business in Egypt. Please do not hesitate to contact us if you have any queries regarding the material set out in this guide or if you require specific legal advice in respect of an establishment in Egypt.

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KEY FACTORS IN FORUM SELECTION CLAUSES AND ARBITRATION CLAUSES INVOLVING ISRAELI PARTIES

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I. Introduction

International practitioners are frequently asked to advise clients as to the propriety of forum selection clauses, choice of law clauses, arbitration clauses, and the like. The purpose of this paper is to provide American lawyers with a general understanding of the uniqueness of Israeli civil litigation in order to enable them to give basic advice to their clients who are considering transactions involving Israeli parties. This paper is *not* a survey of Israeli law and is obviously *not* intended as a substitute for specific legal advice in individual circumstances.

Although Israel can loosely be categorized as a common law jurisdiction, litigation in Israel is different from litigation in the U.S. in several significant respects. The principal areas of difference can be summarized as follows:

- The plaintiff is usually required to pay a filing fee based upon the amount sought in his complaint. Although Israel does not apply the "British Rule" as to lawyers' fees and costs, the obligation upon the losing party to pay *some* costs is a significant factor in litigation strategy;
- "Summary procedure," under which the burden of going forward is shifted to the defendant early in the case, is frequently used (and arguably abused);
- Israeli long-arm jurisdiction extends to all parties to a contract governed by Israeli law even if those parties have *no* other connection to Israel; and
- There are no juries – all trials are before a judge. There are no depositions.

Each of these factors is examined below as to its effect on forum selection, choice of law, and arbitration clauses. In addition, this survey highlights several recent developments under Israeli law and practice concerning international arbitration.

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II. The Four Principal Differences

A. The Filing Fee and other Litigation Costs

1. Filing Fee

A plaintiff in a suit for money damages is generally required to pay a fee to the court upon filing his complaint (the "Filing Fee").¹ The amount of the Filing Fee is a percentage of the monetary sum sought in the complaint, generally 2.5 percent, half of which is due at the time of filing the complaint, and the other half before the first evidentiary hearing in the case.²

Thus, for example, a plaintiff seeking \$1 million in damages must pay a Filing Fee to the court of \$25,000. Even if the plaintiff obtains a judgment in his favor in the full amount of \$1 million, he is *not* entitled to receive a *refund* from the court of any portion of that \$25,000 but may seek to recover from the defendant an amount that includes his Filing Fee by making a post-trial motion to have the defendant pay the plaintiff's "costs."

However, in those cases in which the court succeeds in mediating the parties to a settlement, the filing fee will usually be refunded.

2. Other Costs

A losing plaintiff in Israel loses in at least four ways: it loses the case; it has paid and will not get back its Filing Fee; it must pay its own legal fees; and, perhaps most noteworthy, it will have to pay some amount of the defendant's "costs."

The general rule under Israeli law is for the losing party to pay some amount of its adversary's costs. This is not the "British Rule" of "loser pays all." It is also not the equivalent of Rule 11 of the Federal Rules of Civil Procedure, which requires some showing of "improper purpose" or "frivolousness." Under Israeli law, costs are *routinely* awarded in favor of the prevailing party.

¹ Only a nominal Filing Fee is required by a plaintiff who sues in Israel for recognition of a foreign judgment or a foreign arbitral award.

² One possible method for deferring the Filing Fee is to sue for an accounting of a partnership; under certain circumstances, an international joint venture could be considered a partnership within the meaning of the rule allowing deferral of the Filing Fee.

The amount of costs awarded is within the discretion of the court. The Civil Procedure Rules (1984, "CPR") provide that the court should take into account "the value of the relief actually in dispute" and the "value of the relief awarded" after trial; the court *may* also take into account "the manner in which the parties conducted the trial."³

Although it is difficult to arrive at any "rule of thumb" in this area, costs to be paid by the losing *defendant* rarely exceed fifteen percent of the amount of the judgment granted to the plaintiff.

Costs are also routinely awarded in connection with interlocutory motions.

3. Requirement for Plaintiff to Deposit Security

Not only might the plaintiff have to pay some of the defendant's costs, but the plaintiff might have to do so near the outset of the case. As a general rule, the court has the discretion to order a plaintiff to post security (usually in the form of a bank guaranty) for payment of *all* of the defendant's anticipated costs. Such an order is regularly granted in the case of foreign plaintiffs. When the plaintiff is ordered to give security but fails to do so, the case can be dismissed.

In contract cases, one way for foreign plaintiff to avoid the requirement of posting security is to include a provision in the contract whereby each Israeli party expressly *waives* its right to seek security for costs in any litigation in Israel. *See infra* "Arbitration."

B. Summary Procedure

A plaintiff in Israel can bring an action under the caption "summary procedure," the practical effect of which is to shift the burden of going forward to the defendant. In connection with commercial disputes, a plaintiff may sue by way of summary procedure if there is "written evidence" of the underlying "express or implied" obligation "to pay a liquidated sum of money."⁴ When such a complaint is filed, in order to avoid having a judgment entered against it, the defendant must

³ CPR 512(b).

⁴ CPR 202.

submit an affidavit, setting forth the basis of the defense, along with a motion for "leave to defend."⁵

The conventional wisdom in Israel is that, even when the defendant receives leave to defend, the plaintiff has obtained at least a slight advantage because the plaintiff receives, near the outset of the case, an affidavit from the defendant and an opportunity to cross-examine the defendant on that affidavit – all this without the plaintiff giving any sworn testimony. In a legal system that has no depositions, such a procedure can be valuable. In addition, to the extent that summary procedure causes the defendant to outspend the plaintiff on litigation costs early in the case, summary procedure can be one factor in persuading a defendant to settle early.

As a practical matter, Israeli judges almost always grant leave to defend, and many use the hearing on the motion for leave to defend as an opportunity to explore settlement possibilities.

C. Israeli Long-Arm Jurisdiction

Israel's equivalent to an American long-arm jurisdiction statute is Rule 500 of the Civil Procedure Rules. In addition to the typical domestic basis for jurisdiction, Rule 500 provides for jurisdiction in any of the following cases:

- (1) an action concerning a contract in which:
 - a. the contract was "made" in Israel;
 - b. the contract was made by or through an agent in Israel on behalf of a non-Israeli principal;
 - c. Israeli law applies to the contract (whether expressly or implicitly);
 - d. the alleged breach was in Israel;
- (2) the action seeks an injunction as to activity in Israel;
- (3) the action "is founded upon any action or omission" in Israel;
- (4) the action seeks enforcement of a foreign judgment or arbitration;
- (5) a person outside of Israel is a "necessary of proper party" to an action "rightfully" brought against another defendant duly served in Israel.⁶

⁵ CPR 204. In some respects, Israel's summary procedure is similar to the "motion for summary judgment in lieu of complaint" under § 3213 of New York's Civil Practice Law and Rules.

For American companies doing business with Israeli companies, the most important (and perhaps surprising) aspect of Israel's long-arm statute is the provision extending personal jurisdiction to all cases in which Israeli law applies.

Under American law, a state the law of which is selected in a contract will not necessarily be entitled to exercise personal jurisdiction over a foreign defendant in a contract case merely because that defendant is a party to the contract. Not so under Israeli law. Rule 500 authorizes jurisdiction over a foreign defendant whenever Israeli law applies – "expressly or implicitly" – to a contract to which that defendant is a party.

In other words, any "choice-of-law" clause that reads (in words of substance) "This contract shall be governed by Israeli law" also means: *With respect to any claim relating to this contract, each party hereby submits to the jurisdiction of the courts of the State of Israel.*

This trap for the unwary can be rectified, in most cases, through a contractual provision whereby each Israeli party *waives* its right to assert personal jurisdiction over foreign parties solely on the basis of the choice-of-law clause.

D. No Juries/No Depositions

The lack of a jury system affects all aspect of litigation in Israel. By way of example:

- Money judgments are generally lower than in the U.S. (especially in areas such as product liability).
- Punitive damages are rare;
- Foreign defendants have somewhat less to fear as to local prejudice than they might otherwise have with a lay jury.
- The costs of taking a case to trial can be lower due to savings on jury research, jury selection, preparation of exhibits, and deliberation time.

⁶ Unlike most American long-arm statutes, Rule 500 does not expressly authorize personal jurisdiction over a foreign defendant that, acting tortuously outside the jurisdiction, causes injury within the jurisdiction. As a practical matter, however, personal jurisdiction in such cases can generally be based on the foreign defendant's being a "necessary defendant" to the case in which an Israeli resident (such as a local distributor) has been duly served as a defendant. Therefore, foreign companies that sell their products to Israel are generally subject to personal jurisdiction in Israel for product liability claims.

Because virtually all Israeli judges read and understand English, documents can often be admitted into evidence without being translated onto Hebrew.

The absence of depositions from Israeli civil litigation can mean that discovery is less complex – and less costly – than in the U.S.⁷ As a practical matter, the lack of depositions generally means that, in a lawsuit involving a U.S. company in Israel, the company will not have to send all of its witnesses to Israel twice (for depositions and for trial) but only once, for the trial of the case. On the other hand, even in those cases in which a foreign witness submits a case-in-chief affidavit in English, the party that submitted such affidavit probably will be required to supply an interpreter to enable the opposing lawyer to cross-examine in Hebrew. The costs of an interpreter are usually imposed upon the side that submitted the English-language affidavit.

III. Strategic Considerations

With this general understanding of the uniqueness of Israel civil litigation, the issues of (a) forum selection, (b) choice of law, and (c) arbitration can be examined.

A. Forum Selection

Israeli courts generally honor forum selection clauses⁸ for the same policy reasons that American courts honor them⁹: to do otherwise would frustrate the purpose of the parties' bargain and add uncertainty in an area on which the parties have manifested a desire for certainty. *But see infra* (concerning Israel's Standard Contracts Law).

⁷ However, the savings in discovery costs are often lost at trial: because witnesses have not been deposed before trial, Israeli lawyers cannot focus their cross-examination at trial as well as their American counterparts can. This often results in trial testimony taking longer than it does in the U.S.

⁸ See, e.g., C.A. 566/94 *Salim Snakri v. Julius Blum GmbH* (Nevo 1996).

⁹ See *Nova Ribbon Prods. V. Lincoln Ribbon, Inc.*, 1992 WL 211544 (E.D. Pa. 1992) (enforcing forum selection clause that called for litigation in Israel); see also *Scafuri v. Lumenis Ltd.*, 64 Mass.App.Ct. 1103, 2005 WL 1828814 (Mass.App.Ct. 2005) (enforcing forum selection clause, calling for litigation in Israel, despite former employee's contention that terrorist attacks in Israel would deprive him of his day in court).

Most international practitioners adhere to the following rule: if we must litigate, let's litigate at home. The inclusion in most international commercial agreements of a forum selection clause – in which at least one party agrees to break the "litigate at home" rule – is generally the result of unequal bargaining positions and the insistence by the party with the upper hand that it not be inconvenienced by litigating abroad.

In light of the Filing Fee requirement and the cost issues outlined above, why – other than submission to negotiating pressure – would a foreign company ever agree to litigate in Israel? Because on the nature of a specific transaction, it is possible that the foreign company could expect:

- to be a defendant in any future litigation, and, as such, happy to see the plaintiff forced to sue where it must pay a significant Filing Fee; or
- to be able to take advantage of Israel's summary procedure in the event that it (the foreign company) were to have sue.

In addition, in tort cases (or those in which at least one claim is tort-based), an American defendant might prefer an Israeli judge to an American jury.¹⁰

In this context, the issues of recognition of judgments/enforcement and service of process are examined below.

1. Recognition/Enforcement

American judgments are generally entitled to recognition in Israel. In 2006, an Israeli court even enforced a New York judgment that included an award of *punitive* damages of \$1.5 million.¹¹

Once an American judgment is declared "enforceable" in Israel, it can be executed upon as though it were a judgment of an Israeli court.

¹⁰ See, e.g., *Niv . Hilton Hotels*, 2008 WL 4849334 (S.D.N.Y. 2008), *aff'd*, 2009 WL 5064328 (2d Cir. Dec. 2009) (affirming dismissal on *forum non conveniens* grounds, of claim against American hotel company, where primary claim was negligence in taking precautions against terrorist attack; court found Israeli forum adequate).

¹¹ C.F. (Tel Aviv) 1404/03 *Bamira v. Grinberg* (Nevo, 2006).

Numerous state¹² and federal courts¹³ have enforced Israeli default judgments.

Therefore, both parties to an American-Israeli transaction can generally assume that a judgment from the other country will be enforceable at home.

2. Service of Process Upon Israelis in American Cases

Both the United States and Israel have signed the Convention on the Service Abroad of Judicial and Extrajudicial Documents in Civil or Commercial Matters (commonly known as the "Hague Service Convention" or the "HSC") Under the HSC, each contracting State is required to establish a Central Authority to receive requests for service coming from other contracting states, to have the documents served in accordance with local law, and to certify to the applicant that service of the documents has been made. Israel has designated the Directorate of Courts, 22 Kanfe Nesharim Street, Jerusalem Israel, as the Central Authority for purposes of the HSC.

The Directorate of Courts will not process a request for service of documents unless the request "emanates from a judicial authority or from the diplomatic or consular representation of a contracting state." The Directorate of Courts does not consider a private attorney to be an officer of a foreign court. Therefore, American lawyers seeking service in Israel should put the name and address of a judge, clerk of court, or other judicial official in the space for the information on the applicant and have that official sign the service request.

¹² See *Parson v. Bank Leumi Le-Israel*, 565 So. 2d 20 (Ala. 1990) (affirming grant of summary judgment in favor of an Israeli bank based on an Israeli default judgment); *Israel v. Flick Mortgage Investors*, 23 So.3d 1196 (Fla. 3d App. 2008); *Kam-Tech Systems Ltd. v. Yardeni*, 774 A.2d 644 (N.J. Super. 2001); see also *Dial 800 v. Fesbinder*, 118 Cal.App.4th 32, 48, 50, 12 Cal.Rptr.3d 711, 723, 724 (2d Dist. 2004) ("any Israeli arbitration award would be enforceable in the United States"; "there is no indication that an award, whether rendered by a secular or religious tribunal in Israel, could not have been reduced to a judgment enforceable in California"); *M.E. Jones, Inc. v. Arel Communications*, 2003 WL 1949786 *2 (Ohio App. 2d Dist. 2003) (in connection with motion to stay parallel proceedings, "any ruling issued by the Israeli court is enforceable in Ohio").

¹³ *Menorah Insurance Co. v. INX Reinsurance Corp.*, 72 F.3d 218, 222 n.6 (1st Cir. 1995) (rejecting contention that an American party could avoid an Israeli default judgment after having agreed to arbitrate in Israel; "[i]n the commercial context a forum selection clause, even one for arbitration, confers personal jurisdiction on the courts of the chosen forum"); *Tahan v. Hodgson*, 662 F.2d 662 (D.C. Cir. 1981).

If service were to be carried out in a manner *other* than through the Directorate of Courts, there is a possibility that the Israeli defendant (eventual judgment debtor) could argue, at the recognition stage, that service was defective.¹⁴

3. Service Abroad in Israel Cases

Service *abroad* under Israeli procedure is, in some respects, even stricter than the procedure under the HSC. There is no requirement under the HSC for a plaintiff to obtain *leave of court* to serve a foreign defendant.¹⁵

The procedure is different in Israel: before serving a complaint upon a defendant located in the U.S., the Israeli plaintiff would have to file a motion for *leave of court* to serve abroad. Leave is liberally granted so long as the plaintiff shows that its claim fails within one of the cases enumerated in Rule 500. The Israeli plaintiff is generally required to translate the Hebrew complaint into English and to include both the original Hebrew as well as the translation in the service package.

In summary, although there are some differences in the *mechanics* of service of process in the two countries, in the author's experience, those differences are never a determining factor in forum selection in US-Israeli commerce.

B. Choice of Law

As noted above, this paper is not a survey of Israeli substantive law. Obviously, the decision as to a choice-of-law clause requires taking into account multiple considerations. Nonetheless, a few key issues that are relevant to international litigation should be stressed even in a general survey such as this:

- Israeli courts are more likely than their American counterparts to find the existence of a contract based on what many American business people would consider "mere" negotiations. Similarly, Israeli courts frequently stress the statutory duty upon all parties to *negotiate* in good faith – including at the *pre-contract* stage.

¹⁴ See ENCYCLOPEDIA OF INTERNATIONAL COMMERCIAL LITIGATION (Israel Chapter) (2007) §§ B11.18-11.20.

¹⁵ Thus, for example, when a New York plaintiff wants to sue an Israeli defendant in New York, his counsel serves the summons and complaints pursuant to the HSC (by having them sent to Israel's Directorate of Courts), and the American court has no substantive involvement with the issue of service until and unless the Israeli defendant files a motion to dismiss.

- Under Israel's "Standard Contracts Law" (1982), several types of provisions in "standard contracts" are presumed to be "unduly disadvantageous" and, therefore, subject to annulment or amendment by a court. Those types of provisions include:
 - a. One that denies or limits a customer's right to make certain pleas before judicial authorities or to take any other legal proceedings – except as part of a customary arbitration agreement;
 - b. One that designates an unreasonable place of jurisdiction or confers on the party that drafted the agreement the right to choose unilaterally the place of jurisdiction/arbitration; and
 - c. one that requires referral of a dispute to arbitration when the party that drafted the agreement has greater influence than the other party on the designation of the arbitrator(s) or the place of arbitration.

Although the Standard Contracts Law was enacted primarily to protect consumers, in recent years, numerous plaintiffs have attempted to rely upon that statute in international commercial disputes. The lower courts have rendered *in*consistent rulings with respect to the applicability of the Standard Contracts Law to forum selection clauses in international agreements.¹⁶

- Israeli courts are less likely than their American counterparts to enforce a "merger" or "entire agreement" clause. Under Israeli law, the general rule is that the court may take into account all of the circumstances surrounding the execution of the contract. The more a merger clause looks boilerplate, the less likely it is that an Israeli court will hold that the clause is enforceable pursuant to its terms.
- In Israel, Regional Labor Courts have jurisdiction to resolve disputes arising from or concerning the employer-employee relationships. Inelegantly drafted international *consultancy* and *agency* agreements have sometimes ended up being adjudicated in a Labor Court – simply because the draftsmen accidentally included in those agreements some of the indicia under Israeli law of an employer-employee relationship.

C. Arbitration

Both the United States and Israel are signatories to the Convention on the Recognition and Enforcement of Foreign Arbitral Awards (1958, known as the

¹⁶ For example, in the late 1990's, the Tel Aviv District Court ruled that a clause in a standard contract that called for the litigation of all disputes in France was enforceable notwithstanding the fact that the contract was a standard contract. *See* R.C.A. (T.A.) 200555/98 *Le Club Mediterranee S.A. v. Levonstein (Takdin, 1998)* (contract between Israeli vacationer and French resort hotel).

In 2004, that same district court held that a form contract, in English, entered into by several Israeli purchasers of real estate interests *in the United States*, was a standard contract and that, as a result, a forum selection clause calling for litigation in the United States would not be enforceable pursuant to its terms. *See* C.F. (Tel Aviv) 001919/02 *Lake Marion Golf Estates v. Farvor (Nevo 2004)*.

“New York Convention”). Therefore, the parties to an American-Israeli transaction can assume that arbitral awards from the other country will generally be enforceable at home.

Under Israel's Arbitration Law (1968), parties to a contract may agree to arbitrate virtually any dispute merely by including a provision that states "any dispute arising hereunder shall be resolved by arbitration under Israeli law." Such a "bare bones" arbitration clause will result in the following:

- The arbitration will be before a *sole* arbitrator;
- The arbitrator will not be bound by substantive law; and
- The arbitration probably will be conducted in Hebrew.

In 2008, Israel's Arbitration law was amended to allow parties to provide for an *appellate* level of arbitration. So far, that amendment has not resulted in a significant increase in the use of arbitration.

The best known arbitral institution in Israel is the Israeli Institute of Commercial Arbitration, which is sponsored by the Israeli Federation of Chambers of Commerce. Since 2007, the IICA has maintained a separate set of International Rules.¹⁷

From the perspective of a non-Israeli company, the most noticeable aspect of the International Rules is the general rule that, if the arbitration agreement is in English, the language of the arbitration will be English.¹⁸ As such, the IICA is believed to be the only national arbitral institution in a country in which English is *not* an official language to guaranty that English will be the language for conducting an arbitration, *provided that* the agreement containing the arbitration clause is in English.¹⁹

¹⁷ The International Rules are available at <http://www.borerut.com/foto-in/Rules%20-%20institute%20of%20arbitration.doc>.

¹⁸ See “Israel's New International Arbitration Rules,” 21 *International Law Practicum* 39 (NYSBA, Spring 2008).

¹⁹ Such a rule is a departure from the prevailing practice in Israel. The author has been involved in several Israeli arbitrations that were conducted predominantly in Hebrew, even though the arbitration agreement was in English and a significant number of witnesses were non-Israeli residents who did not speak any Hebrew.

Also, as noted above, under Israeli civil practice, a defendant that is sued in court by a foreign plaintiff has the right to request that the court require the plaintiff to deposit security to ensure that, if the court awards costs against the plaintiff, the defendant will have available, in Israel, a source of funds for collecting on such an award.

The practice of requiring a foreign plaintiff to deposit security has frequently been applied to arbitrations in Israel.

Rule 3.4 of the IICA's International Rules does away with such practice. It provides that, in considering whether to order a party to deposit security for the arbitration expenses, "the arbitrator(s) shall not take into consideration that [a particular] party is based or domiciled outside of Israel or that such party does not have assets in Israel." Such provision recognizes that a non-Israeli party to an international transaction is not likely to consent to arbitrate before an Israeli arbitral institution if it knows that, by so consenting, it could be financially disadvantaged simply because it is a foreign entity.

Finally, an arbitration agreement (or clause) is not worth the paper on which it is written if the courts in the home country(ies) of the contracting parties are unwilling to stay proceedings that might be brought in contravention of the arbitration clause. In this regard, the Israeli Supreme Court has, over the past few years, demonstrated a very pro-arbitration – in particular, pro-New York Convention – approach. In the leading case of *Hotels.com v. Zuz Tours*,²⁰ the Supreme Court held that, when the New York Convention requires a stay to be issued and the parties to be referred to arbitration, Israeli trial courts have virtually *no* discretion under the domestic Arbitration Law to refrain from issuing a stay.

²⁰ C.A. 4716/04 (2005).

Recommended Source Materials

1. International Finance Corporation provides a country by country analysis involving most almost every aspect of doing business. <http://www.doingbusiness.org/>
2. Transparency International rates the corruption level in approximately 178 countries. These countries are rated on a scale of 1 to 10 with 1 being the highest level of corruption.
<http://www.transparency.org/>;
http://cdn.theladders.net/static/pdf/search/TheLadders_search_help.pdf
3. Itim International: Cultural aspect of doing business <http://www.geert-hofstede.com/>
4. Stephen D. R. Taylor & Robert L. Gegios, *"The Ability to Bridge Cultural Differences: A Prerequisite for Good Counsel in International Transactions,"* COMPARATIVE LAW YEARBOOK OF INTERNATIONAL BUSINESS, Vol. 32, Kluwer Law International, 2010. ISBN: 978-1-4303-2526-0 pp. 659-714.
5. Robert L. Gegios & Stephen D. R. Taylor, *"Cross-Cultural Understanding: An Essential Skill in International Advocacy,"* INTERNATIONAL ARBITRATION AND MEDIATION—FROM THE PROFESSIONAL'S PERSPECTIVE, Yorkhill Law Publishing, 2007, ISBN 978-1-4303-2526-0 pp. 55-83.
6. Culture Smart Series: Culture Smart Provides essential information on attitudes, beliefs and behavior in different countries, ensuring that you arrive at your destination aware of basic manners, common courtesies, and sensitive issues. <http://www.globecorner.com/s/117.html>
7. Kiss, Bow or Shake Hands, Terri Morrison (Adam Media, 2006)