

LEGAL SERVICES MARKET OF HAINAN PROVINCE (How Great Is The Potential of Hainan's Legal Services Market?)

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Up until this April, Hainan's number of lawyers had surpassed 4,100, growing by 67% since last year and painting quite a burgeoning scene. However, in the past three decades, the development of Hainan's legal services sector has been largely overlooked, and its prospects deemed unfavorable. Before the island became a province in 1988, Hainan with its 19 municipalities and counties had only 22 law firms and fewer than 100 lawyers. [1] Since then, after three different phases of growth, the island's legal services market eventually achieved its prosperity today.

THE THREE PHASES OF DEVELOPMENT

The first phase kicked off in 1988, and ended around 2003 and 2004, largely corresponding to the rise and collapse of Hainan's real estate industry. After Deng Xiaoping's "Talks in the South" of 1992, Hainan Special Economic Zone boomed with investment as a renowned bridgehead of China's "Reform and Opening Up" policy. At Haikou, the provincial capital, the price of apartments more than doubled in less a year, and for some downtown assets jumped from RMB 1,000 to more than 10,000 per square meter. Such lucrative business attracted many speculators and developers alike, driving up the property sales of Hainan, a province with the smallest population, to the third place in China. It also made the island's economy highly dependent on real estate and greatly destabilized local finances. [2]

In late 1993, the government deployed various macroeconomic tools to cool down Hainan's real estate industry, essentially freezing the many unsold assets. As a result, the financial institutions that lent money to the now defunct developers suffered considerable losses, and many sued to reclaim their funds. Therefore the number of court cases skyrocketed, especially those in the fields of debts, finances and real estate. For example, Hainan's court system registered 78 financial cases, more than tripling the previous year's 20, and the number of real estate litigations jumped from 359 to 605. There was some delay in the rise of disputes over obligations, but the category still witnessed an increase from 760 to 1666 between 1994 and 1995. [3]

[GRAPH]

This wave of litigations quickly overwhelmed the pre-existing legal services providers, and immediately gave birth to a new generation of lawyers and law firms, including Fang Yuan (est. 1992) [4], WeiTe (est. 1993) [5], and Farvision (est. 1994) [6]. The first Hainan office of a major law firm, JunHe Haikou, also moved into its office on Bin Hai Avenue in 1992, right at the climax of Hainan's real estate boom. Throughout the 1990s, Hainan's legal services providers mostly did not have to worry about their business, as the number of professional full-time lawyers rose from 177 to about 530 between the end of 1990 and 2000 [8], marking this phase of early development.

However, as the bubble burst's impacts gradually subsided, Hainan's legal services industry plummeted into yet another period of lukewarm development. Although the average increase in provincial GDP amounted to above 10% during the 10th "Five Year Plan" (2000-2005), such progress was not seen in the legal profession. [9] For example, Ningxia and a population only three fourths of that in Hainan, and a GDP less than 80% of Hainan's, [10] but between 2005 and 2018 it could almost always boast of more lawyers and law firms than Hainan. [11]

[GRAPH]

This paradox might be attributed, to some degree, to the two provinces' economic composition. For instance, in 2011, Ningxia's primary industries (e.g. agriculture and fishery) accounted for merely 8.9% of

its overall added value, while the secondary and the tertiary accounted for 52.2% and 38.9% respectively. In comparison, Hainan's agriculture-based primary industries contributed as much as 26.2% to its total added value, while its industry-based secondary ones contributed only 28.4%. Strangely, Hainan's service industries accounted for 45.4% of the island's added value, significantly higher than Ningxia and almost on par with the more economically advanced regions such as Zhejiang. [12]

Such conditions brought two major problems to the local legal services market of Hainan. First, legal services demands in an agricultural economy not only are small in number, but also tend to be lacking in diversity, thus unable to support a modern legal profession. At the same time, all those technologies and social devices that can help modernize and corporatize agriculture (and stimulate its needs for legal services), such as digitization, mechanization, e-commerce and productive poverty reduction (*chanye fupin*), were still rare in Hainan back then. As a result, the massive primary industry of Hainan was unable to bring about a similar growth in the legal services, or with it a growth in the number of lawyers.

The second problem is the specific composition of the tertiary industry. Although similar in proportion, Zhejiang's service sector encompassed the more advanced and well-regulated industries of finances, securities and insurance, which indicated more IPOs, corporate investments and M&As, all of which are high in added value. On the contrary, Hainan's was mostly composed of small- to medium-sized businesses and tourism, especially the retail industry, which require little professional legal services. [14]

[GRAPH]

But into 2018, along with the decision to turn Hainan into what is called a whole-island Free Trade Zone, the province's legal profession entered into its third phase, one of rapid development. The FTZ policies, together with the Hainan Free Trade Port (FTP) directives proposed in 2020, effectively addressed the two aforementioned issues by bridging the island's three-level industries and modern legal demands while preserving its traditional economic advantages. Moreover, the policies clearly expressed the wish to build "high-quality legal services [to promote the] business environment", "to augment the lawyers' capability of providing foreign-related legal services", and to "put forward a professional, efficient and open-minded corps of lawyers." [15]

PROSPECTS OF LEGAL SERVICES WITHIN THE FTP

(Please see the appendix for more details)

And in order to turn those wishes into reality, Hainan FTP tapped into both the development and renewal of industries and the accumulation of talent simultaneously. Concerning the former, FTP drafted different blueprints for its various fields of interest. Among its eight major industries, [16] for example, efficient tropical agriculture would effectively combine Hainan's sizable agricultural sector with concepts such as finances and technology, opening it up for legal services opportunities. For example, the initiation of international trade of tropical agricultural futures will lead to greater demands of legal assistance for contractual disputes, while the "opening-up" of agricultural business will bring in foreign investment and new opportunities in such arenas as intellectual property.

Within the scope of its secondary industries, the FTP has a focus on the oil and gas, especially the formulation and refinement of their relevant supply and production chains. Since the 1990s, Hainan's industrialization has been following the dual principles of "no environmental pollution" and "no resource depletion", jointly working towards "a recycling and circular economy". [17] These strict standards raised the urgency and necessity of legality and compliance review, and set high entry barriers to the energy programs. Therefore, such policies collectively heightened professional demands for those lawyers that engage in these areas, but at the same time expanded their business scope beyond simple infrastructure construction and monopoly review. [18]

As for its service sector, the FTP champions the four features of digitization, “technicalization”, scaling-up and internationalization, largely overturning the dominance of real estate in Hainan’s tertiary industry [19] and tourism’s lack in diversity. [20] For example, high technology is now an industrial favorite, tasked with the introduction of leading global companies and the development of a digital creative industry. Their relevant services, including the transfer and trade of cultural IPs, [21] the protection of patents, the filing of corporate taxes, warranties and R&D investments [22] all have the potential of becoming the new hotbeds of legal demands.

Other than high tech, another highlight of FTP’s service sector is its multilayered financial system. On one hand Hainan seeks to augment its pre-existing institutions, such as the Hainan Property Rights Exchange (est. 2004) and the Hainan Equity Exchange (est. 2014). These two establishments have rather sophisticated norms and regulations, and there already have been lawyers in their review committees or as consultants. [23] As their scope of transaction continues to expand, and their influence on the rise, it is conceivable that more small- to medium-sized businesses would be listed, a process that would inevitably require the participation of more lawyers specializing in the capital market.

On the other hand, the FTP is also exploring new categories of financial transactions and products, especially a new carbon and energy market. February this year, China has just entered into effect its interim rules for carbon emissions trading management, [24] and the relevant components of a “green economy” are still relatively lacking. [25] Therefore, it is conceivable that as Hainan’s carbon market grows and matures, such products as green bonds, green credits and green capital would most likely rise to prominence, and create a yet untrodden path of legal services.

Another noteworthy characteristic of the FTP legal services market is its demand for interdisciplinary expertise. With Hainan’s highly developed fishery, agriculture and gas/oil exploration, as well as its burgeoning health care and high tech industries, the island’s legal services industry would certainly call for those professional who not only are well-versed in legal matters, but also are so in the other relevant fields. It is possible that this diversification of skills would soon become the norm of Hainan’s legal market, and the centerpiece of a law firm’s competitiveness.

And to appeal to such diverse talents, and to improve the modernity of Hainan’s law firms, the province passed in 2019 its *Lawyer’s Regulations of the Special Economic Zone*. The *Regulations* not only lowered the barriers of entry for limited liability partnerships by allowing other professionals to serve as partners in law firms, but also eased certain restrictions on the registry of new-founded law firms, making it easier for young lawyers and law school graduates to kick start their careers. [26] At Haikou, “excellent foreign-business lawyers” are listed among the other professional talents that can receive rewards in funds and policies, and those joint venture law firms that are capable of handling foreign-related cases are also qualified to receive rent exemptions. [27] Meanwhile at Sanya, another provincial economic hub, its lawyers are incentivized by a one-time cash reward of RMB 1 million, as long as they succeed in introducing, instructing or assisting “good quality firms” in their IPOs or relocation to Hainan. [28]

Finally, the blueprints of Hainan FTP also left plenty of space for alternative and specialized legal services. In 2020 alone, the island witnessed the sequential establishment of Hainan International Arbitration Court, its own International Commercial Mediation Center, and the FTP Intellectual Property Court (IPC), all heralds of a new provincial legal landscape. For example, during the first three months of its initiation, the Mediation Center mediated more than 20 cases with a total bid of more than RMB 3 million, and appointed 244 professional mediators. [29] In the field of intellectual property, the setup of an IPC was a direct response to the gradual increase in numbers of such cases since September 2019, and encouraged the IP lawyers to further hone their skills. [30]

THE IMBALANCE AND ITS OPPORTUNITIES

The impressive growth of Hainan’s FTZ and FTP brought renewed potential to lawyers on and beyond the island, while the uneven distribution of legal services providers within the province is likely to facilitate

the further “deepening” of their business. For example, so far more than half of Hainan’s law firms are located in Haikou and Sanya, two of the island’s largest cities. [31]

As for Danzhou, the third largest municipality (county) of Hainan, despite a GDP nearly half that of Sanya, it only has one fourth as many law firms as the latter. Chengmai, closely tailing Danzhou in economic scale, can boast of its 12 law offices, almost half that of Sanya, but when compared to the latter, the number of lawyers is no more than Sanya’s 20%, suggesting a very low degree of sophistication.

[GRAPH]

Mr. Xia Ruhai, partner of JunHe Haikou, opines on this observation, “After all, Haikou and Sanya are Hainan’s greatest cities by GDP, and the island is not a big one. It takes you no more than 3 to 5 hours to drive across it. As the result, many law firms can encompass the entire island simply by planting an office at either of the two cities. At the same time, the other firms are mostly concentrated at those municipalities around Haikou (such as Chengmai, Wenchang and Ding-an) or those with robust economies (such as Qionghai and Danzhou). This is because these places are where the economic parks are, and possess greater commercial potential. For example, the important Hainan Ecological Software Park is located at Chengmai, the International Aerospace City is at Wenchang, while Danzhou and Qionghai are the homes to Yangpu Economic Development Zone and Bo’ao-Lecheng International Medical Tourism Pioneer Zone, respectively. As for the hinterlands of Hainan, most of their legal demands are of a day-to-day nature, with little commercial or transactional affairs, thus diminishing their appeal to the so-called brand firms or national firms.”

However, such imbalance also spells great potential. Although lacking in the demand for conventionally commercial legal services, the Hainan hinterlands are actively pursuing the agricultural avenue, seeking to improve its scale, build up its name recognition, and increase its productive efficiency by making use of new information technologies, all three of which are likely to involve legal support. For instance, almost all these municipalities and counties have adopted a mode which encourages local cooperatives, leading enterprises, technical colleges and party offices to help modernize local agricultural practices and create recognizable native brands, while also experimenting with e-commerce and village tourism.

At Qiongzong county, by mid-2020, 25 village-level e-commerce stations had been established, and had sold produces worth more than RMB 10 million. [32] At Tunchang, with the establishment of a National Agricultural Park and 8 other countryside tourism spots, the industries of agricultural tourism experienced an impressive increase in volume. [33] Instead, Wuzhishan decided to exploit the local tropical climate by establishing a complete chain of tea production, ranging from botanical research to retail sales, even acquiring from the Ministry of Agriculture a locally certified brandname. [34] The county of Baisha took it one step further by devoting a production park specifically to rural e-commerce, tutoring the local farmers in aspects such as online shop management and advertisement to boost agricultural sales. It is obvious that such measures, on top of reducing local poverty, also require legal safeguards and guidance, giving birth to new niches of legal works.

At the same time, the public, or pro bono, legal services market of Hainan was also experiencing its own stage of prosperity. By the end of 2019, the province finally achieved full coverage of village (block)-level legal consultants, [36] and by the start of 2021, this tropical island proudly announced the completion of its “public legal services loop”, a network of law offices and legal services consultancies ranging from provincial to village levels. With this “loop”, Hainan received more than 87 thousand requests for legal assistance, and responded accordingly. [37] This puts Hainan at the forefront of China’s less populous provinces, indicating a rather optimistic market for basic legal services.

Moreover, the setup of multiple economic parks within the FTZ further raised the hinterlands’ demand for legal talents. Amongst the island’s 13 major economic parks, 7 are situated outside Haikou and Sanya, and their spillover effects are expected to “pull up” the legal services markets of these counties. [38] The *Regulations* also pronouncedly supports “the setup of law firms or their local branches in the less

developed regions, [39] and has achieved some effects. Between September 2019 and June 2020, 57 such offices were established in Hainan, including a branch office of P.H. Law Firm (Beijing) at Qionghai. [40] In September 2020, Jidi Law Firm (Sichuan) followed suit in setting up a local branch at Yangpu, [41] likely a sign that more national or out-of-province law firms would move into Hainan, diversifying its legal services provision landscape while also promoting intra-industry competition.

COMPETITION AND COOPERATION BETWEEN HAINAN AND NATIONAL FIRMS

This trend of law firm proliferation has already produced in Hainan's legal services market two rather profound changes: the business expansion of "national law firms", and the consequential competition between them and the island's native law firms.

On the one hand, in high-end, high-added-value legal matters, the more experienced national firms (including the famed "Red Circle") enjoyed certain first-mover advantages when compared to local firms. For example, the only two Hainan firms whose H shares are listed at The Stock Exchange of Hong Kong sought JunHe as their legal representatives, and retained its services for a considerable period of time after the IPO was completed. [42]

Mr. Zhang Ping, partner and board member of JunHe, also tells us, "With the gradual construction of Hainan FTP, more and more of the province's legal business will involve investment and corporate setups coming from China's other regions or even foreign countries. And these actors are more inclined to pick legal consultants they are more familiar with, namely those professional, brand-name national firms they have cooperated with. When we take into consideration that these firms also deal with cases with higher bids, it is natural to assume that they would continue to dominate the upper echelons of Hainan's legal services markets in the future to come."

On the other hand, such firms also have their local branches digging into the more conventional legal arenas like construction, real estate, or criminal litigation, thus competing with their local counterparts in the more day-to-day business sectors. [43] Some of them even began to replace the local firms in serving at legal consultants for county and municipal governments, and are planning to expand further down into the village-level consultancies. [44]

[GRAPH]

Some national firms are beginning to recruit from their local competitors to fill their own Hainan offices. [45] In the long term, the island will likely witness a wave of mergers between the larger, national law firms and their smaller local rivals. Such challenges might prompt the latter to quicken their pace in their internal developments, such as increasing their staff size, sharpening their skills and expertise in select legal business lines, etc.

For example, Mr. Wang Hangbing, director of Hainan's pioneering Changyu Law Firm, believes that "the introduction of national law firms has positively impacted out brand-building and management styles, and offered us a rare opportunity to improve ourselves, to achieve further expansion, professionalization and internationalization. Furthermore, in order to create a globally influential Hainan-based firm, we must pursue the path of integration, to render ourselves on par with our more national and more famous peers in every major legal sub-field."

Of course, other than potential competition, there also are prospects of cooperation between the two groups. One such example is found in the aforementioned Changyu Law Firm's joining the Elite Global Legal Alliance (EGLA) first started by DHH Law Firm. [46] Since 2018, DHH also began to strengthen its ties with the other leading law firms on the island, including WeiTe. [47] So far, the other legal alliances or law firm networks have not yet penetrated into the province, leaving a void to be filled, possibly by the local law firms that would one day equal, in size and expertise, their out-of-province counterparts.

[Appendix] Legal Demands of the Hainan Free Trade Port