

CROSS-STRAIT TRADE AND INVESTMENT AND THE ROLE OF HONG KONG

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Part I discusses the legal nature of the trade relations among the mainland, Taiwan and Hong Kong and their respective external trade relations as well as any possible effects of the handover of Hong Kong upon these relations. Part II focuses on the role of the Special Administrative Region of Hong Kong (HKSAR) in cross-strait and beyond-strait trade and investment in the post-handover era.

I. THE LEGAL NATURE OF CROSS-STRAIT TRADE AND INVESTMENT

In addressing the legal nature of cross-strait trade and investment and asking whether and to what extent the trade relations among the three major components of The Greater China -- the Chinese mainland, Taiwan, Hong Kong and Macau -- have been affected or are likely to be affected by the handover, one should ask the following questions from the point of view of both pre-handover and post-handover periods of time:

- * Are the trade relations within the so-called Greater China domestic, inter-regional, quasi-international, or international?
- * What are the guiding principles or legal rules governing cross-strait trade and investment from the perspectives of each region?
- * Are the three major parts of China governed or to be governed by the same set of international rules in the field of public and private international trade law?
- * How will the handover affect the prospects of WTO membership for the People's Republic of China and for Taiwan as a special tariffs territory?

A. Nature of Cross-strait Trade Relations

The legal nature of the trade relations among the mainland, Taiwan and Hong Kong is inevitably a question of politics. Prior to July 1, 1997, from the Chinese point of view, Hong Kong was considered part of the Chinese territory temporarily under *de facto* British rule -- China never recognized the validity of the Treaty of Nanking and other treaties that forced the Qing Government to cede Hong Kong Island and Kowloon and lease the New Territory to the British. Given the *de facto* British rule, transactions between Hong Kong and the mainland (and similarly between Hong Kong and Taiwan) before July 1, 1997 could be characterized as *de facto* quasi-international or *de facto* international in a qualified and technical

sense. Now that Hong Kong is officially a part of the mainland, is this type of trade relationship still quasi-international or technically international? Probably not. Once the British are no longer *de facto* in charge, with Hong Kong being part of China in a full sense, the trade relationship between Hong Kong itself and the rest of China (including Taiwan) has technically become domestic or intra-national. In the annex to a decision adopted February 23, 1997 by the Standing Committee of the NPC on the adoption of laws previously in force in Hong Kong under Article 160 of the Basic Law, it was made clear that:

In the case of any provision in which any reference is made to the People's Republic of China or China or similar names, terms or expressions, those names, terms or expressions shall be construed as a reference to the People's Republic of China with the inclusion of Taiwan, Hong Kong and Macau; and where any reference is made to the names, terms or expressions of the mainland, Taiwan, Hong Kong and Macau, whether separately or concurrently, those names, terms or expressions shall be construed as a reference to a component part of the People's Republic of China.¹

Nevertheless, we must bear in mind the concepts of "one country, two systems," "Hong Kong people governing Hong Kong" and the high degree of autonomy guaranteed by the 1982 Constitution of China, the 1984 China-U.K. Joint Declaration and the Basic Law of the HKSAR.² Under the Basic Law, Hong Kong enjoys executive, legislative and independent judicial power,³ retains its free port status,⁴ remains a separate customs territory, and exercises exclusive control over its financial, monetary, trade, industrial and commercial policies, revenues, currency, customs, shipping and civil aviation.⁵ More importantly, the legal system in Hong Kong remains basically unchanged, except for those rules of law in force prior to July 1, 1997 that contravene the Basic Law and are subject to any amendment by the HKSAR legislature.⁶

¹Decision of the Standing Committee of the Nat'l. People's Congress on Treatment of the Laws Previously in Force in Hong Kong, in accordance with Basic Law of the Hong Kong Special Administrative Region of the PRC, Feb. 23, 1997, art. 160 Annex 3, ¶ 8.

²See XIANFA, art. 31 (1982); Joint Declaration of the Gov't of the United Kingdom of Great Britain, Northern Ireland and the Gov't of the People's Republic of China on the Question of Hong Kong, Dec. 19, 1984, ¶ 3 [hereinafter Joint Declaration]; Basic Law of the Hong Kong Special Administrative Region of the P.R.C., April 4, 1990, art. 2 [hereinafter Basic Law].

³See Basic Law, *supra* note 2, at art. 2.

⁴See Basic Law, *supra* note 2, at art. 114.

⁵See Basic Law, *supra* note 2, at arts. 106, 103-13, 115-19, 124-35.

⁶See Joint Declaration, *supra* note 2, ¶ 3, Annex I, § II. See also Basic Law, *supra* note 2, at art. 160.

These facts mean that the trade relationship between Hong Kong and the rest of China is inevitably domestic in a broader sense but differs from purely domestic transactions in a narrower sense. We can properly classify transactions between Hong Kong and the rest of China as inter-regional domestic or cross-system domestic trade relations.

In the case of Taiwan, it is the official policy of both Beijing and Taipei that there is only one China and that Taiwan is part of China. Unlike Hong Kong, which was ruled by the British for over 150 years, Taiwan has been governed by the Chinese people themselves after its return to China from Japan in 1945. Since no foreign country is involved, the trade relationship between the mainland and Taiwan is not international or quasi-international even if Taiwan is *de facto* administered by a separate local Chinese government under a different body of laws. Rather, the phrase inter-regional domestic or cross-system domestic may be used to indicate the nature of such relationship. Nothing has been affected by the change of sovereignty over Hong Kong in this regard.

As for the trade relationship between Taiwan and Hong Kong, a similar change has taken place with the return of Hong Kong to the mainland. Prior to July 1, 1997, such relationship was quasi-international or technically international; after the handover, it has become inter-regional domestic or cross-system domestic even if such transactions may in form appear to be pretty much the same.

B. Laws Regulating Cross-strait Trade and Investment

Given the nature of the political relations between the mainland and Taiwan, questions of law governing the regulation of cross-strait trade and investment, all three sides' resort to choice of law and conflict of law rules in proper cases are inevitable. Subject to mandatory provisions in either of these three legal systems which may not be opted out of, the methods of choice of law and conflict of laws rules which are conventionally used in transnational dealings also apply to cross-strait transactions in an inter-regional domestic context. In fact, the mechanisms of choice of law and conflict of laws rules are not unique to international transactions. They are useful in domestic transactions within certain types of states such as federations and confederations. Therefore, using the techniques of choice of law and conflict of laws rules to solve the issue of governing law does not affect the inter-regional domestic nature of cross-strait trade and investment activities.

It must also be noted that the so-called Greater China is neither a federal state nor a confederation. The concept of one country, two systems or one country, multiple systems is unprecedented and represents a new type of nation-state of its own. Unlike a federation in which there is a

considerable degree of federal regulation of trade between its constituent members, China lacks a centralized system for the regulation of cross-strait trade and investment that can be applied in the Chinese mainland, Taiwan and Hong Kong at the same time. After the handover, only a small number of specifically designated statutes (such as the Nationality Law) enacted by the National People's Congress (NPC) or its Standing Committee are in force in Hong Kong. None of the NPC's legislation is operable in Taiwan and *vice versa*. Within the framework of one country, each maintains its own legal system. In practice, to engage in trade and investment in the mainland, Taiwanese and Hong Kong businessmen have to observe the laws of the P.R.C. Similarly, to do business in Hong Kong or Taiwan, mainland Chinese companies must comply with the local laws of Hong Kong or Taiwan. There does not exist a single and unified body of laws that governs trade and investment across the Taiwan strait.

There is another issue that deserves mentioning. When one body of laws of one system applies either by mandatory provisions, by choice of law, or through the operation of inter-regional conflict of law rules, do all the laws of that system apply or only certain laws? In other words, for the purpose of the applicable law, are the parties to cross-strait transactions considered domestic or foreign? We all know that China maintains two economic contract laws, the 1982 Economic Contracts Law as amended in 1993 which applies to transactions between Chinese parties only (including joint ventures and wholly foreign owned companies in China), and the 1985 Foreign Economic Contracts Law, which applies to transactions between a Chinese party and a foreign party.

The Supreme People's Court of China interpreted in 1987 that the Foreign Economic Contracts Law would apply to contracts involving a party from Hong Kong or Macau.⁷ While the Court did not mention contracts involving parties from Taiwan, in practice the FECL has been applied to Taiwanese traders and investors by analogy. The 1994 Foreign Trade Law is the basic statute for the regulation of China's foreign trade from public law perspectives, but it specifically provides that its application does not extend to China's separate tariff zones (*dandu guanshui qu*).⁸ The central government of China agreed to allow Hong Kong to maintain a separate tariff zone after the handover and considers Taiwan such a zone in a similar manner. Treating Hong Kong and Taiwan as separate customs territories (*i.e.*, separate tariff zones) makes it possible, without affecting the one

⁷See Opinion on the Foreign Economic Contracts Law, item 1(2) (Supreme People's Court, Oct. 19, 1987).

⁸See Decision of the Standing Committee of the Nat'l. People's Congress on Foreign Trade Law of the P.R.C., May 12, 1994, *translated* in CCH CHINA LAWS FOR FOREIGN BUSINESS, ¶ 19-586, art. 43.

country policy, for Hong Kong to continue its membership in the GATT and the WTO and for both the Chinese mainland and Taiwan to become parties to the Agreement Establishing the World Trade Organization and related agreements within the WTO framework.

In the field of investment, Chinese statutes and regulations on foreign investment have been similarly applied by analogy to enterprises established in the mainland and funded in part or in whole by investors from Hong Kong and Taiwan. For example, the 1990 Detailed Rules for the Implementation of the Law on Sole Foreign Investment Enterprises makes it clear that enterprises established or that will be established in China that are wholly owned by companies or individuals from the regions of Hong Kong, Macau and Taiwan must be treated with reference to those Rules.⁹ The 1995 Detailed Rules for the Implementation of the 1988 Sino-Foreign Cooperative Enterprises Law similarly provides that cooperative enterprises (*i.e.*, contractual joint ventures) established or to be established "by companies, enterprises and other economic entities or individuals from the regions of Hong Kong, Macau and Taiwan ... shall be handled *with reference to* [*can zhao*] these Detailed Implementing Rules" (emphasis added).¹⁰ There are other promulgations that treat Hong Kong, Macau and Taiwan differently than other administrative units of China.¹¹ Besides, by special legislation or promulgation, China has accorded preferential treatment to investors from Taiwan under specifically promulgated regulations under which Taiwanese investors, unlike foreign investors who are limited to industries specifically targeted for development, can invest their capital in any category of projects in the mainland.¹² A similar promulgation for attracting Hong Kong and Macau-sourced capital was

⁹See Detailed Rules for the Implementation of the Law on Sole Foreign Investment Enterprises, Dec. 12, 1990, *translated in* CCH CHINA LAWS FOR FOREIGN BUSINESS, ¶ 13-507, art. 85. See also Law of the People's Republic of China on Sole Foreign Investment Enterprises, Apr. 12, 1996, *translated in* CCH CHINA LAWS FOR FOREIGN BUSINESS, ¶ 13-506 (popularly known as the 1986 "Foreign Investment Enterprise Law").

¹⁰See Detailed Rules for the Implementation of the Sino-Foreign Cooperative Enterprises Law, Sept. 4, 1995, *translated in* CCH CHINA LAWS FOR FOREIGN BUSINESS, ¶ 6-105, art. 57. The Sino-Foreign Cooperative Enterprises Law itself was enacted in 1988. See Law of the People's Republic of China on Sino-Foreign Cooperative Enterprises, Apr. 13, 1988, *translated in* CCH CHINA LAWS FOR FOREIGN BUSINESS, ¶ 6-100.

¹¹See Measures for the Administration of Asset Assessment of Foreign Investment, Mar. 18, 1994, *translated in* CCH CHINA LAWS FOR FOREIGN BUSINESS, ¶ 19-590, art. 2 (stating that the measures apply to foreign investors as well as investors from the regions of Hong Kong, Macau and Taiwan).

¹²See Guanyu Guli Taiwan Tongbao Touzi de Jueding [Provisions Concerning the Encouragement of Investments by Compatriots from Taiwan], July 3, 1988, *translated in* LAWS AND REGULATIONS OF THE PEOPLE'S REPUBLIC OF CHINA § 4-16-2-III-12 [hereinafter LAWS AND REGULATIONS].

issued two years later.¹³ A more recent development in this respect was the enactment in 1994 of a statute for the protection of investments by Taiwanese businessmen in the mainland.¹⁴

China's special treatment of Hong Kong and Taiwan reflects a pragmatic approach. On the one hand, drafters of various Chinese statutes and regulations have been careful to distinguish the regions of Hong Kong and Taiwan from foreign countries as well as to distinguish Taiwanese and Hong Kong traders and investors from foreign traders and investors. On the other hand, China also recognizes the technical difficulty of treating Hong Kong and Taiwan in the same category as its other domestic constituents. To promote cross-strait trade and attract Hong Kong and Taiwanese investors, China is realistic enough to have treated Hong Kong and Taiwan as being somewhat external by handling trade and investment relations with Taiwan and Hong Kong with reference to appropriate foreign-related statutes and regulations, by applying certain specially legislated enactments to traders and investors from these regions, and by avoiding the application to Hong Kong and Taiwan laws concerning the regulation of China's foreign trade. Other laws which are for the sole purpose of regulating domestic transactions are of much less relevance to the cross-regional trade and investment relations with Taiwan and Hong Kong.

C. International Agreements Affecting Cross-strait Trade

The next issue is whether the three parts of China are governed by the same set of international rules in the field of international trade law. This section will focus on the impact of private law aspects of international trade law. Consider Hong Kong *vis-a-vis* the mainland. The Basic Law is designed in part to solve the complex issue of partial state succession with respect to treaties but the solution turns out to be less than satisfactory. Under the Basic Law, with regard to those treaties and agreements which are in force in the Chinese mainland but were not in force in Hong Kong prior to the handover, it is for the Central People's Government to decide whether to apply them to the Hong Kong SAR in accordance with the circumstances and needs of the Region, and after seeking the views of the government of the Region.¹⁵

This provision should have been qualified because some treaties and

¹³See Guanyu Guli Huaqiao he Xianggang Aomen Tongbao Touzi de Guiding [Provisions Concerning the Encouragement of Investments by Overseas Chinese and Compatriots from Hong Kong and Macau], August 19, 1990, translated in LAWS AND REGULATIONS, *supra* note 12, at § 4-16-2-III-15.

¹⁴See Zhonghua Renmin Gongheguo Taiwan Tongbao Touzi Baohu Fa [Law of the People's Republic of China on the Protection of Investments by Compatriots from Taiwan], Mar. 5, 1994, translated in LAWS AND REGULATIONS, *supra* note 12, at § 4-16-2-I.4.

¹⁵See Basic Law, *supra* note 2, at art. 153, ¶ 1.

agreements by their nature or express provisions apply to the whole territory of a signatory state, unless that state declares at the time of ratification or afterwards to exclude certain part or parts of its territory from the scope of application. For example, the 1966 Convention on the Settlement of Investment Disputes Between States and Nationals of Other States¹⁶ and the 1924 International Convention for the Uniform of Certain Rules of Law Relating to Bills of Lading¹⁷ both contain such a provision. For these types of treaties or agreements, their automatic extension of application to a newly recovered territory does not depend upon a decision to that effect by the central government of the state concerned.

Treaties and agreements which were in force in Hong Kong and to which China is also a party present no difficulty in their continued application in Hong Kong after the handover. As to those which were in force in Hong Kong but to which China is not a party, the Basic Law provides that they may continue to be implemented in the HKSAR.¹⁸ A similar problem arises where an agreement to which the U.K. is a party was applied in Hong Kong not because Hong Kong was a separate contracting party in its own name but because Hong Kong was considered a colonial territory of the U.K., especially when the agreement itself is only addressed to states. Before China accedes to such an agreement, it would be technically difficult, although not impossible, to have the other contracting states agree to amend the agreement so as to allow a region or an administrative unit of a state to become or remain a party.

In the private law area, international transactions are largely subject to the applicable municipal law (including contract law). However, where private municipal laws affecting international trade have been harmonized into uniform rules, such matters enter the domain of international law. The 1980 United Nations Convention on Contracts for the International Sale of Goods (CISG), which entered into force in 1988, represents a proper example of international efforts towards the unification of private municipal laws. China is one of the 11 original contracting parties to the CISG. Prior to the handover of Hong Kong, the U.K. did not accede to the Convention and is still not a party to it. This, however, does not have a bearing upon Hong Kong even if the U.K. were a contracting state to the CISG. Assuming the U.K. was a party-state and China was not, since the CISG is not of a

¹⁶See Convention on the Settlement of Investment Disputes Between States and Nationals of Other States, Oct. 14, 1966, 17 U.S.T. 1270 (providing that the Convention applies to the whole territory of a signatory State unless a particular part of its territory is specifically excluded by the signatory State in question).

¹⁷See International Convention for the Unification of Certain Rules of Law Relating to Bills of Lading, Aug. 25, 1924, 120 L.N.T.S. 155 (allowing a signatory State to declare to exclude colonies, protected states or areas or the like from the scope of application of the Convention, thereby implying that no such declaration is permitted with regard to any part of the territory *per se* of a signatory State).

¹⁸See Basic Law, *supra* note 2, art. 153, at ¶ 2.

territorial character, it would not be automatically applied to Hong Kong after the transfer of sovereignty takes place. Nor can Hong Kong accede to the CISG in its own name because, unlike some international economic institutions and trade agreements whose membership is flexible enough to accept non-state administrative units, the CISG is open only to states.

As China is already a party-state to the Convention, the Convention may be said to have automatically become operative in Hong Kong since the handover unless (1) the Convention itself would provide against such automatic extension of application, (2) the Convention is not compatible with the Basic Law or otherwise unsuitable to Hong Kong, or (3) China declares to the contrary. None of these is applicable, so the CISG should be considered now in force both in the mainland and Hong Kong as a result of China's resumption of sovereignty over Hong Kong (or, technically speaking, its succession to Hong Kong). Similarly, there are other private international agreements ratified or acceded to by China which affect China's foreign trade transactions and which may be applied in Hong Kong by virtue of the nature or provisions of such agreements as well as agreements which were and continue to be in force in Hong Kong but not in the rest of China.¹⁹

The case of Taiwan is more complicated than that of the HKSAR. On one hand, the international community at large recognizes the Government of the People's Republic of China as the sole legitimate government of China, and the Chinese position that Taiwan is part of China. This makes it impossible for Taiwan to participate in international organizations and conferences which are open only to states and to become a contracting party to international agreements, especially multilateral agreements, entered into between or among states only. The government of the P.R.C. is generally regarded and recognized as the sole legitimate government with the authority to represent the whole China in these types of international organizations, conferences and agreements. On the other hand, unlike the Hong Kong SAR which, save for the policy of "Hong Kong people governing Hong Kong," is now under the actual control and administration of the central government in Beijing, Taiwan is under the *de facto* administration of the local Taiwanese authorities which do not report to the central government. In a sense, if Beijing does not legislate for Taipei, it is similarly difficult for the central Chinese government to adopt international agreements and extend their application to Taiwan.

How, then, can Taiwan, the world's 14th largest trading partner, take

¹⁹In June 1997, Ambassador Qin Huasun, China's permanent representative to the United Nations, submitted to the UN Secretariat a list of treaties and agreements to be applied in Hong Kong after the handover. See *China Notifies UN on Treaties Applying to HK*, Xinhua Eng. Newswire, June 20, 1997, available in WESTLAW, File No. 1997 WL 11182736.

advantage of international trade law conventions and agreements, and how can the rest of the business world expect Taiwanese companies and businessmen to conduct their external business under uniform trade rules or standards? It is unlikely for Taiwan to separately accede and become a party to an international agreement that is concluded between states only. This is particularly so where the government of the P.R.C. represents China as a party to such an agreement. Can it be said that treaties or agreements to which the P.R.C. is a contracting state and which lay down rules of conduct affecting international trade are applicable to Taiwan as well because it is part of China? Most treaties and agreements of this nature are applicable to the entire territory of a contracting state unless they provide otherwise or unless the contracting state in question declares that it excludes certain areas within its territory from their application. We can call this approach the "automatic application-unless" or "auto-unless approach." However, this approach would be difficult to apply in the case of Taiwan because of the sustained political and military hostility between the two sides of the strait. If Taiwan itself wishes to be bound by a given treaty or agreement joined by the P.R.C., the automatic application-unless approach presents no special problem. Where the local Taiwanese authorities are not accepted or are not prepared to be bound by such a treaty, however, the auto-unless approach may not have any practical meaning. Legal scholars and politicians will have to find a way to overcome this difficulty without undermining China's one China or one country policy. Some international trade law treaties such as the CISG are so important and provide so much convenience, clarity and uniformity that they should not be allowed to be indefinitely ignored by or unavailable to Taiwanese businesses simply because Taiwan may not accede to it as a party in its own capacity. It will be up to the two sides of the Taiwan strait to figure out a solution. In the case of the CISG itself, for instance, I tend to favour the auto-unless approach so as to allow Taiwanese exporters and importers to benefit from its convenient and uniform provisions on international sales. If a Taiwanese seller or buyer does not like any part of the CISG which would have otherwise governed the transaction, he or she (or it) may persuade the other prospective party to opt out of the CISG or to derogate from or vary the effect of any of its provisions anyway.²⁰

What about transactions between or among parties from the mainland, Taiwan and Hong Kong? If the CISG, *e.g.*, is in force in the Chinese mainland and Hong Kong, there is no question that a contract between a Hong Kong company and a party from another contracting state such as the U.S. would be governed by the CISG. Then does the CISG

²⁰See U.N. CONFERENCE ON CONTRACTS FOR THE INT'L SALE OF GOODS, 1981, at 178, U.N. Doc. A/Conf./97/19, U.N. Sales No. E.81.IV.3 (1981).

govern a contract between, *e.g.*, a mainland seller and a Hong Kong buyer? There is no definite answer. Clarification is needed by the relevant authorities. It is likely that the CISG may be applied by analogy (or with reference thereto) in such circumstances. The Convention in fact to a large extent reflects international trade practices or usages which may have already been observed in the regions of Taiwan and Hong Kong.

It is appropriate to say that the Chinese mainland and Hong Kong are subject to some common international agreements that affect not only China's (including Hong Kong's) trade with other countries and regions, but also to some degree trade and investment transactions between the mainland and Hong Kong in the sense that they may be applied to the mainland-Hong Kong trade relations, domestic though, by analogy (or with reference thereto). There are also international trade agreements which are in force in the mainland solely but not in Hong Kong and *vice versa*. These latter types of agreements have little, if any, bearing upon transactions between the mainland and Hong Kong, not even by analogy. In the case of Taiwan, China may similarly apply by analogy appropriate international trade law conventions and agreements to the trade and investment links between the mainland and Taiwan. Such international trade law rules to which China adheres may also be extended to cover the entire province of Taiwan for regulating trade relations between Taiwanese companies and foreign parties, unless such application is expressly excluded or the treaty in question does not apply to Taiwan by reason of its provisions. My understanding is that it is China's stated policy that intra-China trade relations among the mainland, Taiwan, Hong Kong and Macau will continue to be handled with reference to relevant international conventions and agreements relating to international trade and economic law. Nevertheless, this policy needs to be enacted into hard law and codified into a systematic legal framework.

D. GATT Rules and the Issue of WTO Membership

In the public law area of international trade regulation, while most instruments are likewise between states, there are some bilateral and multilateral trade agreements which are flexible enough to be open to separate customs territories and similar non-state territorial units within a state. For example, the GATT and the WTO agreements are between contracting governments or contracting parties, not between contracting states.

There can be local governments exercising jurisdiction over designated independent customs zones within a country, but there can not be a local state. Hong Kong became an initial member of the GATT under British representation when the GATT agreement provisionally went into effect in 1947. Under Hong Kong's free trade policy, there has virtually been

no barrier to trade either in tariff (duties on imports) or non-tariff form (such as import quotas and government subsidies). With its trading practice being compatible with the GATT principles, Hong Kong was generally perceived to be a model GATT member.²¹ It is worth recalling that the 1984 Sino-British Joint Declaration provided, *inter alia*, for Hong Kong's continuing participation in international trade and other relevant organizations.²² This provision, together with the fact that the GATT and related agreements are open to non-state territorial units such as separate customs zones, made it possible, with the U.K.'s sponsorship and China's support, for Hong Kong to become a full contracting party in its own right to the GATT in 1986.²³ That development enhanced Hong Kong's standing in the world trading system. Article 116 of the Basic Law more specifically declares the HKSAR to be a separate customs territory which may participate in the name of "Hong Kong, China" in relevant international organizations and international trade agreements, including the GATT and arrangements regarding international trade in textiles.²⁴ This clearer provision of the Basic Law has enabled the HKSAR to continue its membership as a separate customs zone of China since the handover even if China itself (*i.e.*, the rest of China) remains out of the world trading system as of today.

What are the prospects of WTO membership for the People's Republic of China and for Taiwan as a special tariffs territory? China is an original contracting party to the 1947 GATT Agreement and was represented by the then Nationalist government. In 1950, the Nationalist government, which had moved to Taiwan after their defeat in 1949, decided to withdraw in the name of China from the GATT. The validity of that withdrawal is questionable because the defeated Nationalists could no longer act (or withdraw) on behalf of China. Only the legitimate government of China, namely the Government of the People's Republic of China, which should have been allowed to replace the Nationalists in the GATT, could have exercised the right to withdraw if necessary. This is exactly why China maintained from the mid 1980s to 1990s that the issue of its GATT membership is a question of resumption rather than that of accession.²⁵

After preparatory studies and considerations in the early 1980s, China obtained observer status in the GATT in 1984 and, in July 1986,

²¹See PENELOPE HARTLAND-THURNBERG, *CHINA, HONG KONG, TAIWAN AND THE WORLD TRADING SYSTEM* 101 (1990).

²²See Joint Declaration, *supra* note 2, at ¶ 3(10).

²³For a brief account of Hong Kong's relations with the GATT, see HARTLAND-THURNBERG, *supra* note 21, at 101-2.

²⁴See Basic Law, *supra* note 2, art. 116, at ¶ 1, 2.

²⁵See Ming Li, *China Moves Closer to GATT*, BEIJING REV., June 29-July 5, 1992, at 13. But see Qin Ya, *China and GATT: Accession Instead of Redemption*, 27 J. WORLD TRADE 77 (1993).

submitted its formal application for the resumption of its status as an original contracting party to the GATT. The lengthy negotiations on China's membership have lasted more than 12 years and, despite China's good-faith efforts to reorient its economy and foreign trade system in order to integrate its own into the world economy, there remain as of today differences to be resolved between China on the one hand and some members of the WTO on the other. Bilateral negotiations with WTO members and multilateral negotiations with the WTO on China's membership are still dragging on.

One of the major controversies is the issue of whether to admit China as a developing country. From the point of view of developed countries, given China's position in the world trading system, the volume of China's foreign trade, its gross national output and its rate of economic growth in recent years, China should be subjected to the same obligations as members which are developed countries or regions. However, figures in trade volume and the like do not reveal the whole picture of China's reality. When the GNP is shared by the entire population, it becomes so insignificant that economists will not find it difficult to place China among the least developed countries. China's economic development has been remarkably unbalanced from place to place, from urban areas to rural areas and between various groups of people. A considerable portion of the population remains under the poverty line, and another significant percentage is between the poverty line and the so-called middle class. While China is not necessarily a least developing country any more, it certainly remains a typical developing country. China has legitimate reasons to consider itself as such and accordingly demands receiving corresponding benefits available to developing countries in the WTO. On the other hand, the benefits to developing country members are neither very great in terms of substance nor perpetual in terms of time. The mechanism of graduation and phasing out as well as time-limit provisions would significantly reduce the level of actual benefits that China could possibly claim as a developing country. Nevertheless, once the negotiators of major trading powers within the WTO agree to treat China as a developing country for the time being, other issues would be easier to resolve and some of them may not be issues at all.

China has significantly lowered its tariff rates in recent years. As of today, the average tariff level has dropped to 17% in comparison with the pre-1995 level of 40% and the 1995 level of 35%, reflecting a reduction rate of more than 60%. China has also committed itself to reduce its tariff level to 5% or the average level of developing countries in 2000.²⁶ It has also

²⁶See *Commentary Urges USA to Stop Playing the MFN Card* (BBC World television broadcast, Oct. 30, 1997); *Minister Urges EU to Unblock China's Trade Status* (BBC World television broadcast, Nov. 1, 1997).

shown good-faith efforts and plans to reduce and eliminate quantitative trade restrictions as well and liberalize trade in services. A recent indication that China may be ready to cut some of its highest tariffs (such as those on auto imports) would further reduce obstacles to China's entry into the WTO.²⁷ The recent summit meeting between President Jiang Zemin in Washington and the more recent visit to Japan by Premier Li Peng show that progress has been made and is still being made towards solving China's WTO membership issue.

Recently, China is reported to be considering setting up an independent body on the mainland to deal with trade and business disputes.²⁸ It is also said to be considering gradual liberalization of service industries in addition to its reported plans to cut tariffs.²⁹ These plans, if true and carried into practice, would be welcomed by the counterparts of China's trade negotiators and therefore would move China closer to entering into the WTO, which requires all members to have a judicial review system with an appeal body to which foreign exporters or importers have recourse for resolving trade disputes.

There is a consensus among WTO members that it is important for China to integrate its economy into that of the world and that the WTO cannot be a truly worldwide trade organization without China's representation. The U.S. and the EU have persistently so stated. It is now mainly for them to demonstrate their sincerity. The U.S., the EU and others concerned should not demand of China a level which China is neither willing nor able to reach at the present time. Instead, they should be realistic by allowing a reasonable scheme for post-entry adjustments.

As for the region of Taiwan, its trade since 1980 has been regulated mainly by bilateral trade agreements with its trading partners. The terms of such agreements are generally reciprocal and favourable. In late 1987, Taiwan indicated its plan to rejoin the GATT. GATT members have been cautious not to consider Taiwan's request for admission unless the mainland raises no objection. In seeking a seat in the flexible WTO, the Taiwanese authorities have undertaken efforts to liberalize Taiwan's trade and made adjustments in some trade practices and procedures. In comparison with the mainland, Taiwan's current trade practices are closer to the requirements of GATT rules.³⁰ It is the mainland's position that as a separate customs

²⁷For example, China agreed to reduce tariffs on auto imports from the current level of 80% to 50%. Japan has accepted this offer. See F.J. Khergamvala, *Li's Japan Trip Will Focus on Business Alone*, THE HINDU, Nov. 10, 1997, at 16.

²⁸See Sheel Kohli, *Beijing Seen Giving Way In WTO Talks*, SOUTH CHINA MORNING POST, May 22, 1997, at 12.

²⁹See Robert S. Greeberger, *China Tells U.S. It Will Cut Tariff to 10%*, WALL ST. J., Oct. 31, 1997, at A3.

³⁰See HARTLAND-THURNBERG, *supra* note 21, at 123-28.

territory, Taiwan can join the WTO once the membership issue for China *per se* is solved.

One might wonder, since China agreed to allow Hong Kong to become a full GATT member prior to and autonomous from China's own membership, why it cannot allow Taiwan to acquire a similar status in the WTO before China itself is admitted. We need to realize that the case of Taiwan is different from that of Hong Kong. The differences are mainly reflected in two aspects. First, Hong Kong was already a member in the GATT although it was represented by the U.K., while Taiwan, like the mainland, has been isolated from GATT/WTO for nearly five decades. More importantly, supporting Hong Kong to become a full member in the GATT and allowing it to continue that membership in the WTO does not create any impression of "Two Chinas" or "One China, one Hong Kong," for there is no movement in Hong Kong towards independence, whereas in Taiwan there is a long-established movement for independence. In fact, the Taiwanese authorities have been suspected of attempting at creating "Two Chinas" or "One China, One Taiwan" by actively pursuing flexible diplomacy. In other words, Taiwan is so sensitive to the mainland that China will not tolerate Taiwan's entry into the WTO before its own.

It is hard to predict with precision when the issue of China's and Taiwan's WTO membership may be resolved. There has been so much noise in Washington and elsewhere concerning China's admittance into the WTO that there may be no reason to continue negotiations. Nevertheless, China's continuing economic and trade reforms and its continuing efforts towards trade liberalization will certainly have favourable impacts upon the negotiating process. Hong Kong's return to Chinese sovereignty and its continuing economic success under the scheme of "One Country, Two Systems" and "Hong Kong people governing Hong Kong," will also facilitate China's move towards a fuller market economy and its entry into the WTO. China's bid for WTO membership will succeed only when the WTO is ready to admit Taiwan as a separate customs territory of China. Once all parts of China are covered by the same set of GATT rules, cross-strait trade and investment will undergo significant changes.

II. HONG KONG'S ROLE IN CROSS-STRAIT TRADE AND INVESTMENT

In assessing the role of Hong Kong in cross-strait trade and investment, we must ask the following:

- * Has there been or will there be any change in the economic status of Hong Kong and its free trade policy as a result of the handover?
- * What role has Hong Kong been playing in cross-strait trade and investment?
- * Does the handover itself has any positive or negative impact upon

that role of Hong Kong in cross-strait trade and investment?

* Will cross-strait trade and investment and Hong Kong's role in such activities undergo any change along with the desirable but not guaranteed improvements in the relationship between Taiwan and the mainland?

A. Hong Kong after the Handover

Hong Kong is one of the world's busiest transport centers, the seventh or eighth largest trading entity and the third largest financial center in the world. Hong Kong's role in cross-strait trade and investment in the post-handover era depends primarily on whether Hong Kong can maintain its prosperity, economic autonomy and ways of life and business under the concepts of One Country, Two Systems and Hong Kong people governing Hong Kong. We all witnessed the peaceful and smooth handover of Hong Kong by the British to China on July 1, 1997. While the change of sovereignty over Hong Kong has been overwhelmingly welcome, especially among the Chinese community at large and the third world countries, negative reflections did and do exist. For example, there were pessimists who predicted that the economy as well as the society in Hong Kong would begin to collapse and its prosperity begin to disappear after the change of sovereignty on July 1, 1997. Moreover, some believed, the handover would have negative impacts upon trade across the Taiwan strait to, from, and via Hong Kong.³¹

More than two years have passed and this hasn't happened. Despite the Asian financial crisis and its negative impacts, business in and around HKSAR (or SAR) has been normal as usual. Investors and traders have not in any significant sense withdrawn from the area. Rather, there have been back-flows of both capital and people from abroad before and after the handover. The people in Hong Kong, generally speaking, seem to have more confidence than prior to the handover. Moreover, there are suggestions that, while maintaining their own way of life, Hong Kongers should further be integrated into the Chinese family, economically and otherwise. For

³¹See *The Death of Hong Kong*, FORTUNE, June 1995, at 118 (predicting that when the transition takes place in 1997, "[i]t's over" and that "it seems destined to become a global backwater"). See generally LIU GANGPING, JIEFANG XIANGGANG: 1997 DA YUYAN [LIBERATING HONG KONG: PREDICTIONS FOR 1997] (1995) (predicting throughout that revolts, such as the so-called "February the 28th Incident" which took place as a result of the Kuomintang's oppressive policy towards local residents in Taiwan, would take place in Hong Kong after China resumes sovereignty in 1997); LU HAI'AN, XIANGGANG YOU JIU MA? [IS THERE ANY HOPE FOR HONG KONG?] (1984). The June 1995 Fortune Magazine article on *The Death of Hong Kong* has been to variant degrees criticized. See, e.g., Chris Yeung & Rodger Lee, "I see the rules as a stepping stone on the road to universal suffrage": Anson Enters Poll Plan Row, SOUTH CHINA MORNING POST, Sept. 16, 1997, at 1; Glenn Schloss, *Too Soon To Write SAR's Obituary*, SOUTH CHINA MORNING POST, Oct. 29, 1997, at 2.

example, Professor Fan Yaojun, Dean of the School of Business of the Baptist University of Hong Kong, suggests that the Hong Kong economy should be looked at beyond the sphere of Hong Kong's jurisdiction and that Hong Kong should to the greatest possible extent perform its supportive functions in the development of the mainland's economy by further integrating its own into the economic system of the mainland.³² The economy in Hong Kong has been healthy since July 1.³³ Leaders of major trading powers have also indicated their satisfaction with the handover and the state of affairs after the handover.³⁴

Post-handover Hong Kong is not a problem-free and worry-proof society. There are problems. For example, the tourism industry was slow in the initial months after July 1. The recent stock market crisis also raised some concerns among investors. Yet, the drop in the number of tourists has to a significant extent been due to prospective visitors' misunderstanding of China in general and the HKSAR in particular. Media coverage of the handover was blamed for presenting a sensationally negative image. The keenness of the press to show Chinese tanks rolling over the border was not welcomed by Hong Kong's tourism industry. The stock crisis in Hong Kong was not peculiar to the post-handover SAR itself. Of course, there are other problems, too. Nevertheless, if the economy in Hong Kong ever gets derailed at one point or another in time, that would not necessarily be attributable to the change of sovereignty. There is no such a thing as a never-setting sun. Who can guarantee that Hong Kong would be able to maintain its prosperity forever under British rule? I am sure former Governor Patton was faced with pretty much the same amount of problems as Chief Executive Officer Tung Chee Hwa is. After all, as one of the freest economies perhaps the freest (economy) in the world, Hong Kong is still "the best place to do business" in the eyes of foreign investors, with most of them choosing to expand investment or continue business as usual after the handover.³⁵ Really, there is no apparent reason why we should be pessimistic.

B. Hong Kong's Role in Cross-strait Trade and Investment

Since 1949, Hong Kong has served as a conduit not only for trade

³²See *Da Zhonghua Shidai Zazhi*, 大中华时代杂志 [GREATER CHINA TIME MAGAZINE], Oct. 15, 1997, at 47, 49.

³³See *id.*

³⁴For example, during President Jiang Zemin's recent summit meeting with President Clinton in Washington, D.C., President Clinton did not specifically raise the so-called Hong Kong issue because, it was reported, the Presidents of both countries were satisfied with the post-handover operation in Hong Kong. See *US Fears Over Hong Kong Have Dropped Off*, AGENCE FRANCE-PRESSE, Oct. 30, 1997 available in WESTLAW, File No. 1997 WL 13423693.

³⁵See *Foreign Investors Confident in HK's Future*, BEIJING REV., June 23-29, 1997, at 6.

between China and Western countries, but also for indirect transactions between the mainland and Taiwan. For a long time, Hong Kong has been an ideal place to engage in activities by both sides of the strait for various purposes including information gathering, direct trade with Hong Kong, and indirect trade through Hong Kong. The mainland's heavy reliance on Hong Kong for its foreign trade in general and eventually trade with Taiwan in particular has especially been obvious. Today, Hong Kong is the largest trading partner of both the mainland and Taiwan. In 1978, for example, 25.98% of China's total export volume was routed to Hong Kong (US \$2,532 million out of US \$9,745 million). In 1991, that figure was increased to 47.73% (US \$32,137 million out of US \$71,842 million). In 1978, merely 0.68% of the mainland's total imports were from Hong Kong (US \$750 million out of US \$10,893 million). In 1991, the figure dramatically jumped up by 27.7% (US \$17,463 million out of US \$63,790 million).³⁶

Hong Kong provides about two-thirds of all foreign investment in the mainland. Between 1991-95, Hong Kong-based investment in the mainland was estimated at US\$80 billion. Such capital investment provided much of the stimulus for the mainland's rapid economic growth and accounted for an estimated 20 percent of its gross domestic product.

At the same time, Hong Kong is an outlet for 48 percent of the mainland's exports and provides about 40 percent of its foreign exchange. Meanwhile, mainland sources have invested as much as US \$25 billion in over 3,000 companies in Hong Kong, second only to the U.K. and twice the amount from Japan.

As for trade between Taiwan and Hong Kong, it has been reported that in recent years Hong Kong has edged out the U.S. as Taiwan's top export market.³⁷ As Taiwan-Hong Kong trade also includes indirect trade between Taiwan and the mainland, it might be more appropriate to say that Hong Kong and the mainland are each other's largest trading partners while Hong Kong and the mainland together constitute Taiwan's largest export market.

However, trade between the two sides of the Taiwan strait prior to 1978 was so minimal that one could consider it virtually non-existent. With the adoption of an open-door policy in the mainland in the late 1970s, the volume of trade between the two sides began to increase dramatically. It was observed that Hong Kong has played a crucial role in channelling the indirect trade with ships from the mainland passing through Hong Kong before sailing for Taiwan under Panama flags and under Hong Kong

³⁶See generally ZHONGGUO DUIWAI MAOYI NIANJIAN [ANNUAL OF CHINA'S FOREIGN TRADE] (1978-1991).

³⁷See Kevin Platt, *China's New Bridge to Taiwan*, CHRISTIAN SCI. MONITOR, Aug. 14, 1997, at 6.

registration.³⁸ In 1978, imports from Taiwan to the mainland via Hong Kong totalled US \$46,725,000 while the mainland's exports via Hong Kong to Taiwan amounted US \$51,000,000. In 1989, transshipments from Taiwan to the mainland reached US \$2,896,487,000, while those from the mainland to Taiwan totalled US \$586,896,000.³⁹ According to the CCTV, from 1979 to 1996, the total transshipment trade volume between the two sides of the strait was US \$96.5 billion, out of which US \$14.8 billion represented sales of mainland-based goods to Taiwan through Hong Kong and US \$81.7 billion represented goods sold by Taiwan to the mainland. Each year, cross-strait trade involves more than 10 million tons of cargo.⁴⁰ Trade between the mainland and Taiwan for the period of January through August 1997 reached US\$12.08 billion, reflecting a 7.1% increase vis-à-vis the same period of time in 1996.⁴¹

For three decades or so since 1949, Taiwanese authorities banned virtually all links with the mainland. In late 1980s, Taiwanese authorities eased the bans by allowing a range of indirect investments covering about 4,350 investment categories.⁴² Since 1979, and especially since 1988, thousands of Taiwanese manufacturers and other investors, including some of the largest industrial groups in Taiwan, have poured billions of US dollars into the mainland through banks or offices in Hong Kong.⁴³ From the mid-1980s to the end of 1996, more than 35,000 projects with Taiwanese investment were undertaken involving US\$14.1 billion.⁴⁴ For the pre-1992 period alone, it was reported that in recent years the total Taiwanese capital flow to Hong Kong has amounted to over US\$15 billion, of which a portion is channelled to mainland China.⁴⁵ Taiwanese investors were already constantly increasing their investment in the mainland prior to the Hong Kong handover. According to a survey conducted in May 1997 which covered 1,312 Taiwanese businesses with overseas operations, 72.7% in 1996 maintained business contacts with the mainland, six percent higher than 1995.⁴⁶ Statistics indicate that in the first half of 1997, the mainland approved 1,381 Taiwan-funded projects involving a contractual investment

³⁸See generally TED THOMAS & NICOLE TURNER, WHAT'S GOING TO HAPPEN IN 1997 IN HONG KONG (1996).

³⁹See generally HONG KONG STATISTICS BUREAU'S STATISTICS ON RE-EXPORTS 1978 - 1989.

⁴⁰See *Tianya Gong Cishi Magazine* (CCTV television broadcast, Nov. 2, 1997) [hereinafter CCTV Broadcast].

⁴¹See *Freight Firms See Good Gains*, Xinhua (New China) News Agency, Nov. 9, 1997, available in LEXIS, Allnws Library, Xinhua File.

⁴²See *Taipei Allows Wider Range of Investments*, TRADE NEWS 1997.

⁴³See *First Meeting of Top Airlines Form China and Taiwan*, CHINA NEWS, Nov. 12, 1997, available in WESTLAW, File No. 1997 WL 13850524.

⁴⁴CCTV Broadcast, *supra* note 40.

⁴⁵See David Hsi-Cheh Chang, *Relations Between Taiwan and Hong Kong After 1997*, in PROCEEDINGS [OF] THE FUTURE OF HONG KONG SEMINAR 19, 20-21 (1992).

⁴⁶See *Taiwanese Invest More in the Mainland*, BEIJING REV., June 23-29, 1997, at 23.

of \$1.32 billion. In-hand investment amounted to \$1.6 billion.⁴⁷ Taiwan province has become the second largest source of overseas investment in the mainland, second only to Hong Kong. Recently, the Taiwanese authorities decided to allow a wider range of investments in the mainland. This means that previous investment constraints on more than 400 mainland categories have been eased. Such categories include travel agencies, hotels, recreation facilities, warehouses, merchandise agents, rental businesses, saunas, printing machines, sewing machines, and automobile and motorcycle parts. However, capital to the mainland still has to be routed through Hong Kong or a third place like Japan or Singapore. Furthermore, Taiwan continues an outright ban on real estate and large power plant projects comprising nearly 300 items, although small hydropower plants and steam and electricity co-generation facilities with capacities of up to 20 megawatts would be permitted.

C. The Handover and Hong Kong's Role in Cross-Strait Trade and Investment

Does the handover itself have any negative impact upon the role of Hong Kong in cross-strait trade and investment? Are there any obstacles to such indirect trade and investment now that Hong Kong is once again part of China? After the handover, theoretically speaking, links between Taiwan and Hong Kong constitute a kind of direct intra-national link between the two sides of the Taiwan strait. Given Taiwan's no contact policy, will traders and investors across the strait have to refrain from using Hong Kong for transfer trade and turn to other middlemen such as Japan, South Korea and Singapore instead in order to avoid consequences of direct links?

There are technical difficulties, too. We know that Hong Kong has been vital to the growing transshipment trade relations between the two sides of the Taiwan strait. Taiwanese ships carrying the flag of Taiwan and aircraft with a logo of the same flag could freely enter Hong Kong when the colony was under British rule. When China resumes its sovereignty over Hong Kong, the mainland will not tolerate the hoisting of the Taiwanese flag in the territorial waters of Hong Kong, nor would it endure the exhibition of the Taiwanese flag as an airline logo. If these issues could not be resolved, the handover would necessarily have a negative impact on the trade relations between the mainland and Taiwan.

At the same time, we should also note that the Basic Law and other relevant policy-stating instruments of the mainland serve to enhance Hong Kong's importance in bridging the two sides of the strait. One of the

⁴⁷See Wei Ke, *Trade Bonds Mainland, HK, Taiwan*, CHINA DAILY, Nov. 11, 1997, available in LEXIS, Allnews Library, Chidly File.

purposes of the Basic Law is to basically maintain the transparent legal system of Hong Kong after July 1997 and to protect private property, ownership in businesses and externally-sourced investment in Hong Kong.⁴⁸

Taiwanese traders and investors will thus continue to enjoy legal protection in Hong Kong for their trading and investment activities in the post-handover era. The provisions in the Basic Law relating to Hong Kong's free port status,⁴⁹ free trade policy and free movement of goods, intangibles and capital,⁵⁰ its continuing markets for foreign exchange, gold, securities, future commodities and the like and free flow of capital within, into and out of the HKSAR are all favourable to Taiwanese traders and investors continuing their businesses with, in and through Hong Kong.⁵¹ It has been made clear in the Seven Basic Principles and Policy of the Central Government on the Handling by Hong Kong of Taiwan-related Matters After 1997 that after the handover, the mainland encourages and welcomes Taiwanese residents and all sorts of Taiwanese capital to engage in investment, trade and other industrial and commercial activities in Hong Kong and that the legitimate rights and interests of Taiwanese residents and all sorts of capital of Taiwan in Hong Kong will be protected in accordance with the law.⁵²

Prior to the handover, Hong Kong and Taiwan had overcome the technical difficulties mentioned above by entering into a shipping agreement which allows Hong Kong and Taiwan to maintain direct shipping links after the handover, and a prior commercial aviation agreement, which allows the two sides to continue their direct bilateral air links in the post-handover era on similar terms. The agreement on shipping links allows Taiwanese ships to enter Hong Kong on the condition that they hoist no flag.⁵³ As to the aviation links, the mainland not only refused to allow the landing in the HKSAR of any Taiwanese aircraft that displays the Taiwanese flag, but also requested that the Taiwanese authorities allow a Hong Kong airline with mainland interests to fly the route between Hong Kong and Taiwan. In October 1995, China Airlines of Taiwan changed its logo by replacing the Taiwanese flag with a plum blossom. This solved half of the problem. The Taiwanese authorities currently ban any business in Taiwan in which the interests of the mainland are 20% or more. They finally agreed to the mainland's demand by treating the designated airline with 64% mainland

⁴⁸See Basic Law, *supra* note 2, at arts. 6 & 105.

⁴⁹See Basic Law, *supra* note 2, at art. 114.

⁵⁰See Basic Law, *supra* note 2, at art. 115.

⁵¹See Basic Law, *supra* note 2, at art. 112.

⁵²See Vice Premier Qian Qichen, Seven Basic Principles and Policy of the Central Government on the Handling by Hong Kong of Taiwan-related Matters After 1997, Address on behalf of the State Council (June 22, 1995).

⁵³See Daniel Kwan, *Pact "Promotes Direct Links"*, SOUTH CHINA MORNING POST, July 21, 1997, at 8.

holdings, Dragonair, as an exceptional case. The resulting aviation agreement, which was signed on June 13, 1996, allows China Airlines, Eva Airways, Cathay Pacific and Dragonair to operate 254 flights per week between Hong Kong and designated Taiwanese cities for the period of 1996-2001, including 6 cargo flights each for China Airlines and Cathay Pacific.⁵⁴

In April 1997, the Ministry of Communications of the mainland approved six Chinese shipping companies and ten freight agents in Fujian Province for trial direct sailings from Fuzhou and Xiamen to Kaohsiung, which were formerly started on April 19, 1997 when a mainland-owned, St. Vincent-registered vessel made the first cross-strait voyage in nearly five decades.⁵⁵ It is estimated that such direct sailings save 17% to 43% of the shipping costs in comparison with voyages through Hong Kong. However, the present shipping across the strait is not direct shipping links in the real sense, as cargo on the route is only allowed to enter the offshore transshipment center in Kaohsiung.⁵⁶

Nevertheless, given the mainland's clearly stated favourable policy, and with the shipping and aviation issues having been resolved, the handover does not seem to affect Hong Kong's role in linking the mainland and Taiwan in their trade and investment relations. Whether or not three direct links and other direct links between the two sides of the Taiwan strait can be realized in the near future, the handover of Hong Kong is in no sense detrimental to cross-strait trade and investment. If Hong Kong continues to be relied upon as an ideal nexus for indirect trade and indirect investment between the mainland and Taiwan, Hong Kong will continue its role as a trade bridge because the handover itself does not create any barrier to the existing mode of cross-strait trade and investment through Hong Kong.

D. Impacts of Future Direct Cross-strait Links upon Hong Kong

We have witnessed increased improvements in the trade relations between the mainland and Taiwan in the past decade or so. While three noes are still the official policy of the Taiwanese authorities who remain opposed to the mainland's call for direct trade, direct transport and direct communications, that policy has evolved from an absolute ban to a relative concept. In 1987, Taiwan permitted mail to be delivered to the mainland through the Red Cross in Taipei. Later, it legally allowed Taiwanese

⁵⁴See *HK, Taiwan Sign 5-year Airline Pact*, UPI, June 13, 1996, available in LEXIS, Allnws Library, UPI File.

⁵⁵See *Freight Firms See Good Gains*, *supra* note 41; *Trial Direct Sailings Across Taiwan Straits*, BEIJING REV., June 2-8, 1997, at 31.

⁵⁶See *Freight Firms See Good Gains*, *supra* note 41.

residents, subject to some restrictions, to visit relatives in or travel to the mainland via Hong Kong or a third place. In 1988, the Taiwanese authorities somewhat loosened its total ban on visits to Taiwan by mainlanders by permitting them to visit sick relatives or attend funerals in Taiwan. In the same year, Taiwan lifted the burdensome requirement that cargo in trans-shipment between the mainland and Taiwan had to be off-loaded in a third port before sailing to the destination although they could subsequently be re-loaded again on the same vessel. It initially acquiesced in and later legally permitted limited indirect investment by Taiwanese businesses. In April 1997, the Taiwanese authorities for the first time in 48 years permitted trial direct sailings between the ports of Fuzhou and Xiamen and Kaohsiung. More recently, Taiwan enhanced the degree of transparency in its cross-strait trade policy by accepting applications, as of July 1, 1997, by Taiwan companies which had covertly made investments in China through Hong Kong, to register their mainland investment projects and by allowing companies registered in Hong Kong with no more than 20% mainland sourced interests to do business in Taiwan.⁵⁷ The new policy, beginning with July 1, 1997, also allows freighters owned by mainland companies but registered in a third region or country to move between Taiwan and [the mainland] by making stopovers in a third area or country whereas under prior practices, such ships were not allowed to enter any port in Taiwan even if they had made port calls at a third country or area.⁵⁸

The above improvements have undoubtedly worked to the benefit of Hong Kong as the most convenient and important transfer point for increased exchanges in goods and people between the mainland and Taiwan. Then, if the above improvements as well as the handover of Hong Kong have not had any negative impact on Hong Kong's role in cross-strait trade and investment, will that role undergo any change along with the desirable but not guaranteed further improvements in trade and other relationships between the two sides of the Taiwan strait? On this issue, it was observed:

If direct postal, transportation and commercial links as well as direct investment and currency exchanges across the Taiwan Strait[s] are opened... and the two shores make appropriate arrangements, not only will Hong Kong's trade in transferred goods be reduced, but economic and trading relations between Hong Kong and Taiwan will be scaled back as well. However, a substantial bilateral trade volume will remain. This is because: a) the monetary system, port facilities and efficient service sector offered

⁵⁷See Deborah Shen, *Ceilings Set on Investment in Hong Kong and Macau*, FREE CHINA J., July 5, 1997, at 3.

⁵⁸See *id.*

by Hong Kong cannot be replaced by mainland ports altogether. A portion of the trade between Taiwan and the mainland will still be reliant on the services of Hong Kong businesses; b) In the current atmosphere of improving cross-strait[s] relations, Taiwan and Hong Kong industrialists and enterprises are presented with unparalleled opportunities to enter into joint agreements and development projects in [the mainland]. They may even be able to cooperate with their counterparts in [the mainland] to ... enter into international markets....⁵⁹

True, once the barriers to direct links between the mainland and Taiwan are eliminated, Hong Kong to some extent will inevitably lose its importance as an intermediary to both sides of the Taiwan strait. Since a large portion of Hong Kong's trade with the mainland and with Taiwan consists of transshipment or transferred trade, direct cross-strait trade and investment will mean reduced gains for Hong Kong businesses. On the other hand, a decrease in Hong Kong's role will not necessarily be as great as conceived. Possible economic losses for Hong Kong will be largely short-term losses. Hong Kong's role as a middleman will not necessarily disappear immediately following future realization of direct trade and investment links between the two sides of the strait. It will be quite some time before all parties involved in current indirect cross-strait trade and investment become comfortable enough in their own direct transactions to completely discontinue their reliance on the facilities and services of Hong Kong to which they are so much accustomed. More importantly, even if Hong Kong's role as a middleman completely fades away, Hong Kong can look forward to a more constructive and more lucrative role in participating in building a Chinese Common Market and a unified and prosperous Greater China by integrating its economy with that of the mainland and Taiwan.

Another indicator that may be looked at is the general attitude of Hong Kongers towards the economic relations between Hong Kong and Taiwan in general and the possible realization of direct trade links between the mainland and Taiwan. The Asia-Pacific Research Center of the Chinese University of Hong Kong conducted surveys of Hong Kong residents in 1996 and 1997. In 1996, 33.6% of those being surveyed believed that the economic and trade relations between the two regions were complementary to each other while 41.5 responded with competitive. In 1997, 36.3% believed such relations were complementary, an 8.04% increase, while 43.4

⁵⁹See Hsi-Cheh Chang, *supra* note 45, at 23.

believed that they were competitive, a 4.58% increase.⁶⁰

On the question whether the so-called Asia-Pacific Operation [and Transportation] Center (APOC), which has been advocated by Taiwan for the purpose of, among others, replacing Hong Kong after Hong Kong's return to the motherland, will actually replace Hong Kong as an international financial center, 7.1% responded in 1996 that it is very unlikely and 63.2% unlikely. In 1997, 11.2% responded with very unlikely, a 57.75% increase, and 60.9% responded with unlikely, a 3.78% decrease. Those who believed that such replacement would be likely amounted 17% in 1996 and 11% in 1997, a 54.55% decrease, while 0.7% believed the replacement would be very likely in 1996 and 0.6% maintained such belief in 1997, representing a 16.67% decrease.⁶¹ On the question of whether APOC will replace Hong Kong after 1997 as an international shipping center, answers with very unlikely amounted to 5.9% in 1996 and 8.4% in 1997 (a 42.37% increase); answers with unlikely represented 59.7% in 1996 and 59.6% in 1997 (a 1.68% decrease); the percentage for responses with very likely was the same for 1996 and 1997, at 0.4%; answers with likely decreased by 28.19% from 18.2% in 1996 to 14.2% in 1997.⁶²

However, although a majority of opinions in Hong Kong favour the resumption of direct links between the mainland and Taiwan, there is a slight change between 1996 and 1997 in attitudes moving towards disfavouring such direct links. According to the surveys, 1.5% strongly opposed direct cross-strait links in 1997 compared with 1.6% in 1996 (a 6.67% decrease); 15.5% opposed such direct links in 1997 in comparison with 11.2% in 1996 (a 38.39% increase); 70.4% supported the establishment of direct links across the Taiwan strait in 1997 compared with 70.1% in 1996 (a 4.28 increase); only 6.8% strongly supported such links in 1997 compared with the 1996 figure of 11.6% (a 70.59% decrease).⁶³

While the surveys are not conclusive, they may to a certain extent demonstrate the general attitudes of at least some of the residents in Hong Kong towards the trilateral economic and trade relations across the Taiwan strait. More and more people realize that the economic relations between Hong Kong and Taiwan are not necessarily competitive; rather, they can be complementary to one another. Despite Taiwan's attempt to establish the APOC, Hong Kong people remain confident in the status of Hong Kong as an international financial and shipping center. While the numbers of Hong

⁶⁰See Wang Jiaying, *Xiang Gang Ren Duidai Liang An Sandi Guanxi de Taidu yu Bianhua* [The Attitudes and Their Changes of Hong Kongers Towards the Relations among the Three Regions Across the Straits], in XIANG GANG HUIGUI TAI GUANXI [THE RETURN OF HONG KONG AND THE HONG KONG-TAIWAN RELATIONSHIP] 127-49, (Wang Jiaying & Sun Tongwen, eds., 1997).

⁶¹See *id.* at 130.

⁶²See *id.*

⁶³See *id.* at 137.

Kongers opposing the establishment of direct links across the strait seem to be on the rise, those who support such direct links between the mainland and Taiwan remain the overwhelming majority. If direct trade, direct transport, direct communications, direct investment and direct currency exchanges between the mainland and Taiwan are generally welcomed by the people of Hong Kong, we should not be concerned too much with the potential decrease in the role of Hong Kong in cross-strait trade and investment in the future.

III. CONCLUSION

Because of artificial and political barriers to trade between the mainland and Taiwan, particularly due to the three-noes policy of the Taiwanese authorities, Hong Kong has served as a re-export center and a conduit for businesses between the mainland and Taiwan and will continue to do so for an unascertainable period of time in the post-handover era unless and until such barriers are completely removed. Needless to say, the three-noes policy has increased the cost of cross-strait transactions, but it has also provided business opportunities for Hong Kong as a secondary consequence. That is to say, Hong Kong itself has grown rich partly out of its business associations with both the mainland and Taiwan and out of its role in facilitating indirect contacts between the mainland and Taiwan. However, this does not mean that we should keep the status quo indefinitely. While indirect trade with and investment in the mainland were considered profitable at a time when the labour and raw material costs in the mainland were considerably low, such costs have more than tripled in the past decade. Such increase in costs will inevitably curtail the profitability of cross-strait businesses through Hong Kong or other third places. Routes for indirect trade and investment are circuitous and time-consuming. Transportation costs are higher than are necessary. Traders and investors across the strait see no reason why direct links cannot be resumed.

The trade relations among these three parts of China are such that they have to a large extent become interdependent in their economies. We should emphasize common civilization, harmony, consensus and economic interests rather than ideology and political differences. Before the two sides of the Taiwan strait can solve the issue of their political reunification, there is much that can be done towards the formation of an economic union of a Greater China, a true Chinese Common Market. Hong Kong, with its close cultural and economic ties with both the mainland and Taiwan, can bridge the two sides with that goal. Once the political barriers to direct links between the mainland and Taiwan are completely removed, Hong Kong's role as a conduit will not immediately vanish. Rather, it will be a long process of phasing out. Businesses in the mainland and Taiwan are so used to the mode

of indirect trade that they might well for a considerable period of time continue their reliance on Hong Kong as a conduit for the sake of convenience.

During that period, the mainland, Taiwan and particularly Hong Kong should have enough time to re-adjust their economies and businesses so as to keep the negative impacts of future resumption of full direct links across the strait upon Hong Kong at a minimal level. In the long run, Hong Kong has less to lose and more to gain (1) in cooperating with Taiwan to further the mainland's economic reform and develop or upgrade the latter's traditional and newly emerging industries, (2) in building a Chinese Common Market together with the mainland and Taiwan, and (3) in participating in the course of forming a unified, prosperous and advanced Greater China.

At present, with only Hong Kong a member of the WTO, it is not surprising that trade barriers still exist between the mainland and Hong Kong and between Taiwan and Hong Kong, not to mention political obstacles to trade between the two sides of the Taiwan strait. Political obstacles to direct cross-strait links are mainly due to the Taiwanese authorities' long running policy of "no contact, no negotiation, no compromise," (called "the Three Noes") although for the past two decades this policy has been gradually loosened to certain extent. Non-political obstacles such as tariff and non-tariff barriers to cross-strait trade are also mainly one way in the sense that the mainland as a developing economy has a heavier reliance on customs duties to protect its domestic industries. This is especially so in the case of imports from or via Hong Kong to the mainland. Once China and its Taiwan are admitted to the WTO, while free trade within the Greater China will hardly be conceivable within a considerable period of time, the three sides, especially the mainland and Taiwan, will have to at least undertake acceptable trade concessions and other obligations toward one another, as they will have to do with other members. If the Taiwanese authorities are as eager as the mainland to join the WTO and their admissions can be expected for in the near future, there will be a change in Taiwan's policy of "the Three Noes."