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국제학석사학위논문

**A Comparative Analysis of China's FTAs with  
Hong Kong and Taiwan**

중국-홍콩 FTA와 중국-대만 FTA의 비교분석

2018년 8월

서울대학교 국제대학원  
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# 중국-홍콩 FTA와 중국-대만 FTA의 비교분석

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# **A Comparative Analysis of China's FTAs with Hong Kong and Taiwan**

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## **Abstract**

# **A Comparative Analysis of China's FTAs with Hong Kong and Taiwan**

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After China's accession to the *World Trade Organization* (WTO) in December 2001, it has pursued a regional trade strategy by adopting six *FTAs*, two *Closer Economic Partnership Arrangements* (CEPAs) with Hong Kong and Macao respectively, and the *Economic Cooperation Framework Agreement* (ECFA) with Taiwan. Among the trade treaties, the CEPA with Hong Kong and Macao and the ECFA with Taiwan has been viewed as an attempt to achieve the Mainland's long pursued political and strategic goal of "*peaceful unification*" under the principle of "*One Country, two systems*" by fostering mutual economic benefits through concluding preferential treaties.

Despite their geographic closeness, the four areas of the *Chinese Economic Area* (CEA) - the Mainland, Hong Kong, Macao, and Taiwan - represent separate customs territories among which trade and investment is carried out in an external way. The rapid economic development in the CEA called for formal arrangements to regulate trade and investment in a way that guarantees mutual benefits, resulting in the formation of the above mentioned trade treaties. For our discussion in this paper, we will focus on the dynamics between the Mainland, Hong Kong and Taiwan while ignoring the economy of Macao as it is relatively

small compared to the others.

Hong Kong reverted to Chinese rule in 1997 while Taiwan enjoys its de facto independent status. However, the latter is regarded by the Mainland as a "province", which shall surely return to the rule of its Motherland in the near future. According to Beijing's policy of "peaceful unification" mentioned above, Taiwan shall be brought under the Mainland's rule "through a process of economic, social and political integration, facilitated by personal exchanges, cross-strait trade and investment and joint cultural, sporting and education activities" (Hughes, 2001). Although the principle of "One Country, two systems" was originally designed for Taiwan under the rule of Deng Xiaoping, it is widely known that the same strategy has been adopted on Hong Kong, which served as a prototype for Taiwan's future unification process with the Mainland (Bundy 1989; Cooney 1997; Weng, 1987). This is also one of the important reasons why the Taiwanese government, since the late 1990s, has been carefully observing the economic and political development of Hong Kong to draw lessons for itself.

The comparison between the CEPA and the ECFA raised growing concern over the further loss of Taiwan's sovereignty, in view of the "*One Country, Two Systems*" policy under which Hong Kong found itself trapped even more after the signing of the CEPA. However, there are clearly political and economic differences between the two regions, providing evidence that the fear of Taiwan becoming another Hong Kong is not well-founded. From a political perspective, Hong Kong is a semi-autonomous, special administrative region of Mainland China, whereas Taiwan indeed possesses its own formal government, enjoying de facto independence from Mainland China. With regards to the economy, Hong Kong bases its economy on the service industry, while with regards to Taiwan's economy, the manufacturing sector still plays an important role.

The purpose of this dissertation is to compare the two trade treaties signed between China and Hong Kong, and China and Taiwan, and to prove that the concern over Taiwan becoming another Hong Kong is not necessarily well-founded, at least from a legal

perspective. Although the Mainland has long insisted that Taiwan is part of the country, legally speaking, the Mainland treats Taiwan and Hong Kong vastly differently. The differences are explained by carefully analyzing the CEPA and the ECFA and outlining the discrepancies and trying to explore the socio-economic and political reasons that caused these major differences in the legal content and clauses of the treaties. The most significant differences can be found in (1) the political principles of the CEPA and the ECFA; (2) the level of legal protection manifested in legal clauses such as dispute settlement, termination, safeguard, or anti-dumping; and (3) the level of liberalization of trade in goods and services as well as the coverage of the preferential treatment under the two treaties. Given these differences, it becomes evident that the legal status of the CEPA resembles an internal, national arrangement between areas within the same country, whereas the ECFA between China and Taiwan is modelled after standardized international FTAs. This also indicates that there have been socio-economic and political phenomena which have forced China to treat Hong Kong and Taiwan differently.

**Keywords:** China, Taiwan, Hong Kong, FTA, legal analysis, comparison of CEPA and ECFA

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## I. Introduction

After China's accession to the *World Trade Organization* (hereafter abbreviated as "WTO") in December 2001, it pursued a regional trade strategy by adopting six *free trade agreements* (hereafter abbreviated as "FTA"), two *Closer Economic Partnership Arrangements* (hereafter abbreviated as "CEPA") with Hong Kong and Macao respectively, and the *Economic Cooperation Framework Agreement* (hereafter abbreviated as "ECFA") with Taiwan in 2010. Most notably, the CEPA between Mainland China and Hong Kong, and the ECFA between Mainland China and Taiwan were regarded as an attempt to achieve the Mainland's long pursued political and strategic goal of "*peaceful unification*" under the principle of "*One Country, two systems*" with Hong Kong and in particular with Taiwan by fostering mutual economic benefits through concluding preferential treaties.

Despite their geographic closeness, the four areas of the *Chinese Economic Area (CEA)* - the Mainland, Hong Kong, Macao, and Taiwan - represent separate customs territories among which trade and investment is carried out in an external way. Economic integration between these four areas has witnessed rapid development since the reforms and opening up under the former Chinese leader Deng Xiaoping in 1978. Thus, although initially trade between these areas took place under free market forces without any binding of formal trade treaties, the rapid economic development in the CEA called for formal arrangements to regulate trade and investment in a way that guarantees mutual benefits, resulting in the formation of the above mentioned trade treaties.

Apart from the complexities in the trade aspect, also the political relationship between the four areas is rather complex. For our discussion in this paper, we will focus on the dynamics between the Mainland, Hong Kong and Taiwan while ignoring the economy of Macao as it is relatively small compared to the others. Hong Kong reverted to Chinese rule in 1997 while Taiwan enjoys its *de facto* independent status. However, the latter is regarded

by the Mainland as a "province", which shall surely return to the rule of its Motherland in the near future. According to Beijing's policy of "peaceful unification" mentioned above, Taiwan shall be brought under the Mainland's rule "through a process of economic, social and political integration, facilitated by personal exchanges, cross-strait trade and investment and joint cultural, sporting and education activities" (Hughes, 2001). Although the principle of "One Country, two systems" was originally designed for Taiwan under the rule of Deng Xiaoping, it is widely known that the same strategy has been adopted on Hong Kong, which served as a prototype for Taiwan's future unification process with the Mainland (Bundy 1989; Cooney 1997; Weng, 1987). This is also one of the important reasons why the Taiwanese government has since the late 1990s, has been carefully observing the economic and political development of Hong Kong to draw lessons for itself.

Nevertheless, although the Mainland has long insisted that Taiwan is part of the country, legally speaking, the Mainland treats Taiwan and Hong Kong differently. This also represent the main motivation for my analysis.

Current literature on this topic is largely focused on the differences between CEPA and ECFA imbedded in the context of the time period during which the agreements were first signed, putting emphasis on the respective region's background conditions prevailing at that particular time. However, it is worth noting that especially with regards to Taiwan, its development of the political landscape has been changing quite dramatically from when the ECFA was concluded in 2010. When negotiations of the ECFA took place, it was the *Nationalist Party* of Taiwan under the leadership of former President *Ma Ying-jeou* that approached the Mainland for the conclusion of the agreement. The political atmosphere at that time was favorable of business ties between Taiwan and the Mainland as long as the agreement had its focus on economic cooperation, leaving political issues untouched. This favorable political atmosphere however, has drastically changed since the *Sunflower Movements* in 2014 in the latest, and the election of the current President *Tsai Ing-wen* of the

*Democratic Progressive Party* of Taiwan in 2016. With a change in political administration, the further development of the ECFA is likely to be very different from what was anticipated in the previous literature.

Many have approached the issue from a political and economic point of view (Chow, Zhang). The comparison between the CEPA and the ECFA raised growing concern over the further loss of Taiwan's sovereignty, in view of the "*One Country, Two Systems*" policy under which Hong Kong found itself trapped even more after the signing of the CEPA. However, critics have pointed out that there are clearly political and economic differences between the two regions, thus providing evidence that the fear of Taiwan becoming another Hong Kong is not well-founded (Hong). From a political perspective, Hong Kong is a semi-autonomous, special administrative region of Mainland China, whereas Taiwan indeed possesses its own formal government, enjoying de facto independence from Mainland China. With regards to the economy, Hong Kong bases its economy on the service industry, while with regards to Taiwan's economy, the manufacturing sector still plays an important role.

In view of the above, apart from the political and economic point of view, very few have engaged in the research of differences between the CEPA and the ECFA from the legal perspective and what it was that shaped these legal differences even though China at its part considered both regions as part of its own territory. Chow contributed to this part of the research by outlining the discrepancies in liberalization of trade in goods and services as well as investment facilitation. The CEPA focusses on trade in services as Hong Kong is mainly exporting services to the Mainland. Another highlight of the CEPA is found in the detailed provision of investment facilitation measures due to a major flow of FDI coming from Hong Kong into the Mainland, although this is no longer a one-sided issue as the Mainland's FDI flow into Hong Kong has increased tremendously in the recent decade. In addition, both Hong Kong and Mainland China show relatively high openness to market access. The ECFA, though based on its *Early Harvest Program* for now as a formal agreement is yet to be reached, has a much stricter approach to the provision of market access, wherein only a small

part of goods has seen its tariffs successfully removed. With respect to the services sector, the Parties are also reluctant to implement full liberalization due to concerns about intensified competition among Taiwanese and Mainland Chinese services providers, which could have a negative impact on both the Taiwanese as well as the Mainland Chinese economy.

In sum, in the existing literature on the CEPA and ECFA, the agreements have mostly been reviewed separately. The few ones which engage in the comparison between the two agreements, focus on either political or economic factors behind the discrepancies. What is more, these factors and background information were based on the situation at the time when the agreement was first introduced and, at least in the case of the yet pending ECFA agreement, may not be appropriate enough to describe the current and future conditions under which the agreement will be further negotiated. A detailed comparison of the original legal text including the analysis of individual clauses has not yet been found. This may represent a gap for further in-depth research.

As such, the purpose of this paper is to show the different status granted by the Mainland to Hong Kong and Taiwan from a perspective of trade by examining the legal differences between the two major treaties in the CEA - the CEPA between the Mainland and Hong Kong and the ECFA between the Mainland and Taiwan. It will be largely based on the comparison of the individual clauses and provisions under the CEPA and the ECFA. Also, reasons behind the discrepancies will be analyzed and reviewed. Another important goal of this research will be represented by an update of the political and economic conditions surrounding the respective countries and regions which are subject to the agreements. This update is necessary as the change of conditions may, at least in the case of the ECFA, greatly affect the outcome of further negotiations between the parties. To the international community, whether the ECFA can be concluded or not might provide an important sign of the future development of the China-Taiwan relationship. In addition, this particular

relationship may also play an important role in the formation of the future East Asian international order.

The paper starts with an introduction of the background and events leading to the formation of the CEPA and the ECFA respectively and gives an overview of the main provisions of both FTAs. It will then continue with a detailed analysis of the legal differences between the CEPA and the ECFA by examining each of the legal clauses stipulated in the legal text of the FTAs. The analysis will be followed by a conclusion.

The research methods consist of reviewing primary and secondary sources including existing academic literature in the English, German, and Chinese language, governmental statements and press releases as well as newspaper articles. The legal analysis will be conducted by comparing the main legal texts and the supplements and follow-up agreements of the CEPA and the ECFA, including: (1) the CEPA main text and six annexes, ten supplements, two agreements on trade in services, the Investment Agreement, and the Agreement on Economic and Technical Cooperation; (2) the ECFA main text and five annexes, including the Early Harvest Program.

## **II. The CEPA FTA between Mainland China and Hong Kong**

The CEPA FTA between Mainland China and Hong Kong represents a major landmark in Chinese trade history as it is China's as well as Hong Kong's first FTA respectively<sup>1</sup>. At the same time, this FTA also counts as the first FTA between two customs territories that belong to the same country. The CEPA also functioned as a guideline for the Mainland China-Macau FTA (also called CEPA), and the later arranged Mainland China-Taiwan FTA (ECFA). For Hong Kong, the CEPA played a significant role in recovering its economy after the Asian Financial Crisis and the SARS epidemic (Severe Acute Respiratory Syndrome)<sup>2</sup>.

### **1. The background and establishment of the arrangement**

After the reforms and opening up in 1978, Hong Kong and Mainland China's trade flows have increased rapidly. Although initially, there was no formal trade agreement signed between the two territories, natural market forces - low wages in Mainland China in particular - have attracted Hong Kong manufacturers to relocate their production within the Mainland in the 1980s, mostly in Guangdong province due to its geographic closeness to Hong Kong. Along with the development in the trade relationship, transportation was also widely established and facilitated between the two territories to support further growth. To minimize political involvement by the Mainland Chinese government, the Hong Kong government only adopted government policies supporting the trade relationship rather slowly. Instead of using government policies to lead the market development, the Hong Kong government actually implemented policies only after market development had urged them to set up more friendly trade policies towards Mainland China.<sup>3</sup>

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<sup>1</sup> In 2001, China joined the Asia-Pacific Trade Agreement (previous Bangkok Agreement), but this Agreement represents a Preferential Trade Agreement (PTA) which, according to WTO rules, is to be regarded differently from a FTA. The main reason being that in FTAs, the tariff rate should eventually be abolished for "substantially all trade", while with regards to PTAs, the tariff rate mustn't be abolished but merely reduced.

<sup>2</sup> Yun-Wing Sung, "A comparison between the CEPA and the ECFA" in *Economic Integration Across the Taiwan Strait: Global Perspectives*, ed. Peter C.Y. Chow (Edward Elgar Publishing Limited, 2013), 31.

<sup>3</sup> Yun-Wing Sung, *The Emergence of Greater China: The Economic Integration of Mainland China*,



Due to enormous investment in-flows from Hong Kong, Guangdong province quickly emerged as a world factory. In fact in the early 1990s, Guangdong's inward FDI (foreign direct investment) and exports exceeded that of Thailand.<sup>4</sup>

Nevertheless, the economic relationship between the two territories had been an asymmetric one, wherein Hong Kong had been much more open towards the Mainland and the latter much more conservative towards the former. However, with the reforms and opening-up of the Mainland's economy, the discrepancy between the two territories has been narrowed significantly. It is worth noting that though Mainland China's economy had been relatively closed, it was perceived as already much more open towards Hong Kong in particular, in contrast to other countries outside the CEA. This preference of Hong Kong has been further manifested in the conclusion of the CEPA.

When the talks of a possible FTA with Mainland China circulated, many elites in Hong Kong voiced their concerns about the possible adverse effects of deepening ties with the Mainland. At that time, the "one country, two systems" was a newly invented concept which no country had tried before. Hong Kong feared that a deeper integration with the Mainland in economic terms might diminish its political autonomy, resulting in a rather slow progress in policy coordination with the Mainland.<sup>5</sup>

Under these circumstances, the major turning point that changed Hong Kong's mind and made progress faster, can be attributed to the Asian Financial Crisis starting from 1997. Hong Kong's economy suffered severe shocks and its recovery was negatively affected by the 911 terrorist attack on the United States in September 2001. It was then that elites in Hong Kong proposed the idea of accelerating economic integration with the Mainland as a means to recover their economy. Thus, in December 2001, one month after Mainland China had been accepted as a Member of the WTO, Hong Kong proposed an FTA with the

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*Taiwan, and Hong Kong* (Basingstoke and New York: Palgrave Macmillan, 2005), 48-9.

<sup>4</sup> Yun-Wing Sung, P.W. Liu, Richard Wong, P.K. Lau, *The Fifth Dragon: The Emergence of the Pearl River Delta* (Singapore: Addison-Wesley, 1995), 221.

<sup>5</sup> Yun-Wing Sung, *The Emergence of Greater China: The Economic Integration of Mainland China, Taiwan, and Hong Kong* (Basingstoke and New York: Palgrave Macmillan, 2005), 186-7.

Mainland, resulting in the conclusion of the CEPA in June 2003 after long negotiations.<sup>6</sup>

## **2. Main provisions under the arrangement (trade in goods, trade in services, trade and investment facilitation, economic and technical cooperation)**

The CEPA was signed on June 29, 2003 and took effect on January 1, 2004. The provisions under the CEPA already proved that it is a fully-fledged FTA as it states the abolishment of tariffs for "substantially all trade" between Mainland China and Hong Kong (CEPA main text, chapter 1, article 1.1). The agreement has also encouraged further trade liberalization from 2003 when it was signed until the present, fostering additional ten supplements and four agreements: (1) the Agreement between the Mainland and Hong Kong on Achieving Basic Liberalization of Trade in Services in Guangdong (signed in December 2014); (2) the Agreement on Trade in Services (signed in November 2015); (3) the Investment Agreement and Ecotech Agreement (signed in June 2017); and lastly (4) the Agreement on Economic and Technical Cooperation (also signed in June 2017).

Compared to the ECFA, the CEPA is much more advanced in terms of trade liberalization, mainly due to the relatively less complicated political environment. The CEPA was less likely to affect domestic manufacturing in Hong Kong because Hong Kong has always been a free port. In addition, the implementation of the CEPA provided also less chances to harm the Mainland's competitiveness in manufacturing as Hong Kong's economy was mostly service-oriented. Based on these reasons, the CEPA negotiation and conclusion happened relatively smoothly in contrast to the ECFA.

The conclusion of the CEPA has brought two rather different economies together: one being the small but remarkably developed and open economy of Hong Kong, and the other

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<sup>6</sup> Yun-Wing Sung, *The Emergence of Greater China: The Economic Integration of Mainland China, Taiwan, and Hong Kong* (Basingstoke and New York: Palgrave Macmillan, 2005), 199.

being the large but relatively less-developed and conservative economy of Mainland China. The asymmetric nature of the relationship nevertheless brought about certain advantages to each of the parties. For Hong Kong, a preferential opening of the large Mainland obviously means a simultaneous broadening of its market and production capacities including the additional gains resulting from relatively lower wages. For the Mainland, at the first glance it may seem that it has less benefits coming from the CEPA, however as Hong Kong has been by far the largest investor in the Mainland, it is expected that the Mainland will receive a higher influx of investment from Hong Kong under the trade and investment facilitation provisions included in the CEPA. Furthermore, by opening up its relatively protected service sector to Hong Kong, the Mainland can assist its service industries to develop and adapt to global competition. And last but not least, the successful conclusion of the CEPA symbolizes the reunion of Hong Kong with its separated "motherland", and this may particularly attract Taiwan to conclude a similar cross-strait FTA with Mainland China.

The main provisions of the CEPA cover four broad areas, namely trade in goods, trade in services, trade and investment facilitation, and economic and technical cooperation.

### **2-1 Trade in Goods**

Initially, the CEPA granted zero tariffs to Hong Kong manufacturers in 273 product categories, this later expanded to approximately 1900 items (as of January 2018). The initial 273 product categories already covered large segments of Hong Kong's manufacturing industries such as electronic items, textiles and clothing, jewelry and watches, plastic and metal products etc.

Under the CEPA, zero tariff on imported goods of Hong Kong origin can only be fully implemented upon applications by local manufacturers and when the CEPA rules of origin provisions (ROOs) are agreed and met. Imported goods that are prohibited by the Mainland's regulations as well as goods prohibited due to the implementation of other international

treaties binding the Mainland are not included into this category.<sup>7</sup>

All goods exported from Hong Kong to the Mainland must adapt to the ROOs to be eligible to gain zero tariff under the CEPA. To do so, each good passing the border from Hong Kong to the Mainland must possess a certain "Certificate of Hong Kong Origin - CEPA" which is issued by the Trade and Industry Department or by one of the five Government Approved Certification Organizations<sup>8</sup>. However, before the manufacturer is applicable for this certificate, he/she is required to first apply for a Factory Registration (FR) at the Trade and Industry Department to show that he/she is able to produce the goods for exporting with the needed capacity.<sup>9</sup>

Although there are several rules regarding the exportation of products from Hong Kong to China, as for Hong Kong, the CEPA was not designed to revive Hong Kong's manufacturing sector after its gradual decline for the last three decades, because Hong Kong's manufacturing sector was not large to begin with and production costs were much higher than the Mainland. Nevertheless, as intellectual property rights in Hong Kong are much better protected than in the Mainland, the CEPA was expected to benefit the high value-added manufacturing sector and industry sectors in which intellectual property rights played a crucial role. This particular feature would assist Hong Kong manufacturers in the development of brand products targeted at the rising middle class consumer market in the Mainland.<sup>10</sup>

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<sup>7</sup> For detailed information, see "Goods entitled to CEPA Zero Tariff Preference - Mainland 2018 Tariff Codes, Product Description and Rules of Origin (as at 1 January 2018)" at the Trade and Industry Department Hong Kong website, [http://www.tid.gov.hk/english/cepa/tradegoods/rules\\_origin.html](http://www.tid.gov.hk/english/cepa/tradegoods/rules_origin.html)

<sup>8</sup> According to the Hong Kong Trade and Industry Department, these include: the Hong Kong General Chamber of Commerce; the Federation of Hong Kong Industries; the Chinese Manufacturers' Association of Hong Kong; the Chinese General Chamber of Commerce; and the Indian Chamber of Commerce, Hong Kong.

<sup>9</sup> For detailed information, see "Trade in Goods - Relevant Certificates of Origin Circulars" at the Trade and Industry Department Hong Kong website, [https://www.tid.gov.hk/english/cepa/tradegoods/relevant\\_co\\_cir.html](https://www.tid.gov.hk/english/cepa/tradegoods/relevant_co_cir.html)

<sup>10</sup> Yun-Wing Sung, *The Emergence of Greater China: The Economic Integration of Mainland China, Taiwan, and Hong Kong* (Basingstoke and New York: Palgrave Macmillan, 2005), 200.

## 2-2 Trade in Services

The CEPA grants preferential treatment to service suppliers in Hong Kong when they establish business in many service sectors in the Mainland. Initially, this preferential treatment was only applicable to 18 service sectors, but this number expanded to 53 sectors by today<sup>11</sup>, including many sectors in which Hong Kong has a competitive advantage and Hong Kong's main service industries such as: financial services (accounting, banking, insurance, futures and securities etc.), tourism, legal services, consulting services, business and professional services etc. In addition, it also covers important and usually sensitive sectors such as telecommunications, cultural services and air transport services.

The preferential treatment provided under the CEPA is granted in various forms:

- ❖ Lower requirements concerning setting up businesses in the Mainland by Hong Kong firms: China's WTO commitments with regards to entry thresholds have been decreased for Hong Kong companies. Market access requirements such as registered capital requirements by Mainland banks are vastly reduced for Hong Kong firms. Also, asset values and annual sales of Hong Kong retailers are lowered, and requirements of export and import trade are much more relaxed as well. These measures allow more Hong Kong companies to enter the Mainland market, the reason being that Hong Kong businesses are often smaller in size, and with lower market access requirements, many more of them are able to set up their business in the Mainland.
- ❖ Relaxed restrictions over geographical location and business scope: China's WTO commitments in these aspects have also been reduced for Hong Kong firms. Examples of such preferential treatment can be found for instance in retail trade, wherein usually only major cities such as provincial capitals are available for foreign companies. The CEPA grants Hong Kong companies the right to operate in

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<sup>11</sup> For detailed information, see "Trade in Services - Measures and Regulations by Service Sector" at the Trade and Industry Department Hong Kong website, [https://www.tid.gov.hk/english/cepa/tradeservices/trade\\_services\\_requirement.html](https://www.tid.gov.hk/english/cepa/tradeservices/trade_services_requirement.html)

all cities at the prefectural level. This grant is even expanded with regards to the Guangdong province, wherein Hong Kong companies are allowed to operate in all cities at the county level within this particular province. As for the tourism sector, the geographic restrictions on foreign firms are also eliminated for Hong Kong companies.

- ❖ Allowance of wholly-owned operations: Under the CEPA, Hong Kong companies are allowed to establish wholly-owned ventures, while companies from other foreign countries are restricted to joint ventures.
- ❖ Less restrictions in the cultural services sector: The annual film quota for imported films as for 2017 is set around 34 film per year. However, there is no quota system for Hong Kong-produced Chinese language films.
- ❖ Free movement of professionals and residents: Under the CEPA, Hong Kong professionals and residents from services sectors such as securities and insurance industries are able to apply for practice in the Mainland. Permanent residents from Hong Kong are allowed to take the Mainland's legal qualifying examination. Moreover, exchange between Hong Kong and Guangdong province is particularly encouraged. For instance, for operating in Guangzhou and Shenzhen (major cities in Guangdong province), Hong Kong lawyers' residency requirements have been eliminated and Hong Kong residents are permitted to open individually-owned retail stores.

Despite of the preferential treatment of Hong Kong firms and individuals, in terms of movement of natural and juridical persons of Hong Kong, the preferential treatment is only granted if they fulfill the definition of HKSS (Hong Kong Service Supplier) under the CEPA. HKSS defines a natural person as a Hong Kong permanent resident, while a juridical person is applicable to any legal entity constituted or organized under the laws of Hong Kong

(business types such as partnership, corporation, sole or multi proprietorship etc.) and to firms which have engaged in business operations in Hong Kong for at least 3 to 5 years. If a firm or organization falls into the category of juridical person, it has to apply first for a HKSS certificate<sup>12</sup> at the Trade and Industry Department of Hong Kong and then apply for CEPA treatment at authorities in the Mainland. In contrast to juridical persons, a natural person under the CEPA is not obliged to apply for a HKSS certificate.

### **2-3 Trade and Investment Facilitation**

In June 2017, Hong Kong and the Mainland have signed the Investment Agreement to assist the CEPA in investment issues. It aims at facilitating the CEPA provisions by expanding market access commitments to non-services sectors and by setting up obligations for investment protection. The agreement is crucial for maintaining stability of investment regimes in both areas, which in turn should provide more security and confidence for current and potential investors from both sides, and also increase investment liberalization. The Investment Agreement was ratified in January 2018.

The agreement states two major contents: rules regarding the *admission of investments* for Hong Kong businesses in the Mainland on the one hand, and provisions of *investment protection and facilitation* on the other hand. The rules of admission apply to the non-services sectors (including manufacturing and mining sectors, and asset investments). Under this provision, Mainland China offers national treatment to Hong Kong investors and investments in all non-services sectors, the only exceptions being the 26 measures listed in Annex 2<sup>13</sup> of the same agreement (exceptions apply to sectors dealing with petroleum oil and natural gas, mineral products, atomic energy, manufacturing of transportation carriers such as airplanes, traditional arts and crafts and Chinese medicine etc.). However, these

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<sup>12</sup> For detailed information, see "Trade in Services - Notice to Service Suppliers" at the Trade and Industry Department Hong Kong website, [https://www.tid.gov.hk/english/aboutus/tradecircular/ntss/ss\\_maincontent.html](https://www.tid.gov.hk/english/aboutus/tradecircular/ntss/ss_maincontent.html)

<sup>13</sup> For detailed information, see "Annex 2 of the Investment Agreement" at the Trade and Industry Department Hong Kong website, [https://www.tid.gov.hk/english/cepa/legaltext/files/cepa14\\_a2.pdf](https://www.tid.gov.hk/english/cepa/legaltext/files/cepa14_a2.pdf)

exceptions do not mean that Hong Kong investors are completely excluded from investing in these sectors, but should rather indicate that investment should take place in a joint form between Hong Kong and Mainland investors with the latter owning more than 50% of the total shares (majority of shares) and the latter being the controlling shareholder.

The provisions on investment protection and facilitation apply to services and non-services sectors. To provide better investment protection for Hong Kong investors and investments, measures such as restriction on expropriation of investments, loss compensation, investment transfer abroad and return, and reduction of requirements for investments have been introduced. In addition, the agreement contains a mechanism for investment dispute settlement<sup>14</sup> when a dispute arises. Such mechanism includes resolution of disputes through amicable consultation between the parties, complaint handling organizations from both sides, the Committee on Investment, mediation, and administrative review following the laws of either party.

The agreement lists some criteria which investors must fulfill in order to be classified as "Hong Kong Investor". According to the Trade and Industry Department of Hong Kong, an investor is defined as "one side, or a natural person or an enterprise of one side, that seeks to make, is making or has made a covered investment<sup>15</sup>". Investors from Hong Kong, whether they are enterprises or natural persons, are offered preferential treatment by the Mainland if they fulfill the following requirements:

- ❖ In case of a business entity, a Hong Kong investor is an entity that is organized or constituted by Hong Kong laws. In case of a natural person, a Hong Kong investor refers to a Hong Kong permanent resident.

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<sup>14</sup> For detailed information, see "Mechanism for Settlement of Investment Disputes" at the Trade and Industry Department Hong Kong website, <https://www.tid.gov.hk/english/cepa/investment/dispute.html>

<sup>15</sup> According to the Trade and Industry Department of Hong Kong, "covered investment" is defined as "an investment in its area that an investor of the other side owns or controls, directly or indirectly, and exists on the date of entry into force of the Investment Agreement or is made or acquired thereafter".



- ❖ To be granted the preferential treatment for admission of investment, a Hong Kong firm wishing to invest in the Mainland must apply to the Trade and Industry Department for a "Hong Kong Investor Certificate" (HKI Certificate). After obtaining such certificate, the investing firm shall apply to Mainland authorities for investment in the Mainland.
- ❖ Investors who are already investing in the Mainland are not required to apply for the HKI Certificate but are subject to specific requirements of substantive business operation. However, if these investors conduct new investments in non-services sectors which are granted preferential treatment in the Mainland, an application for the HKI Certificate is needed. Similarly, natural persons or investors who conduct investment not in the form of "commercial presence" but in forms such as purchasing financial products, properties, or other forms of intangible assets, as well as investors who invest in non-services sectors that are not granted preferential treatment, do not have to acquire the HKI Certificate.

#### **2-4 Economic and technical cooperation**

In June 2017, the Mainland and Hong Kong signed the Agreement on Economic and Technical Cooperation (Ecotech Agreement) to modify and enhance the economic and technical cooperation activities of the CEPA as a response to the ongoing development trends in both sides. The Ecotech Agreement also incorporates aspects of the recent "One Belt, One Road" initiative of Mainland China, encouraging Hong Kong's economic integration into important national development strategies of the Mainland.

The parties of the agreement agreed to promote cooperation in 22 areas including the following: deepening cooperation in economic and trade areas of the "Belt and Road" Initiative; cooperation in legal and dispute resolution services; culture; education; Intellectual Property; deepening cooperation in Pan-Pearl River Delta region; trade and investment promotion; mutual recognition of professional qualifications; financial

cooperation; accounting; environment; electronic commerce; trademark and branding; supporting the participation of Hong Kong in the development of Pilot Free Trade Zones; quality supervision, inspection and quarantine; tourism; convention and exhibition; innovation and technology; small and medium enterprises; traditional Chinese medicine and Chinese medicinal products; deepening cooperation between Hong Kong and Qianhai, Nansha and Hengqin; and cooperation in transparency.<sup>16</sup>

### **III. The EFCA between Mainland China and Taiwan**

Vastly different from the CEPA, the ECFA represents an FTA between two rivalling political regimes who do not recognize one another officially and sovereign disputes are very frequent since the end of the Chinese Civil War in the year 1949, when the People's Republic of China has been established and the Republic of China has been settled in Taiwan.

Furthermore, the conclusion of the ECFA is not only important for the institutionalization of the legal framework governing Cross-Strait relations, but also plays a major role in forming trade relations across the Asian region through the Domino effect. As an example, it was believed that the ECFA negotiations would divert Chinese imports from South Korea to Taiwan, thus giving incentive to South Korea to conclude a similar FTA with China in order to secure its exports. This, in fact, had already happened when China and South Korea officially signed the China-Korea FTA in 2015.

#### **1. The background and establishment of the agreement**

At first, when China opened up in 1978 and desired an improvement in Cross-Strait relations, Taiwan maintained its Three-Noes policy which was first established by President Chiang Ching-kuo of the Republic of China in 1979. This policy was used to ban all interactions with the Communists, meaning no contact, no compromise and no negotiation.

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<sup>16</sup> For detailed information, see "Agreement on Economic and Technical Cooperation - Major New Cooperation Activities" at the Trade and Industry Department Hong Kong website, [https://www.tid.gov.hk/english/cepa/files/further\\_liberal\\_2017.pdf](https://www.tid.gov.hk/english/cepa/files/further_liberal_2017.pdf)

On the other hand, Taiwan has always been observing Hong Kong's economic and political development, and as Hong Kong shares some similarities with Taiwan, the latter has regarded the former as a qualified model of how to interact with China. As Hong Kong's economic integration with China accelerated after the reform and opening, Taiwan acknowledged Hong Kong's rapid economic surge. Hong Kong's economic success, especially its production based in Guangdong province, has a negative impact on Taiwanese export shares as competition between Taiwanese and Hong Kong products in overseas markets rises.

As a counteract, Taiwan decided to lift the ban on visits to China in 1987, which resulted in a dramatic surge in Cross-Straits trade and investment. Though economic interactions was encouraged, overall liberalization was very cautiously handled due to political and security concerns on the Taiwan side.<sup>17</sup> It was only until 2008, when President Ma Ying-jeou of the Nationalist Party had taken political leadership, that Taiwan eliminated bans on direct links with regards to air and shipping with China, but economic integration nevertheless happened at full speed. Within five years after Taiwan lifting bans, Taiwan became one of the largest investor in China following Hong Kong and China became the most popular outward FDI destination of Taiwanese investors. With regards to markets, China became the largest market for Taiwanese exported products by the early 2000s and much like Hong Kong, Taiwanese production had been largely relocated to China.<sup>18</sup> It is worth mentioning though, that the trade, investment and visitors flow from Taiwan to China was undeniably larger than the flow other way around, as Taiwan still restricted the influx of Chinese goods and people to avoid too much influence of China. Thus, Taiwan has a large trade surplus with China, which is being balanced by deficits in visitor's expenditures as well as bilateral investments.

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<sup>17</sup> Yun-Wing Sung, *The Emergence of Greater China: The Economic Integration of Mainland China, Taiwan, and Hong Kong* (Basingstoke and New York: Palgrave Macmillan, 2005), 61-8

<sup>18</sup> Yun-Wing Sung, *The Emergence of Greater China: The Economic Integration of Mainland China, Taiwan, and Hong Kong* (Basingstoke and New York: Palgrave Macmillan, 2005), 149.

As mentioned, after China's accession to the WTO in late 2001, China pursued a regional trade strategy by negotiating FTAs with various partners in the Asian Pacific. Among these, the China-ASEAN FTA had the greatest impact on Taiwan, as the ASEAN countries are very important trading partners of both China and Taiwan. At the same time, Taiwan failed to build its own trade network, mostly due to China's interference and opposition. Thus, to avoid increased marginalization in the trade field, Taiwan had great incentives to engage in an FTA with China to secure its trading position. In the absence of the ECFA, Taiwan's exports to China may not be sustainable as competition from the ASEAN countries' products rises. Furthermore, at the time of ECFA negotiations, Japan and South Korea also had interest in concluding a trade treaty with China, further prompting Taiwan to counteract its gradual marginalization by engaging with China.

At the same period, Nationalist Party Leader Ma Ying-jeou was elected president in Taiwan in early 2008, putting an end to the conservative policies of the prior pro-independence Democratic Progressive Party. Ma eagerly engaged in Cross-Strait negotiations and initiated two consecutive rounds of talks in the first year of his presidency, which lifted the previous ban on direct air and shipping links. Two additional rounds of talks took place one year later, during which agreements were made to enhance cooperation in the areas of finance and investment, other trade facilitation programs including customs inspections, and food safety. With the new political leadership and Taiwan's ambitions to remain competitive in the international trade arena, the negotiations on ECFA took less than one year until it was signed in late June 2010.<sup>19</sup> As for China, the ECFA is more than desired as it integrates Taiwan into the Mainland. China is also willing to offer much more concessions to Taiwan with the aim to realize its One-China principle.

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<sup>19</sup> Hsieh, Pasha L., "The China-Taiwan ECFA, Geopolitical Dimensions, and WTO Law" in *Journal of International Economic Law*, 14(1) 2011, 136-8.

## 2. Main provisions under the Early Harvest Program

As explained, the CEPA between China and Hong Kong is a full-fledged FTA which aims at abolishing all tariffs and non-tariff barriers of trade between the Parties. In contrast to the CEPA, the ECFA cannot be categorized as a comprehensive FTA yet, as it is merely a “framework agreement” or “interim agreement” under WTO law, which shall eventually lead to a full agreement between Taiwan and China. Nonetheless, the ECFA contains an Early Harvest Program (EHP) which eliminates or reduces tariffs for a number of selected goods over a time period of three years. The EHP has been implemented since January 2011 and covers approximately 15 percent of trade between Taiwan and China. Though the ECFA only provides selected goods with tariff reductions, the trade volume covered is still quite significant when for instance compared to the EHP of the China-ASEAN FTA, which only covers roughly 2 percent of trade between the signatories. In addition, the ECFA is probably the only EHP in the world that includes facilitation of services trade.<sup>20</sup> Apart from that, along with the signing of the ECFA, a Cross-Straits IPR (Intellectual Property Protection) Agreement was signed by the Parties. This is in sharp contrast to the CEPA, which does not cover any IPR clauses in detail. For further negotiations, the ECFA stipulates that within a period of six months after the ECFA taking effect, the Parties are required to begin talks on follow-up agreements including further liberalization of trade in goods and services, investment and, most importantly, a dispute settlement mechanism.

The EHP of ECFA is quite substantial but at the same time also very asymmetric. It covers tariff removal of 539 Taiwanese products and 267 Chinese products. With Chinese concessions both in the number of products and trade value exceeding Taiwanese concessions (Chinese concessions exceed Taiwanese concessions by nearly five times), the ECFA was said to be much more tailored to Taiwanese needs as to the needs of China. In fact, under the EHP China agrees to eliminate tariffs on 539 Taiwanese products with an import

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<sup>20</sup> Hsieh, Pasha L., “The China-Taiwan ECFA, Geopolitical Dimensions and WTO Law” in *Journal of International Economic Law*, 14(1) 2011, 140-3.

value of nearly US\$ 140 million, equivalent to more than 15 percent of Taiwanese exports to China. In contrast, Taiwan agrees to abolish tariffs on only 267 Chinese products with an import value of approximately 10 percent of Chinese exports to Taiwan.<sup>21</sup> What is more, the asymmetry is deepened by the discrepancy of concessions concerning the agricultural sector, wherein China agrees to grant preferential tariff to 18 Taiwanese products while Taiwan will maintain its MFN-violating ban on more than 800 Chinese products and declares no intention to lower such tariffs for more than 1400 such goods.<sup>22</sup>

Concerning the liberalization of services under the EHP, the provisions on both sides are much more restrictive. Among all liberalized sectors, the liberalization in the banking services is the most significant. Chinese banks are now allowed to establish branches in Taiwan to engage in New Taiwan Dollar businesses and as an exchange, Taiwanese banks are provided the opportunity to do the same in China.<sup>23</sup>

In overall, the CEPA covers almost every aspect of trade and investment cooperation between Hong Kong and China, while the ECFA is a tentative framework agreement which cautiously handles Cross-Strait trade between Taiwan and China. The latter provides the Parties with limited trade liberalization and highlights IPR protection and the importance of dispute settlement mechanism.

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<sup>21</sup> Hsieh, Pasha L., "The China-Taiwan ECFA, Geopolitical Dimensions and WTO Law" in *Journal of International Economic Law*, 14(1) 2011, 143.

<sup>22</sup> Hsieh, Pasha L., "The China-Taiwan ECFA, Geopolitical Dimensions and WTO Law" in *Journal of International Economic Law*, 14(1) 2011, 143.

<sup>23</sup> Hsieh, Pasha L., "The China-Taiwan ECFA, Geopolitical Dimensions and WTO Law" in *Journal of International Economic Law*, 14(1) 2011, 144-5.

#### IV. Main differences between the CEPA and the ECFA (legal text)

**Table 1.** Legal differences between the CEPA and the ECFA

	<b>CEPA</b>	<b>ECFA</b>
<b>Name of the FTA</b>	Closer Economic Partnership <i>Arrangement</i>	Economic Cooperation <i>Framework Agreement</i>
<b>Signatories and Negotiation</b>	<i>Government of the People's Republic of China and the Government of the Hong Kong Special Administrative Region of the People's Republic of China.</i>	<i>Straits Exchange Foundation in Taiwan (SEF) and the Association for Relations Across the Taiwan Straits in Mainland China (ARATS)</i>
<b>Preamble</b>	<i>Joint economic prosperity and development</i>	<i>Equality</i>
<b>Objectives</b>	Reduction or elimination of <i>substantially all</i> barriers in trade of goods and services	Reduction or elimination of a <i>substantial majority</i> of barriers in trade of goods and liberalizing a <i>large number of sectors</i> in trade in services
<b>Principles</b>	<i>"One Country, two systems"</i>	<i>None</i>
<b>Non-application of specific provisions in China's WTO accession legal documents</b>	❖ <i>Art. 15</i> <sup>24</sup> (Antidumping and Countervailing measures) and <i>Art. 16</i> <sup>25</sup>	<i>None</i>

<sup>24</sup> Price Comparability in Determining Subsidies and Dumping: In determining price comparability the importing WTO Member shall use either Chinese prices or costs for the industry under investigation or a methodology that is not based on a strict comparison with domestic prices or costs in China if the producers under investigation cannot clearly show that market economy conditions prevail in the industry producing the like product with regard to manufacture, production and sale of that product.

<sup>25</sup> Transitional Product-Specific Safeguard Mechanism

	<p>(Safeguard measures) of the "Protocol on the Accession of the PRC to the WTO"</p> <ul style="list-style-type: none"> <li>❖ <i>Paragraph 242<sup>26</sup> of "Report of the Working Party on the Accession of China"</i></li> </ul>	
<b>Trade in Goods:</b>		
<b>Tariff</b>	<ul style="list-style-type: none"> <li>❖ HK applies <i>zero tariff</i> to all imported goods of Mainland origin</li> <li>❖ China applies <i>zero tariff</i> to all imported goods of HK since 1 Jan 2006</li> </ul>	<p><i>Early Harvest Program</i> since 2011</p> <ul style="list-style-type: none"> <li>❖ <i>267 products</i> in the product list on the Taiwanese side</li> <li>❖ <i>539 products</i> in the product list on the Mainland side</li> </ul>
<b>Tariff rate quota &amp; non-tariff measures</b>	<ul style="list-style-type: none"> <li>❖ <i>No non-tariff measures inconsistent</i> with WTO rules</li> <li>❖ <i>No tariff rate quota</i> applied to HK products by Mainland</li> </ul>	<i>Under consultation: TBT and SPS etc.</i>
<b>Anti-dumping</b>	<i>No anti-dumping measures</i> to goods imported and originated from other side	<i>Not mentioned</i>

<sup>26</sup> Textile-specific safeguard provisions



<b>Subsidies &amp; countervailing</b>	<i>No countervailing measures to goods imported and originated from each other</i>	<i>Under consultation: Agreement on Implementation of Art. VI of the GATT 1994, the Agreement on Subsidies and Countervailing Measures, Agreement on Safeguards of the WTO applicable</i>
<b>Safeguard</b>	In case of serious injury or threat to cause serious injury, <i>consultations</i> to reach an agreement.	See <i>Subsidies and Countervailing</i>
<b>Rules of Origin</b>	<ul style="list-style-type: none"> <li>❖ <i>Wholly obtained goods</i></li> <li>❖ Not wholly obtained goods only in case of "<i>substantial transformation</i>"</li> </ul> <p>"Substantial transformation" means:</p> <ul style="list-style-type: none"> <li>❖ Manufacturing or processing operations</li> <li>❖ Change in tariff heading</li> <li>❖ <i>Value-added content</i> <math>\geq</math> 30% of the FOB value</li> <li>❖ <i>Other methods</i> agreed by both sides in determining</li> </ul>	<ul style="list-style-type: none"> <li>❖ <i>Wholly obtained goods</i></li> <li>❖ Not wholly obtained goods only in case of "<i>specific rules</i>"</li> </ul> <p>"Product specific rules" means:</p> <ul style="list-style-type: none"> <li>❖ Change in tariff classification</li> <li>❖ <i>Regional value content (RVC)</i> <math>\geq</math> 90%</li> <li>❖ <i>No other methods</i></li> </ul>

	"substantial transformation"	
<b>Trade in Services:</b>		
<b>Specific Commitments</b>	<p>Specific commitments set out in <i>Annex 3 of CEPA II</i></p> <p>Wide range of liberalization for sectors from business, financial, education, to cultural and telecommunication sector, qualification examinations for professionals, trade mark, patent, and individually owned stores)</p>	<p><i>Early Harvest Program</i> since 2011:</p> <p>Liberalization in sectors listed in <i>Annex 4 of ECFA</i></p> <ul style="list-style-type: none"> <li>❖ <i>Taiwan</i>: 11 sectors in non-financial services and a few sectors in the financial services sector including banking and other financial services (excluding securities, futures and insurance)</li> <li>❖ <i>Mainland</i>: 11 sectors in non-financial services and a few sectors in financial services including banking and other financial services (including securities, futures and insurance)</li> </ul>
<b>Service supplier</b>	<ul style="list-style-type: none"> <li>❖ <i>Natural person</i>: citizen of PRC or permanent resident of HK SAR.</li> <li>❖ <i>Juridical person</i>: any</li> </ul>	<ul style="list-style-type: none"> <li>❖ <i>Natural person</i>: person holding the identity certificate of either Party</li> </ul>

	<p>legal entity duly constituted or organized under applicable laws of Mainland or HK.</p> <ul style="list-style-type: none"> <li>❖ Specific criteria for juridical service suppliers</li> <li>❖ <i>Contractual service provider</i> is entitled to preferential treatment temporarily</li> </ul>	<ul style="list-style-type: none"> <li>❖ <i>Juridical person</i>: any entity that is constituted in either Party according to its regulations</li> <li>❖ Specific criteria for juridical service suppliers</li> </ul>
<b>Agreement on Trade in Services</b>	<ul style="list-style-type: none"> <li>❖ National Treatment and Most Favoured Treatment for all services sectors (exceptions for reserved restrictive measures, telecommunications, cultural services)</li> <li>❖ Investment facilitation</li> </ul>	Signed but <i>not ratified</i> on Taiwan side due to mass protests
<b>Financial cooperation</b>	<p>Strengthened cooperation in the areas of banking, securities and insurance.</p> <ul style="list-style-type: none"> <li>❖ <i>Mainland</i>: using HK's superior financial services sector to restructure and develop its own</li> </ul>	<i>No specific clause</i>

	<ul style="list-style-type: none"> <li>❖ <i>HK</i>: obtains large Mainland market by being granted preferential treatment for companies operating in the financial sector</li> </ul>	
<b>Cooperation in tourism</b>	<i>Individual Visitors Scheme</i> allows residents in Guangdong Province to visit HK individually	<i>No specific clause</i>
<b>Mutual recognition of professional qualifications</b>	Sectors for mutual recognition: accounting, construction, taxation, engineering, real estate, printing	<i>None</i>
<b>Trade and Investment Facilitation</b>		
	<p><i>Agreement on Economic and Technical Cooperation</i></p> <ul style="list-style-type: none"> <li>❖ Facilitation of trade procedures such as customs clearance, commodity inspection and quarantine, quality and standardization</li> <li>❖ E-commerce</li> <li>❖ Transparency in laws and regulations</li> </ul>	<p><i>Investment (Chapter 2 Article 5)</i> under consultation:</p> <ul style="list-style-type: none"> <li>❖ Investment protection</li> <li>❖ Transparency</li> <li>❖ Reduce restrictions on mutual investments</li> </ul> <p><i>Economic Cooperation (Chapter 3 Article 6):</i></p> <ul style="list-style-type: none"> <li>❖ Protection of intellectual property</li> </ul>

	<ul style="list-style-type: none"> <li>❖ Cooperation in Chinese traditional medicine</li> <li>❖ Protection of intellectual property</li> <li>❖ Cooperation in education</li> <li>❖ Mutual recognition of testing and certification results</li> </ul>	<ul style="list-style-type: none"> <li>❖ Customs procedures</li> <li>❖ E-commerce</li> <li>❖ Small and medium-sized enterprises cooperation and enhance competitiveness</li> </ul>
<b>Other provisions</b>		
<b>Exceptions</b>	Exception measures consistent with the rules of the WTO allowed	Same as CEPA
<b>Dispute settlement</b>	<i>None</i>	<ul style="list-style-type: none"> <li>❖ Establishment of appropriate dispute settlement procedures <i>under consultation</i></li> <li>❖ Before that: dispute settlement through consultations by the <i>Cross-Straits Economic Cooperation Committee</i></li> </ul>
<b>Institutional arrangements</b>	<ul style="list-style-type: none"> <li>❖ <i>Joint Steering Committee</i></li> <li>❖ Functions: supervision of implementation of CEPA, interpretation of provisions of CEPA, resolving disputes,</li> </ul>	<ul style="list-style-type: none"> <li>❖ <i>Cross-Straits Cooperation Committee</i></li> <li>❖ Functions: Conclusion of consultations, monitoring and evaluating the</li> </ul>

	<p>drafting additions and amendments, etc.</p> <ul style="list-style-type: none"> <li>❖ At least meet once a year, or special meetings within 30 days upon request</li> <li>❖ Decision-making by consensus.</li> </ul>	<p>implementation of the ECFA, interpreting provisions, settling any disputes</p> <ul style="list-style-type: none"> <li>❖ Meeting regularly on a semi-annual basis or ad hoc meetings (last meeting in 2017)</li> </ul>
<b>Termination</b>	<i>None</i>	<ul style="list-style-type: none"> <li>❖ Notification in writing</li> <li>❖ Consultation within 30 days of notice</li> </ul>

### 1. The Naming of the respective FTAs

Before proceeding to detailed explanation of the divergences in substantive contents between the CEPA and the ECFA, it is worth noting that there is a vast difference in the naming of the two FTAs.

The CEPA (*Closer Economic Partnership Arrangement*) represents a domestic "arrangement" between two regions of the same country, whereas the ECFA (*Economic Cooperation Framework Agreement*) is explicitly called an "agreement" between two different countries. When the CEPA was signed, the authorities agreed upon using the term "arrangement" instead of "agreement" on purpose, mainly to avoid giving the impression that the CEPA has the status of an international agreement. In vast contrast to this, when Taiwan and China were discussing the possibility of an FTA, the ECFA was initially named "Comprehensive Economic Cooperation Agreement" or "CECA"<sup>27</sup>, however this

<sup>27</sup> Cooke, Terry, "Cross-Strait Matrix: The Economic Cooperation Framework Agreement" in *China Brief*, Vol.9, Issue:11, 2009.

abbreviation was seen as being too similar to the CEPA between China and Hong Kong. Taiwan insisted that CECA being changed to ECFA, not only to avoid confusion resulting from similar names of the FTAs, but also to avoid giving the impression that CECA would follow the footsteps of CEPA and undermine Taiwan's political sovereignty.

These concerns were not unfounded, as the ECFA has often been compared with the CEPA particularly because it was suspected that the conclusion of the ECFA is likely to deteriorate Taiwan's sovereignty by attracting it to the trap of "One Country, two systems" policy which was exactly the case with Hong Kong by signing the CEPA in 2003. In fact, the PRC government wanted to conclude a PTA with Taiwan, as the experience of signing the CEPA with Hong Kong had resulted in greater cooperation in economic, cultural and political aspects. Thus, the PRC wished to path the way for a closer economic cooperation first, while gradually turning it into a political cooperative relation. This is why in February 2009, when the Taiwanese National Security Council's Secretary General, Su Chi, for the first time officially announced that the Taiwanese government was planning to sign the CECA with China, this announcement immediately grasped public attention.<sup>28</sup> The announcement was so sudden that the Anti-Chinese associations had no time to organize counter initiatives, only leaving the industry associations in favor of the Cross-Strait agreement to voice their support. However, two months later when public debate was warmed up, opposing voices under the lead of the Democratic Progressive Party began to put pressure on the Nationalist Ma administration. This resulted in a number of adjustments to the CECA proposal, among which the changing of the name of the agreement from CECA to ECFA played the most significant role.

## **2. Signing Parties and Negotiation Process:**

The signing Parties and negotiation pattern to the CEPA and to the ECFA are quite different. As for the CEPA, the signing took place between the Vice Minister of Commerce,

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<sup>28</sup> Cooke, Terry, "Cross-Strait Matrix: The Economic Cooperation Framework Agreement" in *China Brief*, Vol.9, Issue:11, 2009.

representing the *Government of the People's Republic of China*, and the Financial Secretary representing the *Hong Kong Special Administrative Region of the People's Republic of China*. The negotiation of the CEPA was based on the consensus and mutual acceptance of the "*One Country, two systems*" arrangement between Hong Kong and the Mainland. It was signed on 29 June 2003 and ratified on 1 January 2004.

The initial negotiations of a possible FTA between Hong Kong and China were spurred by business circles in Hong Kong as well as by the *Hong Kong General Chamber of Commerce* (HKGCC) in a response to an unstable and unpredictable future of the Hong Kong economy resulting from the Asian financial crisis and consequent economic downturn in 2001 as well as the devastating effects of the SARS epidemic. Another important purpose was for Hong Kong to secure its position as a gateway between foreign investors and Mainland China. However, after China's accession to the WTO in late 2001, Hong Kong feared that it will lose its relative advantages when China opens its market to all WTO members. An FTA before China's opening to the world could serve Hong Kong's purpose. As the need to recover Hong Kong's economy strengthened, the government of Hong Kong picked up the initiative proposed by the HKGCC and reported its intentions to the central government of China. As for China, an FTA with Hong Kong so soon after its accession to the WTO had its own merits. As the Chinese were inexperienced in conducting trade with foreign nations, first opening up to Hong Kong would provide them with the latter's vast experiences and the latter would also serve as a valid model to develop Chinese business sectors enough to face future foreign competition. Last but not least, China also needed an initiative linking Hong Kong closer to the Mainland both politically and economically. The CEPA was more of a symbolic move that proved China's efforts to maintain Hong Kong's prosperity, although critics saw it as a kind of compensation for the very restrictive political reforms after Hong Kong reverted to Chinese rule in 1997.<sup>29</sup>

As a result, in the absence of major public debates concerning the conclusion of the

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<sup>29</sup> Cabrillac, Bruno, "A Bilateral Trade Agreement Between Hong Kong and China: CEPA" in *China Perspectives*, Issue 54, 2004.



CEPA, the negotiations took only eighteen months until the CEPA was signed.

As for the ECFA, the signatories and the negotiation process were much more complicated. First of all, the agreement was signed between two semi-official institutes namely the *Straits Exchange Foundation* (SEF) of Taiwan and the *Association for Relations Across the Taiwan Strait* (ARATS) on June 29, 2010 along with a Cross-Straits IPR Agreement. Both agreements were ratified in September 2010 and the EHP under ECFA took effect on January 1, 2011.

Before the negotiations of ECFA took place, Cross-Strait interactions have been undertaken through unilateral actions of one side awaiting responsive actions of the other side. After 1991, when Taiwan officially declared that it will abandon political contact with China, it nonetheless announced that it will continue unofficial exchanges with China. For this purpose, the Taiwanese government established the SEF to handle Cross-Strait interactions with China, and one year later, the Chinese government set up a semi-official body called ARATS to form an appropriate counterpart of the SEF. Since their establishment, the SEF and the ARATS have been in charge of Cross-Strait issues. The SEF-ARATS process was, however, shut down when the Democratic Progressive Party in Taiwan gained political leadership in 2000.

After 11 years of silence, Nationalist president Ma Ying-jeou revived the SEF-ARATS process to start negotiations on ECFA. The first mentioning of a possible FTA between Taiwan and China emerged during Ma's electoral campaign leading to the presidential election in February 2008. The issue was further supported by eliminating bans on direct air and shipping links in June 2008 any also by the talks between the Nationalist Party's Chairman Lien Chan at that time and Chinese President Hu Jintao at the Asia-Pacific Economic Cooperation (APEC) meeting in November 2008. Formal talks about CECA (later ECFA) surfaced in a more serious form in March 2009.<sup>30</sup> At that time, Taiwanese incentives

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<sup>30</sup> Cooke, Terry, "Cross-Strait Matrix: The Economic Cooperation Framework Agreement" in *China Brief*, Vol.9, 38

to conclude a trade pact with China were at peak as the global economy worsened. It was then when Ma's administration launched aggressive campaigns promoting the pros of the ECFA concept among the public, presenting the ECFA as "inevitable" and as a stepping stone for Taiwan to recover its economy and boost its GDP by 1.4 percent, and most importantly, as a crucial necessity to put an end on the marginalization process which Taiwan was forced to endure after China's accession to the WTO and its subsequent conclusion of multiple regional FTAs. However, it was not without efforts to conclude the ECFA. As public debate over this issue rose, the Ma administration had to make several adjustments in order to gain full support and belief from the Taiwanese people. As mentioned earlier, the naming of the ECFA was one important part of the adjustment process. In addition to that, given Taiwan's democratic society, the public demanded a fully transparent negotiation process and public consensus on the concept of the ECFA before the actual signing of the agreement with China.<sup>31</sup>

Talks of a Cross-Strait Common Market emerged subsequently. This concept, originally developed by Vice-President Siew Wan-chang during Ma's presidency, was inspired by the early EU model, which had its focus on trade liberalization, trade reduction and harmonization as pre-conditions for an eventual common market with a common currency, abolishment of borders and shared institutions. This model was very attractive for China as well, though China's aim was other than mere trade facilitation.<sup>32</sup> The talks on a common market, however, were later abandoned along with the Taiwanese people's objection of the conclusion of the trade in services agreement through the Sunflower Movement in 2014.

Apart from political difficulties, content-wise and legally-speaking, the Taiwanese government announced that the framework of the agreement was largely modeled on the

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Issue:11, 2009.

<sup>31</sup> Cooke, Terry, "Cross-Strait Matrix: The Economic Cooperation Framework Agreement" in *China Brief*, Vol.9, Issue:11, 2009.

<sup>32</sup> Cooke, Terry, "Cross-Strait Matrix: The Economic Cooperation Framework Agreement" in *China Brief*, Vol.9, Issue:11, 2009.

"China-ASEAN" Framework Agreement in 2002. It is, however, doubtful given that there are considerable differences between China-ASEAN members and Taiwan. As Mainland China and the ten ASEAN members accessed to the WTO as developing countries, they are enabled to conclude preferential trade agreements in a more flexible manner (for instance by incorporating the "enabling clause") often in the name of a "Framework Agreement" stipulating the preliminary scope of trade and services being included in the future agreement and often accompanied by *Early Harvest Programs*<sup>33</sup>. Taiwan, however, renounced its status as a "developing country" upon its joining of the WTO. Thus, the argument that the ECFA has been modeled on the *China-ASEAN Framework Agreement* can be misleading. Given the circumstances, the only legal basis for the content stipulated in the ECFA shall be Article XXIV of the GATT. But given the fact that the Parties to the ECFA do not aim at liberalizing "substantial all trade" in goods and services in the immediate future but rather wishes to "gradually reduce or eliminate" trade barriers in a "substantial majority" of goods and services<sup>34</sup> (ECFA main text, chapter 1, article 2), the ECFA shall represent an "interim agreement" pursuant to paragraph 5 of Article XXIV of the GATT. If this is the case, paragraph 5(c) of Article XXIV stipulates that "any interim agreement shall include a plan and a schedule for the formation...within a reasonable length of time". The definition of "reasonable length of time" can further be derived from "Understanding on the interpretation of Article XXIV of the GATT 1994" and usually "shall exceed ten years only in exceptional cases". According to this interpretation, Taiwan and China should eliminate trade barriers within ten years of time after the conclusion of the ECFA. However, given the rather slow progress of follow-up treaties under the ECFA (for instance an Agreement on Trade in Goods is still under consultation and an Agreement on Trade in Services has been signed but not ratified on the Taiwan side due to political protests arising from its citizens), it is doubtful

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<sup>33</sup> Roberto V. Fiorentino, Luis Verdeja, Christelle Toqueboeuf, "The Changing Landscape of Regional Trade Agreements: 2006 Update" in *Discussion Paper No 12 of Regional Trade Agreements Section, Trade Policies Review Division*, WTO.

<sup>34</sup> For detailed information, see Article 2 of the ECFA.

whether further development can be expected in any near future. Besides, the ECFA does not even contain a plan or time schedule for further negotiation processes, making it a "*pending trade pact*"<sup>35</sup> lacking precise commitments apart from the *Early Harvest Program*.

Comparing the CEPA and the ECFA, it is clear that whereas the CEPA was negotiated in a swift manner as a plan to recover both parties' economies, the ECFA underwent a much more complex negotiation process. Although Taiwan's incentives were also led by economic interests, the public was not willing to trade in Taiwan's sovereignty in exchange for economic benefits and succeeded in persuading the Taiwanese government to carefully think about its decision. In contrast, Hong Kong's public did not or could not raise objection to the concept of CEPA when it was being negotiated between the governments, although the conclusion of an arrangement such as the CEPA clearly undermined Hong Kong's political flexibility even further.

### **3. Preamble**

An important difference between the two FTAs can also be found in the Preamble in the main legal text of the respective agreements. In the legal text of the CEPA, the Preamble states that the arrangement between Mainland China and Hong Kong is to "promote *joint* economic prosperity and development of the two sides" (CEPA main text, Preamble), emphasizing the "*joint*" economic development of both sides, but at the same time also indicating that there is a much stronger bond between the two Parties that leads them to a future with joint economic prosperity.

In contrast to this "joint" characteristics under the CEPA, the Preamble of the ECFA states that the agreement between Mainland China and Taiwan should "adhere to the principles of *equality*, reciprocity and progressiveness" and should be carried out "*in line with the basic principles of the WTO*" and "*in consideration of the economic conditions of the two Parties*" (ECFA main text, Preamble). Given the fact that the Taiwanese Government,

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<sup>35</sup> Tsai-Lung (Honigmann) Hong, "*ECFA: A Pending Trade Agreement? Also a Comparison to CEPA*"

at the time of negotiation, was very cautious about any wording that could suggest deterioration of Taiwan's sovereignty, the wording of these statements suggests that the ECFA is more based on "equality" between the two Parties, which could be interpreted as keeping the two Parties distinct from each other, while striving for economic cooperation, much like an ordinary agreement between two distinct countries. In addition, according to official remarks by the Mainland Affairs Council of the Taiwanese government, the inclusion of the wording "*in consideration of the economic conditions of the two Parties*" in the Preamble was to safeguard Taiwan's interests and economic identity. The Taiwanese government promised to not include an exact timeline for liberalization of trade with China in order to carefully select the product industries and categories to liberalize. It further promised not to fully lift the current restrictions on Chinese agricultural and industrial import products, to protect the interests of local producers. To calm opposition parties, the Taiwanese government also reassured to the public that the possibility of a "One-China market" will absolutely not happen after signing the ECFA as the government will ensure taking small and careful steps to liberalize trade with China and will only allow trade liberalization in industries that are beneficial to Taiwanese people.<sup>36</sup>

#### **4. Objectives**

The objectives stated in the main legal text of the two FTAs is also quite different.

As for the CEPA, the objectives agreed upon are to "reduce or eliminate tariff and non-tariff barriers on substantially all the trade in goods" and to liberalize trade in services by "reducing or eliminating *substantially all* discriminatory measures" (CEPA main text, chapter 1, article 1.1 & 1.2). This suggests that the implementation of the CEPA is aimed at eliminating eventually "*all*" trade barriers in trade in goods as well as in trade in services.

As for the ECFA, however, the objectives the two Parties aim for are to "gradually reduce or eliminate tariff and non-tariff barriers to trade in a *substantial majority* of goods"

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<sup>36</sup> "Remarks by Minister Lai on the Preparatory Consultations for the Economic Cooperation Framework Agreement" in *Mainland Affairs Council, the Fifth Chiang-Chen Talks*, June 24, 2010.

and as for trade in services, the goal is to "gradually reduce or eliminate restrictions on a *large number* of sectors" (ECFA main text, chapter 1, article 2). The wording in this part may suggest that as for the agreement between Taiwan and the Mainland, the range of liberalization of trade is not as vast as in the case of the CEPA. Instead of reducing or eliminating *all* trade barriers, the ECFA focusses on reducing or eliminating trade barriers merely to a chosen batch of goods, and as for trade in services, the ECFA only tries to lift restrictions on a selected number of services sectors, while the CEPA's goal is to reduce or eliminate *all* discriminatory measures. These sentences again strengthen the view that compared to the CEPA, the trade liberalization of the ECFA is much more conservative.

## **5. Principles**

An important legal clause which greatly differentiates the CEPA from the ECFA is imbedded in Chapter 1 Article 2 of the CEPA. This specific article states five important principles which both Parties have to abide. Among the five principles, one requires the two Parties to abide by the "one country, two systems" principle. This principle is significant in differentiating the CEPA from the ECFA as the latter does not possess such a principle. The fact that the CEPA particularly outlines this principle suggests that Hong Kong, at least at the time of concluding the arrangement, had accepted to abide by the "*one country, two systems*" policy which was implemented by the Mainland as a means to signal political unification with Hong Kong as well as Taiwan. While the latter does not accept this principle and remains its de facto independence, Hong Kong - at least as seen from the CEPA - is regarded as part of the Chinese territory in both economic and political aspects.

## **6. Non-application of specific provisions in China's WTO accession legal documents**

Another legal clause which demonstrates how the Mainland treats Hong Kong and Taiwan differently, can be derived from the content of Chapter 1 Article 4 which is related to the non-application of specific provisions in China's WTO accession legal documents.

Article 4 reads as follows: "the two sides recognize that through over 20 years of reform and opening up, the market economy system of the Mainland has been continuously improving, and the mode of production and operation of Mainland enterprises is in line with the requirements of a market economy. The two sides agree that Articles 15 and 16 of the *Protocol on the Accession of the People's Republic of China to the WTO* and paragraph 242 of the *Report of the Working Party on the Accession of China* will not be applicable to trade between the Mainland and Hong Kong."

Thus, according to this Article, Hong Kong must accept the Mainland as a *market economy*. Article 15<sup>37</sup> (Antidumping and Countervailing measures) and Article 16<sup>38</sup> (Safeguard measures) of the "Protocol on the Accession of the PRC to the WTO", as well as paragraph 242<sup>39</sup> of "Report of the Working Party on the Accession of China" are not applicable under the CEPA, meaning that as for the trade between the Mainland and Hong Kong, no anti-dumping and countervailing measures, and no safeguard measures can be used, regardless of the extent of injury that may occur from the trade between the two Parties.

The ECFA does not possess any clause preventing the two Parties to use anti-dumping measures or safeguard measures.

## **7. Provisions concerning the Trade in Goods**

### **7-1 Tariff**

With respect to the reduction of tariffs, the CEPA has been amended several times, finally reaching zero tariff on all imported goods of Hong Kong origin to Mainland China, while the ECFA is still in the use of an Early Harvest Program (hereafter "EHP") for trade in goods as stipulated in Article 7 of the agreement.

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<sup>37</sup> Price Comparability in Determining Subsidies and Dumping: In determining price comparability the importing WTO Member shall use either Chinese prices or costs for the industry under investigation or a methodology that is not based on a strict comparison with domestic prices or costs in China if the producers under investigation cannot clearly show that market economy conditions prevail in the industry producing the like product with regard to manufacture, production and sale of that product.

<sup>38</sup> Transitional Product-Specific Safeguard Mechanism

<sup>39</sup> Textile-specific safeguard provisions

Under the CEPA, Hong Kong promised to continue applying zero tariff to all imported goods of Mainland origin. The initial deal was that from 1 January 2004, the Mainland will apply zero tariff to import of goods of Hong Kong origin listed in Table 1 of the Annex 1 of the original CEPA arrangement. The initial list of Hong Kong origin products applicable to zero import tariff by the Mainland consisted of 273 different products. This number already included important product segments of Hong Kong’s manufacturing industries such as electronics, clothing, jewelry and watches and so on and so forth. The number was then extended several times until in 1 January 2006, the zero import tariff treatment was applied to all imported goods of Hong Kong origin. Whether a product fulfills the CEPA Rules of Origin requirement and is thus eligible for preferential treatment is determined by whether the product type can pass the respective examination after submitting the application “Certificate of Hong Kong Origin”. The Mainland authorities then will determine whether a product type can be regarded as originating from Hong Kong or not, depending on the ratio of *substantial transformation*, which will be discussed later under the headings of “Rules of Origin”. As of April 30, 2018, the statistics on the granting of Certificate of Hong Kong origin shows that an average percentage of 97 of applying product types received approval, suggesting that the actual admission procedure is likely not to be very strict on the Chinese side.

**Table 2.** Statistics on Certificate of Hong Kong Origin – CEPA, as of 30 April 2018:

<b>Product Types</b>	<b>Cumulative No. of CO(CEPA) Applications Received</b>	<b>Cumulative No. of CO(CEPA)s Approved</b>
Food and Beverages	48,526	47,242
Food Residues and Animal Fodder	344	341
Mineral Products	1	-
Chemical Products	9,558	9,371



Pharmaceutical Products	3,699	3,645
Cosmetics	389	366
Plastics and Plastic Articles	35,843	35,389
Leather and Fur skin Articles	1,511	1,480
Paper and Printed Articles	4,109	4,012
Textiles and Clothing	28,984	28,224
Glass and Glassware	2	-
Jewelry and Precious Metals	782	775
Base Metal Products	6,478	6,438
Machinery and Mechanical Appliances	1,069	1,042
Electrical and Electronic Products	2,224	2,161
Optical, Photographic and Cinematographic Instruments & Parts	1,043	973
Medical Instruments and Massage Apparatus	18	17
Measuring and Checking Instruments and Parts	167	167
Clocks and Watches and Parts	1,038	1,012
Furniture	36	34
Toys and Games or Sports Requisites	1	1
Miscellaneous	5	5

<b>Total</b>	<b>163,697</b>	<b>160,300</b>
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*(Source: Website of Trade and Industry Department of the HKSAR)*

The significant facilitation in trade in goods, realized by the removal of tariffs, however, is not the main purpose of the CEPA at least in Hong Kong’s view. The FTA was not designed to boost Hong Kong’s manufacturing sector after decades of decline, because Hong Kong’s manufacturing sector was not very large in size to begin with and production costs were much higher than compared to China, making the Hong Kong manufacturing sector specializing in trade in services rather than trade in goods. Representing the service hub in China’s trade, Hong Kong is often referred to as a “services economy”. The services sector accounts for more than 90 percent of Hong Kong’s GDP, while the agricultural sector has almost no contribution to its GDP at all due to scarcity in natural resources. But, although the manufacturing sector accounts for only 7 percent of Hong Kong’s overall GDP, exports and imports of merchandises to and from China have surged over the years after CEPA was implemented.

The CEPA made possible for Hong Kong to get access to the vast market of Mainland China while offering Hong Kong manufacturers to enjoy the significantly lower production costs especially in the Guangdong province that is closely located to Hong Kong and represents a popular destination for the establishment of production facilities. As such, trade in goods between Hong Kong and the Mainland have increased steadily, making China the largest import and export partner of Hong Kong, with a share in domestic exports of 45.6 percent as well as for re-exports (54.9 percent), and a share in imports of 47.8 percent as well as the main origin for re-exports (61.9 percent), according to the Trade and Industry Department of the HKSAR. Reciprocally, according to the Ministry of Commerce of the PRC, Hong Kong counts as the Mainland’s fourth largest trading partner and as one of its major export markets.

**Table 3.** Hong Kong's Exports to/Imports from China:

<b>Year</b>	<b>Import (US\$ thousand)</b>	<b>Import partner share (%)</b>	<b>Export (US\$ thousand)</b>	<b>Export partner share (%)</b>
2002	91,947,900.79	44.21	78,949,842.20	39.10
2003	101,082,788.49	43.34	95,446,079.80	41.73
2004	117,955,274.16	43.21	114,315,649.04	43.04
2005	134,965,924.70	44.96	130,425,877.77	44.65
2006	153,659,480.37	45.77	149,510,940.70	46.34
2007	170,556,001.12	46.08	168,603,725.67	48.26
2008	181,232,806.05	46.12	178,621,253.21	48.24
2009	161,214,307.02	45.77	164,285,682.66	49.87
2010	197,089,548.28	44.65	210,291,123.26	52.48
2011	220,581,981.94	43.18	246,581,686.78	54.13
2012	251,996,214.29	45.53	284,360,806.23	57.69
2013	266,876,652.91	42.95	320,687,678.11	59.92
2014	268,260,873.86	44.66	300,429,691.15	57.33
2015	261,109,483.50	46.69	287,481,665.80	56.31
2016	244,351,476.53	44.66	285,501,328.80	55.27

*(Source: World Bank Data)*

**Table 4.** China's Exports to/Imports from Hong Kong:

<b>Year</b>	<b>Import (US\$ thousand)</b>	<b>Import partner share (%)</b>	<b>Export (US\$ thousand)</b>	<b>Export partner share (%)</b>
2002	10,726,243.18	3.63	58,463,145.18	17.96
2003	11,118,661.38	2.69	76,274,373.62	17.41
2004	11,796,722.32	2.10	100,868,565.58	17.00

2005	12,224,784.36	1.85	124,473,251.85	16.34
2006	10,779,762.65	1.36	155,309,068.12	16.03
2007	12,804,323.87	1.34	184,438,213.74	15.12
2008	12,915,845.84	1.14	190,729,034.56	13.33
2009	8,711,578.90	0.87	166,216,920.15	13.83
2010	12,260,254.72	0.88	218,301,359.50	13.84
2011	15,492,482.95	0.89	267,983,736.81	14.12
2012	17,895,803.90	0.98	323,445,330.29	15.79
2013	16,206,575.26	0.83	384,497,866.93	17.41
2014	12,621,374.46	0.64	363,077,143.71	15.50
2015	12,745,813.19	0.76	330,462,787.18	14.54
2016	16,700,667.26	1.05	287,251,662.04	13.69

*(Source: World Bank Data)*

The rapid liberalization process of the CEPA was made possible mainly due to the complementary character of the Hong Kong-China trade relationship. While Hong Kong's economy almost exclusively focusses on services trade, China is still relying on the manufacturing sector for its economic growth, as will be discussed in later sections of "Trade in Services". Thus, as manufactured products are not in direct competition, the two Parties were able to liberalize trade in goods without major obstacles.

In contrast, the ECFA has yet to determine the exact range of liberalization of trade in goods. The Parties have however started the implementation of a EHP right after the ECFA was signed in 2010 and agreed upon conducting consultations on an agreement on trade in goods no later than six months after the ECFA enters into force. This supposed agreement on trade in goods has, however, not been concluded yet.

Vastly different from the CEPA, which stipulated detailed timelines to implement zero tariffs on imported goods originating from either side, the Taiwanese government worked hard to not incorporate such timelines into the process of trade liberalization under the ECFA. According to official remarks by the then Minister of the Mainland Affairs Council, Lai Shin-yuan, the Taiwanese government gained consent from the Chinese side that, after the negotiations on trade in goods had started, the signing Parties will not set any deadlines with regards to the completion of negotiations. Thus, even after signing the ECFA, Taiwan has the right to move forward gradually and in a planned manner, and will not be forced to fully liberalize trade within a distinct time period, which usually would be the case. In such way, Taiwan could select industries to open up, in accordance to the conditions and interests of the Taiwanese market, putting the initiative of the liberalization process into Taiwanese hands, which shall avoid Taiwan to be forced into the establishment of a “One-China market”.<sup>40</sup>

In view of the above, the chapter that probably has the most immediate effect on the Taiwanese economy is the *Early Harvest Program* (EHP). However, the Early Harvest list, as it had been negotiated and ratified, still heavily protects Taiwanese economic interests, whereunder Chinese concessions are much larger. First of all, as opposed to the CEPA which among liberalizing trade in goods and services also vastly liberalizes the movement of people, the Early Harvest list under the ECFA does not mention the movement of natural persons at all. Taiwan maintains its strong position of not allowing an increased influx of Chinese workers and refusing certified Chinese professionals to engage in business in Taiwan. This is because Taiwan wants to protect the employment opportunities of local blue- and white-collar workers.

In the case of trade in goods, the EHP includes 267 products in the product list on the Taiwanese side and 539 products in the product list on the Mainland side, which are subject to reduced tariff treatment under the EHP. The goods included in the ECFA EHP are divided into three categories: (1) goods subject to immediate tariff elimination; (2) goods subject to

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<sup>40</sup> “Remarks by Minister Lai on the Preparatory Consultations for the Economic Cooperation Framework Agreement” in *Mainland Affairs Council, the Fifth Chiang-Chen Talks*, June 24, 2010.

phased tariff reduction; and (3) goods subject to exceptions and others. In addition, the EHP implements a tariff reduction arrangement which allows the Parties to determine the tariff reduction time period for each product individually. In the following, the tariff reduction arrangement for products under the EHP on both sides will be briefly explained.

**Table 5.** The tariff reduction arrangement for products under the EHP on the Taiwan side is as follows:

	Import Tariff in 2009 (X%)	Agreement Tariff Rate		
		The First Year of Implementing the EHP	The Second Year of Implementing the EHP	The Third year of Implementing the EHP
1	$0 < X \leq 2.5$	0		
2	$2.5 < X \leq 7.5$	2.5	0	
3	$X > 7.5$	5	2.5	0

(Source: ECFA Annex I, page 12 )

The import tariff in 2009 refers to the non-interim import tariff rate that Taiwan generally applied to other members of the WTO in the year 2009. For Taiwan, the products with an original import tariff ranging from 0 to 2.5 will be subject to zero tariff after one year after the entry into force of the EHP. Products imported from the Mainland with an original tariff of 2.5 to 7.5 will be subject to 2.5 import tariff one year after implementation of the EHP and subject to zero tariff two years after the implementation of the EHP. As for products with an original tariff rate of above 7.5%, the tariff rate will be reduced to 5% the year following the implementation of the EHP, then to 2.5% in the second year after implementation of the EHP, and finally to zero tariff in the third year after implementation of the EHP.

**Table 6.** Tariff reduction arrangement for products under the EHP on the Mainland side

	Import Tariff in 2009 (X%)	Agreement Tariff Rate		
		The First Year of Implementing the EHP	The Second Year of Implementing the EHP	The Third year of Implementing the EHP
1	$0 < X \leq 5$	0		
2	$5 < X \leq 15$	5	0	
3	$X > 15$	10	5	0

(Source: ECFA Annex I, page 32)

The import tariff in 2009 refers to the non-interim import tariff rate that the Mainland generally applied to other members of the WTO in the year 2009. The products with an original import tariff ranging from 0 to 5% will be subject to zero tariff after one year of the entry into force of the EHP. Products imported from Taiwan with an original tariff of 5 to 15 will be subject to 5 import tariff one year after implementation of the EHP and subject to zero tariff two years after the implementation of the EHP. As for products with an original tariff rate of above 15%, the tariff rate will be reduced to 10% the year following the implementation of the EHP, then to 5% in the second year after implementation of the EHP, and finally to zero tariff in the third year after implementation of the EHP.

It is worth noting that the Early Harvest list explicitly excludes agricultural and fishery products. As such, Taiwan will maintain its import restrictions and tariffs on agricultural and fishery products imported from China (currently 1,415 agricultural products), and will not allow any new agricultural or fishery imports from China. In turn, the Taiwanese negotiators made sure that 18 Taiwanese agriculture and fishery products are included in the Early Harvest list, largely benefitting Taiwanese farmers.

Apart from protection of the agricultural sector, the second group receiving great benefits from the EHP is represented by small and medium-sized enterprises (SMEs). Taiwan sought SMEs interests before starting consultation on the Early Harvest list with China and managed to include items into the list which largely benefit Taiwanese SMEs. According to statistics generated by the *Ministry of Economic Affairs* (MOEA), the number of SMEs potentially earning direct benefits from the EHP exceed 23,000 with a cumulative export value of US\$ 2.77 billion annually. These benefits are also indirectly improving the lives of more than 426,000 employees that work for the respective SMEs in Taiwan.<sup>41</sup>

In general, the EHP provides much more benefits to Taiwan than China. Not only do the 539 Taiwanese products exceed the 267 Chinese products in number, but the trade value of the Taiwanese goods is also much higher than of the Chinese goods included in the Early Harvest list. The Taiwanese goods covered by the EHP have a trade value of approximately US\$14 billion, as opposed to the US\$2.86 billion of trade value derived from the Chinese goods covered by the EHP. This means that Taiwanese items cover 4.8 times more than Chinese items. In fact, the US\$13.83 billion worth Taiwanese items equal 16.1 percent of Taiwanese total exports to China, while the US\$2.86 billion worth Chinese items only equal 10.5 percent of Chinese total exports to Taiwan.

**Table 7.** Comparison of Concessions made by Taiwan and China:

<b>Item</b>	<b>Number of Mainland Tariff Concessions to Taiwan</b>	<b>Number of Taiwan Tariff Concessions to Mainland</b>	<b>Ratio</b>
Number of listed goods	539	267	2:1

<sup>41</sup> “Initial Estimates of Taiwan SMEs Directly Benefiting from the ECFA Early Harvest List for Trade in Goods” in Statistics by Small and Medium Enterprise Administration of the *Ministry of Economic Affairs* (MOEA), 2009.



Export value of the listed goods (US\$ 1 billion)	13.83	2.86	4.8:1
Ratio of said export value to total exports to the other side (%)	16.1	10.5	1.5:1

(Source: Mainland Affairs Council – Statistics on ECFA)

**Table 8.** Comparison of Concessions made by Taiwan and China – broken down into product categories:

Sector	Concessions by China		Concessions by Taiwan	
	Items	Trade value	Items	Trade value
Petrochemical	88	59.44	42	3.29
Textile	136	15.88	22	1.16
Machineries	107	11.43	69	4.74
Transportations	50	1.48	17	4.09
Others	140	49.97	117	15.3
Agriculture	18	0.16	-	-
<b>Total</b>	<b>539</b>	<b>138.38</b>	<b>267</b>	<b>28.58</b>

(Source: Hsu, 2011)

Moreover, the Taiwanese products covered by the EHP can be categorized in two different types.<sup>42</sup> The first type consists of up- and mid-stream goods coming from capital-intensive, traditional industries including petrochemicals, machinery manufacturing, and the textile and clothing industry. These industries receive relatively more competition

<sup>42</sup> Zhao, Hong “Taiwan-Mainland Economic Cooperation Framework Agreement” in *EAI Background Brief* No.549, 2010, 2-3.

from China and are being threatened by products originating from ASEAN countries. The inclusion of the products coming from these industries in the EHP can ease the burden of Taiwanese manufacturers and assist them in maintaining their overseas market shares. The second type of products covered by the EHP is represented by labor-intensive, traditional industries. These typically include automobile and automobile components, small electrical appliances, and accessories etc. Before implementation of the EHP, China maintained high tariff barriers on the importation of goods from these industries, making it difficult for Taiwanese exporters to penetrate the Chinese market. Thus, by including these items into the Early Harvest list also eases the access to the vast Chinese market.

Comparing the CEPA and the ECFA in terms of tariff reduction, apparently the former is much further liberalized than the latter. Although the EHP under the ECFA is already fully implemented, the product range is far narrower and the selection of product categories is also much more cautious than the CEPA. As can be seen from the number of product categories liberalized in both sides, it can be said that compared to Taiwan, the Mainland is much more open to its trading partner. Generally speaking, the EHP includes mostly items in which Taiwan and China are not in direct competition with each other, the biggest reason being that the Taiwanese government made promises to the public that signing the ECFA will not undermine Taiwan's sovereignty and will not allow Taiwan's economy to grow overly dependent on China. However, critics argue that the items in the EHP only make up a small amount of total exports to each other and that in the future, the two Parties may be forced to touch upon much more sensitive sectors.<sup>43</sup> Critics argue that future negotiations on ECFA may push Taiwan to open up against the Mainland in economically and politically sensitive areas such as finance and banking, telecommunications etc., much like Hong Kong in the case of CEPA.<sup>44</sup> In fact, the ratification of the EHP sparked street protests in Taiwan

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<sup>43</sup> Zhao, Hong "Taiwan-Mainland Economic Cooperation Framework Agreement" in *EAI Background Brief* No.549, 2010, 3.

<sup>44</sup> Zhao, Hong "Taiwan-Mainland Economic Cooperation Framework Agreement" in *EAI Background Brief*

opposing the trade pact in June 2010. Although the government tried hard to achieve the best criteria to protect Taiwan's interests, the public as well as opposing parties were concerned that the ECFA could mean the beginning of a Chinese takeover. The opposition party DDP's leader even demanded a referendum in order to decide about whether the ECFA shall be signed or not, but failed in the end. Protestors blamed the Nationalist government for signing a trade treaty that could turn Taiwan into the next Hong Kong, and for giving away the democracy the Taiwanese people have fought hard for. Nevertheless, public polls suggested that the majority of Taiwanese people were supporting the ECFA and the Ma administration's policy to foster closer ties with China, resulting in the ECFA being signed and the EHP being ratified at last.<sup>45</sup>

#### **7-2**      Tariff rate quota and non-tariff measures

Concerning tariff rate quota and non-tariff measures, the CEPA specifically stresses that neither side shall apply non-tariff measures inconsistent with WTO rules and more importantly, that the Mainland will not apply tariff rate quota to imported goods of Hong Kong origin.

As for the ECFA, the content is still under negotiation. The agreement merely states that non-tariff measures including but not limited to technical barriers to trade (TBT) and sanitary and phytosanitary measures (SPS) are to be considered as part of an agreement on trade in goods, which has not been concluded yet. Though it is still under negotiation, it appears, however, that non-tariff measures and tariff rate quota are restricted in the ECFA as compared to the CEPA. Also, the Mainland did not promise that it will not apply tariff rate quota to imported goods of Taiwanese origin.

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No.549, 2010, 3.

<sup>45</sup> Chris, Hogg. "China-Taiwan trade pact sparks street protest in Taipei" in BBC News, Asia Pacific, June 26, 2010.

### **7-3**      Anti-dumping

As mentioned above in 4.6, under the CEPA, both Parties agreed that "no anti-dumping measures are applicable to goods imported and originated from the other side", indicating that no trade remedy measures resulting from possible dumped goods will be tolerated.

The ECFA does not mention whether anti-dumping measures will be allowed or not. Thus, Taiwan is also differently treated from Hong Kong with respect to the judgement whether Mainland China should be considered a *market economy* or not.

### **7-4**      Subsidies and Countervailing measures

According to the CEPA, no countervailing measures are applicable to goods imported and originated from each other, whereas in the ECFA, subsidies and countervailing measures are still under consultation. The ECFA nevertheless does state that trade remedy measures including measures set forth in the Agreement on Implementation of Article VI of the GATT 1994 and the Agreement on Subsidies and Countervailing Measures should be included in a follow-up agreement of trade in goods under the ECFA. As such, it is expected that similar to the anti-dumping provisions, the ECFA will incorporate certain subsidies and countervailing measures.

### **7-5**      Safeguard measures

With regards to safeguard measures, the CEPA states that "in case of serious injury or threat to cause serious injury, the affected side may, after giving written notice, temporarily suspend importation of the concerned product and shall at request of the other side, promptly start consultations under Article 19<sup>46</sup> of the CEPA to reach an agreement." Furthermore, the temporary safeguard measure shall be implemented no longer than one year, until it is removed. This suggests that measures other than consultation among the parties are not

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<sup>46</sup> Article 19 of the CEPA stipulates Institutional Arrangements, including the duties of the Joint Steering Committee with regards to various issues such as interpretation and implementation of the CEPA as well as dispute settlement.

considered in the event of serious injury, which is very uncommon for a trade treaty considered as FTA. In this sense, it is obvious that China does not consider the CEPA as a trade treaty between two countries of their own sovereign status, but rather as a national arrangement between two members of the same country. Consultation as the only option to settle issues arising from serious injury in either industries is seen as an internal measure to deal with internal issues wherein no international standards are usable, preventing the issue from going public.

The ECFA's safeguard provisions are still under negotiation. The legal text, however, foresees that trade remedy measures such as safeguard measures should follow the *Agreement on Safeguards* of the WTO and the safeguard measures agreed upon applicable to the trade in goods between the two Parties. The details of safeguard measures and their applicability shall be discussed in an Agreement of trade in services under the ECFA framework, which, at least up to date, has not been concluded yet. Nevertheless, it is clear that in case of the CEPA, difficulties arising from the increasingly liberalized trade in goods between the parties should be settled in a private matter, only involving the two Parties. The content of the current version of the ECFA in contrast suggests that trade remedy measures and disputes arising from trade between Taiwan and the Mainland shall be solved by WTO rules, wherein not only the two Parties of the agreement are involved in, but also general rules on world trade, making possible disputes not private but rather public in nature. Thus, in the case of ECFA, the products listed in the EHP are subject to the provisional rules of origin under the ECFA. In the event of serious injury caused by trade liberalization under the ECFA, the parties are allowed to implement provisional trade remedy measures without consultation with the other party. External measures applicable include measures stipulated in the *Agreement on Implementation of Article VI of the GATT 1994*, the *Agreement on Subsidies and Countervailing Measures* and the *Agreement on Safeguards* of the WTO.

## 7-6 Rules of Origin

The differences in Rules of Origin can be summarized as the CEPA having relatively loose, while the ECFA as having relatively stricter Rules of Origin. The Rules of Origin of both agreements also differ in the determination of whether a good is entitled to zero tariff treatment or not, as well as in the differentiation between goods which are wholly-obtained in one side (thus eligible to zero tariff treatment) and goods which are not wholly obtained in one side (thus normally not eligible to zero tariff treatment) but somehow are eligible to preferential treatment if certain conditions are met. In the CEPA, if a good is not wholly-obtained in one side, the good can still be considered as originating from one side when it has been "*substantially transformed*" in one side. The similar process in determining whether a non-wholly-obtained good in one side can be eligible to preferential treatment in the ECFA is covered under the "*product specific rules*", which a good has to fulfill in order to be subject to preferential treatment.

**Table 9.** Comparison of Criteria for determining Rules of Origin:

<b>CEPA</b>	<b>ECFA</b>
Wholly obtained goods	Wholly obtained goods
Substantial transformation: $VAC \geq 30\%$	Product specific rules: $RVC \geq 90\%$
Other methods possible	No other methods

(Source: CEPA Annex 2 & ECFA Annex II)

According to the CEPA, goods entitled to zero tariff and directly imported have their origin determined by two principles: (1) goods which are wholly obtained in one side are regarded as originating in that side; and (2) goods which are not wholly obtained in one side are regarded as originating in that side only if they have undergone "*substantial transformation*" in that side (CEPA Annex 2, 2(1) & 2(2)).

As for wholly obtained products, both the CEPA and the ECFA have similar criteria.

These typically include: live animals born and raised in one party, or products obtained from these live animals; plants or plant products harvested, picked or gathered in one party; goods obtained by hunting, trapping, fishing, farming, gathering or capturing in one party; minerals extracted in one party; products obtained by one party from its relevant waters or goods processed or manufactured on board factory ships registered in one party; and waste and scrap articles collected in one side which are produced from the consumption in that side; etc. Similarly, both the CEPA and the ECFA have similar criteria determining minor processing activities such as transportation or storage of goods, packaging and delivery as well as distribution of goods, and these are not considered in the determination of whether a good originates from one side or not.

The criteria for determining whether a good fulfills the rules of origin are determined using several different methods. The first method is related to the manufacturing or processing operations method used when producing a good. When a good is manufactured or processed in one Party's territory, and the product has gained substantial characteristics during the process, the good is regarded as originating from one side. The second method is found in the change in tariff headings. When a product manufactured by non-originating materials is processed and results in a good under different four-digit tariff headings under the "Product Description and Harmonized System Codes", then that product can be regarded as originating from one side. The last method in determining the rules of origin concerns with the *Value-added content* (VAC). The VAC is calculated as 
$$VAC = \frac{RM + CP + LC + PDC}{FOB} \times 100\% \geq 30\%$$
, wherein: VAC refers to the value of raw materials; RM refers to the value of raw materials; CP refers to the value of component parts; LC refers to the labor costs; and PDC refers to the product development costs. A good can be seen as originating from one side if the total value of RM, CP, LC and PDC occurred in one side is no less than 30 percent of the FOB value (CEPA Annex 2, 5(4)). This VAC requirement can be seen as relatively loose compared to other FTAs. For instance, the

China-ASEAN FTA requires that a product possesses a VAC of no less than 40 percent; the China-Korea FTA requires even more local content to be achieved when counting a product as originating from one side (no less than 90%! ). As such, it is clear that the rules of origin under the CEPA are designed to put relatively less rules and pressure on manufacturers operating in Hong Kong or China. Moreover, it is not difficult for foreign producers to fulfill these requirements and conduct business in the respective areas.

The determination of originating products under the CEPA is, however, loosened by the existence of "other criteria", under which the both sides can negotiate or agree on methods in determining "substantial transformation" other than "manufacturing or processing operations", "change in tariff heading" and "value-added content" and still make the product in question be regarded as originating product from one side (CEPA Annex 2, 5(5)). This means that even if a product does not comply with the rules of origin set out in the CEPA, it is still possible to apply other methods to accept it as originating from one side through negotiations. These are measures which make the criteria more flexible and which the ECFA does not include at all.

According to the ECFA, a product is considered as originating in one Party when: (1) the good is wholly obtained in one Party; (2) a good is produced entirely in one or both parties, exclusively from originating materials; or (3) a good is produced in one or both parties using non-originating materials, and conforms to the "*product specific rules*" (ECFA Annex II, Article 2).

The product specific rules under the ECFA determine whether a good which is not wholly obtained in one Party should still be regarded as originating from one side or not. These rules include a change in tariff classification similar to the requirements stipulated in the CEPA rules of origins, and an equation determining the *Regional Value Content* (RVC).

The RVC is calculated as 
$$RVC = \frac{FOB - VNM}{FOB} \times 100\%$$
, wherein VNM refers to the value of non-originating materials. The VNM shall be adjusted based on the value of CIF (price for



imported goods including insurance and freight). Both FOB and CIF values are determined by the *Customs Valuation Agreement and the Generally Accepted Accounting Principles* (ECFA Annex II, Article 6).

According to the above rules and Article 10 (*De Minimis*) of Annex II of the "*Provisional Rules Origin Applicable to Products Under the EHP for Trade in Goods*" under the ECFA, a product that cannot meet the first criterion of change in tariff classification can nonetheless be regarded as originating from one side provided that (1) the VNM which fails to meet the first criterion of change in tariff classification does not exceed 10% of the FOB value of the given good; and (2) the good meets all the other applicable requirements of the provisional rules. In this aspect, the CEPA only requires that a given good possesses non-originating materials not exceeding 30% of its total FOB value, whereas the ECFA requires a given good to possess less than 10% non-originating materials or no less than 90% originating materials of its total FOB value. In this sense, the rules of origin of the CEPA is much more relaxed than its counterpart in the ECFA. Furthermore, the fact that local content shall be no less than 90 percent is similar to the conditions under the rules of origins of the China-Korea FTA. This reinforces the view that the ECFA enjoys a status of an international agreement between two distinct countries. It also means that Taiwan is much more protective of its economy and sovereignty than Hong Kong.

Apart from the stricter rules of origin requirements, the ECFA also stipulates that originating good which claim for preferential tariff treatment must be directly consigned between the Parties. If a good's transportation has to go through one or more third parties, there are several requirements it must follow in order to be regarded as originating from one side. These requirements include geographically or transportation-wise justifiable reasons for transit entry; rules regarding non-consumption, non-trade and non-commerce in the third party during the transit period; and rules prohibiting operations other than unloading and reloading, repackaging, or any operation required to keep the good in good condition in the territory of a third party (ECFA Annex II, Article 16.1-16.4). It is also worth noting that the

ECFA, as opposed to the CEPA, does not allow any "other criteria" negotiable between the two Parties when it comes to the determination of the origin of goods.

## **8. Provisions concerning the Trade in Services**

The CEPA and the ECFA differ also in the provisions concerning the trade in services. While the CEPA already has a full-fledged agreement on trade in services, the ECFA has its provisions regarding trade in services only roughly stipulated in Article 8 of the ECFA and in the EHP for trade in services. The two Parties agreed upon conducting consultations on an agreement on trade in services no later than six months after the entry into force of the ECFA. However, the follow-up agreement on trade in services in the case of ECFA was signed but failed to be ratified due to heavy protests among the Taiwanese public in the first half of the year 2014. Opposition escalated and talks on the agreement on trade in services under the ECFA was suspended with no sign of conclusion in the near future. The details will be elaborated in later parts of this chapter.

### **8-1 Commitments**

With regards to specific commitments in the liberalization of trade in services, the CEPA states that from 1 January 2004, Hong Kong will not impose any new discriminatory measures on Mainland's services and service suppliers and the Mainland will apply to services and service suppliers of Hong Kong the specific commitments listed in Table 1 of Annex 4 of the original CEPA. This list was further extended in Annex 3 of the CEPA II. The liberalized services sectors cover a wide range of services sectors including business services (including professional and computer related services), communications services (including audiovisual services such as videos and cinema theatre, motion pictures, and other cultural services), construction and engineering services, distribution services, transport services (including maritime, air, and road transporting services), and even financial and banking services including securities and futures.

A unique feature of the CEPA Agreement on trade in services deals with service sectors which are not stipulated in the GNS/W/120 of the *WTO Services Sectoral Classification List*. These include services concerning qualification examinations for professionals and technicians, trademark agencies, patent agencies, and services offered by individually-owned stores. The list of liberalized services sectors was further extended in the Agreement on Trade in Services signed between Hong Kong and Mainland China, which will be discussed in later parts of this paper.

It is worth mentioning that similar to the provisions under safeguard measures, the CEPA states that if the implementation of the liberalization of services trade under this Annex causes an adverse effect on trade and relevant sectors of either side, the two sides may conduct *consultations* on the provisions in question at request of either side and come to a conclusion based on *consensus*.

The ECFA has not concluded an Agreement in Trade in Services in the same sense as the CEPA yet (for various political reasons which will be dealt with in the part under the heading “Agreement on Trade in Services” in later parts of this chapter). It has, however, an EHP for trade in services which is already in force. The liberalization measures are listed in Annex 4 of the ECFA and include similar services sectors as mentioned in the CEPA, although on a much tighter basis. Similar to the provisions of trade in goods, in the liberalization of trade in services, the Mainland is expected to show more openness to Taiwan than vice versa. Mainland China is expected to open its market in 11 service sectors including banking, securities, insurance, hospitals and accounting, whereas Taiwan has only promised to provide wider market access for 7 services areas with the most significant liberalization in banking and movies services sectors.

#### 8-2 The definition of "service supplier"

As for the definition of "service supplier", both the CEPA and the ECFA have similar

requirements. Both FTAs differentiate between a service supplier who is a *natural person* and a service supplier who is a *juridical person*. For the latter category, a stricter verification process is required in both FTAs.

Under the CEPA (Annex 5 of the original CEPA), a *natural person* refers to a citizen of the People's Republic of China or a permanent resident of the Hong Kong Special Administrative Region, while a *juridical person* refers to "any legal entity duly constituted or organized under applicable laws of the Mainland or Hong Kong, whether for profit or otherwise, whether privately-owned or governmentally-owned, including any corporation, trust, partnership, joint venture, sole proprietorship, association etc.". If a service supplier is categorized as a juridical person, specific criteria have to be fulfilled in order for it to obtain preferential treatment under the CEPA. Such specific criteria typically require the services supplier being founded according to the laws of Hong Kong, holding a valid Business Registration Certificate and other licenses or permits, paying corporate tax to Hong Kong or owning the needed operation facilities for offering the service. A qualified services supplier shall also have been engaging in substantive business operations in Hong Kong for no less than three years, and this time span can be extended to five years for more complex industries such as engineering, construction, banking and insurance. Also, another common criterion is related to local employment. Under the CEPA, a services supplier is eligible for preferential treatment when it employs more than 50 percent of the staff locally.

In addition to fulfilling the above criteria, a service supplier entitled to preferential treatment under the CEPA should also obtain a number of documents such as the Certificate of Incorporation issued by the Companies Registry of the Hong Kong SAR, the Business Registration Certificate of the Hong Kong SAR, annual reports or audited financial statements, documents verifying that the service supplier in question owns or rents business premises in Hong Kong, Profit Tax Returns and other documents capable of verifying the

requirements which must be fulfilled. These documents shall be submitted to the Trade and Industry Department of the Hong Kong SAR first, and then to the Mainland examining authorities. An interesting point is that the CEPA stipulates that in case of divergent views on the qualification of a service supplier, it is the Mainland authority which shall inform the Hong Kong service supplier and the Ministry of Commerce who shall then notify the Trade and Industry Department of the Hong Kong SAR regarding the matter. This suggests that the final decision power determining a service supplier's status lies within the hands of the Mainland examining authorities. This also gives the impression that the CEPA is designed much like an internal arrangement with China having the upper hand in the decision-making process.

As mentioned earlier, the definition of a "*service supplier*" under the ECFA is quite similar to the one under the CEPA. It also differentiates between a *natural person* and a *juridical person*, wherein the former refers to a person holding the identity certificate of either Party, and the latter refers to "the entity that is constituted in either Party according to its regulations, which includes any company, trust partnership, joint venture, sole proprietorship or association". Similarly, a service supplier falling within the category of *juridical person* has to fulfill some additional criteria. Much like the CEPA, a service supplier eligible for preferential treatment under the ECFA is also required to have at least been in business operations for no less than three years. For some services, this time span is lengthened by two additional years. It is worth noting that while most of the definitions and requirements involving the categorization of service suppliers are very similar, the ECFA differentiates itself from the CEPA in the requirement concerning the required timeframe in which a services supplier should have engaged in business operations. Whereas the CEPA merely requires the service supplier to have engaged in the relevant business operations for at least three to five years, the ECFA requires that the service supplier having engaged in the same business operations for at least three to five *consecutive* years, making it relatively

more difficult for services suppliers to fulfill this requirement.

Another difference between the two FTAs is that the CEPA has added the provisions for "*contractual service providers*" in the Supplement X of the CEPA. A contractual service provider is "a natural person who possesses a Hong Kong Special Administrative Region identity document and enters the Mainland to provide temporary service for the performance of the service contract secured in the Mainland by his/her employer. The employer should be a Hong Kong service supplier without commercial presence in the Mainland. During the stay in Mainland, the contractual service provider cannot involve in any service activities irrelevant to the contract." This newly added supplement allows a natural person service supplier who is neither a permanent resident of Hong Kong nor a citizen of the People's Republic of China to enter the Mainland and provide services covered with preferential treatment under the CEPA. For the ECFA, there is no such a provision enabling natural persons to enter the Mainland to provide temporary services covered by the preferential treatment under the ECFA. Thus, in the liberalization progress in trade in services too, the CEPA takes the lead.

### 8-3 The "Agreement on Trade in Services" under the CEPA

Compared to the ECFA which has no follow-up agreement on trade in goods or services signed after the implementation of the EHP, the CEPA has several supplements concluded since its entry into force. After Supplement X was completed in late August 2013, Hong Kong and Mainland China signed the *Agreement between the Mainland and Hong Kong on Achieving Basic Liberalization of Trade in Services in Guangdong* in December 2014, followed by an even more comprehensive *Agreement on Trade in Services* concluded in November 2015 and implemented in June 2016, which has been designed largely based on the provisions of the former agreement.

Similar to the aims of trade in goods between the two sides, the Agreement on Trade in

Services strives to reduce or eliminate substantially all discriminatory measures on trade in services and to further enhance cooperation between Hong Kong and Mainland China. The most notable provisions include Article 4 National Treatment, Article 5 Most-Favored Treatment, Article 6 Prudential Principle on Financial Services, Article 7 Safeguard measures (allowed), and Article 8 Exceptions (allowed if consistent with Article XIV of the GATS).

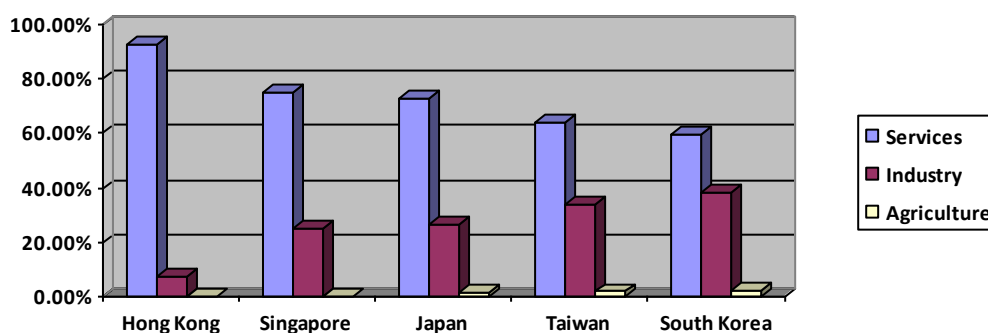
Though vast liberalization in trade in services between the two sides has been realized, there are nonetheless some restrictions with respect to National Treatment and Most-Favored Treatment of reserved restrictive measures of one side set out in Table 1 of Annex 1 and Annex 2. These include services sectors such as legal services, accounting services, taxation services, engineering services, architecture services, and medical services etc. wherein restrictions concerning the commercial presence of Hong Kong service suppliers is stipulated. Such restrictions typically require Hong Kong service suppliers to be second to Mainland service suppliers or vice versa with regards to the control or the ownership of the firm. Moreover, National Treatment and Most-Favored Treatment is not applicable to government procurements, subsidies, government loans, guarantee and insurance. In the telecommunications and cultural services sectors, some specific liberalization measures prevail.

In the area of investment facilitation related to the trade in services, the Mainland grants Hong Kong service suppliers who invest in the liberalized sectors of the Mainland facilitated administrative procedures with regards to contracts, establishment of businesses and change of enterprises. However, these facilitations do not apply to above mentioned telecommunications or cultural services sectors and also do not apply to financial institutions.

The high liberalization level in the CEPA services agreement can be attributed to the very different composition of economy between Hong Kong and China. As mentioned in the

trade in goods part, Hong Kong's economy is largely based on services, while China, although gradually shifting from manufacturing to services sector, still relies heavily on manufacturing and agricultural sectors for their economic growth. The high level of liberalization of services is beneficial for both parties. For Hong Kong, as it specializes in high value services sectors, opening up to the Mainland does not cause too much competition, while gaining access to a large market. For China, it is a good opportunity to learn from Hong Kong's experience and expertise, especially in the field of financial services.

**Figure 1.** GDP composition of selected Asian economies (2016):



*(Source: Commerce and Industry Research Office of the Hong Kong Government, 2016)*

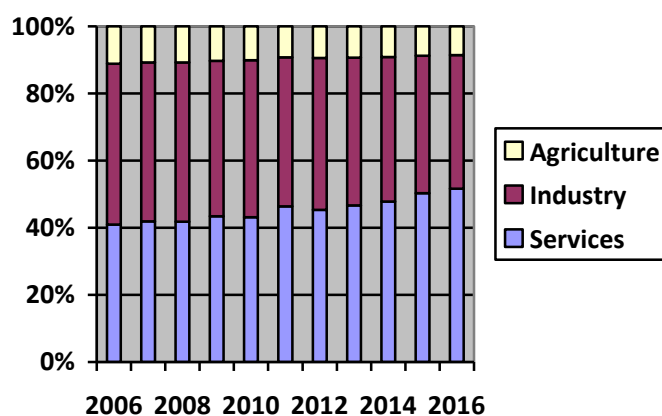
Hong Kong's economy is a services economy. Its GDP composition is largely generated by the services sector (92.7 percent), followed by the industry sector (7.2 percent), with a negligible share of agricultural sector (only 0.1 percent). The GDP generated in the services sector were mainly derived from financing and insurance, real estate, professional and business services, which continue to increase their shares in GDP. The most important key services sub-sectors are import and export services, wholesale and retail trade services which covered a share of 24.1 percent of Hong Kong's GDP in 2014. This number is followed by services in the public administration, social and personal services sector with 17.2 percent; financing and insurance services with 16.6 percent; and real estate, professional and business



services with a percentage of 10.9 of Hong Kong’s GDP composition in the year 2014.<sup>47</sup> Moreover, in 2015 employment in the services sector took up 88.3 percent of total employment in 2016.<sup>48</sup>

China’s GDP growth, in contrast, still relies heavily on the industry and agricultural sector. Its agriculture sector including industries related to forestry, hunting, fishing, and cultivation of crops and livestock production takes up 39.8 percent, nearly half of China’s GDP. Also China’s industry sector including mining, manufacturing, construction, electricity etc. has a share of 8.6 percent of total GDP. The services sector is gradually growing, with a share of 51.6 percent of China’s GDP in the year of 2016.<sup>49</sup>

**Figure 2.** GDP composition of China, 2016:



(Source: National Bureau of Statistics of China, 2016)

**Table 10.** Imports and Exports of services between Hong Kong and China:

Year	Services import	Import share	Services export	Export share
2000	212210	61.4	44089	18.9

<sup>47</sup> *Hong Kong Trade and Industry Fact Sheet* of the Government of the Hong Kong Special Administrative Region, 2014 <https://www.gov.hk/en/about/abouthk/factsheets/docs/trade&industry.pdf>

<sup>48</sup> Chapter 3 „The Economy“ of the yearbook, Government of the Hong Kong Special Administrative Region, 2016 <https://www.yearbook.gov.hk/2016/en/pdf/E03.pdf>

<sup>49</sup> GDP Composition of China, National Bureau of Statistics of China, 2016.

2001	207185	60.7	46966	20.4
2002	200403	58.7	63256	25.4
2003	191394	56.9	69202	27
2004	213720	54.8	78912	25.2
2005	243449	55.8	87116	24.3
2006	281709	57	94059	22.8
2007	289686	54.2	115976	23.7
2008	291550	51.8	129129	24.3
2009	223445	47.4	1390440	28.5
2010	252482	46.4	185577	30.1
2011	250092	43.5	234137	33.8
2012	252883	42.8	269358	36.6
2013	235908	40.7	317151	40.6
2014	216521	38	321650	40.2
2015	221651	38.9	310792	39.8
2016	220991	38.5	296363	40.1

*(Source: National Bureau of Statistics of China, 2016)*

The facilitation of trade in services generated remarkable results in the trade volume between the two parties. Amidst all, the year 2014 marks a milestone for Hong Kong service providers as in that year, services exports exceeded services imports for the first time, turning Hong Kong's services trade with China from a deficit into a surplus. According to the data derived from the National Bureau of Statistics of China, the structure of services trade suggests despite the growth of the Chinese services sector, competition between China and Hong Kong is kept on a moderate level, as the services sub-sectors they focus on differ quite sharply from each other. Chinese services exports focus largely on traditional service sub-sectors such as manufacturing services (more than 50 percent), tourism services (10

percent), transportation services (more than 10 percent) etc. These three sub-sectors alone accounted for more than 80 percent of total services in the year 2012. As opposed to that, Hong Kong's services sector focusses on modern service industries including finance and banking, electronic references and other commerce services. These sub-sectors are still underdeveloped in the Chinese services sector.

#### 8-4 Financial Cooperation under the CEPA

What is more, under the CEPA the two sides have arranged several provisions enhancing and encouraging financial cooperation between them. The main sectors aimed at are banking, securities and insurance sectors. Financial cooperation between the two sides largely takes form in the Mainland trying to attract further Hong Kong investment and using the relatively more advanced Hong Kong financial sector to restructure and develop its counterpart in the Mainland; as for Hong Kong, the advantages of such financial cooperation arrangements mainly result from preferential treatment in setting up banks or financial institutions, including insurance and securities companies in the Mainland, especially in the Guangdong area, as well as the acquisition of a vastly larger market for its financial services, which represents a crucial part of their market profile. The arrangements largely focus on measures supporting the relocation and local development of Chinese banks and international treasury as well as foreign exchange centers in Hong Kong. The measures also encourage making full use of Hong Kong's financial intermediaries and international financial platform to develop the Chinese financial sector one the one hand, but reciprocally, these measures also facilitate the procedures required for setting up Hong Kong based joint venture securities companies, fund management and futures companies in China in order to enhance integration between the parties.

#### 8-5 Cooperation in Tourism under the CEPA

Apart from the cooperation framework concerning trade in goods and services, and

financial sectors, the CEPA also provides the two sides with a comprehensive cooperation framework for their tourism sectors, which the ECFA lacks in. Tourism between the two sides forms a large part of profit income for either side

Under Article 14 Cooperation in tourism, the Mainland allows residents in Guangdong Province to visit Hong Kong on an individual basis. This provision was implemented as a trial basis first in the areas of Dongguan, Zhongshan and Jiangmen, which was further extended to the entire Guangdong province in July 2004. Other provisions include heavy promotion programs surrounding the Pearl River Delta area and encouraging mutual entry of tourism enterprises and investment such as travel agencies, joint personnel training etc. These measures helped boosting the number of visitors from China to Hong Kong rapidly. As of the year 2017, the number of Chinese visitors to Hong Kong amounted to more than 44 million people, taking up a share of 76 percent in total.

**Table 11.** Number of Visitors from China to Hong Kong:

<b>Year</b>	<b>Number of visitors</b>	<b>Total visitors</b>	<b>Share (%)</b>
2011	28 100 129	41 921 310	67.03
2012	34 911 395	48 615 113	71.81
2013	40 745 277	54 298 804	75.04
2014	47 247 675	60 838 836	77.66
2015	45 842 360	59 307 596	77.30
2016	42 778 145	56 654 903	75.51
2017	44 445 259	58 472 157	76.01

*(Source: Tourism Commission – Commerce and Economic Development Bureau of the Government of the Hong Kong Special Administrative Region)*

#### 8-6 The Mutual Recognition of Professional Qualifications under the CEPA

Closely related to the liberalization of trade in services, the two sides have agreed upon

*Mutual Recognition of Professional Qualifications* stipulated in Article 15 of the CEPA. The aim is to promote the exchange of professionals between the two sides when supplying services. The Joint Steering Committee is in the process of designing specific methodologies for mutual recognition of professional qualifications, thus this provision is still under further negotiation. It includes, however, accounting, construction, taxation, engineering, real estate and printing qualifications up to date.

#### 8-7 The “Agreement on Trade in Services” under the ECFA

The Mainland and Taiwan signed the *Cross-Strait Service Trade Agreement (CSSTA* or *Cross-Strait Agreement on Trade in Services)* in June 2013, however, this agreement has not been ratified yet by the Taiwanese legislature. The main reasons for the failure of ratification were mass protests during the Sunflower Movement in March 2014, wherein students protested against the conclusion and ratification of the CSSTA mainly due to the lack of transparency during the negotiation and conclusion process of the treaty and controversial opinions on the *Kuomintang* in Taiwan who negotiated and attempted to ratify this treaty without democratic consensus of the people. The treaty was designed to incorporate facilitation for service sectors such as banking, medical, tourism, cultural sectors such as film, telecommunications etc. Also, businessmen from both Parties were promised the possibility obtaining indefinitely renewable visas for their stay in the other side.

The government’s unilateral decision to conclude the services trade pact sparked wide dissatisfaction among the Taiwanese people. Protestors raised their opposing voices due to the lack of a “clause-by-clause” review by the legislating bodies. This issue later escalated into a fierce demand for the government to reject the trade pact altogether and to pass a legislation which shall allow the crowd to closely monitor future trade arrangements with China. The protesting parties even discussed a constitutional amendment on this issue.<sup>50</sup> In contrast to the smooth trade liberalization process for trade in services under the CEPA, the

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<sup>50</sup> Chris, Wang „Groups protest service trade agreement” in Taipei Times, December 23, 2013.

mass was successful in blocking the ratification and further negotiations on trade liberalization in services under the ECFA. Up to date, there has been no progress in the CSSTA or any kind of trade in services agreement under the ECFA. The only cooperation in trade in services currently in process has been granted by the EHP of trade in services under the original ECFA.

**Table 12.** Commitments of China and Taiwan under Early Harvest Program:

	<b>China's commitments</b>	<b>Taiwan's commitments</b>
<b>Business services</b>	<ol style="list-style-type: none"> <li>1. Accounting, auditing, book-keeping</li> <li>2. Software implementation, data processing</li> <li>3. Research and Development</li> <li>4. Convention</li> <li>5. Special design</li> <li>6. Audiovisual services</li> <li>7. Hospital</li> <li>8. Aircraft repair and maintenance</li> </ol>	<ul style="list-style-type: none"> <li>❖ R&amp;D</li> <li>❖ Convention</li> <li>❖ Exhibition</li> <li>❖ Special design</li> <li>❖ Motion picture</li> <li>❖ Commission agent's services</li> <li>❖ Sporting and other recreational services</li> <li>❖ Computer reservation systems</li> </ul>
<b>Financial sector</b>	<ul style="list-style-type: none"> <li>❖ Banking and other financial services</li> <li>❖ Insurance and related services</li> <li>❖ Securities, futures, and other related services</li> </ul>	Banking and other financial services

(Source: Sung, 2013)

The level of trade liberalization under the ECFA is much more restricted than under the CEPA. Also, Chinese commitments in trade in services is also much higher than Taiwanese

commitments with China opening up 11 sectors in total and Taiwan only 9 sectors. Among these sectors, Taiwan focused on the liberalization of trade in motion pictures.

There are a number of issues that differ from the CEPA. First, the EHP on trade in services is entirely irrelevant with the movement of human resources, which is in sharp contrast to the granting of the *Individual Visitor Scheme* or measures for mutual recognition of professional service suppliers under the CEPA. The Taiwanese government held on to its promise to keep cheap Chinese labor out of its territory in order to guarantee the highest protection possible for its local workers. Second, the most significant change under the EHP can be seen in the liberalization in the banking sector, under which Chinese and Taiwanese banks are able to set up branches in each other's territory to conduct foreign currency business.

## **9. Trade and Investment Facilitation**

The provisions with regards to trade and investment facilitation in both FTAs have similar purposes, mainly to provide greater transparency, standard conformity, reducing restrictions and facilitating cooperation in investment and economy, and to enhance information exchanges between the Parties. In the CEPA, the relevant provisions are granted under the *Agreement on Economic and Technical Cooperation*, while in the ECFA, similar provisions are stipulated in Chapter 2 Article 5 and Chapter 3 Article 6 under the headings *Investment* and *Economic Cooperation* respectively. The details are discussed in the following parts.

### 9-1 The "Agreement on Economic and Technical Cooperation" under the CEPA

This agreement contributes to cooperation between the two sides mainly in the form of facilitating trade procedures, enhancing transparency, encouraging cooperation between firms originating from both sides, and promoting shared cultural heritages. The facilitated areas of cooperation include a wide variety of activities such as the facilitation of trade procedures (including customs clearance, inspection and quarantine, food safety, sharing information etc.), enhancing transparency of laws and regulations and developing mutual

recognition processes for testing and certification submission. A new area being dealt with under this agreement is represented by cooperation in the electronic business sector. The two parties promised to support the cooperation of small and medium enterprises which engage in electronic businesses and tackle branding activities together.

Another new area of cooperation is related to the IPR protection. This was the first time, after the original CEPA agreement was signed in 2003, that the two parties have mentioned the issue of IPR protection, although in a very vague sense without any details in progress yet. This is in sharp contrast to the ECFA, which was signed along with an agreement in IPR protection when negotiation first started.

The agreement also enhances the establishment of shared cultural heritages. Most notably, Hong Kong agreed to cooperate with China on the development of traditional medicine and related medical products sectors. In addition, joint engagement in cultural, environmental, innovation and technology sectors has been discussed in the agreement, in order to foster mutual competitive advantages in the global market and to enhance Chinese soft power.

The cooperation mechanism is mostly based on setting up special working groups with members of both sides. This arrangement facilitates information exchange and sharing, promotes joint research and joint development of rules and regulations. The details are set out in Annex 6 of the CEPA.

The agreement did not bring about any significant change to the investment interactions between Hong Kong and China. Since the past, Hong Kong has always been the largest investor in China with an investment amount of US\$52.57 billion in 2016, followed by Taiwan (US\$3.26 billion), Singapore (US\$2.81 billion), Japan, the United States, South Korea etc.<sup>51</sup> In the recent decade, Chinese investment in Hong Kong has also been increasing steadily. In early 2017, Chinese investment in Hong Kong had risen to US\$501.37

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<sup>51</sup> “Top ten nations and regions with investment in China”, Ministry of Commerce, PRC, 2016.



billion, taking up 52.5 percent of the total investment stock in Hong Kong.<sup>52</sup> Due to the relatively loose definition of a Hong Kong service supplier (such as requiring that the supplier must be registered in Hong Kong and have operated in the business for three to five years, paying Hong Kong profit tax and employing local staff) and requirements, it is not difficult for foreign investors to acquire control of local companies and making investments in Hong Kong. Thus, the FDI influx into Hong Kong has increased gradually. Foreign banks have also acquired small and medium-sized local Hong Kong banks to enter the Mainland market due to the lower asset requirements granted to Hong Kong service suppliers as opposed to other parts of the country.

Moreover, China's National 13<sup>th</sup> five-year plan even dedicated a whole chapter to Hong Kong and Macao's investment development ("the Dedicated Chapter"). The National five-year plans count as the most important blueprint of China's development for the coming next five years and determine major national policies. The fact that Hong Kong and Macao are included in China's most important national plans, especially into the new "Belt and Road Initiative" signals that China considers Hong Kong as having significant functions in the national development. It also obviously means that Hong Kong is being treated entirely as part of the country, whose economic development is planned in line with China's national economic development plans, whereas for Taiwan, no such plans are being made. China has displayed clearly its full support of Hong Kong in enhancing its status as an international financial and trade center and encourages Hong Kong businesses to open up in the Belt and Road Initiative to gain vast access to new markets.<sup>53</sup>

## 9-2 Investment and Economic Cooperation under the ECFA

Under the ECFA, both investment and economic cooperation provisions are still under further consultation, lacking an all-bound framework such as seen in the CEPA.

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<sup>52</sup> "Investment in Hong Kong", Ministry of Commerce, PRC, 2017.

<sup>53</sup> "A Dedicated Chapter on Hong Kong and Macao in the National 13<sup>th</sup> Five-Year Plan", News website of the government of the Hong Kong Special Administrative Region, March 17, 2016.

Investment cooperation largely takes place in the form of establishing an investment protection mechanism, increasing transparency on investment-related regulations, gradually reducing restrictions in the area of mutual investments, and promoting investment facilitation between the two Parties.

Economic cooperation is similarly presented as its counterpart of the CEPA. It covers the most important areas of trade and economy of both Parties, including most importantly IPR protection, customs facilitation procedures, electronic commerce, the support of small and medium-sized enterprises to cooperate with their counterparts in the two parties and supporting them to develop competitiveness for a global market, and the establishment of trade offices in each other's territory to promote trade interactions. The investment scenario in Taiwan has, however, seen no significant changes in the FDI inflow and outflow from and to China.<sup>54</sup>

It is worth noting, however, that the proposed provisions do not touch upon the topic of cultural or educational cooperation, as opposed to the CEPA which actively promotes common cultural heritages such as Chinese traditional medicine and standardized education (involving historic incidents etc. which may differ between Hong Kong, Taiwan, and Mainland China). The Taiwanese government stressed during negotiations of the ECFA that the agreement will only be an economic one, not involving any political or cultural issues whatsoever and has kept its promise so far.

## **10. Exceptions**

Both the CEPA and the ECFA allow the Parties of the FTA to maintain or adopt exception measures which are consistent with the rules of the WTO system.

## **11. Dispute Settlement**

A significant difference can be observed in the provisions regarding dispute settlement

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<sup>54</sup> "FDI Country Fact Sheets 2017", UNCTAD Website, 2017.

and dispute settlement mechanism. Surprisingly, the CEPA has no clause explaining the dispute settlement mechanism in the event of disputes arising from the implementation or interpretation of the CEPA arrangement.

Although dispute settlement mechanisms in FTAs are not seldom actually utilized, it is common for the FTA signatories to at least include a dispute settlement mechanism, regardless of the level of comprehensiveness. The CEPA, however, does not state anything about a dispute settlement mechanism at all. According to the WTO categorization of “*Dispute Settlement Mechanisms in Regional Trade Agreements*”<sup>55</sup>, dispute settlement mechanisms can be classified into three different types: starting from the political/diplomatic type, which has the lowest degree of legalism, to the quasi-judicial type with a moderate level of legalism, and to the judicial type which displays the highest degree of legalism. The CEPA case falls into the category of political/diplomatic type of dispute settlement mechanism with the least level of legality. At the time when CEPA was concluded, the majority of RTAs have used at least a quasi-judicial DSU model, which grants the parties with an automatic right of access to third-party adjudication at some stage of the dispute settlement process. In the Asia Pacific, all RTAs made use of at least the quasi-judicial type of DSU, except for China’s FTA with Hong Kong and Macao. In this case, if a dispute arises under the CEPA, no third parties are allowed to get involved into dispute settlement. Problems will only be allowed to be settled privately between China and Hong Kong. This also raises concerns about the objectivity in case of dispute settlement under the CEPA. The CEPA DSU is a mechanism without defining the rules of procedure and does not mention any information about the way a dispute is proceeded, terminated or suspended. There are no rules guarding the terms of references, communication methods, time periods, notification, confidentiality or advice from experts etc. This lack of concrete rules may become a serious problem if a dispute arises as there will be no guidelines on how to properly settle the dispute.

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<sup>55</sup> Claude Chase, “Mapping of Dispute Settlement Mechanisms in Regional Trade Agreements – Innovative or Variations on a Theme?”, Staff Working Paper of the WTO Economic Research and Statistics Division, June 10, 2013.

Furthermore, without any legal force of the DSU, even if a decision is made on both sides, this decision will have no legal binding power and the injured party may have no means to demand compliance from the other party.

In contrast, the ECFA, although still under consultation, specifically stipulates the will to negotiate a comprehensive dispute settlement mechanism in Chapter 5 Article 10 of the ECFA agreement. Before the final dispute settlement agreement is completed and ratified, disputes arising from the ECFA will be solved through consultations by the two Parties or in an appropriate manner by the *Cross-Straits Economic Cooperation Committee*.

## **12. Institutional Arrangements**

Institutional arrangements are similar between the CEPA and the ECFA. Both FTAs have seen the setting up of joint committees to facilitate the handling of issues arising from the implementation of the FTAs.

In case of the CEPA, a *Joint Steering Committee* comprising of senior representatives or officials designated by the two sides was set up. The Steering Committee set up liaison offices (the *Ministry of Commerce of the Central People's Government* and the *Commerce, Industry and Technology Bureau of the Hong Kong Special Administrative Region Government* respectively). The obligations of the Steering Committee include the supervision of implementation of the CEPA, the interpretation of the provisions of the CEPA, resolving disputes and drafting additional amendments when needed etc. The Committee meets regularly at least once a year or in case of emergency, special meetings within 30 days upon request can be called. Decisions are made by consensus in "a spirit of friendship and cooperation".

As for the ECFA, a *Cross-Straits Cooperation Committee* was established, consisting of representatives designated by the two Parties. Their duties include the conclusion of consultations, monitoring and evaluating the implementation of the ECFA, interpreting provisions of the ECFA, notifying important economic and trade information, and settling

disputes arising from the ECFA at least before a formal dispute settlement mechanism and a dispute settlement body is decided. Furthermore, the Committee may also set up working groups to handle matters in specific areas. The Committee is supposed to meet on a regularly or semi-annually basis and is allowed to call ad hoc meetings when necessary with the consent of the two Parties. So far, the Committee has met up to seven times, the last time on 29 January 2015, after a long interruption of meetings in 2014 due to the protests against further ECFA negotiations during the Sunflower Movement.

### **13. Termination**

A further significant aspect in which the two FTAs differ from each other lies within the fact that the CEPA has no termination or withdrawal clause while the ECFA does.

The ECFA states in Chapter 5 Article 16 the relevant procedures concerning termination of the agreement and specifies the time frame which shall be followed by the two Parties in case of termination. If a Party wishes to terminate the ECFA, that Party shall notify the other Party in a written manner. Then the two Parties are required to start consultations within 30 days from the date the written termination notice has been issued. In the case that consultations fail to reach consensus, the agreement will be terminated on the 180<sup>th</sup> day from the date the written termination notice has been issued by the notifying Party. In the aftermath, within 30 days from the date of termination of the ECFA, the two Parties must engage in consultations on the issues arising from the termination.

Apparently, the inclusion of a termination clause served as one of the pre-conditions for Taiwan to engage in ECFA negotiations. As the CEPA lacks in a termination clause, the Taiwanese government insisted on a properly designed termination clause to safeguard Taiwan's interests in the event of unforeseen injuries caused by increased liberalization of trade with China. For a legally binding termination of the agreement, the party initiating termination can terminate the agreement on a unilateral basis after notifying the other party without requiring consent of the other party.

## V. Conclusion

In the last two decades, the world has witnessed the formation of regional trade blocs in the Asia Pacific. China's FTAs with Hong Kong and Taiwan represent important RTAs among others. Although China has been insisting on developing a *Chinese Economic Area* (CEA), it has not been fully successful due to discrepancies in political ideologies among the nations. Although China has been widely successful in integrating Hong Kong into the Mainland's economy through the CEPA, the Taiwan case has been proven to be much more challenging, even though the ECFA has come into effect since 2010. The reasons for the different development of Hong Kong and Taiwan's path can be summarized as having different political status and different levels of political awareness on the one hand, and having diverging economic structures on the other hand.

Comparing the legal clauses, it becomes evident that there are several fundamental differences between the CEPA and ECFA. In general, whereas the CEPA's provisions are relatively loose and liberal, the ECFA shows a much more restrictive and protective form. Some significant differences can be found in the naming and principles of the agreements, the negotiation process, the different level of liberalization in the provisions of trade in goods and services, the safeguard measures, dispute settlement mechanism, and the provisions on termination of the agreements. It is worth noting that the CEPA possesses none of the protective clauses which usually are included in FTAs to secure the parties' interests in the event of serious injury – namely the safeguard measures, dispute settlement measures, and the termination clause. The ECFA, however, resembles the majority of FTAs between two sovereign countries, incorporating all the legal protection clauses usually found in trade pacts, with an emphasis on IPR protection, safeguard, dispute settlement, and termination. This vast difference gives the strong impression that the CEPA is modeled after domestic trade arrangements, while the ECFA clearly has all the characteristics that can be found in international agreements. Thus, from a legal perspective, China's treatment of Hong Kong and Taiwan are vastly different.

The CEPA has brought about joint economic prosperity to both China and Hong Kong. The quick liberalization process and in many aspects relatively loose requirements were made possible because of the complementary character of the economies of China and Hong Kong. While Hong Kong has long been a services economy and has been specializing in high-value services sectors, the Mainland still relies heavily on industry sectors such as manufacturing and agricultural sectors. As Hong Kong has originally been a free port, and its manufacturing sector has been very small to begin with, opening up to China did not diminish their economic benefits. As for China, although in recent years it has been trying to shift its economic focus on services sectors, it is still lagging behind Hong Kong as Chinese services sectors are largely based on traditional services rather than high-value services. Thus, the conclusion of CEPA and its follow-up agreements has been going smoothly, since both could gain from the other party and their economies are not in direct competition. The most significant change after the CEPA can be derived from the implementation of the *Individual Visitor Scheme* and the mutual recognition of professionals, which both allow the free movement of people and the establishment of mutual recognition of certificates related to professional services providers. This greatly enhanced the exchange of human resources and helped integrating Hong Kong into the Mainland on a new level.

In contrast, the ECFA, although initially supported by the majority of Taiwanese people, has been increasingly rejected by the Taiwanese public, the most obvious reason being concern over Taiwan's sovereignty. The Taiwanese government initiated talks on ECFA in 2009 and the Ma administration then promised to the public repeatedly that the trade pact would enhance Taiwan's GDP growth and only be focused on economic issues, not touching upon politics. The Early Harvest Program (EHP) has been implemented in early 2011, facilitating both trade in goods and trade in services. However, when a follow-up agreement on trade in services was signed and in the process of being ratified, the nontransparent way of the government's negotiations and the anticipated ambiguous outcomes have sparked mass protests against the conclusion of the trade pact. The public claimed that the

government had failed to keep its promise of protecting local industries and giving a chance to China to interfere with its political sovereignty. The liberalization level of the ECFA was quite restrictive to begin with, with the EHP only including items favorable for Taiwan and completely excluding concessions on agricultural products to protect Taiwanese farmers and other local industries. This is due to the similar economic structure between China and Taiwan, both focusing on manufacturing on a considerable amount, while trying to develop its services sector. It is also due to the growing anti-China sentiment since the Nationalist government's failure to process negotiations with China on a transparent and democratic way, which led to mistrust among the public. With the change of political leadership from the Nationalists to the Democratic Progressive Party in 2016, talks on further negotiation on the ECFA have been suspended and there is no clear sign of development in the near future.

To sum up, it is clear that the different structure of the agreements can be largely derived from the divergent economic structures prevailing in Hong Kong and Taiwan, as well as from the different attitudes towards integration into the Chinese economy. For Hong Kong, a trade pact with China was the best option to recover its economy from the economic crisis in 1997 and the SARS epidemic, whereas for Taiwan, although enhancing trade with China has always been important, it is not willing to do so if that means that it would diminish Taiwanese sovereignty. Thus, although China insists on its "One Country, two systems" principle when dealing with Hong Kong and Taiwan, it treats them vastly different. Therefore, popular concerns about Taiwan becoming another Hong Kong after the ECFA seem to be exaggerating, as the political and economic situation in Taiwan is clearly different and thus the outcome of the trade pacts are also bound to be very different from each other.



## VI. References

The legal text of the CEPA agreement includes:

- CEPA Main Text and Six Annexes (29 June 2003 & 29 Sept 2003)
- Supplement I to CEPA (27 Oct 2004)
- Supplement II to CEPA (18 Oct 2005)
- Supplement III to CEPA (27 June 2006)
- Supplement IV to CEPA (29 June 2007)
- Supplement V to CEPA (29 July 2008)
- Supplement VI to CEPA (9 May 2009)
- Supplement VII to CEPA (27 May 2010)
- Supplement VIII to CEPA (13 Dec 2011)
- Supplement IX to CEPA (29 June 2012)
- Supplement X to CEPA (29 Aug 2013)
- Agreement between the Mainland and Hong Kong on Achieving Basic Liberalisation of Trade in Services in Guangdong (18 Dec 2014)
- Agreement on Trade in Services (27 Nov 2015)
- Investment Agreement (28 June 2017)
- Agreement on Economic and Technical Cooperation (28 June 2017)

(Obtained from the website of the Trade and Industry Department of the Government of the Hong Kong SAR; Online source:

[https://www.tid.gov.hk/english/cepa/legaltext/cepa\\_legaltext.html](https://www.tid.gov.hk/english/cepa/legaltext/cepa_legaltext.html))

The legal text of the ECFA agreement includes:

- ECFA (9 Jan 2014)
- Annex I Product List and Tariff Reduction Arrangements (9 Jan 2014)
- Applicable to Products (Operational Procedures) (9 Jan 2014)
- Annex II Provisional Rules of Origin (9 Jan 2014)

- Annex III Safeguard Measures Between the Two Parties (9 Jan 2014)
- Annex IV Sectors and Liberalization Measures (9 Jan 2014)
- Annex V Definitions of Service Suppliers (9 Jan 2014)

(Obtained from the website of the Ministry of Economic Affairs of the ROC, Bureau of Foreign Trade; Online source: <https://www.trade.gov.tw/english/Pages/List.aspx?nodeID=1072>)

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的前景——兼论 ECFA 与 CEPA 的区别“ *In Forum of World Economics and Politics* 世界经济与政治论坛, (1), 127-139.

## 국 문 초 록

### 중국-홍콩 FTA 와 중국-대만 FTA 의 비교분석

중국은 2001년 12월 세계무역기구(WTO)에 가입한 이후, 6개의 자유무역협정(FTA), 각각 홍콩과 마카오와 체결한 2개의 경제협력강화협정(Closer Economic Partnership Arrangement, CEPA) 그리고 대만과의 경제협력기본협정(Economic Cooperation Framework Agreement, ECFA)을 체결하였다. 상기 자유무역지대 가운데 홍콩 및 마카오와의 경제협력강화협정과 대만과의 경제협력기본협정은 특혜협정 타결로 인한 상호경제이익 증진을 통해 중국이 오랫동안 추구해 온 정치적, 전략적 목표인 ‘일국양제(一國兩制)’ 원칙에 입각한 ‘화평통일(和平統一)’을 이루기 위한 시도로 해석되어왔다.

지리적 근접성에도 불구하고 ‘중화경제지구(Chinese Economic Area, CEA)’를 구성하는 본토, 홍콩, 마카오 그리고 대만은 각각 무역과 투자 정책이 독립적으로 이루어지는 별개의 관세 영역을 구성한다. 이 지역의 급격한 경제 발전은 상호 경제이익을 증진시킬 수 있도록 무역과 투자를 규율하는 합의의 필요성을 불러 일으켰고 그 결과로 위의 세 협정이 체결되었다. 본 논문에서는 상대적으로 규모가 작은 마카오와의 협정은 배제하고 중국과 홍콩, 중국과 대만 간 협정에 집중하고자 한다.

홍콩은 1997년 중국으로 반환되었고, 대만은 사실상 중국으로부터 독립적인 지위를 향유한다. 그러나 북경 정부는 대만을 곧 자신의 통치 하에 반드시 들어올 하나의 ‘성’으로 간주한다. 중국의 ‘화평통일’ 정책에 따르면, 중국은

대만이 ‘인적 교류, 양안 간 무역 및 투자 그리고 공동 문화, 체육, 교육 활동으로 촉진되는 경제, 사회 그리고 정치적 통합을 통해’ 본토의 관할 하에 들어올 수 있도록 해야 한다(Hughes, 2001). 비록 ‘일국양제’가 본래는 대만과의 통일을 위해 덩샤오핑에 의해 도입되었지만, 동일한 전략이 중국과 홍콩 관계에 적용되었고 이것이 오히려 대만과의 추후 통일 과정에서의 모델로 작동하고 있다(Bundy 1989; Cooney 1997; Weng 1987). 이러한 점에서 대만 정부는 1990년대말부터 중국과 통합된 홍콩의 경제적, 정치적 발전을 면밀하게 검토하여 자신에게 주는 시사점을 도출하고자 한다.

중국-홍콩 간 CEPA와 중국-대만 간 ECFA를 비교하면서 대만에서는 홍콩이 CEPA 체결 이후 그랬던 것처럼 ‘일국양제’ 하에서 자신의 주권을 더욱 상실할 수 있다는 우려가 커지고 있다. 그러나 대만과 홍콩의 정치적, 경제적 차이를 고려하면 대만이 홍콩처럼 될 것이라는 우려의 근거가 충분치 않다고 보인다. 정치적으로는 홍콩은 중국에 속하는 반자치구역이자 특별행정구역의 성격을 지니는데 반해 대만은 독자적 정부를 지니고 중국 본토와는 별개로 독립적 지위를 누리고 있다. 경제적으로 홍콩은 서비스 산업이 경제의 주를 이루고 있지만 대만은 제조업 부문이 경제의 큰 부분을 차지하고 있다.

본 논문은 중국-홍콩 CEPA와 중국-대만 ECFA를 비교하여 대만의 주권 상실 우려가 적어도 법적으로는 근거가 충분치 않다는 것을 보이려고 한다. 중국 정부는 대만 역시 중국의 일부라고 주장하지만 중국의 대만과 홍콩에 대한 법적 대우는 확연히 다르다. CEPA와 ECFA에서 드러나는 협정 내용과 조문의 차이와 이러한 차이를 발생시킨 사회경제적, 정치적 원인에 대한 분석을 통해 두 지역에 대한 중국 정부의 상이한 대우를 설명하고자 한다. 가장 분명한 차이점은 첫째, CEPA와 ECFA의 정치적 목적, 둘째, 분쟁해결절차, 종료절차, 세이프가드 또는 반덤핑에 관한 조항에서 드러나는 법적 보호 정도 그리고 셋째, 상품과 서비스 무역 개방의 정도와 특혜적 조치의 범위의 정도에서 발견된다. 상기 차이점에

근거하면 CEPA 의 법적 지위는 지역간의 국내적 협정을 연상시키는 반면, ECFA 는 표준적인 국제적 FTA 를 모델로 하였다는 것을 알 수 있다. 또한, 이러한 차이점은 중국이 홍콩과 대만에 대한 대우를 다르게 할 수 밖에 없었던 원인으로 사회경제적, 정치적 고려가 작용했다는 것을 암시하기도 한다.

**주요어:** 중국, 대만, 홍콩, FTA, 법적 분석, CEPA 와 ECFA 의 비교

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