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**REPORT FROM THE COMMISSION TO THE COUNCIL
AND THE EUROPEAN PARLIAMENT**

**Annual Report by the European Commission on the Hong Kong Special Administrative
Region**

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HONG KONG: Annual Report 2002

1. INTRODUCTION

As in the Commission's previous annual reports, this 2002 report aims to assess the state of development of the Hong Kong SAR and its relations with the European Union.

In accordance with the Commission's mandate, the report analyses progress in the implementation of the "One Country, Two Systems" principle, and reviews developments in the legislative, institutional and individual rights fields. The document also provides an assessment of economic developments, and reports on the main aspects of EU-Hong Kong relations.

2. REAFFIRMATION AND IMPLEMENTATION OF THE "ONE COUNTRY, TWO SYSTEMS" PRINCIPLE

– *Reaffirmation of the principle*

The Central Government of Beijing again reiterated its adherence to the "one country, two systems" principle in its official statements. In a speech to the National People's Congress (NPC) on 5 March 2002, Prime Minister Zhu Rongji stated:

"We should fully implement the principle of "one country, two systems" and the Basic Law of Hong Kong and Macao Special Administrative Regions. It is our firm and unswerving objective to maintain the long-term stability, prosperity and development there. The Central Government will continue to render full support to the efforts of the governments and Chief Executives of Hong Kong and Macao to govern the regions in accordance with the law, and it will further strengthen economic, trade, scientific, technological, cultural and education exchanges and cooperation between the Mainland and Hong Kong and Macao. We have full confidence in the futures of Hong Kong and Macao."

In a speech during the 1 July celebrations on the fifth anniversary of Hong Kong's return to China and the inauguration of the second term of the HKSAR government, President Jiang Zemin said: "In a nutshell, what we have learnt in the past five years is that the policy of "one country, two systems" and the Basic Law of the Hong Kong SAR must be implemented in a comprehensive and accurate manner under all circumstances."

– *Implementation of the principle*

• *The practice of Falun Gong*

The Falun Gong, a legally registered group in Hong Kong, continues to enjoy the freedom to practice and does so in venues which include those run by government departments (Leisure and Cultural Services Department).

Nevertheless its practice and sit-in protest outside the Central People's Government Liaison Office on 16 March was considered as causing obstruction. The police moved 16 Falun Gong demonstrators, including four from Switzerland, from outside the Central Government Liaison Office. Both police and demonstrators claimed to have sustained injuries during the removal.

The 16 were subsequently arrested and charged with obstruction or assault. The trial started on 16 June with about 30 Falun Gong practitioners and a representative from the Swiss Consulate in Hong Kong in attendance. The verdict, delivered in mid-August, found all 16 guilty of causing public obstruction. Three were also convicted of assaulting police officers. They were fined between HK\$ 1,300 and HK\$ 3,800, well below the maximum penalties.

In his verdict, the magistrate recalled that the right to protest and hold demonstrations is not absolute and its exercise requires a very delicate balance. The magistrate ruled that the arrests were lawful, noting that the 16 had ignored repeated warnings and that police officers had been sensible and reasonable in asking the practitioners to move on.

- *Right of abode*

The Court of Final Appeal ruled on 29 January 1999 with a broad definition of the right of abode of mainland Chinese in Hong Kong. The Court's interpretation was then overturned in June 1999 by the interpretation of the Standing Committee of the National People's Congress, made at the request of the HKSAR Government.

5,073 applicants in the appeals who considered themselves to be in the same situation as the parties to the case of 29 January 1999 claimed that they should have their claims for right of abode re-examined in accordance with the Appeal Court's judgement.

In a new ruling on 10 January 2002, the Court of Final Appeal ruled by a majority of four judges to one, that most of the claimants did not have the right of abode. However it recognised that several hundred appellants had a "legitimate expectation" based on reassurances from government departments and would be entitled to the same right of abode, as those involved in the Court's 29 January ruling. The fifth judge's opinion was that all the applicants should benefit from the notion of "legitimate expectation".

The majority verdict of the Court was warmly welcomed by academics, lawyers and the government, although some politicians and various social bodies urged the government to grant the right of abode to all applicants on humanitarian grounds. The SAR government decided to keep to the ruling of the Court of Final Appeal, but together with mainland authorities, agreed to a period of grace until the end of March to allow unsuccessful claimants to return to the mainland without being charged for illegally entering or overstaying in Hong Kong. Many of the unsuccessful claimants returned voluntarily ahead of the 31 March deadline. The government removed others who tried to remain illegally.

The 10 January ruling of the Court of Final Appeal laid down broad legal principles in the handling of right of abode cases and -this could help to avoid future disputes over abode.

3. INSTITUTIONAL DEVELOPMENTS

– *Election of the Chief Executive for a second term*

In the secondelections for Chief Executive in Hong Kong, the Chief Executive Mr Tung Chee-hwa was the only validly-nominated candidate. His nomination was supported by 714 of the 800-member Election Committee. Other candidates were de facto excluded, as nominations needed to be supported by at least 100 members, following the adoption of the Chief Executive Election Bill in 2001. Mr Tung was therefore elected for a second term at the end of February, without a formal vote.

The legislator from the Legal constituency Margaret Ng, urged democratic forces to unite and make immediate preparations for the third Chief Executive elections. She apologised to the people of Hong Kong on behalf of the democratic parties for not having participated in the second election process (the democratic parties had an extensive debate about whether to participate in the election and failed to put up candidates in time).

– *Introduction of the accountability system*

As announced in his Policy Addresses of 2000 and 2001, the Chief Executive unveiled the accountability system for members of Government on 17 April 2002. The new scheme means that political appointees rather than senior civil servants have been put in charge of government departments. These new Secretaries serve for a contract period not exceeding the term of the Chief Executive, and are answerable to him for both policy-making and policy implementation. The Secretaries are fully accountable and may be required to resign for serious failure in policy outcome, serious mishaps in implementation or for grave personal misconduct.

According to the Chief Executive, the new accountability system will have the following implications :

- All Secretaries will also become members of the Executive Council (ExCo), which advises the Chief Executive and also includes members from the community and some legislators.
- The top senior civil servants in each government department will be renamed Permanent Secretaries. Their responsibilities will be limited to policy implementation, rather than policy-making as in the past.
- The government will seek to improve its working relationship with the legislature. All Secretaries will work personally with Legislative Council (LegCo) members and seek their support for policy and other initiatives.

The new system was widely debated by academics, the media and LegCo members, who called for the new Secretaries to be also held accountable to LegCo by appearing for audition before appointment and by agreeing to resign should a motion of no confidence be adopted. Nonetheless, LegCo passed a government motion on 29 May endorsing the new system. On 24 June, the Chief Executive announced the composition of his new government, after approval by the Central Government. The new government took up its duties on 1 July, the date of commencement of the Chief Executive's second term.

The first six months of the new system saw Government members become aware of their images vis-à-vis public opinion and LegCo members. This led some of them to make public statements on policy issues without apparent prior coordination within ExCo. After a public protest by an ExCo member, the Chief Executive called several brainstorming and co-ordination meetings to establish more cohesion in the new government.

The introduction of the accountability system on 1 July resulted in the traditional October Policy Address by the Chief Executive being postponed until January 2003.

– ***Pace of democratisation***

The Basic Law stipulates that, after a review in 2007, elections for Chief Executive and all members of LegCo may be held by universal suffrage, which is the “ultimate aim” set by the Basic Law. An interview with Chinese Vice-Premier Qian Qichen in the South China Morning Post at the end of June triggered concerns among some about the commitment to these aims by both the Central and Hong Kong SAR Governments.

Vice-Premier Qian encouraged Hong Kong to “design its own path for development according to its actual conditions and proceed gradually” and not to “blindly copy the experience of other places.” He appeared to rule out universal suffrage by saying that the current system of election should be kept, as the current model, based on functional constituency elections, was an “effective way to ensure that people from all walks of life have a balanced participation in public life.” Controversy grew when Chief Secretary Donald Tsang appeared to agree with Vice Premier Qian, by saying that the election system should be something “home-grown”, “representative but not necessarily simply cloned from Westminster or US Congress”.

While the then chairman of the Democratic Party, Martin Lee, said Vice-Premier Qian’s statement “disregarded or violated the Basic Law”, some leaders of other parties such as Ambrose Lau of the Hong Kong Progressive Alliance and Eric Li of the Breakfast Group also said that Mr Qian’s remarks were only “personal views” and should not affect Hong Kong people’s right to define their constitutional system.

The then Secretary designate for Constitutional Affairs, Stephen Lam, said the Government would explore constitutional development “on the basis of the Basic Law and the “one country, two systems” principle.” However, when representatives of democratic groups submitted a petition to the Chief Executive at the end of July, calling for a constitutional review and elections by universal suffrage, Mr Lam replied that the Government did not have a firm agenda for the public consultation exercise but that it would ensure that there was adequate time for it to be completed before 2007.

– ***Proposals to subsidise legislative elections***

As there would be legislative elections in 2004, Secretary for Constitutional Affairs Stephen Lam suggested in December that the government should partly subsidise the campaign expenses of those candidates who are elected or who receive at least 5% of the vote. Each valid vote received by such candidates would be subsidised to an amount of ten Hong Kong dollars, subject to a ceiling of half of the total expenses, the aim being to encourage the participation of parties and independent candidates in the election process.

This suggestion was well received by Hong Kong political parties. However, the government stated that it is inappropriate to draft a bill on political parties.

The European Commission welcomes the idea of subsidising election expenses, as it will encourage more Hong Kong citizens to participate in the democratisation process.

4. LEGISLATIVE DEVELOPMENTS

– *Article 23 of the Basic Law*

On 24 September 2002, the Security Bureau of the Hong Kong Special Administrative Region Government published a Consultation Document on the legislative proposals to implement Article 23 of the Basic Law. Article 23 requires the HKSAR to “enact laws on its own to prohibit any act of treason, secession, sedition, subversion against the Central People’s Government”. It also deals with the issues of State secrets and the activities of foreign political organisations in Hong Kong.

Many of the issues raised by Article 23 are considered politically sensitive. Ever since the Basic Law was published in 1990 and brought into effect in July 1997, there have been anxieties over the implementation of Article 23. During the first five years following the handover, the HKSAR Government made no move to legislate on Article 23. At the time, its priority was the smooth transition and implementation of the “one country, two systems” principle. After the Secretary for Justice, Miss Elsie Leung, went on a consultation visit to Beijing at the end of February, it was reported that Mr Qiao Xiaoyang, Deputy Chairman of the Legal Work Committee of the National People’s Congress, had reiterated that in compliance with the Basic Law, the HKSAR is obliged to enact Article 23. In an interview with Hong Kong media at the end of June, Vice-Premier Qian Qichen stated again that “one of the tasks before the SAR Government is to enact Article 23 of the Basic Law”.

Soon after Chief Executive Tung’s reappointment in July 2002 for another 5-year term, the Government decided that the time was right to put forward legislation.

The Consultation Document set out, in broad terms, what the SAR Government intended to do. Hong Kong already had domestic legislation on treason, sedition, State secrets, activities of and ties with foreign political organisations inherited from the British period, and the SAR Government proposed to amend the existing legislation in order to reflect the current realities. The offences of subversion and secession have been added for the first time. The Consultation Document proposed to create a new power to proscribe organisations affiliated with any Mainland organisation that had been proscribed there on the grounds that it endangered national security. The document also recommended granting special investigative powers (emergency search) to the police for these offences.

The public consultation period ended on 24 December 2002. The SAR Government intended to draft legislation to be tabled in the Legislative Council by February 2003. The Government wanted to see the legislation enacted in July 2003, but stated this was not an absolute deadline.

The three-month consultation produced a record 97,000 submissions and 340,000 signatures. Although initial reactions to the document were quite mild, as time passed and political parties, human rights organisations, business and international communities started raising concerns, Article 23 became a major political issue in Hong Kong.

Most local and foreign associations, bodies and parties recognise that the HKSAR Government has a constitutional obligation to legislate on this matter. Others, who initially claimed that there was no need for anti-sedition laws in Hong Kong, have increasingly

stressed the defence of civil liberties and press freedom. The Democratic Party and the Frontier, as well as major local and international NGOs and associations (Amnesty International, Human Rights Watch, Hong Kong Human Rights Monitor, Hong Kong Journalists Association, etc.) are strongly opposed to the Article 23 proposals. They have expressed serious concerns that freedoms in Hong Kong will be eroded and that the perception of the outside world of Hong Kong as a place to do business may be affected.

Part of the business community also expressed fears that Article 23 runs contrary to the principle of transparency and openness of information. Similar concerns were expressed by the banking sector.

Almost all parties that contributed to the debate over Article 23 seemed to agree on the fact that in the absence of draft legislation, it was impossible to make an accurate assessment of the possible effects in respect of human rights and fundamental freedoms. Several local and international associations, with the Hong Kong Bar Association at the helm, called on the Government to provide a text in the form of a white bill and to undertake a second round of public consultation before drawing up the blue bill for first reading in the Legislative Council. The Hong Kong General Chamber of Commerce, who, however, underlined the need for timely legislation to implement Article 23, also echoed this position. Furthermore, Mrs Anson Chan, former Chief Secretary for Administration of HKSAR, argued that the “devil is in the detail”. She stressed that it was more important to get the legislation right than to rush to meet a deadline, and that a white bill would be “reassuring for all”.

On the international front, the EU, the United Kingdom, USA, Canada and Australia, as well as the Chambers of Commerce of the UK and USA in Hong Kong issued statements on the Consultation Document. The EU, in its statement of 23 December 2002, noted the concerns that had been raised in Hong Kong and in particular the extra-territorial effect of some proposed offences as well as the broad definition of those offences, and called on the HKSAR Government to ensure that this legislation and its implementation would not undermine the principles of the rule of law and that the rights and freedoms outlined in the Joint Declaration and the Basic Law would be protected.

On 19 December 2002, the European Parliament adopted an unanimous resolution calling on the HKSAR Government to ensure that Article 23 proposals would not be used to silence opposition, restrict freedom of speech, the freedom of the press and of publication, freedom of association, freedom to demonstrate, the right and freedom to form trade unions, to strike and undertake other cultural activities in accordance with Articles 27 and 34 of the Basic Law. Additionally, it called on the Government to publish a draft bill setting out clearly detailed provisions to be followed by further consultations.

The HKSAR Government defended its proposals and had as at the end of 2002 refused to provide draft legislation in the form of a white bill. Nevertheless, senior government officials tried to reassure the public by arguing that the proposals under Article 23 would be consistent with human rights guarantees in the Basic Law and in the International Covenants on Civil and Political Rights and on Economic, Social and Cultural Rights. The Government would review the proposals in the light of the submissions received, in particular with regard to the offence of possessing seditious publications, the investigative powers of police and the avenues of appeal if a local organisation were to be banned. The Government also stressed that the best safeguard to Article 23 was already in place, namely Article 39 of the Basic Law, which stipulates that no law can be validly enacted if it contravenes international standards of human rights.

Article 23 legislation is undoubtedly the most important and sensitive legislation to be introduced in Hong Kong since the handover in July 1997. Its potential impact on freedom in Hong Kong and the territory's lifestyle is far-reaching. Over the three-month consultation period, the gap between the camps for and against Article 23 was a divisive factor in Hong Kong society. There were two major public demonstrations in December 2002 about Article 23, one against (estimated 60,000 people) and one for (est. 40,000 people).

The fact that these views were expressed freely reflects the openness and freedom of Hong Kong. Article 23 is a matter that touches the heart of "one country, two systems". The European Commission will continue to monitor this important issue very closely, paying particular attention to its effects on the respect of human rights and civil liberties.

– ***Anti-terrorism legislation***

As Chair of the OECD's Financial Action Task Force (anti-money laundering body) (FATF), Hong Kong hosted a FATF plenary session in January and played a leading role in formulating the Recommendations of the Financial Action Task Force on money laundering.

As part of China, Hong Kong is also required by the Central Government to take appropriate measures to implement United Nations Security Council Resolution UNSCR1373. On 17 April, the SARG introduced the United Nations (Anti-Terrorism Measures) Bill to the Legislative Council. The bill aims at strengthening Hong Kong's ability to counter the flow of funds to terrorists and terrorist organisations.

Several aspects of the Government's initial draft Bill were hotly debated in LegCo as they raised fears on civil liberties and the Government subsequently amended several points (the Chief Executive's power to gazette the names and property of terrorists, the right to apply to the Court of Appeal for compensation, etc). All but one government motion for amendment was passed. LegCo finally approved the United Nations (Anti-Terrorism Measures) Ordinance on 12 July.

– ***The first steps towards legislation on racial discrimination?***

The Home Affairs Department wrote to 54 ethnic groups and NGOs seeking their views and input on racial discrimination issues. The majority of NGOs expressed support for the introduction of anti-racial discrimination legislation in Hong Kong. In January, the chairwoman of the Equal Opportunities Committee also urged the government to enact a law to prohibit racial discrimination.

The HKSAR government responded by creating a Race Relations Unit in the Home Affairs Bureau and a "Committee for the Promotion of Racial Harmony", comprising government officials and NGO representatives.

These steps were taken in response to concerns raised by the United Nations Committee on the Elimination of Racial Discrimination whose chairman, Ion Diaconu, visited Hong Kong in early November 2002. He reiterated the Committee's concern about the absence of a Racial Discrimination law in Hong Kong. The SAR government reaffirmed that public consultation procedures were underway but no final decision had yet been taken.

5. RIGHTS OF ASSEMBLY AND DEMONSTRATION.

Hong Kong people continue to enjoy their basic fundamental rights and freedoms following the handover and many demonstrations and protests took place. However the exercise of these rights has resulted in some incidents and controversies relating to the Government's handling of demonstrations.

Three Hong Kong political activists of the radical April 5 Action Group defied the Public Order Ordinance by organising a rally on 10 February without obtaining a "letter of no objection" from the police. They were subsequently arrested on 9 May on the charge of organising an unauthorised assembly. This was a significant development, insofar as since the handover the SAR Government had been lenient in handling such demonstrations and no specific group had ever been prosecuted for breaching the Public Order Ordinance.

A local court found the three political activists guilty on 25 November 2002. They were each bound over to be of good behaviour for three months and ordered to sign a HK\$500 bond. The Chief Magistrate rejected the claims that the Public Order Ordinance had breached the provisions of the Basic Law and the Bill of Rights Ordinance. Secretary of Justice Elsie Leung denied suggestions that the case was politically motivated. She argued that the case had been taken to court because the main issue was about whether or not a crime had been committed.

After the Court of Final Appeal's ruling of 10 January in the right of abode case, a series of demonstrations and sit-ins were organised in Chater Garden (next to the Legislative Council building) by defendants who had lost their claim. On 24 April 300 police officers, together with immigration operations personnel moved in to Chater Garden to clear abode-seekers who refused to be sent back to Mainland China. The clearing operation came one day after more than 100 abode-seekers had trapped Secretary for Security Mrs Regina Yip in her car outside the Legislative Council for an hour, as they protested against their treatment. Scuffles broke out during the clearing operation and the police handcuffed two media personnel. This incident drew strong criticisms from media organisations and some legislators, who accused the police of using excessive force and suppressing press freedom.

On 1 October, an activist was apprehended burning the Chinese national flag in a protest staged by the radical April 5 movement against the National Day celebration. The new Director of Central Government Liaison Office, Mr Gao Siren appealed to the police to prosecute the activist for an offence against the National Flag Ordinance. This appeal was criticised by pro-democracy legislators and human rights activists for interfering in HKSAR issues. Secretary for Security Mrs Regina Yip said that the Justice Department would decide whether to prosecute the demonstrator after considering the evidence.

Whilst it understands the necessity of maintaining public order, the European Commission hopes that the practice of the right of assembly and demonstration exercised in lawful conditions will not be affected.

6. THE ECONOMY

Hong Kong has been undergoing a serious adjustment process in the years following the Asian financial crisis. The year 2002 registered a deepening of this trend. Asset prices and wages continued to decline. While the export sector rebounded strongly in the latter half of the year, domestic demand remained weak and investment spending continued to move downwards. GDP achieved a moderate growth of 2.3% in real terms for 2002.

Two major economic issues captured most of the public attention, the fiscal deficit and unemployment, which both peaked in 2002. The Hong Kong SAR Government was under considerable pressure to tackle these problems swiftly.

The SAR Government recorded growing fiscal deficits in two consecutive years, contrary to its tradition of running a balanced or small deficit budget in the past. The fiscal deficit for 2002-2003 reached HK\$70 billion or about 5.5% of its GDP, following HK\$65.6 billion in 2001-2002. The deficit was caused by a combination of cyclical and structural factors. Among other things, land sale and property-related taxes that used to be an important source of revenue have been declining. On the expenditure side, an attempt to cut civil servants' salaries came up against legal and constitutional constraints. Tackling the deficit will be a major policy area for the SAR Government in the next few years.

However, Hong Kong continues to enjoy a comfortable reserve position. Its reserves stood at HK\$303 billion as at the end of the financial year of 2002-03, compared to HK\$369.8 billion at the end of 2001-02.

The unemployment rate peaked at 7.8 % in the middle of the year and then dropped to 7.2% at the end of the year. Despite the cyclical factors during economic downturn, a rising trend of relocating some support service operations to Mainland China was noted. This affected in particular the middle aged, the less-skilled or less-educated part of the work force, as well as manufacturing and construction workers.

The property sector, an important contributor to growth in past years performed poorly, and, in an attempt to revitalise the market, the government introduced a new set of housing measures in November. Under the new policy, provision of public flats for sale to low-income groups has been suspended, and land sale activities have been frozen until the end of 2003. These measures were devised to redress the oversupply situation and avoid competition with the private sector.

On the external front, Hong Kong's exports of goods and services to Mainland China continued to increase. More than 90% of Hong Kong's total exports were re-exports. Of the total re-exports, about 60% were of Chinese origin and 40% of goods were destined for China. Exports of goods to China fared well in 2002. In the tourism and retail sectors, Chinese visitors boosted the local economy. The abolition of the quota system for the Hong Kong Group Tour Scheme for Chinese visitors as from January 2002 stimulated tremendous growth in visitor arrivals. In 2002, the number of Mainland Chinese visitors registered a year-on-year growth of 53% (about 6.8 million), accounting for about 40% of the total visitor arrivals, China thus becoming the largest source of visitors.

There were notable developments in establishing closer links with Mainland China, especially with the Pearl River Delta. The SAR Government actively pursued the proposal of building a bridge linking Hong Kong, Macao and Zhuhai. The Western corridor linking Hong Kong and Shenzhen was at the detailed planning stage and is due to be completed in 2005. 24-hour crossings at Lok Ma Chau-Huanggang checkpoints were agreed upon. Further liberalisation of flows of people between the two places was also noted.

The Closer Economic Partnership Arrangement (CEPA) consultations commenced in January 2002 between the HKSAR Government and the Central Government. The definition of Hong Kong companies for the purposes of benefiting from the proposed bilateral arrangement was one of the issues that generated some anxiety in the business community. Both Hong Kong and Mainland China reiterated that the arrangement would be in accordance with WTO rules. The European Commission will closely monitor that the final arrangement will be WTO-compatible and in particular will not discriminate against foreign companies established in Hong Kong.

A trade policy review of Hong Kong was conducted at the WTO in 2002, the second since the establishment of the SAR in 1997. It concluded that Hong Kong's institutional and policy framework had remained largely unchanged since its reversion to China and was in accordance with the principle of "one Country, two Systems". Hong Kong had also maintained its traditional openness to both trade and investment. However, the review also noted that the lack of -appropriate legislation might hamper the effective application of fair competition in Hong Kong.

7. EUROPEAN UNION - HONG KONG RELATIONS.

– Exchange of visits and high level contacts

As in previous years, high-level visits and meetings continued to enhance EU-Hong Kong relations. Commissioner Michel Barnier paid a short visit to Hong Kong at the end of January where he met the Chief Executive, Mr Tung Chee Hwa and discussed political and economical developments both in the EU and Hong Kong.

The Chief Secretary for Administration, Mr Donald Tsang, paid his second official visit to the European Commission in May, the first having taken place in November 2001. During his stay in Brussels, Mr Tsang met the President of the European Commission, Romano Prodi and Commissioners Pascal Lamy and Antonio Vitorino. Discussions focused on developments in Hong Kong and EU-Hong Kong relations in the five years since the SAR's handover to China on 1 July 1997. Other topics covered during Mr Tsang's visit were the EC-HK Customs Cooperation Agreement and the finalisation of the EC-HK Re-admission Agreement.

Contacts took also place in the margins of international events between Commissioner Lamy and the Secretary for Trade and Industry, first Mr Brian Chau and then Mr Henry Tang. Discussions mainly focused on the Doha multilateral trade negotiations and on the development of the trade relations between Hong Kong and Mainland China.

Mrs Rita Fan, President of the Hong Kong Legislative Council (Legco), visited the European Parliament in both Strasbourg and Brussels in September. The purpose of the visit was to study the facilities and architecture of the EP's buildings, as the Legco was planning to build a new complex by 2007. Mrs Fan also had important political meetings with members of the

European Parliament. She was received by Mr Colom i Naval, Vice-President of the EP, Mrs Plooij-Van Gorsel, Chairperson of the EP's Delegation with China, Hong Kong and Macao and Mr Priestley, Secretary-General of the EP.

A delegation from the Economic and Social Committee, led by president of the study group on the relations between EU and China, Mr Sukhdev Sharma, visited Hong Kong in July. It had meetings with local NGOs, human rights groups and academics. The visit focused on economic, social, human rights and environment issues.

– ***EC-Hong Kong Re-admission Agreement***

An agreement between the European Community and the Hong Kong Special Administrative Region (SAR) of the People's Republic of China on the readmission of persons residing without authorisation was signed on 27 November 2002 in Brussels. This agreement is the first-ever readmission agreement signed between the European Community and a third country or territory. It will enable Hong Kong and the EC to ensure, on a reciprocal basis, the rapid and effective identification and return of persons entering or remaining illegally in their respective territories.

The agreement was signed jointly by Commissioners Chris Patten and Antonio Vitorino, responsible for, respectively, External Relations and Justice and Home Affairs, and by Antony Leung, Financial Secretary of Hong Kong SAR. It follows the Community's March 2001 decision to grant visa-free access to Hong Kong SAR passport holders.

Negotiations for this agreement were finalised at the end of 2001, and the agreement was initialled on 22 November 2001 on the occasion of Hong Kong Chief Secretary for Administration Donald Tsang's visit to Brussels. The conclusion of re-admission agreements is part of the EU's broader strategy for combating illegal immigration, adopted by the European Council at its meetings in Tampere, Laeken and Seville. Commissioners Patten and Vitorino emphasised the valuable role such agreements play in this respect.

Commissioner Patten and Antony Leung also exchanged views on the overall political and economic situation and perspectives in Hong Kong, on the SAR Government's fiscal and budgetary policies, and on closer economic ties with Mainland China, in particular the Pearl River Delta.

– ***Customs Cooperation***

Customs cooperation between the European Community and the HKSAR continued in 2002 on the basis of the 1999 Agreement on Cooperation and Mutual Administrative Assistance in Customs Matters. The fourth Joint Customs Cooperation Committee was concluded in Hong Kong on 5 December, with constructive and profitable results.

– ***Intellectual Property Rights***

In spite of a very complete legal and administrative array in terms of protection of intellectual property rights, several EU companies point out a recrudescence of counterfeit goods in transit on the HK territory, in particular in the sectors of luxury goods, of new information and communication technologies. Furthermore, the recent seizures in Hong Kong of counterfeited pharmaceutical products raised concerns amongst the EU industries of the sector.

– ***Business Cooperation Committee***

The Business Cooperation Committee brings together business representatives from the EU and Hong Kong to discuss economic developments and other matters of mutual interest. The Fourth Plenary Session of the Committee was held in Brussels on 21 – 22 May and was attended by Commissioner Lamy and Chief Secretary Donald Tsang, who both gave speeches at the opening dinner. There was high-level participation on both sides. HK placed emphasis on the economic integration in the Pearl River Delta, whilst the EU highlighted the completion of the EMU and its political significance.

– ***EU presence and interests in Hong Kong***

The EU was Hong Kong's third largest supplier in 2002 after Mainland China and Japan, and was the third biggest market for Hong Kong's exports, after Mainland China and the United States. Total bilateral trade decreased further to 29.6 billion Euro (imports from Hong Kong: 9.7 billion Euro; exports to Hong Kong: 19.9 billion Euro, i.e. a 10 billion Euro surplus for the EU).

In terms of foreign investment, the EU was the fourth largest source of external investment for Hong Kong in 2001, after Mainland China, British Virgin Islands and Bermuda. The total inflow of investment from the EU reaching HK\$ 7 billion or 1 billion Euro in 2001. The stock of direct investment from the EU amounted to HK\$ 289,2 billion (41,2 billion Euro), accounting for 8,8% of the investment total.

EU companies are an important group of market players in the financial services of Hong Kong. In the insurance sector, the EU continued to top the list of overseas insurers operating in Hong Kong in 2002. Out of a total of 107 overseas banks licensed in Hong Kong, 36 were incorporated in the EU as of the end of December 2002, the largest number of foreign banks in Hong Kong.

In the public works sector, EU companies were awarded contracts totalling 46 million Euro in 2002.

In 2002, there were 266 EU companies using Hong Kong as their regional headquarters and 572 as their regional offices. It is estimated that 40,330 EU citizens were residing in Hong Kong at the end of 2002.

8. CONCLUSION

The introduction of the government accountability system at the start of the second term of the Chief Executive is a first step towards the development of a more democratic constitutional system. The European Commission hopes that this first step will soon be followed by the launch of public consultation on the election of both the Chief Executive and all members of the Legislative Council by universal suffrage, as provided for under the Basic Law.

The Commission welcomes the Article 23 consultation process which revealed that the people of Hong Kong attach great importance to the rule of law and the respect of fundamental freedoms. Many feared that the enactment of Article 23 of the Basic Law might threaten these freedoms which characterise Hong Kong's system. The Commission finds some encouragement in the fact that the Hong Kong Government amended its initial proposals to take account of public reactions and suggestions, and calls on the SAR Government to continue to take into consideration opinions expressed by the Hong Kong people and the international community.

The Commission believes that the rule of law and the continued respect of the fundamental freedoms guaranteed by both the Basic Law and the international human rights covenants are the foundation-stones of a free and vibrant Hong Kong society. It will continue to monitor closely the implementation of Article 23 before and after the adoption of the new legislation.

The Commission acknowledges the consultations between Mainland China and the HKSAR on a "Closer economic partnership arrangement" (CEPA). Such an arrangement should be WTO-compatible and not discriminate against other WTO members. Hong Kong's further economic integration with Mainland China is an asset for both, provided that Hong Kong retains its individual personality within the framework of the "one country, two systems" principle.

The signing of a readmission agreement in November was a major step forward in EU-Hong Kong relations, and the Commission looks forward to its coming into force in 2003.

Hong Kong's economic adjustment is understandably a long and difficult process. The people of Hong Kong should remain confident about future economic developments and continue to take full advantage of the assets the SAR has as an international financial centre and services-oriented economy.