No. 81 (9/98) CAPS

THE PARADOX OF HONG KONG
AS A NON-SOVEREIGN
INTERNATIONAL ACTOR

by

Professor James C. Hsiung

Faculty of Social Sciences
Lingnan College
Hong Kong
June 1998
THE PARADOX OF HONG KONG AS A NON-SOVEREIGN INTERNATIONAL ACTOR

CAPS and CPPS Working Papers are circulated to invite discussion and critical comment. Opinions expressed in them are the author's and should not be taken as representing the opinions of the Centres or Lingnan College. These papers may be freely circulated but they are not to be quoted without the written permission of the author. Please address comments and suggestions to the author or the series editors.
© James C. Hsiung

Professor James C. Hsiung is the Head of Department of Politics and Sociology and Chair Professor of Political Science, Lingnan College, Hong Kong.

Faculty of Social Sciences
Lingnan College
Tuen Mun
Hong Kong
Tel : 2616 7429-32
Fax : 2591 0690
THE PARADOX OF HONG KONG AS A NON-SOVEREIGN INTERNATIONAL ACTOR

- James C. Hsiung -
- Lingnan College, Hong Kong; New York University, NYC -

Introduction

In social science parlance, a “paradox” is a phenomenon marked by a conflict between, in game-theoretic language, dominant strategy and optimal outcome.¹ For our purpose here, a paradox mainly denotes a discrepancy, or a complex of discrepancies, between expectations and outcome. For example, there had been a near-unanimous consensus (expectation), on the part of Western media and many commentators, that Hong Kong after reversion on July 1, 1997 would not be able to enjoy, under the watchful eyes of its Chinese sovereign, its promised high degree of autonomy. Subsequent events have, paradoxically, proven these expectations to be false, at least during the first year. In Taiwan, Hong Kong’s most hard-nosed critic, a highly placed official – Dr. King-yuh Chang, director of the Mainland Affairs Office – responding to questions in the Legislature, gave an unequivocal, though somewhat grudging, answer that “in the nine months since the hand-over, Beijing did not excessively interfere, but let Hong Kong govern itself as a highly autonomous entity.”² Even the usually skeptical London-based Economist had to admit, with a straight face, that two “common predictions” about how Hong Kong would fare without British rule “have refused to come true: the Communists in Beijing have refused to call the shots; and the chief executive, Tung Chee-hwa, despite being a deeply conservative fan of ‘Confucian’ authority, has not become an oriental despot” (The Economist, March 28, 1998, p 25). Despite widespread speculation before 1997 that the HKSAR would be dragged into the abyss of corruption under Chinese influence, a survey in April 1998 showed that the SAR’s corruption during the past nine months following the handover had been at an all-time low in five years.³

² “Taiwan Says Mainland Has Kept Its Promise Regarding Hong Kong’s Autonomy,” Ming Bao (Hong Kong), March 12, 1998, p. 13.
³ “SAR Corruption Lowest in 5 Years, Survey Shows,” South China Morning Post (hereinunder cited as SCMP), April 6, 1998, at B-2. Speculating about Hong Kong catching the corruption virus from
On the international front, many pundits, including international-law experts, had expected the Hong Kong Special Autonomous Region (HKSAR) to enjoy a high international profile, endowed as it was with a legal capacity, and political versatility, to function as an international actor in its own right, despite its lack of sovereignty after reversion, as before. But, as we shall see below, things have not turned out quite as expected, owing to unforeseen extraneous factors (including wildcat foreign judicial assaults on Hong Kong’s jūs stāndī). Hence, a paradox.

In fact, most of the prophets of doom were apprehensive about the domestic scene of Hong Kong, given its unprecedented “one country, two systems” model installed after handover to China. Few had doubts, however, about the territory’s international capacity to act, as the latter was guaranteed by the devolution agreement embodied in the 1984 Sino-U.K. Declaration on the territory’s return to Chinese sovereignty and, in addition, by the SAR’s Basic Law. Furthermore, one could point to a body of well-established precedents (international custom), as evidence of general practice accepted as binding in general international law. Instead, domestically, the Hong Kong SAR has had few surprises. It is, by contrast, in the international arena that the Hong Kong SAR, through no fault of its own, has not quite fully lived up to expectations. As such, the contrast is a giant paradox in itself.

In this paper, I shall not have the luxury of looking equally into the SAR’s domestic performance. Instead, I shall focus on the inchoate evidence of how the HKSAR has met with circumstances or treatment by foreign countries quite at variance with many pundits’ expectations regarding Hong Kong’s international status and capacity to act. To illustrate this point, we need to examine some existing cases. But, for an easier flow of discussion, I propose that we first look at some juridical cases that will demonstrate how Hong Kong’s international capacity to act has been

China almost became a Taiwan pastime; see, e.g., “ICAC Fights Corruption Creeping into Hong Kong from the North,” in 19 Inside China Mainland 9:9-12 (No. 205, 1997) (Taipei).


5 This language suggesting the relationship of practice and custom to general international law was borrowed from Art. 38 (1)(b) of the Statute of the International Court of Justice.
given a short shrift by foreign tribunals and judicial organs. Following that, we shall extend our inquiry to non-legal cases and issues.

**Foreign Judicial Test**

Let me preface this discussion by noting that, while the HKSAR’s international capacity is provided for and defined by the 1984 U.K.-PRC Joint Declaration, the SAR’s Basic Law, and general international law, the exact nature of this capacity has to be tested in real cases. Although the cases presented here were decided shortly before the 1 July 1997 handover date—in one case, only three days before—we have reasons to believe that these decisions have set the frame of reference for future cases, ceteris paribus.

The first, and most revealing, case to be examined in this connection is *Matimak Trading Co. v. Albert Khalily & D.A.Y. Kids Sportswear, Inc.* (1997). This was a case involving non-payment by the defendant totalling US$80,000 for goods shipped, in which Matimak Trading, a Hong Kong corporation, sought relief by suing in U.S. courts for breach of contract by D.A.Y. Kids Sportswear.

Plaintiff Matimak invoked the court’s diversity jurisdiction under 28 U.S.C. Section 1332(a)(2), which provides jurisdiction over any civil action arising between “citizens of a State [in the Union] and citizens or subjects of a foreign state.” In June 1996, the District Court for the Southern District of New York raised the issue of its own subject matter jurisdiction. And, in August 1996, after allowing the parties to brief the issue, the district court dismissed the Complaint for lack of subject matter jurisdiction. The court concluded that Hong Kong was not a “foreign state” under the diversity statute, and, consequently, Matimak was not a “citizen or subject” of a “foreign state.” Upon dismissal by the District Court, however, the case was appealed to the U.S. Court of Appeals for the Second Circuit (118 F. 3d 76; 1997 U.S. App. LEXIS 15889).

At issue was whether a Hong Kong corporation was either a “citizen or subject” of a “foreign state” for purposes of alienage jurisdiction. Matimak was incorporated

---

6 I am indebted to Prof. Hungdah Chiu, of the University of Maryland Law School, for obtaining for me a full copy of the decision by the U.S. Court of Appeals during my absence from my home base in New York, while on a visiting assignment in Hong Kong.
under Hong Kong law—to be exact, the Companies Ordinance 1984 of Hong Kong—and was entitled to the protection of Hong Kong. More precisely, the question whether Matimak, a Hong Kong corporation, had the right to sue in the U.S. federal court system, turned on the precise legal status of Hong Kong.

In the *stare decisis* of U.S. jurisprudence, a precedent was *Cedec Trading Ltd. V. United American Coal Sales, Inc.* (556 F. Supp. 722-724, & n.2 [S.D.N.Y., 1983]). In that case, the Court held that corporations of the Channel Islands, a province which was part of the United Kingdom proper, governed by British law, and whose foreign affairs were entirely controlled by the United Kingdom, was a citizen or subject of the United Kingdom. Hence, it had the right to sue in American federal courts.

Before arriving at its decision in the *Matimak* case, the Appeals Court, in analyzing the background of the lower-court decision under review, discussed a number of basic issues in trying to navigate what it called “shoal-strewn area of the law.” The United States Judicial Code, the Appeals Court began, tracks the constitutional language used in Art. III, Sec. 2, Cl. 1, of the U.S. Constitution—which extends the federal judicial power to “all cases between a State [of the Union], or citizens thereof, and foreign States, Citizens or Subjects” – by providing diversity jurisdiction over any civil action arising between “citizens of a State and citizens or subjects of a foreign State” (28 U.S.C. Sec.1332(a)(2)). This judicial power is referred to as “alienage jurisdiction.”

Neither the U.S. Constitution nor Sec. 1332(a)(2) of the United States Code defines “foreign state.” In relevant cases decided by U.S. courts, it was generally held that a foreign state was one formally recognized by the executive branch of the U.S. Government (C. Wright, A. Miller, and E. Cooper, *Federal Practice & Procedure*, Sec. 3604 (1984)).

While both plaintiff and defendant in the present case agreed that the United States had not formally recognized Hong Kong as a foreign state, Matimak, however, contended that Hong Kong had received “de facto” recognition as a foreign state by the United States. It pointed to the latter’s diplomatic and commercial ties with Hong Kong as evidence of this de facto recognition.

After reiterating the habitual judicial deference to the Executive Branch on matters of recognition of foreign states (e.g., *Iran Handicraft; Abu-Zeineh v. Federal Labs*,
Inc. Bank of Hawaii v. Balos, etc.), the Appeals Court then turned to the U.S. Hong Kong Policy Act, which Congress enacted in 1992, to govern U.S. relations with Hong Kong beyond the end of British colonial rule on July 1, 1997. While expressing a strong U.S. “interest in the continued vitality, prosperity, and stability of Hong Kong” beyond its reversion to become a special administrative region of China, the Act “makes equally clear, however, that the United States did not regard Hong Kong as an independent, sovereign political entity,” the Court concluded.

The parties also quarreled over the significance of the British Nationality Act of 1981, which delineates British citizenship in detail. This Act, the Court declared, “fails to support Matimak’s assertion that a Hong Kong corporation is a citizen of the United Kingdom.” The Act, it added, “applies only to natural persons, not corporations.”

Citing Matimak as “stateless,” as it was not a “citizen or subject of a foreign state,” the Appeals Court affirmed the District Court’s dismissal of the suit for lack of subject matter jurisdiction.

The decision by the U.S. Court of Appeals for the Second Circuit, handed down on June 27, 1997, or three days before Hong Kong’s return to Chinese sovereignty, thus definitively concluded that no Hong Kong corporation had the right to sue in a U.S. federal court. The question arises as to whether the territory’s reversion makes any difference. The answer, it appears to me, depends on whether the Cedec Trading Ltd. case, cited earlier, can find a parallel situation in the HKSAR.

The key link, which the Court found missing in the Matimak case, was that Cedec Trading was a corporation of the Channel Islands, a province which was part of the United Kingdom proper, governed by British law, and whose foreign affairs were entirely controlled by the United Kingdom. As such, Cedec Trading was a citizen or subject of the United Kingdom, a foreign state properly recognized by the executive branch of the U.S. government.

By contrast, the U.S. Appeals Court did not similarly consider Hong Kong as part of the United Kingdom proper, and, although still a British colony at the time of the Court’s ruling (27 June 1997), the Hong Kong colony’s autonomy relative to Channel Islands deprived Hong Kong of the same juridical link tying the latter to the British sovereign. By the same token, the [future] HKSAR’s high degree of autonomy, such
as is guaranteed by the Basic Law, would likewise, following the court’s logic, deprive Hong Kong of its link to the Chinese sovereign after its 1997 handover. What a paradox!

Below, I shall offer my critique of the U.S. Court’s ruling from the perspective of both the intent of the 1992 U.S. Hong Kong Policy Act and, equally, earlier cases decided by U.S. federal courts relevant to the Matimak case. Here, however, let me reiterate that despite the pre-1997 expectations held by many well-qualified pundits and international-law experts, the ruling of the U.S. Appeals Court, upholding the lower court’s dismissal of the Complaint, threatens to take away whatever certainty there may have been from Hong Kong’s international eligibility to act in asserting claims or espousing causes, either in behalf of or through its juridical persons (corporations).

->Jerry Lui vs. the U.S. (110 F.3d 103; US Court of Appeals, 1st Cir., March 20, 1997).7

On December 19, 1995, pursuant to 18 U.S.C.A. Sec. 3184 (West Supp. 1996), the United States Attorney’s office filed an extradition complaint in the District Court of Massachusetts against Lui Kin-Hong (a.k.a. Jerry Lui), setting forth the United Kingdom’s extradition request on behalf of Hong Kong. In response, Magistrate Judge Karol issued a warrant for Lui’s arrest. Since December 20, 1995, when Lui was arrested upon disembarking from a plane at Boston’s Logan Airport, he was in custody pending the completion of his extradition proceedings. At the end of these proceedings, the District Court of Massachusetts granted a writ of habeas corpus to Mr. Lui, preventing his extradition to the Crown Colony of Hong Kong pursuant to two extradition treaties between the United Kingdom and the United States. Thereupon, the United States appealed before the U.S. Court of Appeals for the 1st Circuit. The court of appeals (per Lynch, J.) reversed the judgment of the district court and ordered that Lui continue to be held without bail, pending extradition to Hong Kong.8

---

7 In this discussion I am relying on Prof. James D. Wilets’s summary in 91 American Journal of International Law 3:537-541 (1997).
8 According to Daniel Fung, the HKSAR’s Solicitor General, in a personal communication dated 11 March 1998, Lui would be extradited and was scheduled to arrive in Hong Kong on 22 May 1998.
In this straightforward case, a couple of things merit our attention as they pertained to both Hong Kong’s reversion to China and the territory’s international capacity. First, although United Kingdom requested Lui’s extradition in behalf of Hong Kong, pursuant to two outstanding extradition treaties, there was only a passing reference made to Hong Kong’s international capacity. This came in the Appeals Court’s brief mention of a new extradition treaty that the U.S. President had signed with the incoming government of the HKSAR, which was pending in the Senate. The court, however, did not address the complex issues related to the entry of the United States into a treaty with a not yet existent entity.

Second, the appeals court, as the district court before, correctly noted that Hong Kong was soon to revert back to China, a country with which the United States had no existing extradition treaty. Both courts were clearly concerned over the prospect that, if extradited, Lui might be tried and punished by the Chinese, who would soon take over Hong Kong. The district court had argued that Lui “cannot be extradited to a sovereign hat is not able to try and punish him [a reference to the United Kingdom, which was soon to relinquish its sovereignty over the colony], any more than he could be extradited to a non-signatory nation (Lui Kin-hong, 957 F.Supp.at 1287).” However, Sec. 201(b) of the U.S. Hong Kong Policy Act clearly stipulates: “For all purposes, including actions in any court in the United States, Congress approves the continuation in force on and after July 1, 1997, of all treaties and other international agreements,” entered into before such date between the United States and the United Kingdom and applied to Hong Kong, unless or until terminated in accordance with law (italics added).” Covered by this provision was the U.S.-U.K. Extradition Treaty of 1972, which per its Art. II(a) applied to Hong Kong (28 U.S.T. 227; TIAS, No. 8468). If the U.S. appeals court were to apply the law, the political factor (i.e., Hong Kong’s forthcoming handover to China) should have no juridical consequence and would have been immaterial. But, apparently, both the appeals court and the lower court were swayed by political exigency (i.e., Hong Kong’s return to China), to the neglect of the law.

Third, both the lower court and the appeals court seemed to be blowing hot and cold at the same time. While they recognized the separate existence of the Hong Kong SAR, they also seemed to suggest that the validity of the new US-HKSAR
extradition treaty (assuming it was ratified with Senate advice and consent) was contingent upon the good faith of the Government of the People’s Republic of China in respecting the independent judicial system and laws of Hong Kong. The upshot was, for our interest here, that Hong Kong’s capacity to act as a non-sovereign international entity was nearly totally glossed over by both the District Court of Massachusetts and the U.S. Court of Appeals, 1st Circuit. Sovereignty, it seems, still was the controlling desideratum to the courts, despite all the claims regarding Hong Kong’s status as a non-sovereign international actor. But, as we shall see below, both courts seemed to be selectively applying the sovereignty test, conveniently putting a blind eye to the fact that after reversion, the HKSAR by dint of the Basic Law, its mini-constitution, will enjoy a high degree of autonomy in all aspects except in foreign relations and defense. Like the Channel Islands in the Cedeck Case, the HKSAR will be a part of China, hence a subject region of a recognized foreign state, by virtue of the fact that its foreign relations will be controlled by its Chinese sovereign. The US district and appeals courts, however, chose not to give judicial cognizance to this crucial fact. Had they done so, their decision would have been totally different.

< > Regina v. Secretary of State for the Home Department, ex parte Launder (1 W.L.R. 839; House of Lords, UK, May 21, 1997).

Unlike the two previous cases, this case took place in the United Kingdom. The UK Secretary of State for the Home Department appealed a decision by the Divisional Court of the Queen’s Bench Division (Q.B. Div’l Ct., 6 August 1996), quashing a warrant for the return of applicant, Ewar Quayle Launder, to Hong Kong, to face trial for corruption. The House of Lords upheld the appellant. But, the reasoning was interesting.

Technically, this case arose in a somewhat different procedural posture from that found in the Lui v. U.S., as discussed above. In that case, because of the provisions of the U.K.-U.S. Extradition Treaty, the issue of whether the extradited individual would

---

\(^9\) For this point, see Wilets’s report in ibid., at 540.
\(^{10}\) This goes against the grain of a rising literature which argues that sovereignty is in decline and that non-sovereign actors are becoming both more numerous and more important in their effects on international relations. See, for example, Robert H. Jackson, Quasi-States: Sovereignty, International Relations, and Third World (Cambridge University Press, 1990).
face trial and judgment by the same country requesting extradition was a predominant concern. Hence, the transition in Hong Kong’s status from a British colony to a special administrative region of China was perforce a central issue. In the present Launder case, the issue was whether the accused would face oppression or injustice upon extradition to Hong Kong.

Despite the technical difference, however, the Law Lords were in reality preoccupied with the fixation of China’s takeover of Hong Kong. The court, in the final analysis, weighed the significance of the political situation in Hong Kong for the sake of determining whether the Secretary of State for the Home Department had exceeded his discretion in ordering applicant’s extradition. It observed:

“The question whether it is unjust or oppressive to order the applicant’s return to Hong Kong must in the end depend upon whether the P.R.C. can be trusted in implement of its treaty obligations to respect his fundamental human rights, allow him a fair trial and leave it to the courts, if he is convicted, to determine the appropriate punishment (1 W.L.R. [1997], at 857).” (Italics added)

Like in the Lui case, the controlling question turned on the P.R.C., or, to be exact, the prospect of Launder facing oppression and injustice under the Chinese, who were scheduled to take back Hong Kong after 1 July 1997. There was no consideration of Hong Kong’s post-reversion autonomy, including an independent judiciary, guaranteed both by treaty and by the Basic Law, much less its international capacity as a non-sovereign actor. More than the Lui case, the UK court’s fixation with the Chinese takeover and the wisdom and merit, under the circumstances, of extraditing Launder back to Hong Kong, where he was wanted for corruption, in retrospect, looked almost arrogant and preposterous, if not totally absurd. Of interest to us, nonetheless, is that the U.K. court was obsessed with the question whether Hong Kong’s rule of law would not prove illusory after the end of British rule. Even more important to our interest here is that there was no deliberation by the British court of the Hong Kong SAR’s capacity to handle an extradition case externally and to ensure a fair trail of an extradited individual on corruption charges internally. More than the Lui case, the international status of the HKSAR was a total non-issue in the eyes of the British Law Lords in the present case.
Critique of the Matimak Decision

The U.S. Court of Appeals for the Second Circuit, before reaching the Matimak decision, turned for guidance to the U.S. Hong Kong Policy Act of 1992 and, as noted above, concluded that under the Act “the United States did not regard Hong Kong as an independent, sovereign political entity.” This conclusion was technically right, but was in fact violative of the spirit of the 1992 Act, as I shall attempt to demonstrate. In doing so, my purpose is to highlight that both the appeals court and the district court, in their anxiousness to disclaim subject matter jurisdiction by characterizing Matimak as “stateless,” were preoccupied with the political turn of events (i.e., Hong Kong’s handover to China in 1997), but not with the law, much less with the legal capacity of HKSAR under the “one country, two systems” formula. In their neglect of the law, both courts overlooked a stricture judiciously established in an earlier case (Upright vs. Mercury Business Machines Co. [Supreme Court of New York, Appellate Div., 1961]), to which we shall return below, that “defendant buyer cannot escape liability merely by alleging and proving that it dealt with a corporation created by an unrecognized government, or, as in the Matimak case, by a political entity not recognized by the U.S. government as a “foreign state.”

<>The U.S. Hong Kong Policy Act of 1992 (Public Law No. 102-383). In first introducing the bill on the Senate floor, on September 21, 1991, Senator Mitch McConnell pointed out that the coming return of Hong Kong to Chinese sovereignty in 1997 would necessitate a revision of the relevant U.S. laws which had previously guided American relations with the territory. Close American relations with Hong Kong’s British rulers, in the past, had precluded the necessity of formulating a specific U.S. policy for Hong Kong by Congressional action. Now, however, with the forthcoming transfer of sovereignty to the People’s Republic of China and growing US trade and business links with Hong Kong, he noted, actions must be taken to ensure that these interests were maintained and protected after the 1997 handover.

The bill had near-unanimous support in both chambers of the U.S. Congress, as well as among government officials and experts called to testify. Nevertheless, concerns were voiced that, while the United States continues to develop its multifaceted relations with Hong Kong, caution must be taken, lest its concerns should signal to China unwanted interference into Chinese exercise of sovereignty.
over the territory.\textsuperscript{11} Consistent with this cautious move, the Act simultaneously speaks of U.S. concern for Hong Kong’s autonomy after reversion and calls for respect for the sovereignty of China. For example, in Section 1(2), the Act expresses a Congressional “wish to see full implementation of the provisions of the Joint Declaration” of 1984, between the United Kingdom and the PRC, which guaranteed the HKSAR’s autonomy. The United States, as a matter of policy, is committed to playing an “active role, before, on, and after July 1, 1997, in maintaining Hong Kong’s confidence and prosperity.” The Act also spells out how this policy is to be achieved. On the other hand, at a number of places in the Act, the United States is also obliged, in efforts at continuing and expanding its relations with Hong Kong, to consult the People’s Republic (e.g., Sec. 103(10)). In another instance, the United States is said to “continue to recognize airplanes registered by Hong Kong in accordance with applicable laws of the People’s Republic of China (italics added).” These linguistic genuflections in China’s direction, symbolically, bespeaks of U.S. respect for Chinese sovereignty over the HKSAR.

Thus, by implication, the 1992 Act, while at times highlighting the imperative of Hong Kong’s autonomy, minces no words in recognizing the fact that the post-reversion Hong Kong is part of China. And, this should be read with the HKSAR’s Basic Law, under which the HKSAR’s autonomy notwithstanding, its foreign affairs and defense shall fall under the jurisdiction of the central government of the People’s Republic of China (Arts. 12, 13, and 14). While under Arts. 150 through 154 of the Basic Law the HKSAR may participate in international organizations, conclude international agreements with foreign parties, and even sit on the PRC’s delegations in international organizations in which Hong Kong is not already a member, all this, however, has to be authorized by the central government of the PRC. Under the U.S. Hong Kong Policy Act of 1992, the United States is given the leeway of entering into international agreements with the HKSAR. And all existing laws of the United States “shall continue to apply with respect to Hong Kong, on and after July 1, 1997, in the same manner as ... before...(Sec. 201(a)).” Likewise, under the Basic Law, the HKSAR also has the competence to enter into the kind of agreements as envisaged in

the U.S. Hong Kong Policy Act.

All told, both under the 1992 U.S. Hong Kong Policy Act and under the Basic Law, the Hong Kong SAR is considered to be both an autonomous entity distinct from China and, equally, a subject region whose foreign affairs are controlled by the PRC, its post-1997 sovereign. This situation unmistakably recalls the status of the Channel Islands within the British Empire, as enunciated in the Cedec Trading case. As such, the Hong Kong SAR is an inseparable part of the People's Republic of China; in fact, the SAR was established under Art. 31 of the PRC Constitution. As such, Hong Kong is not "stateless"; nor are its corporations, so long as they were duly incorporated under Hong Kong law.

Furthermore, in anticipation of Hong Kong's return to China, the United States concluded three international agreements in regard to Hong Kong. Two of them, concerning the surrender of fugitive offenders (December 20, 1996) and the transfer of sentenced persons (April 15, 1997) respectively, were signed with Hong Kong per se. The third, regarding the Maintenance of the United States Consulate-General in Hong Kong, was signed on March 25, 1997, directly with the Chinese government in Beijing. The last act legally signified U.S. recognition of Chinese sovereignty over Hong Kong, which ipso facto casts doubt on anyone questioning Hong Kong's "statelessness."

The U.S. Court of Appeals for the Second Circuit, in upholding the lower court's decision dismissing the Matimak case on the ground that it was a Hong Kong corporation, hence "stateless," was both doing an injustice to the spirit of the 1992 Act and, no less important, departing from the well-established recent (1983) precedent of Cedec Trading, which the appeals court cited but quixotically dismissed as inapplicable to the case on hand.

Coming back to the Upright case (13 A.D.2d 36, 213 N.Y.S. 2d 417), it is instructive to bear in mind that defendant Mercury Business Machines Co., like the D.A.Y. Kinds Sportswear Co. in the Matimak case, failed to honor its liability to pay (in the amount of US$27,307.45) for a shipment of business typewriters delivered to it by a foreign corporation. Like in the Matimak case, the district court had dismissed

12 Texts in 36 International Legal Materials 4 (1997), 844-855; 858-865; and 814-816, respectively.
the complaint on the ground that the foreign corporation was a creature, and in fact an arm and instrument, of an entity (the Communist East Germany) not recognized by the U.S. Government. A nonrecognized entity, from the point of law, was a non-entity. The appeals court (The Supreme Court of New York, Appellate Division) struck out the defense as insufficient. Among other things, the appeals court ruled that, despite the U.S. nonrecognition of the foreign entity, “[t]he lack of jural status for such [entity] or its creature corporation is not determinative of whether transactions with it will be denied enforcement in American courts, so long as the government is not the suitor (italics added).” Another important, perhaps the most decisive, basis for the appeals court’s reversal was found in the following passage:

“Of course, nonrecognition is a material fact but only a preliminary one. The proper conclusion will depend upon factors in addition to that of nonrecognition. Such is still the case even though an entity involved in the transaction be an arm or instrumentality of the unrecognized [entity]. Thus, in order to exculpate defendant from payment for the merchandise it has received, it would have to allege and prove that the sale upon which the trade acceptance was based, or that the negotiation of the trade acceptance itself, was in violation of public or national policy. Such a defense would constitute one in the nature of illegality and if established would, or at least might, render all that ensued from the infected transaction void and unenforceable (italics added).”

Hence, the appeals court in the Upright case concluded: “Defendant buyer cannot escape liability merely by alleging and proving that it dealt with a corporation created by and functioning as the arm and instrumentality of an unrecognized [foreign entity].”

Analysis: Admittedly, there were a number of differences between the two cases. For one, in the Upright case, the non-recognized entity was the Communist government of East Germany during the Cold War era. Secondly, the nonrecognition issue in support of dismissal was raised by the defendant buyer in its attempt to escape payment. And, thirdly, the foreign corporation coming to the U.S. courts for relief was not just a creature of the nonrecognized foreign entity, but an arm and instrumentality of it.

In the Matimak case, on the other hand, the non-recognized entity was not the
Hong Kong government\textsuperscript{13}, but the Crown colony of Hong Kong (soon to be the HKSAR) per se. But, the same rebuttal offered by the appeals court in the Upright case should hold true in the present case, namely that the controlling desideratum was that “the lack of jural status for such [non-recognized entity] or its creature corporation is not determinative of whether transactions with it will be denied enforcement in American courts, so long as the [nonrecognized entity] is not the suitor.”

As to the second difference, the issue of whether Hong Kong was a recognized “foreign state,” in the Matimak case, seemed not to originate from the defendant, but from the district court in its inscrutable search for a ground for dismissal. The defendant debtor could not possibly have found a better amigo en curia!

The third difference is obvious: Whereas in the earlier case the plaintiff foreign corporation, though suing via an assignee, was an official arm and instrumentality of the nonrecognized foreign country, plaintiff Matimak was a private corporation incorporated under Hong Kong law. The tenuous link between the plaintiff corporation and the nonrecognized foreign entity was, therefore, even more tenuous, to the point of irrelevant.

Despite these procedural differences, however, the two cases share much in common, and the main reasons supporting the appeals court’s reversal in the Upright case should be true in the Matimak case as well. In the first place, to reiterate, the lack of jural status for Hong Kong (not being a “foreign state”) should not be determinative of whether commercial transactions with its private corporations would be denied enforcement in US courts. At issue was whether a contract properly executed on American soil was enforceable in U. S. courts. Secondly, Hong Kong, the nonrecognized foreign entity, was not a suitor in court; but Matimak Trading, a Hong Kong corporation, was. Thirdly, and most important, defendant buyer, D.A.Y. Kids Sportswear, should not be allowed to escape its liability, for the payment of US$80,000 for goods ordered and delivered, merely because technically Hong Kong, where Matimak was incorporated, happened to be not recognized as a “foreign state.” And, finally, the trade on the basis of which defendant debtor’s nonpayment created

\textsuperscript{13} It is to be recalled that the United States Government concluded in early 1997 an extradition treaty with the incoming government of the future HKSAR.
an outstanding liability in the Matimak case, as in the earlier case, was not found to be “in violation of public or national policy.”

In Upright vs. Mercury Business Machines Co, the appeals court even went further to question the tenuous link between recognition of a foreign entity and the “jural capacity” of its corporations to “trade, transfer title, or collect the price for the merchandise they sell to outsiders, even in the courts of non-recognizing nations.” By contrast, however, in the Matimak case neither the district court nor the appeals court took heed of this crucial point about the tenuous link, possibly for one reason. And, the reason might well have been that both courts were preoccupied with the imminent transfer of sovereignty over Hong Kong in its scheduled reversion to China. If true, this would be a sad instance in which US federal courts were diverted from a cool-headed deliberation on the merits according to law, for the administration of which the courts were created in the first place, by a fortuitous political turn of events looming on the horizon.

The same sad commentary can, mutatis mutandis, be made on the two other cases discussed above, Lui vs. the U.S.; and the Launder case.

As has been shown above, in both cases, the respective courts were fixated with the forthcoming departure of British rule in the Hong Kong colony, and raised -- erroneously, I think -- what at best was an oblique, if not totally irrelevant, question, viz.: What would happen if the individual offender should be extradited to Hong Kong after the Chinese takeover? Although the right decision was made in the end, whereby both Lui and Launder\(^4\) would be extradited, the fact is that the controlling desideratum was the anticipated political turn of events surrounding Hong Kong’s return to China, which was blown out of proportion, relative to what was required by law. This judicial faux pas led to the courts’ glossing over of the prospect of an independent judicial capacity of the HKSAR, which was a non-issue in the courts’ deliberations. It also led to the neglect by the appeals court in one case (Lui vs. U.S.), of an important provision in the 1992 U.S. Hong Kong Policy Act, to the effect that the coming handover should in no way affect the continuing in force of all existing treaty obligations applicable between Hong Kong and the United States as before 1

\(^4\) Launder was extradited to Hong Kong, where his trial on 13 corruption charges began on April 20, 1998. See SCMP, 4/21/98, p. 3.
July 1997, which therefore would mean uninterrupted effect of the UK-US extradition treaty, as it applied to Hong Kong before the specified date.

In retrospect, the intuitive assumption that the new Chinese sovereign would ipso facto be expected to trample upon the rights of the extradited offenders, including one wanted on corruption charges in Hong Kong, and that China would deprive the HKSAR of an independent judiciary in violation of treaty obligations, does not look very bright in the glow of hindsight, to put it in the most charitable terms.

In the frame of reference for this paper, the wide discrepancies between the foreign courts’ obvious expectations (about what was going to befall on Hong Kong) in the cases just examined and the actual outcome, as seen from the afterglow of the handover, present a giant paradox.

Commentary

For fear that the uninitiated may draw the wrong conclusions from the above discussions, a clarification, it seems to me, is in order on the question of Hong Kong’s international capacity. First, despite the Matimak setback, neither Hong Kong nor its corporations are without recourse in defense of their interests internationally. In the United States, for instance, resort to state courts is nevertheless open to Hong Kong and its corporations, in the event they have to seek legal relief for the protection of their rightful interests. The Matimak decision merely means that a Hong Kong incorporated entity, as Hong Kong itself, cannot sue before a U.S. federal court. Despite this limit to its access, the fact that Hong Kong has the capacity to sue before other forums attests to what we in these pages have called the territory’s legal capacity to act as a non-sovereign international actor.

Another evidence of the SAR’s legal capacity as such is found in the U.S. vs. Peter Yeung case, in which a China mainland-born U.S. citizen was wanted for alleged conspiracy to defraud the U. S. Government, smuggling clothes into the United States and importing clothes labelled with false country-of-origin tags on 91 occasions. The U.S. government’s hunt for the fugitive began in 1992, after the New York District Court issued a warrant for Yeung’s arrest over 183 alleged offenses said to have taken place between February 1990 and April 1991 and to involve US$11 million. Yeung escaped from the United States in mysterious circumstances, surfaced
in Macau, and later went to Hong Kong, where he was arrested on March 30, 1997. The U.S. extradition request was a first following Hong Kong’s handover to China. While at the time of this writing, the SAR’s chief executive was still pondering over the U.S. extradition request, the fact that the request from Washington was filed directly with the HKSAR, but not through its Chinese sovereign, is a good testimony to Hong Kong’s international legal status as an autonomous entity with a capacity to act despite its lack of sovereignty.

**Hong Kong’s Intermediary Function**

**Between China and the Outside World**

There were high hopes, among many quarters, that after reversion Hong Kong’s role as an entrepot for China would increase and that the SAR would also double as China’s conduit to the world. Hence, its intermediary function, serving as a window for China on the world and, in return, as the world’s window on China, would provide a “reversible window” effect.

Those hopes were based on both (a) a solid record over the past one and a half decades, in respect of Hong Kong’s entrepot role and its economic ties with the mainland, and (b) a theory of synergism, which sees an ever-deepening interdependence, generated by mutual complementarily (see below). Part of the past record showed, for example, that Hong Kong had been a very important source of China’s foreign exchange earnings, accounting for up to one-third of total prior to the 1980’s. In other statistics, the Hong Kong entrepot trade rose to the highest level ever in 1996, at US$120 billion, or 41% of China’s total foreign trade. Hong Kong’s investment (FDI) in mainland China amounted to US$78.6 billion, or 59% of cumulative foreign direct investments (FDI) in China. In return, Hong Kong was also recipient of 80% of China’s outward FDI.

---

16 Cf. James C. Hsiung, “Hong Kong as a Non-Sovereign International Actor,” at 239.
The synergist view comprised a number of propositions: (i) that Beijing would not kill the goose that lays golden eggs by trying to siphon off Hong Kong’s vast foreign exchange reserves19 (as Pres. Lee Teng-hui of Taiwan was fond of saying to whoever cared to listen throughout 199720); (ii) that China needed a prosperous Hong Kong to be prosperous itself; (iii) Hong Kong needed an independent monetary policy to maintain its attractiveness to investors; and (iv) that China needed an independent monetary policy to maintain the macroeconomic stability necessary for its own prosperity.21

While the jury is still out at the time of this writing, in the sense that more up-to-date statistics are yet to roll in, we are nevertheless able to offer some tentative comments on whether the pre-handover expectations have come true on the question of Hong Kong’s intermediary role for China vis-a-vis the world. Although this paper does not purport to get into Hong Kong’s domestic economy, nor the Hong Kong-China economic ties per se, some of the points developed below, nevertheless, do peripherally touch on these questions, for a reason. We cannot, in my opinion, really get to the heart of Hong Kong’s intermediary role, without first examining the political parameters within which the SAR has to operate as an economic actor vis-a-vis both China and the outside world. Nor can we do without touching on, at least en passant, the obvious question of whether some sort of an economic integration would not emerge from the conjoining of the two dynamic economies, China and Hong Kong.22

Before going any further, I have to pause to observe that in the months since 1 July 1997, Hong Kong does offer evidence that it can be a useful beachhead for foreign interests seeking entry into China proper. For example, Britain’s biggest bus company, First Group, announced in early 1998 that it would use its successful bid to run all Hong Kong’s major public bus services as a stepping stone to the mainland’s

19 Kueh and Voon, ibid., n. 12 above.
20 As quoted in Ming Pao Daily (Hong Kong), 28 June 1997, p., 16.
21 Lok-sang Ho, “The Economy of Hong Kong as a Special Administrative Region of China,” 24 Asian Affairs 4:227-236, at 230. S
giant public transport market. Another similar instance concerns the Stagecoach Holdings, billed as the world’s largest bus company, which announced its plans to invest HK$1.39 billion for a potential 28 per cent stake in Hong Kong-listed mainland toll-road investor Road King Infrastructure, the first British company to gain access to the mainland’s lucrative toll-road sector. Stagecoach, which had failed in its bid for a bus franchise in Hong Kong itself in March, 1998, sought this alternative route to gain entry into the mainland.

Furthermore, an unrelated bizarre incident quite indicative of Hong Kong’s value as a conduit to China was the discovery of a HK$5.7 million smuggled armored troop carrier, intercepted and seized by Hong Kong customs officials from aboard a container ship bound for a Chinese destination. While the incident may not be an orthodox use of the Hong Kong conduit, it nevertheless demonstrates, perhaps dramatically, the territory’s prized usefulness as a channel through which to reach Destination China.

There is no question that, contrary to the rampant pre-1997 prophecies of doom, Hong Kong’s continuing economic strength as well as its ties with China have been facilitated by the economic freedoms guaranteed by the Basic Law, under which the SAR is for all practical purposes a separate economy. And, as such, the trade and investment flows between Hong Kong and China proper are treated, albeit anachronistically, as international flows. On the basis of the insufficient data on hand, I would venture to suggest that at least two lessons relevant to this discussion can be drawn from the experience of the HKSAR in its first year.

The first lesson is that, although 1997 was a year of economic prosperity for the SAR (even after controlling for the adverse effects of the financial turbulence hitting the Asia Pacific region from the fall of 1997 onward), the watershed year for Hong Kong’s economy was not 1997, but 1979. In that earlier time period, when China began its epochal economic reform and opening to the outside world, Hong Kong, which had lost its hinterland during the Cold War era, regained it as a result.

The second lesson is what Yun-wing Sung calls the “impossibility of a formal Hong

24 “UK Bus Giant Eyes 28pc Road King Stake to Tap Mainland Sector,” SCMP, May 1, 1998, B-1.
25 “Arms Dealer in $5.7 Million Plen,” SCMP, 1 February 1998, p. 3.
26 Yun-wing Sung, ibid. n. 11 above, at 705.
Kong-mainland trade bloc.  

The first of the two lessons simply confirms the absolute importance of the Chinese hinterland to Hong Kong. Since its reversion serves to solidify, or institutionalize, the hinterland-periphery relationship, the HKSAR’s continuing economic dynamism should come as no surprise. Nowhere was this hinterland advantage driven home more pungently than when China’s new premier, Zhu Rongji, announced at his first news conference upon assuming office that China would “do everything within its power” to bail out Hong Kong, should the SAR be in trouble under the crushing blows of the on-going financial turbulence hitting the region. With China’s US$142.8 billion foreign exchange reserves, lining up behind Hong Kong with its own US$95 billion, that unequivocal assurance surely helped to instill confidence among Hong Kong’s residents, as well as foreign commercial interests, in the future of the SAR’s economy. Some natives were already wondering aloud if the British colonial rulers would have made the same commitment, had they been here and should they be able to do so.

The second lesson needs a word of explanation. Borrowing from the experience of other regions (e.g., European Union [or EU], North American Free Trade Association [or NAFTA], among others), integration theorists may have legitimate reasons to expect that the amalgamation of Hong Kong into what could be the nascent shell of an eventual Greater China entity may lead to the tantalizing option of forming a trade bloc, beginning perhaps with a customs union, with China proper. Before the jury is in, however, a respectable economist—Professor Yun-wing Sung, of the Chinese University of Hong Kong—has already ruled out the option as unrealistic. Given the free-port status of Hong Kong, guaranteed by both the Basic Law and international agreement, Sung said, “the only way that the mainland and Hong Kong could form a customs union would be for the mainland to abolish all of its tariffs.” This, to Sung, would be “judicious and utopian.” In fact, for Hong Kong to enter into an economic union, after the EU model, would violate sections of the Basic Law.

---

37 Ibid., at 707.
38 See report in SCMP, March 30, 1998, p. 1. While on a European tour, Zhu further explained that one important reason why Chinn would hold out against devaluing the Chinese renminbi was that it would badly damage the Hong Kong SAR’s economy; SCMP, April 6, 1998, p. 1.
Creating a common market would imply that the HKSAR had given up on regulating migration from China, a consequence far beyond the territory’s physical capacity to bear, given its overpopulation and already tightly overcrowded space. An economic union, Sung continued, would also require that the SAR give up its independent currency, making it impossible for Hong Kong to function as an international financial center, because the Chinese renminbi is far from freely convertible. Despite its reversion to Chinese sovereignty, Hong Kong, according to Sung, is institutionally more closely integrated with most other economies than with China. The extent of Hong Kong-mainland integration is less than that between Greece and Ireland, Sung suggested.29

I do not doubt this analysis to be true: The bottom line, however, is that the vast gap between the common-sensical expectations of greater Hong Kong-China integration and the hard reality that turns out to be just the contrary, as Yun-wing Sung pointed out, confirms our paradox thesis regarding post-reversion Hong Kong as a non-sovereign actor.

Another related paradox is in the discrepancy between prior speculations about the HKSAR being tainted by Chinese ideological influence and what, on the other hand, may be called, as a short-hand label, the “roaring mouse” syndrome, which finds China actually at the receiving end of influence. While this remains to be further developed with more up-to-date evidence, two different existing sources have identified the syndrome. One is Yuchu Xie’s study showing that, both because of the current ideological vacuum pervading mainland China and also Hong Kong’s cultural pluralism, representing the best of both Western and Eastern traditions, it is the SAR, not mainland China, which is the dispenser of influence.30 The other expose for this line of inquiry is an extremely thought-provoking report by Daniel Fung, Hong Kong’s Solicitor General. Rather than Hong Kong’s law being subject to the pollution by China, he noted, evidence pointed to the other direction. Starting even before Hong Kong’s reversion, going as far back as the 1980’s, at least three law schools in China have been studying Hong Kong’s law as a specialty. The Hong Kong

29 Yun-wing Sung, op. Cit., at 707f.
Attorney General’s Chamber (AGC) had been supplying the Legislative Affairs Commission of the National People’s Congress (NPC) in Beijing copies of the territory’s bankruptcy law, companies legislation, and other commercial legislation. The NPC consulted these in drafting their own laws, which in part accounts for the sudden orgy of new commercial laws coming into existence in the 1990s. And, since 1992, when Shenzhen was granted by Beijing its special legislative autonomy status, the neighboring Chinese town enacted in the following three and a half years approximately 250 pieces of primary and subsidiary legislation, two thirds of which were copied from Hong Kong’s laws.\(^{31}\) I have no evidence of a let-up in this trend beyond July 1997. On the contrary, the first group of law professors and government officials from China proper who came in September 1997 for an advanced training course in common law, under a special funded program, at the Hong Kong University law school, graduated at a diploma-awarding ceremony on May 13, 1998.\(^{32}\) The reversal, as such, of the earlier speculated directional flow of ideological influence, if continued, would also be a paradox unto itself.

This point is important, because as a result of China’s methodic borrowings from Hong Kong’s laws and legal tradition, the outcome (as testified to by the recent flurry of commercial laws enacted by the NPC, modeled after Hong Kong’s laws and practices) may well be that China’s economic structure as well as legal system will be brought more in line with the outside world. To the extent that this development will make China more fit to be integrated into the international main stream, such as through membership in the World Trade Organization (WTO), then the HKSAR’s alleged intermediary function between China and the outside world will be more than fulfilled, thanks to the paradoxical “roaring mouse” syndrome.

As a Catalyst for Taiwan-Mainland Liaison

Although the relations between Taiwan and the mainland of China are not an international issue, any move by both sides, in an unlikely turn of events, toward

\(^{31}\) Fung’s address before the Heritage Foundation, in Washington, D.C., on January 6, 1996.

reunification or some similar peaceful solution would inevitably excite many foreign powers at both regional and global levels. In the event Hong Kong could play a catalyst role in bringing together the two sides in any endeavoring toward a permanent resolution of their unfinished civil war since the 1940’s, it would spell a crowning success for Hong Kong in its role as a non-sovereign international actor.\(^{31}\)

Because of its strategic location, situated in the interstice between Taiwan and the mainland, Hong Kong has been a crucial hubub of cross-Taiwan connecting air traffic and transshipping, for passengers and cargo, ever since Taiwan opened the floodgates to visitors to the mainland in 1987, after 38 years of an armed stand-off. The SAR would, presumably, be an ideal location for any serious bilateral mainland-Taiwan negotiations, should both sides want to seek a break-through in the current impasse of no direct air or maritime links. Indeed, a break-through of sorts was reached whereby a mainland cargo vessel was reported to have docked at the southern Taiwan port city of Kaohsiung in early March, 1998, after a stop in Okinawa. According to news reports, the 6,269-ton Tungshun was the first mainland ship ever to operate cross-strait cargo services via a third port since Beijing and Taipei officials held informal shipping talks in February. In fact, it was the first time officials from both sides ever met, and did so on third-party soil. The bigger surprise, however, was that the talks were held, not in Hong Kong, but in the more remote Bangkok.\(^{31}\)

I can think of two possible reasons why Hong Kong was not chosen as the negotiating site: One, after its reversion to China, Hong Kong is no longer “foreign soil” that Taiwan could consider as neutral ground. Second, the SAR presumably would have too high a visibility for Taiwan to feel comfortable as a site for conducting sensitive talks with Beijing.

If so, then it proves that, despite earlier speculations to the contrary, Hong Kong’s return to Chinese sovereignty made it less desirable as a place for official or semi-official contacts between the mainland and Taiwan. In this light, the offer of Malaysia by Prime Minister Mahamad Mahathir, made to the visiting Taiwan Vice President Lian Zhan during the latter’s recent unofficial visit, as a possible venue for

---


\(^{34}\) “Freighter’s Arrival to Herald Warming of Ties,” SCMP (Hong Kong), March 3, 1998, p. 1, citing Taiwan’s China Times Express as its source.
future Beijing-Taipei talks,\textsuperscript{35} would make more sense than meets the eye. In both instances, Hong Kong’s role as a medium between the opposing sides across the Taiwan Strait, much heralded before the departure of British rule, has not lived up to its full potentials. Again, a paradox.

In fact, despite its high autonomy enjoyed under the “one country, two systems” arrangement, the HKSAR does not have unimpeded freedom in respect of its dealings with Taiwan. Guidelines for Hong Kong’s relations with Taiwan were spelled out in the so-called “Qian Seven Points,” named after PRC Foreign Minister, Qian Qichen, as he outlined Beijing’s policy on 22 June 1995. The policy contains essentially two parts. First, while Taiwan’s pre-existing offices plus its 3,000 private firms are permitted by Beijing to continue their presence and activities in the Hong Kong SAR, they are bound to respect the Basic Law. Second, and more important for our interest here, any official activities between Hong Kong and Taipei must have Beijing’s prior endorsement. Although this two-part policy of Beijing has been known since 1995, what is new is that, despite wishful thinking to the contrary in some quarters, the policy has been strictly carried out since Hong Kong’s return to Chinese sovereignty.\textsuperscript{36}

For the legally minded, it bears noting that, while matters relating to Taiwan are strictly speaking not “foreign” affairs, the sort of “Big Brother” watch Beijing maintains on Hong Kong in regard to the latter’s relations with Taiwan, nevertheless, reminds one of the two areas in which the SAR, according to the Basic Law, is not autonomous: foreign relations and defense.

In the circumstances, the room left for Hong Kong to play a catalyst role, in prompting Taiwan and the mainland to move toward a final peaceful resolution of their division, is very restricted. That eventuality would depend on the outcome of the SAR’s experiment with the “one country, two systems” model. If, over a prolonged period of time, the model has proven to be a reliable and duplicable success in the HKSAR, then the reason for Taiwan’s official rejection of the model\textsuperscript{37} as an answer to the remaining Taiwan piece in the jigsaw puzzle of Chinese unification — although the model would have to be modified to suit the island’s different political ecology --

\textsuperscript{35} “Malaysia Offers Venue for Unification Talks,” SCMP (Hong Kong), March 6, 1998, p. 12.

\textsuperscript{36} Timothy Ka-ying Wong, “Post-1997 Hong Kong-Taiwan Relations,” in Hong Kong Policy Research Institute, Ltd., Policy Bulletin, No. 2 (Nov. 1997), at 9f.

\textsuperscript{37} Taipei’s official reason is that the “one country, two systems” model will not work in Hong Kong.
would lose its validity, hence legitimacy. More especially, if the success should so transform world opinion and, a fortiori, Washington’s perception that sufficient pressures would mount on Taiwan in its wake, the island’s public opinion would hardly remain unswayed. Add to this some hard statistics from the conjoining of the two economies after Hong Kong’s return to China: (a) their combined GNP (US$885 billion) was four times that of Taiwan; (b) their combined foreign trade at US$652.3 billion, admittedly including their mutual trade as well, was three times Taiwan’s trade of US$215 billion; and (c) their combined foreign reserves, totalling US$220 billion (as of September 1997), was two-and-a-half times Taiwan’s US$85 billion.38 Add further the World Bank’s forecast that by the year 2020 the People’s Republic of China will be the world’s second largest economy, next only to the United States.39 The consequential bridging of the gap between a fast growing mainland China and an already prosperous Taiwan (as measured by its per capita income of US$12,000) of today will most likely make mainland China less foreboding as a partner to the majority of the Taiwan compatriots. Under the circumstances, Taipei’s decision makers, by then long after Lee Teng-hui’s departure from the political scene, would probably find untenable any continued rejection of the time-tested “one country, two systems.” The ensuing result might well prove that Hong Kong will have played a catalyst’s role in that it has made Taiwan’s acceptance of the “one country, two systems” model an almost foregone conclusion. But, this is the preview of an outcome compelled by pure logic, whose surety, however, is not likely to be seen in the next few years, certainly not at the time of this writing.

Other than that remote development, the predictions among many quarters for more trade and investments between Taiwan and the mainland by way of Hong Kong, to an extent more than before, are hard to ascertain in the absence of more up-to-date figures. Nonetheless, it seems obvious that despite Taiwan’s initial suspicions, Hong Kong in fact has grown more, not less, important to Taiwan’s economy.40 Even when the first year’s data are in, as they are not at the time of this writing, it would be hard

38 Hsiung, op. cit., at 241.
to gauge whether they can be considered as having established a pattern from which we can gain confidence in predicting the future, more especially when these data are most likely to be tainted by the direct or indirect effects of the unforeseen financial crisis hitting the Asia-Pacific region since October 1997.

**As a Factor in U.S.-China Relations**

The point of departure is the high stakes of the United States in Hong Kong, where it has an aggregate investment of over US$13 billion, 1,000 American firms, and 30,000 U.S. citizens. Its official concerns stemming from these high stakes are attested to by the U.S. Hong Kong Policy Act of 1992. In declaring its “wish to see full implementation of the provisions of the Joint Declaration” between China and the United Kingdom on Hong Kong’s return to Chinese sovereignty, the Act acknowledges Hong Kong’s “important role in today’s regional and world economy.” Concerns for the protection of U.S. interests are shown in the commitment it made for the United States to “play an active role in maintaining Hong Kong’s confidence and prosperity, Hong Kong’s role as an international financial center, and the mutually beneficial ties” between the peoples of Hong Kong and the United States.

In aggregate, the various provisions of the Act amount to a pledge by the United States to commit itself to replacing British influence after 1 July 1997. Save for that implicit goal, the entire Act, more especially its provisions for periodic reporting by the Secretary of State to Congress on the conditions in Hong Kong, would make no sense, and would not even be worth the paper on which it was written. In this sense, the HKSAR is an important factor in US-China relations.

In the past, during the Cold War era, U.S. policy was to build a cocoon around Hong Kong, so that it would not be an entrepot for the transfer of strategic goods destined for China in violation of the wishes of the Coordinating Committee for Multilateral Export Controls (COCOM), the watchdog body for the United States and its allies in enforcing the ban on strategic goods exports to Communist bloc countries. Sec. 103(8) of the Act made this concern explicit for the future: “The United States should continue to support access by Hong Kong to sensitive technologies under the agreement of the [COCOM] for so long as the United States is satisfied that such
technologies are protected from improper use or export (italics added).” In Senator Mitch McConnell’s remarks while introducing on the Senate floor his bill that later became the 1992 Act, as we have noted earlier, he made references to close British cooperation over U.S. relations with Hong Kong before. That cooperation presumably included U.K. support of COCOM policy, and the Hong Kong colony’s laws that prohibited transfer of sensitive technologies to and from China. The justification for a special legislation, such as the 1992 Act, was that in view of Hong Kong’s forthcoming reversion to China, the United States had to make sure that U.S. interests would not be left unprotected. Whereas after the end of the Cold War the COCOM was deactivated, its function has been taken over by two systems identified respectively with the newly-created Nuclear Suppliers Group (NSG) and the Missile Technology Control Regime (MTCR). A principal concern of the United States is that, as before, Hong Kong should not become an entrepot for China in the import-export of sensitive technologies, such as those associated with the manufacture of weapons of mass destruction. A subsequent agreement concluded by the U.S. Department of Commerce with the HKSAR government, in September 1997, was precisely meant to ensure continuance of Hong Kong’s previous trade policy on the transfer of sensitive technologies. As a reward in return, the SAR was given a Q trading status, one usually reserved for a Western industrially developed trading partner.41

Such being the case, the discovery and seizure by the SAR’s customs officials of a smuggled armored personnel carrier bound for China from Thailand via Hong Kong, as noted earlier, was thus of grave concern to the United States. Hong Kong’s forceful action in levying stiff fines on the captain of the ship caught in carrying the smuggled vehicle, in accordance with a 1955 ordinance banning such smuggled goods, assured Washington that Hong Kong’s past policy banning sensitive trade transshipments did not change with the transfer of sovereignty.42

In this connection, any incident involving even the unwitting use of Hong Kong as a point of transfer of sensitive technologies could, conceivably, constitute an

41 Cf. Remarks by Dr. Wei-xing Hu, of Hong Kong University, in transcripts from a forum discussion on “Hong Kong in Sino-US Relations,” held on December 6, 1997, under the auspices of the One Country-Two Systems Economic Research Institute, Ltd. (Hong Kong), at p. 4.
42 Ibid., p. 3.
irritant in Sino-U.S. relations. If in the U.S. perception Hong Kong -- should the latter lower its guard and lose control -- is by any chance becoming a point of entry and departure for illicit transfer of sensitive goods and/or technologies, Washington conceivably could be forced to resort to a number of countermeasures, such as: (a) declaring that Hong Kong is no longer able to protect sensitive technologies from leaking to the mainland, and therefore technology control will be applied to Hong Kong itself; (b) determining that Hong Kong is no longer sufficiently distinct as an entity from mainland China to permit the United States to continue to treat Hong Kong as a separate tariff area, as defined in the 1992 U.S. Hong Kong Policy Act; and (c) slapping restrictions on China's exports to the United States. In any event, any of these measures, if enforced when warranted by the circumstances, would drive Sino-U.S. relations back at least twenty years. Hong Kong, in that eventuality, would also be a loser.

The above discussion, I hope, amply highlights a two-part lesson, namely: Just as US-Hong Kong relations will affect US-China relations, the state of Sino-US relations will likewise have untold effects on Hong Kong, in terms of its relations with both Washington and Beijing.

Another development that should be noted before we leave this discussion of the US-China-Hong Kong triadic relationship is that, after reversion, there is a potentially fractious shift in the way in which Hong Kong's export trade is counted. Unavoidably, it becomes part of China's aggregate foreign trade to U.S. Customs. As a result, China's combined trade surplus with the United States will become more exaggerated. In 1993, for example, some US$8.2 billion Hong Kong exports to the United States was counted by U.S. Customs as China's exports to America, thus exaggerating the Chinese surplus in Sino-US trade by 133%.

Thus, Hong Kong as a factor in Sino-U.S. relations should not be seen in all roses. Even if there are roses, beware of the prickly thorns that come with them! Contrary to previous expectations, especially among some Chinese quarters, that tended to see Hong Kong's return as nothing but a plus even in China's relations with

---

43 Kenneth Lieberthal, in a position paper drafted for the Asia Society (New York) for dissemination to the mass media in preparation for the forthcoming handover of Hong Kong to China in 1997, at p. 23.
44 Clyde Kaulman, "Asia Pacific Economic Links and the Future of Hong Kong," in a special issue on Hong Kong of The Annal (September 1996), at 164.
the outside (including the United States), this conclusion, however tentative, seems to caution us that it, paradoxically, is not necessarily true.

**Concluding Remarks**

My original hope in writing this paper was to update my 1997 study on post-reversion Hong Kong as a non-sovereign international actor. As my previous paper was written in early October 1997, or three months after the handover, I was drawing upon the prevailing views of qualified pundits and international-law scholars, but otherwise had little to go on, as available supporting evidence was scanty.

In writing this follow-up paper a few months later, however, I began by taking stock of subsequent developments in and around the SAR across different areas, with a view to gaining a broader perspective from which to approach the topic I was to focus on. To my great astonishment, and amusement, too, I found consistent, wide discrepancies between earlier projections and subsequent outcomes, as we came to know them in the first half of 1998. Two findings stand out, among others: (a) Earlier prophecies of doom about Hong Kong after the departure of British rule were, paradoxically, proven either unsubstantiated or plainly wrong, almost across the board; and (b) Earlier prognostications about Hong Kong’s international capacity to act, such as in asserting claims and espousing causes, including its corporations’ eligibility to seek relief before foreign courts, were proven specious, as Hong Kong’s jus standi (through no fault of its own) was found either frustrated, as in the Matimak case (involving US federal courts), or glossed over in other foreign court decisions because of an apparently irresistible fixation gripping these courts with the political turn of events culminating in China’s actual takeover of Hong Kong from British rule (and conceivably viewed with a jaundiced eye), as we have noted in the Lui and Luander cases. In addition to examining these judicial cases, I have extended the scrutiny to other aspects of Hong Kong’s external role or capacity to effect change, i.e., as a conduit for China and the outside world, as a catalyst in the Taiwan-mainland tangle, and as a factor in Sino-U.S. relations.

---

45 “Hong Kong as a Nonsovereign International Actor,” supra n. 4.
With little exception, the search turned up evidence showing that the SAR’s external capacity as such had been constrained, at times severely, by unforeseen extraneous factors beyond its control. In fact, as noted, its high profile and visibility proved to be a fortuitous disadvantage for the Hong Kong SAR to serve as a literal meeting ground for sensitive negotiations between the two sides straddling the Taiwan Strait. Contrary to expectations by integration theorists, too, a Hong Kong-mainland economic union, after the EU model, has thus far been found elusive and even well-nigh improbable. Besides, any abusive but successful use by illicit smugglers of the Hong Kong conduit, for the transfer of contrabands or sensitive technologies to and from China, would not only damn the SAR’s reputation, but also arouse alarm among supporters of the NSG and MTCR regimes and, most probably, poison Sino-US relations. A shift in the practice of U.S. Customs, to counting the SAR’s exports as part of the aggregate Chinese exports, would unduly exaggerate China’s surplus in Sino-U.S. trade, thus exacerbating an outstanding irritant in the bilateral relations. In all these instances, a distinct commonality was a discrepancy, at times inexplicable, between earlier expectations and subsequent outcomes.

An especially ironic development came to public knowledge in early May, involving “interviews” conducted by the British consular officers with certain local candidates for the HKSAR’s May 24 Legco election. When the news broke, the Chinese Foreign Ministry in Beijing literally “threw the book” at the British consulate, by reminding it of the obligations incumbent upon foreign consular agents under the 1962 Vienna Convention on Consular Relations. Art. 55 of the Convention, which codifies the international norms on consular immunities and privileges, explicitly prohibits consular agents from interfering into the domestic affairs of their host state. In self-defense, the British consulate-general claimed that it was within usual consular practice to keep in touch with politicians of all colors in the land of the host state.\(^46\) While this argument sounds as if Beijing had an equal right to rubbing shoulders with IRA leaders in Northern Island, if just for the sake of keeping “informed,” the matter no doubt remains a case in contention. But, what is relevant

here is the paradox it presents. The British, who had not been in the least expected to be even minimally interested in the SAR’s elections following the handover, were indeed showing more interest and, by the close contact they admit to keeping with certain of the local candidates, seem to be more directly involved in the SAR’s first elections than was Beijing, which thus far seemed to take a deliberate lay-back position. By contrast, prior expectations seemed to have pointed to just the opposite, that Beijing as the SAR’s sovereign would do the meddling. The contrast is in itself paradoxical.

This list of discrepancies, between prior expectations and subsequent outcome, could go on. But the examples are enough to verify our thesis of a paradox surrounding the SAR’s developments, certainly certifiable in the area we have examined in this paper. The biggest paradox is found in the contrast between what has happened on the domestic scene, and what has happened to Hong Kong’s much heralded international capacity to act. Whereas earlier prophecies of doom were all aimed at Hong Kong’s domestic scene after the handover, there have been few surprises domestically thus far. Despite speculations about the corruption bug hitting Hong Kong, for example, a latest survey showed that, instead, corruption in the SAR was at an all-time low in five years. This paradox is auspicious in that it shows Hong Kong better off than predicted. It is, indeed, in the external domain that the failure of subsequent developments to bear out the felicitous projections for Hong Kong’s future under the Chinese flag has generated the most acute disappointment. The paradox found in the external dimension of the SAR is in contrast an inauspicious one.

If discrepancy between expectations ex ante and real developments ex post is a paradox, as we defined the term, our discovery of paradoxes actually pervades both the domestic and the external domains, even though this study is focused on the latter. As has been shown, the biggest paradox is found in the stark contrast of developments going totally opposite directions between the SAR’s domestic and external domains. These findings can be said to be truly counter-intuitive.

I wish to offer an obiter dictum. The thrust of the major findings from this study, as such, is nevertheless in keeping with the fact that much of social science theory is counter-intuitive. The reason is that many phenomena in the human experience often turn out to be contrary to what our intuition usually leads us to believe. For instance,
in the euphoria generated at the close of the Cold War, we were given to believe that
the world was in for a windfall of hefty “peace dividends.” Over one and a half
decades later, however, we are just beginning to come to the hard realization that not
only have there been no peace dividends, but most nations have been left worse off
than during the Cold War. The United States, for one, can no longer lead by merely
holding out to allies and friends the promise of its nuclear protective umbrella as
before. Its leadership now has to be staked on an array of qualifications as befitting
the new era of geoeconomics. They include an ability to call the shots in decision
making in the world’s financial and economic forums, possession of sizable
exportable capital, an industrial capacity to supply state-of-the-art products and
expertise at the cutting edge of modern technology, etc.\textsuperscript{47} During Clinton’s first term
in office, the United States, still weighed down economically because of the
prolonged effects of overspending in defense, found itself in the awkward position for
not being able to capitalize on its longest suit, its massive nuclear arsenal. Instead, it
had to compete for leadership with the world’s economic stalwarts from a position of
relative economic weakness. Hence, Washington was lying low in foreign relations
until Clinton’s second term, when America’s economy had recovered some of its
earlier prowess.

For former U.S. followers, on the other hand, the vanishing of the value of the
American nuclear protective umbrella meant they had to fall back on national means
of defense. Hence, from Europe to Asia Pacific, a general trend in recent years has
been, following the security-dilemma dictate in international-relations (IR) theory, a
spiral of competitive increased defense expenditures, so much so that Thomas Klare
was prompted to characterize the trend as “the great arms race.”\textsuperscript{48}

China, another example, used to be a textbook case of tertius gaudens (literally
the laughing third), or the weakest player in the former US-Soviet-China strategic
triangle which nevertheless could always reap more gains than its power warranted,
simply because both the other two more powerful players were competing for China’s

\textsuperscript{47} Robert E. Hunter, “The United States in a New Era,” in U.S. Foreign Policy after the Cold War, ed.
support in the strategic triadic game. But, not any more. Following the end of the Cold War and the collapse of Soviet power, there is no more strategic triadic game. Japan, for its part, used to enjoy a habitual “free ride” with absolute impunity in its trade relations with the United States, precisely because Washington needed Japan to be on the free world’s side, as an exemplar to the Third World of the virtues of capitalism in the West’s ideological race with the Communist camp. After 1990, when the value of this exemplar role diminished, Japan for the first time has been made to pay for its free rides. This, plus domestic ills that surfaced following the collapse of the long-reigning Liberal-Democratic Party, has caused an unraveling of the Japanese success story. In the course of the recent financial crisis hitting the Asia Pacific region, Japan was almost reduced from a “bubble economy” to a basket case. Who would have anticipated this outcome in 1990, at the close of the Cold War era?

Again, this list could go on. But the examples given here are sufficient, I hope, to illustrate that the prognostications of post-Cold War “peace dividends” have been proven wrong by subsequent counter-intuitive outcomes. Our study here focusing on the paradox of Hong Kong as an international actor has, without doubt, added one more to a long list of such counter-intuitive phenomena in human experience.

49 I have developed this point, drawing on George Simmel’s theory, in Beyond China’s Independent Foreign Policy (New York: Praeger, 1985), ch. 7.
50 Cf. James C. Hsiung, Asia Pacific in the New World Politics (Boulder, CO: Lynne Rienner, 1993), chs. 1, 4, and 11.
Research Fellows

Centre for Asian Pacific Studies

Professor Kueh, Yak-yeow, Director
Dr. Bridges, Brian, AEP
Dr. Chan, Che-po, UL
Dr. Cheung, Kui-yin, AEP
Dr. Fan, C. Simon, UL
Dr. Hiroyuki, Imai, AEP
Mr. Kwok, Hong-kin, ATP
Dr. Lee, Keng-mun, William, AEP
Dr. Lei, Kai-cheong, UL
Dr. Leung, Kit-fun, Beatrice, AEP
Dr. Li, Pang-kwong, UL
Dr. Ren, Yue, ATP
Dr. Voon, Thomas, AEP
Dr. Wei, Xiangdong, UL
Dr. Wong, Yiu-chung, UL

Centre for Public Policy Studies

Professor Ho, Lok-sang, Director
Dr. Che, Wai-kin, USL
Dr. Fan, C. Simon, UL
Dr. Law, Wing-kin, Kenneth, UL
Dr. Lee, Keng-mun, William, AEP
Dr. Leung, Kit-fun, Beatrice, AEP
Dr. Li, Pang-kwong, UL
Dr. Lin, Ping, ATP
Ms. Siu, Oi-ling, ATP
Dr. Voon, Thomas, AEP
Dr. Wei, Xiangdong, UL

All the Research Fellows listed above are staff of Faculty of Social Sciences. Interested staff from other academic departments of the College and other institutions are welcome to join the Centres as Research Fellows or Research Associates. Please contact Dr. Raymond Ng (Tel. 2616 7427) for further information.

AEP = Associate Professor
ATP = Assistant Professor
USL = University Senior Lecturer
UL = University Lecturer