

LEGISLATIVE COUNCIL BRIEF

**FREE TRADE AGREEMENT BETWEEN HONG KONG
AND THE MEMBER STATES OF
THE EUROPEAN FREE TRADE ASSOCIATION**

INTRODUCTION

At the meeting of the Executive Council on 31 May 2011, the Council ADVISED and the Chief Executive ORDERED that the outcome of the negotiations with the Member States of the European Free Trade Association (EFTA States), namely Iceland, Liechtenstein, Norway and Switzerland, on a bilateral free trade agreement (the Agreement) and commitments therein should be endorsed, and the Agreement and the related side agreements with the four EFTA States should be signed.

JUSTIFICATIONS

Key Outcomes of the Free Trade Agreement (FTA) Negotiations

2. The Agreement is comprehensive in scope and the commitments therein are of high quality, some going beyond the respective commitments undertaken by Hong Kong and the four EFTA States under the World Trade Organisation (WTO). They provide for more favourable treatment to the other side. Key outcomes of the FTA negotiations and the expected benefits that the Agreement would bring about are summarised in paragraphs 3 to 19 below.

(A) Trade in Services

3. Acknowledging that trade in services plays a key role in the economies of Hong Kong and the EFTA States, the two sides achieved a high quality outcome on trade in services, building on their existing rights

and obligations under the WTO General Agreement on Trade in Services.

Market Access

4. In terms of market access, Hong Kong service providers will enjoy under the Agreement preferential opportunities in the EFTA States in terms of legal certainty for market access, national treatment and most-favoured-nation (MFN) treatment for the supply of a comprehensive range of services. Many of these preferential opportunities go beyond those already enjoyed under the WTO (i.e. WTO-plus).

5. The EFTA States' specific market access commitments are comprehensive in terms of sectoral coverage. The sectors with WTO-plus commitments encompass those areas where Hong Kong has traditional strengths, such as telecommunication services, logistics services including maritime transport services, audiovisual services and various business services (such as architectural services, engineering, services incidental to manufacturing, related scientific and technical consulting, and convention services). They also include areas identified with potential for further development in Hong Kong, namely, education services, environmental services, medical services, innovation and technology, and cultural and creative industries⁽¹⁾. Switzerland and Norway, as well as Liechtenstein, have essentially bound their existing regimes across the board for all services sectors, except for a limited number of areas sensitive to them⁽²⁾. The market access package of Iceland also generally mirrors their latest offers under the WTO Doha Round of negotiations.

6. As for Hong Kong, we have also made broad commitments covering a wide variety of services, many of which go beyond our commitments under the WTO and exceed our offers made under the ongoing WTO Doha Round of service negotiations (i.e. WTO-plus and

Note ⁽¹⁾ In respect of the key industry of Testing and Certification Services, the four EFTA States have already made full commitment for technical testing and analysis services under the WTO and will make the same commitment under the Agreement.

⁽²⁾ Sensitive areas of individual EFTA States vary. Examples of such sensitive areas include provision of subsidies, audiovisual services, internal waterway transport, certain energy-related services, certain education services as well as certain health services and social services.

Doha-plus). These preferential commitments are specifically targeted at the EFTA States' priority interests, such as financial services, telecommunication services, logistics services including maritime transport services, energy-related services and various business services.

7. Both Hong Kong and the EFTA States made WTO-plus commitments on the movement of natural persons, and the commitments from the two sides are generally comparable. Without compromising legitimate immigration control, business persons of Hong Kong in the categories of Business Visitors (BV), Intra-corporate Transferees (ICT), Installers / Servicers (IN), Contractual Service Suppliers and Independent Professionals in specified sectors would be granted temporary entry into relevant EFTA States in accordance with the commitments of individual EFTA States. On the other hand, BV, ICT and IN of the EFTA States in specified service sectors will be granted temporary entry into Hong Kong in accordance with Hong Kong's commitments. Our commitments are by and large a reflection of Hong Kong's existing liberal regime on temporary entry of business persons. Similar to the commitments we made under the Closer Economic Partnership (CEP) Agreement with New Zealand, Hong Kong will waive the economic needs test (ENT) requirements⁽³⁾ for entry into Hong Kong for employment in respect of ICT from the EFTA States in specified sectors. Since our commitments on ICT are confined to senior and high-skilled positions (i.e. Senior Manager and Specialist) only, we do not envisage the waiving of the ENT will have significant impact on Hong Kong's employment market, in particular the low-skilled sector.

General Obligations

8. Apart from market access commitments, the two sides have also agreed on disciplines on domestic regulation (DR) to ensure that measures affecting trade in services are transparent and administered in a reasonable, objective and impartial manner. Hong Kong, Switzerland, Liechtenstein and Iceland have also agreed to further develop and conclude a comprehensive set of DR disciplines, covering licensing requirements and procedures, qualification requirements and procedures,

Note ⁽³⁾ The test comprises the economic benefits test (i.e. whether the person can make a substantial contribution to Hong Kong's economy) and labour market test (i.e. whether the person possesses a skill, knowledge or expertise that is not readily available locally).

technical standards, and other related matters, within one year after the entry into force of the Agreement. The Agreement also contains specific provisions⁽⁴⁾ to further facilitate trade of the two sides in telecommunication services and financial services, which are sectors important to both sides.

(B) Trade in Goods

9. Under the Agreement, the EFTA States commit to abolishing import tariffs on all industrial goods as well as fish and certain marine products originating in Hong Kong upon its entry into force. The EFTA States will also accord tariff concessions to Hong Kong's processed agricultural products⁽⁵⁾ exported to the EFTA States. As regards basic agricultural products, given the EFTA States' diverse interests and sensitivities in the agricultural sector, basic agricultural products are dealt with separately under bilateral agricultural agreements (see paragraph 14 below). On Hong Kong's part, we commit to binding our existing zero import tariff regime for all goods originating in the EFTA States after the Agreement takes effect.

10. For the purpose of claiming preferential tariff treatment in accordance with the Agreement, the two sides have formulated a set of preferential rules of origin. Under the Agreement, the origin of different products may be determined by either "process-based" rules⁽⁶⁾ or "value-based" ones⁽⁷⁾. Currently, the Trade Descriptions Ordinance

Note ⁽⁴⁾ The Annex on Telecommunication Services comprises obligations such as competition safeguards, licensing procedures, use of scarce resources, etc. The Annex on Financial Services includes obligations such as transparency, expeditious application procedures, right for maintenance of domestic regulations on prudential grounds.

⁽⁵⁾ It is EFTA's practice to impose different preferential treatments and arrangements for industrial goods and processed agricultural products in their FTAs given the sensitivities of the latter.

⁽⁶⁾ "Process-based" rules means goods would be regarded as originated from Hong Kong if they last underwent in Hong Kong a process which substantially changed their shape, nature, form or utility of the basic materials used in their manufacture.

⁽⁷⁾ "Value-based" rules means goods may claim Hong Kong origin on the basis of the proportion (which may be different for individual categories of goods) of the value added in Hong Kong or the value of non-originating materials used in their manufacture as against the total value of the goods.

(TDO) (Chapter 362 of Hong Kong Laws) only caters for the description of the origin of goods determined by “process-based” rules. As such, the TDO would need to be amended to cater for the description of goods with origin determined by “value-based” rules under the Agreement. Our current plan is to consult the Commerce and Industry Panel of the Legislative Council on the proposed amendments in July 2011.

11. On the application of trade remedy measures⁽⁸⁾, the Agreement includes disciplines additional to the relevant WTO Agreements, which will better safeguard Hong Kong’s trade interest. As Hong Kong is not a user of trade remedy measures, the agreement to the additional disciplines would not pose any problem to us. On the other hand, the Agreement will bring about complete elimination of anti-dumping measures by the four EFTA States. On countervailing and safeguard measures, while Norway has committed to not applying such measures against Hong Kong products, Iceland, Liechtenstein and Switzerland will comply with the enhanced disciplines in the Agreement when taking such measures. Under the Agreement, Hong Kong and the EFTA States will enhance their communication and cooperation in the areas of sanitary and phytosanitary measures⁽⁹⁾ and technical barriers to trade⁽¹⁰⁾. The Agreement also includes trade facilitation measures. They would reduce and simplify documentation and formalities. They would also increase transparency of trade-related laws and regulations of the EFTA States and predictability in their implementation. These measures will benefit Hong Kong traders by reducing costs to business and promoting efficiency.

Note ⁽⁸⁾ Trade remedy measures refer to anti-dumping, countervailing and safeguard measures. Imposition of these measures by the importing economy could result in additional duties (being one of the usual forms) on top of tariffs and other charges or other import restrictions on certain imports.

⁽⁹⁾ Sanitary and phytosanitary measures are any measures applied: (i) to protect human or animal life from risks arising from additives, contaminants, toxins or disease-causing organisms in their food; (ii) to protect human life from plant- or animal-carried diseases; (iii) to protect animal or plant life from pests, diseases, or disease-causing organisms; and (iv) to prevent or limit other damage to a country from the entry, establishment or spread of pests.

⁽¹⁰⁾ The disciplines of technical barriers to trade cover all technical regulations, standards and conformity assessment procedures that may directly or indirectly affect trade in goods between parties to an FTA, regardless of the origin of the goods.

(C) Investment

12. The Investment Chapter includes provisions that will facilitate two-way investment flows between Hong Kong and the EFTA States by providing investors with legal certainty on national treatment and other safeguards in respect of their investments in non-services sectors⁽¹¹⁾. The commitments agreed by both sides are WTO-plus and comparable.

(D) Other Areas in the Agreement

13. Apart from trade in services and goods as well as investment, the Agreement contains provisions to promote competition, ensure effective protection of intellectual property rights, facilitate access to each other's government procurement market, and enhance protection of the environment through trade initiatives. Commitments and cooperation in these trade-related areas would have the positive effect of facilitating, directly or indirectly, trade and investment flows between Hong Kong and the EFTA States. The Agreement also provides for an effective, efficient and transparent process for consultations and settlement of possible disputes arising thereunder.

(E) Bilateral Agreements on Agriculture

14. In view of the EFTA States' diverse interests and sensitivities in the agricultural sector, basic agricultural products are dealt with separately under the bilateral agricultural agreements between Hong Kong and the individual EFTA States. Under the three bilateral agreements, Iceland, Norway and Switzerland⁽¹²⁾ will eliminate import tariffs for a number of basic agricultural products originating in Hong Kong, including those in which we have export interests. These bilateral agreements will enter into force on the same date as the Agreement, and would remain in force as long as the Agreement remains in force.

Note ⁽¹¹⁾ National treatment and other safeguards in respect of investments in services sectors are covered by the Chapter on Trade in Services.

⁽¹²⁾ The bilateral Agreement on Agriculture between Hong Kong and Switzerland will also apply to Liechtenstein.

(F) Side Agreement on Labour

15. Alongside but separate from the Agreement, Hong Kong and the EFTA States have also concluded an Agreement on Labour. Whilst respecting each other's right to regulate and implement its own labour laws and policies, the agreement provides a formalised framework within which both sides can address labour matters of mutual interest or concern through dialogue and cooperation. The agreement also sets out the shared understanding of the two sides not to use labour laws and policies for trade protectionist purposes. The Agreement on Labour will also enter into force on the same date as the Agreement.

Economic and Strategic Value of the Agreement

16. Overall speaking, we consider that it is in Hong Kong's interest to have an FTA with the EFTA States. In broad terms, the Agreement with the EFTA States will open up new business opportunities particularly with respect to trade in services in the market of the four EFTA States for Hong Kong in view of the enhanced legal certainty in the regulatory regime. This will increase trade and investment flows, thereby benefiting our economy and our traders. Among the EFTA States, Switzerland is one of our major trading partners, ranking 13th among our trading partners in the world in 2009 on trade in services and 11th on trade in goods in 2010; while Norway ranked 32nd and 33rd respectively⁽¹³⁾.

17. Specifically on trade in services, the Agreement will provide for early harvest of the EFTA States' Doha offers and some Doha-plus commitments on almost all of our priority service sectors. Hong Kong service providers will enjoy secured market access and legal certainty in the continuation of non-discriminatory treatment in the EFTA States' markets. This would be conducive to their entering into and operating in these markets. The trade facilitation measures including transparency enhancing initiatives under the Agreement will help reduce transaction costs in bilateral trade with the respective EFTA States. With a better understanding of the situation and potential of the Hong Kong market through the conclusion of the Agreement, it may also attract further

Note ⁽¹³⁾ The European Union is counted as one single entity for the rankings.

investment from the EFTA States to Hong Kong.

18. On trade in goods, while the Agreement would result in definitive tariff elimination for all the industrial goods and certain agricultural products of Hong Kong origin, we reckon that the resultant tariff saving from this Agreement would not be significant. This is because the tariff rates currently imposed on our major domestic exports to some EFTA States are already at a very low level. The absolute value of our agricultural products exported to the EFTA States is also minimal. Hence, the major economic benefits of the Agreement will not come from tariff savings. Instead, the Agreement is expected to have a trade creation effect as it will foster closer trade and investment ties which may induce trade in goods and services which are not currently traded between Hong Kong and the EFTA States. In turn, this will stimulate further growth in trade related services, e.g. transportation and logistics, professional services, tourism and travel related services in Hong Kong.

19. Apart from the economic benefits, the Agreement also carries significant strategic value for Hong Kong. The Agreement is the second FTA Hong Kong has with foreign economies. The successful conclusion of the Agreement, in the year following that in which the CEP Agreement with New Zealand was signed, would reinforce the signal to our trading partners that Hong Kong is keen in fostering closer economic partnership through concluding high quality FTAs. These will have a positive effect on our continued pursuit of FTAs with other trading partners to improve the conditions of access for our goods, services and investment in overseas markets.

BASIC LAW IMPLICATIONS

20. The proposal is in conformity with the Basic Law, including the provisions concerning human rights. Negotiations and conclusion of FTAs is within the high degree of autonomy of the Hong Kong Special Administrative Region (HKSAR) as provided for under Article 151 of the Basic Law. The Article provides, inter alia, that the HKSAR may on its own conclude and implement agreements with foreign states in the economic, trade and other appropriate fields.

FINANCIAL AND CIVIL SERVICE IMPLICATIONS

21. Additional resources, if any, required for the implementation of

the Agreement, including that related to the relevant enforcement activities, will be absorbed by existing manpower resources of relevant Bureaux/Departments through redeployment of resources as appropriate.

ECONOMIC IMPLICATIONS

22. The Agreement with the EFTA States has positive economic implications for Hong Kong. In broad terms, the Agreement will provide Hong Kong with better access to the markets of the EFTA States and create more business opportunities beneficial to Hong Kong's long-term economic growth. It will also strengthen Hong Kong's role as an international trade and commerce centre.

SUSTAINABILITY IMPLICATIONS

23. The Agreement with the EFTA States will bring more and better access to the markets of the EFTA States, create more business opportunities for Hong Kong businessmen and increase trade and investment flows between Hong Kong and the EFTA States. This will in turn bring benefits to other trade related sectors in the Hong Kong economy, including banking, insurance and transportation. All these would help to sustain the economic development of Hong Kong and reinforce Hong Kong's position as an international trade, economic and financial hub.

ENVIRONMENTAL IMPLICATIONS

24. The Trade and Environment Chapter in the Agreement has positive environmental implications for Hong Kong. The Chapter seeks to enhance protection of the environment through the promotion and facilitation of trade and investment in goods and services that are beneficial to the environment.

LEGISLATIVE IMPLICATIONS

25. Implementation of the Agreement would require legislative amendments as set out in paragraph 10 above.

PUBLIC CONSULTATION

26. We conducted a public consultation exercise on the FTA negotiations between Hong Kong and the EFTA States in 2009 to help develop our negotiation positions and better gauge the local business community's areas of interest. We have sought views from major trade and industrial associations, traders of our key export interests to the EFTA States, professional bodies and the general public, and their feedback was generally positive.

PUBLICITY

27. A signing ceremony for the Agreement was held on 21 June 2011 in Liechtenstein. Details of the Agreement were made public upon formal signing by Hong Kong and the EFTA States. A press release was issued and a spokesperson is available to answer media enquiries.

BACKGROUND

28. Hong Kong commenced formal FTA negotiations with the EFTA States in January 2010. After five rounds of talks, the negotiations were concluded in March 2011 in Switzerland. Subject to the domestic procedures of both sides, the Agreement is expected to enter into force around June 2012.

29. Total bilateral merchandise trade between Hong Kong and the EFTA States amounted to about HK\$ 76 billion in 2010 while total bilateral service trade amounted to about HK\$ 10 billion in 2009.

ENQUIRIES

30. For enquiries, please contact Mr Raistlin Lau, Assistant Director-General of Trade and Industry Department, at 2398 5309.

Trade and Industry Department
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