

SECTION 3: TAIWAN

Introduction

Cross-Strait relations in 2015 were essentially stable. At the same time, concern in Taiwan about increasing cross-Strait economic integration with China* intensified—as manifested in the 2014 Sunflower Movement, during which Taiwan citizens occupied the legislature in part to protest expanding cross-Strait economic ties. Taiwan citizens' wariness of China, spurred by the Mainland's increasing economic interconnectedness with Taiwan, appears to be partially responsible for flagging public confidence in Taiwan's Kuomintang (KMT)-led government. With Taiwan's national elections approaching in January 2016, and the Democratic Progressive Party (DPP), Taiwan's opposition and traditionally pro-independence party, leading in presidential polls, China-Taiwan relations may be facing a major shift. Meanwhile, China's continued military modernization poses a growing threat to Taiwan, and the balance of power in the Taiwan Strait continues to shift strongly in China's favor.

Outside the cross-Strait relationship, Taiwan is making progress addressing several economic and security challenges. Despite China's restrictions on Taiwan's participation in multilateral institutions, Taiwan continues to attempt to expand its status and legitimacy in international affairs by actively pursuing both regional economic integration and fisheries agreements with its maritime neighbors. U.S.-Taiwan relations also remain strong, with annual bilateral trade reaching a record high of \$67.4 billion in 2014 and continued growth expected in 2015.¹ In the security realm, increased U.S.-Taiwan security cooperation demonstrates the U.S. commitment to Taiwan's defense.

This section examines the state of cross-Strait ties, Taiwan's international engagement, Taiwan military and security issues, and U.S.-Taiwan relations, and ends with a discussion of the implications of these developments for the United States. It is based on the Commission's meetings with Taiwan officials in Washington, consultations with U.S. and foreign nongovernmental experts, and open-source research and analysis.

Cross-Strait Relations

A series of events that occurred in Taiwan in 2014 continue to shape its political environment and the cross-Strait relationship. The first of these events, and perhaps the most influential for cross-Strait ties, was the Sunflower Movement. The Sunflower Movement started as a grassroots student-led occupation of Tai-

*For the purposes of this section, China refers to mainland China (the Mainland), or the People's Republic of China.

wan's national legislature, the Legislative Yuan, for 23 days between March and April 2014 in opposition to the Ma Ying-jeou Administration's handling of a major cross-Strait economic deal, the Cross-Strait Services Trade Agreement (CSSTA) (discussed later in the section). The protests sparked a public debate in Taiwan about whether the services agreement would create unfair competition and enable China to exercise excessive economic leverage over Taiwan. The Sunflower Movement delayed ratification of the services agreement and effectively postponed negotiations on other cross-Strait agreements.* The protests also played a role in pushing the Legislative Yuan to craft an oversight mechanism for cross-Strait agreements.² As of the writing of this Report, the Legislative Yuan has yet to pass legislation to establish such a mechanism.†

Eight months after the student-led occupation of the Legislative Yuan, the KMT suffered a landslide defeat to the DPP in Taiwan's November 2014 local elections.‡ Polls conducted in the aftermath of the elections found the public's rejection of the Ma Administration's performance was the main reason for the KMT defeat.³ Most voters in the elections were primarily concerned with local issues, such as wages, housing prices, and food safety. Cross-Strait relations did not appear to play a sizable role in voting patterns. Nevertheless, some—particularly younger voters—may have voted for the DPP due to suspicion of China's intentions and unease with China's growing influence over Taiwan.⁴ Following the poor results of the local elections for the KMT, President Ma (who was also KMT chairman) resigned as party chairman in December 2014 in response to pressure from the party elite.⁵

Taiwan citizens' affinity for and identification with mainland China appears to be decreasing. According to a 2014 survey of Taiwan citizens conducted by National Chengchi University in Taipei, when asked how they view their national identity, over 60 percent of respondents—an all-time high since the survey was first conducted in 1992—said they self-identified as Taiwanese instead of Chinese or a combination of the two. Those who identified as both Taiwanese and Chinese comprised 32.5 percent.⁶ By comparison, the survey conducted in 2013 found about 57 percent identified themselves as Taiwanese (35.8 percent as Taiwanese and Chinese), and in 2008, when President Ma was first elected, it found that less than 50 percent identified themselves as Taiwanese (43.1 percent as Taiwanese and Chinese).⁷ The survey results suggest that Taiwan citizens in general view identity more in terms of citizen-

* For more information on the Sunflower Movement, see U.S.-China Economic and Security Review Commission, *2014 Annual Report to Congress*, November 2014, 482–484.

† The idea for an oversight mechanism on cross-Strait agreements is not new. The DPP and KMT debated the idea of an oversight mechanism in 2010 before Taiwan and China signed their Economic Cooperation Framework Agreement (ECFA). Kuomintang, "KMT's Response to the DPP's 'Five Questions' for Chairman Ma," February 12, 2010.

‡ On November 29, 2014, Taiwan held a series of local elections for 11,130 positions, including mayors, county magistrates, city and county councilors, township chiefs, and village and borough chiefs. The KMT won six races for mayor and county magistrates, while the DPP won 13; three others went to independent candidates. In the popular vote for these 22 races, the DPP earned 47.6 percent of the vote and the KMT earned 40.7 percent. In other local elections, the KMT won a larger number of city and county councilor seats than the DPP, but the DPP increased its share of seats by 12.8 percent. The DPP also raised its number of township seats by 58.8 percent. In the elections for village and borough chiefs, the DPP increased representation from 52 to 390, but the KMT retained its majority with 1,794 seats. Matthew Southerland and Kevin Rosier, "Taiwan's 2014 Local Elections: Implications for Cross-Strait Relations," *U.S.-China Economic and Security Review Commission*, December 30, 2014, 2.

ship than ethnic or cultural identity.⁸ This trend shows that China's efforts to move Taiwan politically and culturally closer to the Mainland are not necessarily successfully promoting cross-strait cultural integration or affinity for the Mainland by Taiwan citizens. It also seems to reflect Taiwan citizens' increasing skepticism about China.

Informing Taiwan's growing pessimism about the Mainland's political encroachment is the ongoing political turmoil in Hong Kong. In a July 2015 speech at the Brookings Institution, Mainland Affairs Council (MAC)* Minister Andrew Hsia said, "... [O]bviously we are also concerned with the level and the latitude of freedom and democracy given to the people of Hong Kong. We are disappointed, of course, and we certainly hope that the Beijing regime will respect the people of Hong Kong and its freedom to choose."⁹ Hong Kong's fight for democracy serves as a warning that, if Taiwan were reunified with China, Beijing would not likely adhere to any promise it might make to protect Taiwan's civil liberties. (For more information on recent developments in Hong Kong, see Chapter 3, Section 4, "Hong Kong.")

China also has taken unilateral actions that appear to be designed to move Taiwan closer to the "one country, two systems" framework that Beijing uses for interacting with Hong Kong and Macau. Through these measures, Beijing seeks to move Taiwan closer politically to the Mainland and further constrain its sovereignty. For example, China in July 2015 passed a National Security Law that states, "The sovereignty and territorial integrity of China cannot be encroached upon or divided. Maintenance of national security and territorial integrity is a shared obligation of all the Chinese people, including compatriots from Hong Kong, Macau, and Taiwan."¹⁰ The Ma Administration responded by issuing a formal protest with the Chinese government, and the DPP called the law a "disrespectful decision" toward the Taiwan people.¹¹ China also announced a new requirement for Taiwan citizens traveling to the Mainland to use entry permit cards similar to those used by Hong Kong residents in place of passports.¹² Opponents of the decision in Taiwan criticized it as a "downgrade" of Taiwan's status.¹³

Cross-Strait Political Relations

As the KMT and DPP vie for power, the Chinese government appears to be increasingly uneasy about the prospect of the DPP winning Taiwan's presidency in the January 2016 elections.¹⁴ With the DPP's chairperson and presidential candidate Tsai Ing-wen leading all other candidates in the polls,¹⁵ observers assess that Beijing is worried that if DPP Chairperson Tsai is elected, she may not accept the notion that the Mainland and Taiwan are part of one country and may seek to steer Taiwan toward *de jure* independence.¹⁶ Bonnie Glaser, senior advisor for Asia at the Center for Strategic and International Studies (CSIS) and Jacqueline Vitello, program associate at CSIS, assert that this fear is based on Chair-

*The Mainland Affairs Council is a cabinet-level agency in Taiwan's executive branch that is responsible for overseeing Taiwan's cross-strait policies.

person Tsai's unwillingness to agree to the "one China" principle* and her role in creating the "two states theory"† when she served as a senior advisor in the Taiwan government in 1999.¹⁷ Despite Beijing's perception that Chairperson Tsai would damage cross-strait ties, her stated position of "maintaining the status quo" in cross-strait relations indicates a pragmatic approach.¹⁸

Beijing is also concerned, in part, because the last time the DPP held power (from 2000 to 2008), the administration of then president Chen Shui-bian pursued a pro-independence policy.¹⁹ Throughout 2015, Chinese President and General Secretary of the Chinese Communist Party (CCP) Xi Jinping, Premier Li Keqiang, and other senior officials have made statements insisting that Taiwan follow the "1992 Consensus,"²⁰ a tacit understanding reached between the two sides that interprets the "one China" principle such that each side maintains its own definition of "one China."²¹ While President Ma has cited the 1992 Consensus as the basis for seven years of positive cross-strait relations, the DPP has rejected the term.²²

KMT and DPP Views on Cross-Strait Relations

Although it is unclear how cross-strait issues will influence the outcome of Taiwan's elections, the two leading political parties' cross-strait policies will have important implications for future relations between Taiwan and the Mainland.

President Ma has defended the KMT's adherence to the 1992 Consensus and "Three No's"—no unification, no independence, and no use of force—as the keys to successfully reaching cross-strait agreements on trade and investment.²³ The KMT appears to be trying to sell Taiwan citizens on its accomplishments in deepening and stabilizing cross-strait ties, warning that any changes to cross-strait policy would invite instability. In an April 2015 speech at Taiwan's MAC, President Ma said, "By adhering to the [1992 Consensus], cross-strait relations are bound to flourish. Divergence is sure to result in deterioration. And opposing the 1992 Consensus is sure to create turmoil."²⁴

Facing low poll numbers and the prospect of losing both the presidential election and the majority of seats in the Legislative Yuan, the KMT in October 2015 decided to replace its presidential candidate, eight term legislator Deputy Legislative Speaker Hung Hsiu-chu, with KMT chairman and mayor of New Taipei

*The "one China" principle states that both Taiwan and China are a part of a single "China." China's Taiwan Affairs Office and State Council, *The One-China Principle and the Taiwan Issue*, February 21, 2000.

†In 1999, then Taiwan president Lee Teng-hui proposed the "two states theory," which considered Taiwan a separate state from the Mainland, leading to the suspension of cross-strait talks and political discord. Tsai Ing-wen served as senior advisor on Taiwan's National Security Council at the time and is said to be one of the key architects of the theory. Goh Sui Noi, "Tsai Ing-wen: The 'Doc' who Nursed DPP Back to Health," *Straits Times* (Singapore), July 27, 2015; Taiwan Panorama, "A Woman of Many Parts: Tsai Ing-wen," July 1, 2012.

**KMT and DPP Views on Cross-Strait Relations—
Continued**

City Eric Chu.* Ms. Hung upon her July 2015 nomination as the KMT's presidential candidate was seen by some KMT party members as a controversial choice due to statements she made that were viewed as more pro-China and pro-unification than the KMT mainstream.† Mr. Chu, by contrast, is a popular KMT centrist who has pledged to uphold the 1992 Consensus and follow President Ma's cross-Strait policy.²⁵ A KMT government in 2016 probably would continue to pursue a strategy of rapprochement with Beijing and seek improved economic, cultural, and people-to-people ties, though it would likely face the same obstacles that the Ma Administration has encountered in recent years.

Meanwhile, DPP Chairperson Tsai has left her party's cross-Strait policy purposefully vague, stating the DPP supports "maintaining the status quo" without agreeing to the 1992 Consensus or any form of the "one China" principle.²⁶ In a speech during her visit to the United States in June 2015, Chairperson Tsai said, "[If] elected President, I will push for the peaceful and stable development of cross-Strait relations in accordance with the will of the Taiwanese people and the existing [Taiwan] constitutional order. [The accumulated outcomes of more than 20 years of negotiations and exchanges] will serve as the firm basis of my efforts . . ." ²⁷ Her comments suggest that she will not seek to reverse the accomplishments of the 1992 Consensus.²⁸ By leaving ambiguity in the DPP's cross-Strait policy, Chairperson Tsai appears to be seeking to avoid alienating both the DPP's staunch pro-independence base and mainstream Taiwan voters who seek stability in the cross-Strait relationship. A DPP government in 2016 likely would seek to create greater transparency in cross-Strait negotiations. If elected, Chairperson Tsai could also slow the pace of rapprochement with Beijing due to Taiwan citizens' fear of the Mainland's increasing influence in Taiwan.²⁹

*On October 17 at a special party congress, 812 out of 891 KMT delegates voted to remove Ms. Hung as the party's presidential candidate. A majority of delegates then voted to replace Ms. Hung with Mr. Chu, and he accepted, though he had previously said he would not run for president. Stacy Hsu, "Presidential Campaign: KMT's Eric Chu Takes Over Campaign," *Taipei Times*, October 18, 2015; Yuan-Ming Chiao, "Hung Ouster Settled, Chu Begins Bid," *China Post* (Taiwan), October 18, 2015; and Austin Ramzy, "Fearing Election Losses, Taiwan's Governing Party Drops Its Presidential Candidate," *New York Times*, October 17, 2015.

†In May 2015 when Ms. Hung was a prospective candidate, she proposed a framework for cross-Strait relations, "one China, same interpretation," which interpreted the "one China" principle such that each side agrees to the same definition of "one China," which was widely viewed as inconsistent with the party's 1992 Consensus. As a prospective candidate she also made provocative comments, such as denying the existence of Taiwan, calling for ending arms procurement from the United States, and proposing a peace agreement with China. In July 2015 prior to the KMT party congress where party delegates nominated their candidate, Ms. Hung agreed to drop her "one China, same interpretation" stance and instead follow the KMT's party platform. Goh Sui Noi, "Hung Hsiu-chu: KMT's 'Little Chilli' Spices Up Race," *Straits Times* (Singapore), July 27, 2015; Ricky Yeh, "The Challenging Road for Taiwan's Newest Presidential Candidate," *Diplomat*, July 19, 2015; Loa Lok-sin, "Hung Vows to Drop 'Same Interpretation': Lawmakers," *Taipei Times*, July 10, 2015; Yuan-Ming Chiao, "Hung Draws Criticism for Her 'Can't Say ROC Exists' Stance," *China Post* (Taiwan), July 4, 2015; and Central News Agency (Taiwan), "One China, Same Interpretation' Is Cross-Strait Status Quo: KMT's Hung," May 7, 2015.

Cross-Strait Agreements and Diplomatic Relations

Since April 2014, progress on major cross-Strait negotiations has slowed and Taiwan's ratification of signed cross-Strait agreements has stalled, in large part due to President Ma's waning public support and political gridlock in the Legislative Yuan. In March 2014, protestors occupying the Legislative Yuan during the Sunflower Movement demanded the government adopt an oversight mechanism to enhance transparency in the approval process of future cross-Strait agreements. The protestors proposed a mechanism to grant the Legislative Yuan the right to manage and engage in negotiations on all cross-Strait agreements with China.³⁰ This effort remains stalled in the Legislative Yuan, which has yet to debate the nine proposed draft versions of the bill. Much of the political logjam is the result of disagreement over the respective roles of the Legislative Yuan and the Executive Yuan (Taiwan's executive branch of government) in the oversight process.³¹ Although implementing the oversight mechanism is one of President Ma's top priorities before leaving office, it appears increasingly unlikely that he will achieve this goal.³² Nevertheless, when this oversight mechanism is eventually adopted, it will have significant implications for all future cross-Strait agreements.

Major cross-Strait agreements pending completion include the following:

- *Cross-Strait Services Trade Agreement (CSSTA)*: Awaiting ratification in the Legislative Yuan, the CSSTA, signed in 2013, was designed to open up the services sectors of China and Taiwan to cross-Strait trade. The agreement is one of the most important cross-Strait economic deals promoted by the Ma Administration under the 2010 Economic Cooperation Framework Agreement (ECFA), the main framework for cross-Strait economic integration.* If ratified, the services agreement would have a significant impact on Taiwan's services industries, a key driver of Taiwan's economy, accounting for over 62 percent of its gross domestic product (GDP) and 59 percent of its workforce.³³ By eliminating investment restrictions and other barriers across 64 service industries in Taiwan and 80 services industries in China, the CSSTA would primarily benefit Taiwan's financial and retail industries, according to observers.³⁴ However, public and legislative opposition to the agreement has effectively stalled the ratification process. The DPP and other opponents argue the CSSTA will create unfair competition, marginalize Taiwan's low-end service sector businesses, and expose Taiwan to increased economic and political influence from the Mainland.³⁵
- *Cross-Strait Trade in Goods Agreement*: Progress on the proposed cross-Strait trade in goods agreement under the ECFA

*The ECFA lays out a roadmap for four subsequent agreements concerning investment protection, dispute settlement, trade in goods, and trade in services. Kerry Brown, Justin Hempton-Jones, and Jessica Pennisi, "The Economic Cooperation Framework Agreement (ECFA)," in *Investment Across the Taiwan Strait*, Chatham House, November 2010, 20–33; Alan D. Romberg, "Ma at Mid-term: Challenges for Cross-Strait Relations," *China Leadership Monitor* 33 (Summer 2010), 1–4.

also has slowed considerably since negotiations started in 2010. The deal would cut tariffs on 10,000 categories of goods shipped between China and Taiwan—impacting industries that comprise about 30 percent of Taiwan’s exports—including automotive parts, display panels, machine tools, and petrochemicals.³⁶ After a nearly 11-month pause due in part to competing cross-Strait priorities and the Sunflower Movement, talks restarted in September 2014.³⁷ The most contentious issue in the negotiations is whether Taiwan will enjoy preferential tariff status for its key export industries.³⁸ Taiwan negotiators are seeking to obtain concessions greater than South Korea did in its recent free trade agreement with China, since Taiwan and South Korea compete for the Chinese market in several industries.* (Some reports indicate that during talks concluded in April 2015 mainland authorities rejected Taiwan’s efforts to obtain preferential status over South Korea.)³⁹ Though Taiwan officials hope to conclude the agreement by the end of 2015, lack of progress on this crucial issue casts doubt on an agreement being reached in the near term.⁴⁰

Despite this slow progress on cross-Strait deals, low- and high-level meetings continued over the past year, covering a broad range of cross-Strait issues, including party-to-party, economic, and security concerns. These meetings included the following:

- In May 2015, KMT Chairman Eric Chu, prior to being nominated as his party’s presidential candidate, in a party-to-party capacity met CCP General Secretary Xi in Beijing. Chairman Chu was the highest ranking KMT official to meet with a top CCP official since 2008.⁴¹ The meeting strengthened high-level cooperation between political parties and promoted the 1992 Consensus as the guiding framework for cross-Strait ties. For Beijing, the meeting appeared to serve as an opportunity to endorse the KMT’s cross-Strait policies and emphasize the need to continue along this path for continued stability in the relationship.⁴² At the meeting, CCP General Secretary Xi underscored the “political foundation” of cross-Strait relations as acceptance of the 1992 Consensus and opposition to Taiwan independence.⁴³
- In May and October 2015, MAC Minister Andrew Hsia and Taiwan Affairs Office † Director Zhang Zhijun met in Kinmen, Taiwan and Guangzhou, China respectively. The talks built on the historic February 2014 meeting between the heads of those offices held in Nanjing, China—the first between government officials from each side of the Taiwan Strait since Taiwan and

*The China-South Korea free trade agreement has a significant impact on the Taiwan-China trade in goods negotiations and other free trade negotiations under the ECFA. Taiwan competes with South Korea in key industries, particularly liquid crystal display (LCD) panels, petrochemicals, and steel. Taiwan’s Ministry of Economic Affairs estimates Taiwan exporters could lose up to \$6 billion over the next 20 years as a result of the China-South Korea free trade agreement. Other sources estimate much higher losses. Tang Pei-chun and Scully Hsiao, “Cabinet Urges Faster Trade Talks as China, S. Korea Sign FTA,” *Focus Taiwan*, June 1, 2015; Amy Chyan, “China-S. Korea FTA to Hurt Taiwan,” *China Post* (Taiwan), November 11, 2014.

†The Taiwan Affairs Office is an agency under China’s State Council that is responsible for overseeing China’s cross-Strait policies.

China split in 1949 following the Chinese civil war. The meetings in 2015 did not result in considerable progress on key diplomatic agreements, but helped reinforce this channel as a high-level cross-Strait policy dialogue.⁴⁴

- After an 18-month pause between meetings, in August 2015 Taiwan's Straits Exchange Foundation and China's Association for Relations Across the Taiwan Strait* met for the 11th round of cross-Strait talks in Fuzhou, China. The two sides signed agreements on double taxation and aviation safety. Under the taxation agreement, any business based in Taiwan that invests in the Mainland, including via a third country, will not have to pay extra taxes to China. In addition, foreign companies with subsidiaries in Taiwan can now access the Chinese market without incurring additional taxes. Meanwhile, the flight safety agreement allows Taiwan and Chinese carriers with cross-Strait flights to use each other's technicians and maintenance facilities for routine aircraft inspections.⁴⁵ Notably, the two sides decided shortly before the meeting to set aside a proposed agreement that would allow Chinese flights to make transit stops in Taiwan.⁴⁶
- After five rounds of talks, Taipei and Beijing in March 2015 settled a dispute over one of China's four new civilian aircraft routes in the Taiwan Strait.⁴⁷ One of the routes, M503, announced in January, would pass as close as 8 kilometers (km), or approximately 5 miles (mi), away from Taiwan's air space (the median line of the Taiwan Strait). Taiwan found M503 problematic due to its proximity to Taiwan air traffic and the potential security risks to Taiwan's airspace. China agreed to a compromise, relocating the route 18–19 km (about 11 mi) west and suspending the three other flight routes along the Chinese coast that would have intersected with M503.⁴⁸

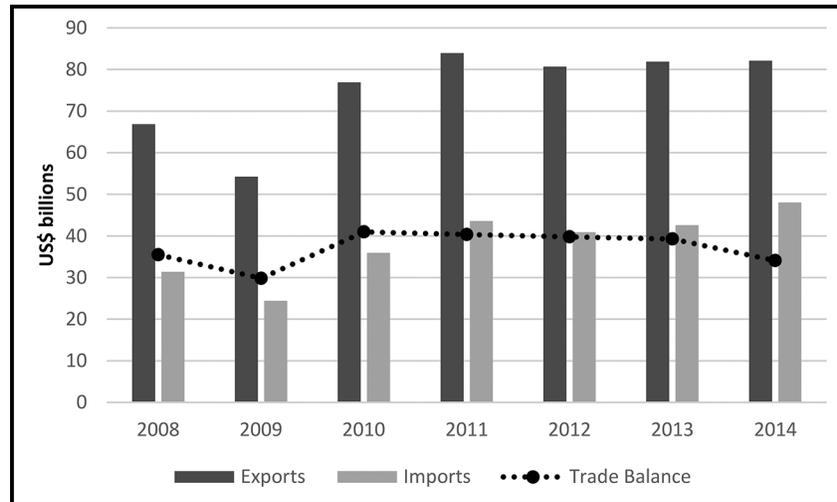
Cross-Strait Trade and Investment

As of August 2015, China remains Taiwan's largest trading partner, top source of imports, and biggest export market.† In 2014, annual cross-Strait trade reached \$130.2 billion, comprising 22.1 percent of Taiwan's total trade. Since President Ma took office in 2008, bilateral trade has increased by over 32 percent (see Figure 1).⁴⁹

*The Straits Exchange Foundation and the Association for Relations Across the Taiwan Strait facilitate cross-Strait negotiations in the absence of formal ties between the governments of Taiwan and China. Although the two bodies are semiofficial organizations, they receive direction from their respective governments.

†Based on purchasing power parity, China's GDP in 2014 was \$17.6 trillion, while Taiwan's GDP was \$1.07 trillion. China's GDP per capita was \$12,880 that year; Taiwan's was \$45,853. Although GDP and GDP per capita figures can be estimated in different ways, purchasing power parity helps minimize the effect of exchange rates on the calculations. International Monetary Fund, "World Economic Outlook Database;" Bureau of Foreign Trade (Taiwan), "Trade Statistics."

Figure 1: Taiwan's Trade with China (2008–2014)



Source: Bureau of Foreign Trade (Taiwan).

Taiwan's exports to China in 2014 were \$82.1 billion, comprising 26.2 percent of Taiwan's exports to the world. Year-on-year, Taiwan's exports to China grew less than one percent in 2014, and Taiwan's trade surplus with China for that year was \$34.1 billion, the lowest since 2009.⁵⁰ The declining growth of Taiwan's exports is explained in part by the rise of Chinese competitors, pricing Taiwan's exports out of the market.⁵¹ Semiconductor-related products dominate exports to China, supporting Taiwan's largest industry.* In 2014, three of the top five exports—microchips, semiconductors, and printed circuit boards—made up over a quarter of total exports to China.⁵² While exports of all of these products increased in 2014, microchips, Taiwan's largest export to China, grew by nearly 17 percent from 2013 to 2014.†

In 2014, China's exports to Taiwan reached an all-time high, exceeding \$48 billion and comprising a record 17.5 percent share of Taiwan's imports. That year, China replaced Japan as Taiwan's largest source of imports and remains in the same position as of August 2015.⁵³ Just as microchips dominate Taiwan exports to China, they are also China's top export to Taiwan. (Taiwan firms generally design and manufacture unfinished microchips and other semiconductor-related products in Taiwan for assembly and testing in China. China then typically exports the finished products back to Taiwan.)⁵⁴ However, Taiwan's other top imports from China are more diverse than Taiwan's exports to China; they are cell phones,

*Of note, Taiwan Semiconductor Manufacturing Company is the largest semiconductor foundry in the world, and together with another Taiwan semiconductor foundry, United Microelectronics Corporation, accounted for over 60 percent of the industry's global revenue in 2014. U.S.-China Economic and Security Review Commission, *Monthly Analysis of U.S.-China Trade Data*, August 5, 2015, 11.

†In 2014, microchips alone accounted for nearly 20 percent of all Taiwan exports to China. Bureau of Foreign Trade (Taiwan), "Trade Statistics."

electronic computers, flat-rolled stainless steel, and chemical elements for use in electronics.⁵⁵

According to official Taiwan data, Taiwan foreign direct investment (FDI) to the Mainland in 2014 was approximately \$10.3 billion, nearly double U.S. FDI to China that year.* However, analysts believe this amount grossly understates the actual scale of investment. According to a 2011 study by Daniel H. Rosen and Zhi Wang, many Taiwan firms use third-party companies, primarily in Hong Kong, to invest in the Mainland, which accounts for the discrepancy.⁵⁶ Official Taiwan FDI flows have nevertheless been declining since 2010, with the exception of a 13 percent increase in 2014. Much of the increase in 2014 was due to new Taiwan FDI in China's electronic parts manufacturing and computer manufacturing sectors, which together comprised over a quarter of all outbound Taiwan FDI that year. Aside from semiconductor-related manufacturing, in 2014 Taiwan FDI in the Mainland was concentrated in the financial and insurance industry (16.1 percent) and wholesale and retail trade (10.7 percent).⁵⁷ In 2015, Taiwan FDI into China from January to August was approximately \$6.8 billion, slightly exceeding 2014 numbers through August.⁵⁸ Taiwan's decision in August 2015 to lift restrictions on Taiwan firms from owning more advanced semiconductor manufacturing plants in China (for 12-inch wafer fabrication) could help stimulate greater investment flows into the Mainland.⁵⁹

Meanwhile, official Taiwan statistics on Chinese FDI into Taiwan showed FDI flows in 2014 remaining steady at \$335 million, largely unchanged since 2012.⁶⁰ In 2014, the main sectors of Chinese FDI in Taiwan were wholesale and retail trade (40 percent), banking services (18.3 percent), and chemical products manufacturing (12.9 percent).⁶¹ Despite restrictions on inbound FDI from the Mainland,† Chinese FDI to Taiwan more than tripled between 2010 and 2012, due in large part to the Ma Administration's loosening of investment caps and regulations on mainland investment into Taiwan.‡ However, with negotiations on cross-Strait economic agreements at a standstill, Taiwan's easing of its restrictions on Chinese inbound investment has slowed down, limiting increases in FDI flows. From January through August 2015, mainland investment in Taiwan was \$79.2 million, dropping nearly 67 percent compared to the same period in 2014 when it was \$239 million.⁶² But according to some reports, mainland investment in Taiwan could still recover to reach record-high levels if several large potential deals are finalized.§

* According to official Mainland data, Taiwan FDI to China in 2014 was \$14.7 billion, the fifth largest source of FDI to China. U.S. government data show U.S. FDI to China reached \$6.3 billion that year. U.S. Department of Commerce, Bureau of Economic Analysis, *China Factsheet*, July 31, 2015; Ministry of Economic Affairs, Overseas Chinese and Foreign Investment Commission (Taiwan), *Monthly Report*, December 2014.

† All investments require Taiwan government approval, and the Taiwan government prohibits individuals from having stakes in or appointing managers to mainland investments.

‡ For example, in March 2012, Taiwan lifted mainland investment caps of 10 percent stakes in local firms and 50 percent in joint ventures in Taiwan's semiconductor, electronic, and metal tool manufacturing sectors. PWC, "Chapter 4: The Bigger Picture—China's Impact on the Semiconductor Industry 2012 Update," September 2012.

§ One of the deals involves a joint venture between Taiwan-based CTBC Financial Holding Co. and China's CITIC Group Corp. The other deal is a proposed NTD (New Taiwan dollars) 48 billion (approximately \$1.5 billion) sale of Mandarin Oriental Taipei to a Shanghai-based company. John Liu, "Mainland Chinese Investment in Taiwan Slows Down," *China Post* (Taiwan), June 22, 2015.

Taiwan's International Engagement

Beijing's insistence on the "one China" principle precludes any country or international organization from simultaneously recognizing China and Taiwan, thereby restricting Taiwan's full participation in the international community. Taiwan as a result of Chinese pressure in the UN and other international organizations is unable to participate in the UN Framework Convention on Climate Change, the International Atomic Energy Agency, the International Civil Aviation Organization, the International Maritime Organization, and the International Criminal Police Organization (Interpol), among others.⁶³ Such restrictions limit the existing few diplomatic levers at Taiwan's disposal to engage on important issues.

For example, Nepal in April 2015 rejected Taiwan's offer to provide search and rescue teams to help look for survivors following its massive 7.8 magnitude earthquake, though the Nepalese government eventually worked with Taiwan officials to arrange delivery of monetary and medical aid through Taiwan nongovernmental organizations.⁶⁴ The Nepal government reportedly cited the lack of diplomatic relations and the "great distance" between Nepal and Taiwan as reasons for its initial decision.⁶⁵ As a result, Taiwan delivered a \$300,000 donation check through Nepal's embassy in India due to Nepal's refusal to accept the funds in country.⁶⁶ Although Chinese pressure on Nepal was not explicit, Nepal probably did not want to anger China by accepting official assistance from Taiwan.⁶⁷

Nevertheless, Taiwan actively pursues greater international space through its official diplomatic relations with 22 countries,* expanding participation in international organizations that do not require members to be recognized as sovereign states, and strengthening economic and unofficial diplomatic partnerships with countries other than China. Examples of Taiwan's progress over the past year include the following:

- In March 2015, President Ma visited Singapore, a country that has official diplomatic relations with China, to pay his respects to deceased Singapore founding father and former prime minister Lee Kwan Yew. The visit was the first to Singapore by a Taiwan president since 1989 and President Ma's first overseas travel to any country with diplomatic relations with China aside from transit stops in the United States.⁶⁸
- Taiwan and Japan in March 2015 signed an updated fisheries agreement, following their landmark 2013 deal to jointly manage fishing in the East China Sea near the disputed Senkaku Islands. The updated agreement established new regulations on sharing fisheries and could serve as an example of successful dispute resolution to other claimants involved in disputes in the East and South China seas.⁶⁹ (For more information about the agreement and Taiwan's other helpful efforts to promote cooperation in the region, see "Taiwan's Response to Chi-

* Taiwan has diplomatic relations with Belize, Burkina Faso, the Dominican Republic, El Salvador, Guatemala, Haiti, the Holy See, Honduras, Kiribati, the Marshall Islands, Nauru, Nicaragua, Palau, Panama, Paraguay, Saint Kitts and Nevis, Saint Lucia, Saint Vincent and the Grenadines, Sao Tome and Principe, the Solomon Islands, Swaziland, and Tuvalu. Taiwan's Ministry of Foreign Affairs, "Diplomatic Allies."

na's Assertiveness in the East and South China Seas," later in this section.)

- In June 2015, Taiwan signed two memoranda of understanding with South Korea to accelerate the governments' existing cross-border patent review and approval process by fast-tracking applications for companies with an existing patent under one of the governments and shortening the review process, among other efficiencies. Together the agreements appear to mostly benefit the electronics and semiconductor industries, sectors that comprise 65 percent of Taiwan's exports to South Korea.⁷⁰

The U.S. government has supported the expansion of Taiwan's participation in international organizations. In April 2015, U.S. Assistant Secretary of State for East Asia and Pacific Affairs Daniel Russel, in testimony to Congress, expressed support for Taiwan's participation in international institutions, including Interpol. Assistant Secretary Russel said, "[The Administration wants] Taiwan to be a member of organizations for which statehood is not a prerequisite, and we want Taiwan appropriately to interact, whether as an observer or as the beneficiary of technical programs and other kinds of institutions. . . . We very much agree that Taiwan is a net contributor to international law enforcement, and we are looking for ways to build on that."⁷¹

Taiwan Explores Regional Economic Integration

The Taiwan government has expressed interest in joining regional trade and investment regimes to encourage economic growth and new market opportunities and expand its international footprint. President Ma has supported Taiwan becoming a member of the Regional Comprehensive Economic Partnership (RCEP), led by the Association of Southeast Asian Nations (ASEAN), the U.S.-led Trans-Pacific Partnership (TPP),* and China's Asian Infrastructure Investment Bank (AIIB), emphasizing the benefits of regional economic integration for Taiwan's economy.⁷² Meanwhile, KMT Chairman Eric Chu during his visit to Beijing in May 2015 voiced support for Taiwan's participation in China's 21st Century Maritime Silk Road, part of President Xi's "One Belt, One Road" initiative.⁷³

Announced in 2013 with negotiations planned to conclude this year, ASEAN's Regional Comprehensive Economic Partnership (RCEP) is a proposed free trade agreement among the countries of ASEAN and six additional Asian countries † that currently account for over half of Taiwan's annual trade.⁷⁴ China is among the most influential participants in the RCEP negotiations, and insists Taiwan conclude all ECFA-related agreements before join-

* For more information on Taiwan's aspirations to participate in TPP, see "The Role of Taiwan in the U.S. Rebalance to Asia" later in this section.

† ASEAN's members are Brunei, Burma (Myanmar), Cambodia, Indonesia, Laos, Malaysia, the Philippines, Singapore, Thailand, and Vietnam. The other six RCEP negotiators are Australia, China, India, Japan, New Zealand, and South Korea.

**Taiwan Explores Regional Economic Integration—
Continued**

ing RCEP.⁷⁵ Taiwan thus is unlikely to accede to the RCEP in the near term, given the delays in finalizing cross-Strait economic agreements with China.

In contrast to RCEP's initial closed membership, the AIIB had an open application process with the opportunity to become a founding member if applications were submitted before March 31, 2015. Under the terms of the AIIB, only founding members have the ability to propose new rules.* On the day of the AIIB's deadline for founding members, Taiwan submitted its application, which faced pushback from the DPP and other opposition groups.† On April 16, China announced 57 founding members of the AIIB, but rejected Taiwan's application over its implicit status. In Beijing's view, by using an "improper name" ("Taiwan"),‡ Taiwan's application implied independence from China.⁷⁶

If Taiwan joins the AIIB when China admits a new round of members, as Chinese officials have said is likely, membership could lead to increased Taiwan regional investment opportunities and could widen Taiwan's international economic presence.⁷⁷ For example, the Taiwan Ministry of Finance stated that successfully joining the financial institution would increase Taiwan's chances of joining RCEP and other free trade agreements. Through the AIIB, Taiwan could strengthen dialogue with other regional and global partners, which would help expand its visibility.⁷⁸ Many questions remain, however. It is still unclear what Taiwan's status in the AIIB would be and whether it would have the same access and influence within the institution compared to other members. The DPP and other opposition parties warn that Taiwan should proceed cautiously and carefully examine the political and economic implications of acceding to the bank.⁷⁹ With the AIIB set to begin operating by the end of 2015, Taiwan will have an opportunity to observe the institution in action and study how it could impact Taiwan prior to submitting a revised application.

*For more information about the AIIB, see Chapter 1, Section 1, "Year in Review: Economics and Trade."

†The DPP and other opposition groups were upset that the Ma Administration failed to consult with the legislature prior to submitting the application. They also protested the Ma Administration's handling of the application submission; the Taiwan government used the same channel it uses for cross-Strait agreements instead of the channel it normally uses when applying for membership in an international organization. *Apple Daily* (Taiwan), "Entering the Asian Infrastructure and Investment Bank, Ma: If Restricted, We Will Drop Out," April 1, 2015. Staff translation; Chu Pu-ching, "Asian Infrastructure and Investment Bank Controversy, Tsai Ing-wen: The Government is Making International Affairs a Cross-Strait Issue," *Taiwan People News*, April 1, 2015. Staff translation.

‡Taiwan often participates in international organizations under creative names to avoid opposition from China. For example, Taiwan joined the World Bank as "Separate Customs Territory of Taiwan, Penghu, Kinmen, and Matsu." After China joined the Asian Development Bank, Taiwan was required to participate under a different name, "Taipei, China." Jenny W. Hsu, "China Thwarts Taiwan's Bid to be a Founding Member of AIIB," *Wall Street Journal*, April 13, 2015; Tseung Ying-yu, Lawrence Chiu, and Lilian Wu, "Taiwan Submits Letter of Intent to Join AIIB," *Focus Taiwan*, March 31, 2015; and Heh-Song Wang, "Taiwan and the Asian Development Bank," *ABA Journal* (2007).

**Taiwan Explores Regional Economic Integration—
*Continued***

Proposed by President Xi in 2013, the 21st Century Maritime Silk Road aims to enhance regional connectivity through trade and investment in maritime Asia. (See Chapter 3, Section 2, “China and Southeast Asia” for further discussion of China’s 21st Century Maritime Silk Road.) Beijing has encouraged Taiwan to participate in this initiative, in contrast to its rejections of Taiwan’s other efforts to participate in RCEP and the AIIB. This is probably because the “One Belt, One Road” project is Beijing’s diplomatic initiative and not a formal international institution that would allow Taiwan a greater voice in the international community.⁸⁰ So far, Taiwan officials have been cautious in approaching the initiative, as it is unclear if Beijing will tie political conditions to Taiwan’s participation.⁸¹

Taiwan’s Response to China’s Assertiveness in the East and South China Seas

While China has been increasingly assertive in the East and South China seas, Taiwan has proposed diplomatic frameworks and signed agreements with other claimants to encourage the shelving of territorial disputes and promotion of joint resource development. (See Chapter 3, Section 2, “China and Southeast Asia,” for further discussion of the territorial disputes in the South China Sea.) In addition, Taiwan has taken steps to clarify its own claims according to international law and thereby differentiate its claims from those of China. Despite overtures from the Chinese government, Taiwan has refused to support China’s expansive sovereignty claims on disputed territory in the region, though, to Beijing, Taipei’s claims are the same as its own.⁸²

Since 2012, Taiwan has played a role in promoting cooperation in the East China Sea. Taiwan is one of three claimants to the Senkaku Islands (known as the Diaoyutai in Taiwan and Diaoyu in China)* and has long considered the waters around the islands important fishing grounds to support its fishing industry, one of the world’s largest.⁸³ In August 2012, President Ma announced an East China Sea Peace Initiative calling for all parties with conflicting claims “to replace confrontation with dialogue, shelve territorial disputes through negotiations, formulate a Code of Conduct in the East China Sea, and engage in joint development of resources.”⁸⁴ The initiative led Taiwan and Japan to sign a landmark fisheries agreement in 2013 to set aside sovereignty claims; share fishing grounds between their respective overlapping exclusive economic zones; † and extend the fishing area for both sides by 1,400 square nautical miles (nm).⁸⁵ The international community praised the agreement as a constructive model for jointly managing resources in disputed waters.⁸⁶ U.S. Secretary of State John Kerry

* Other claimants of the Senkaku Islands are Japan and China.

† An exclusive economic zone is a 200 nm zone extending from the coastline of a state’s mainland and from the coastline of any territorial land features. UN Convention on the Law of the Sea, “Part 5: Exclusive Economic Zone.”

in a 2014 speech said, “Japan and Taiwan . . . showed last year it’s possible to promote regional stability despite conflicting claims.”⁸⁷ In an updated fisheries agreement reached in March 2015, each side agreed to several amendments designed to avoid frictions by taking turns operating in certain contested areas of the East China Sea and increasing the distance between boats.⁸⁸ Taiwan’s fisheries agreements with Japan provide an example for other claimants in the region of setting aside disputes and realizing mutual benefits through sharing resources.

Over the past two years as tensions in the South China Sea increased, Taiwan has made helpful contributions to encourage cooperation among claimants. As one of six claimants of islands and features in the South China Sea,* Taiwan administers and occupies Itu Aba Island (also known as Taiping)—the largest natural land feature in the Spratly Island archipelago and the wider South China Sea—and Pratas Island (also known as Dongsha).⁸⁹ In May 2015, President Ma announced the South China Sea Peace Initiative, a proposed framework similar to his 2012 initiative in the East China Sea.⁹⁰ This new framework calls for all claimants in the South China Sea to exercise restraint; respect the spirit of international law and seek peaceful settlement through dialogue; ensure all concerned parties are involved; shelve sovereignty disputes and establish a regional mechanism for joint resource development; and establish coordination and cooperation mechanisms.⁹¹ The South China Sea Peace Initiative demonstrates Taiwan’s goodwill and cooperative intentions with its maritime neighbors while making China’s position look increasingly recalcitrant. As the East China Sea Peace Initiative contributed to finalizing a Taiwan-Japan fisheries agreement, this new Initiative could help lead to a breakthrough in negotiations that have been ongoing since 2013 between Taiwan and the Philippines on a similar fisheries agreement.⁹²

Taiwan also has taken steps to clarify its claims in the East and South China seas in accordance with the UN Convention on the Law of the Sea and international law.† For example, Taiwan recently asserted its claims are derived from land features with the surrounding waters granted through the Law of the Sea, as opposed to China’s expansive sovereignty claims to nearly all of the land and sea within its nine-dash line‡ claim.§ Such statements

*Other claimants in the South China Sea are Brunei, China, Malaysia, the Philippines, and Vietnam.

†DPP Chairperson Tsai has not addressed all of Taiwan’s claims within its 11-dash line, but she has said that she would pursue dialogue with all claimants in the South China Sea and defend Taiwan’s claims of the Senkaku Islands and Itu Aba Island. Ralph Jennings, “Taiwan Candidate Proposes Dialogue on S. China Sea,” *Voice of America*, September 22, 2015; Lao Iok-sin, “Tsai Reiterates DPP Stance on Diaoyutai Islands,” *Taipei Times*, July 30, 2015; and Ko Shu-ling, “FOCUS: Taiwan Ponders Dash-line Claim Over South China Sea,” *Kyodo News* (Japan), June 29, 2015.

‡Although China’s claim in the South China Sea is often depicted by a “nine-dash line,” Beijing in recent years has issued new maps with ten dashes. Ishaan Tharoor, “Could this Map of China Start a War?” *Washington Post*, June 27, 2014; Euan Graham, “China’s New Map: Just another Dash?” *Australian Strategic Policy Institute* (Strategist blog), September 17, 2013.

§In a September 2014 speech, President Ma said, “[T]he principle that sovereignty over land determines ownership of the surrounding waters, which is set out in [UNCLOS], applies to disputes concerning sovereignty over both land and sea.” Other official statements reflect Taiwan’s increasing clarity on its own claims within its 11-dash line—serving as the basis for Taiwan’s claims in the South China Sea since 1947. Lynn Kuok, “Times of Change: Taiwan’s Evolving Position in the South China Sea and Why Other Actors Should Take Notice,” *Brookings Institution*

can help encourage other claimants to follow international law and define their own claims, thereby clarifying intentions and avoiding misunderstanding. Some observers have noted that Taiwan could contribute more to managing territorial disputes in the South China Sea by clarifying its 11-dash line in a way that puts political pressure on China to clarify its own claims, benefiting other claimants and the United States.⁹³ Bonnie Glaser, senior advisor for Asia at CSIS, argued in her testimony to the Commission, "... [If] Taiwan were to say, 'We claim the following land features,' which would probably be all of them within the dashed line, ... it would not include all of the waters. It would not provide jurisdiction over all of the energy exploitation or all of the fishing, for example." According to Ms. Glaser, taking such a position would make China's expansive claim appear all the more extreme by comparison.⁹⁴

Taiwan Military and Security Issues

Cross-Strait Military Balance

Although relations between Taipei and Beijing have improved since 2008, China's military modernization continues to focus on improving its ability to conduct military operations against Taiwan and deter the United States from assisting with Taiwan's defense.⁹⁵ Over the past decade, the balance of power across the Taiwan Strait has shifted significantly in China's favor; China now enjoys both a quantitative and a qualitative advantage over Taiwan and is capable of conducting a range of military campaigns against Taiwan.*

- China's offensive missile forces, known as the Second Artillery, have a large and sophisticated arsenal of ballistic and cruise missiles, including more than 1,200 short-range ballistic missiles (SRBM) and 200–500 ground-launched land-attack cruise missiles (LACM)† that are designed primarily to strike Taiwan.⁹⁶ Although China's inventory of SRBMs has only increased slightly since the late 2000s after a rapid expansion earlier in the decade, the force has become more lethal as China has gradually replaced older missiles lacking a true precision-strike capability with new SRBMs and more recent generations of existing SRBMs that feature longer ranges and improved accuracies and payloads. In a potential military conflict,

tion, May 2015, 6–8; Office of the President, Republic of China (Taiwan), "Spotlight Issues: Safeguarding Sovereignty, Shelving Disputes, Pursuing Peace and Reciprocity, and Promoting Joint Exploration and Development," September 9, 2014.

*Some analysts argue, however, that the Taiwan military is superior to the PLA in certain areas. Ian Easton, research fellow at the Project 2049 Institute, asserts that the Taiwan military has a qualitative advantage over the PLA due to the Taiwan military's training alongside the United States, the PLA's lack of professionalism, and widespread corruption in the PLA. Ian Easton (Research Fellow, Project 2049 Institute), August 11, 2015, interview with Commission staff.

†Official U.S. and Taiwan estimates of China's number of SRBMs and LACMs vary. For example, Defense Intelligence Agency Director Lieutenant General Vincent R. Stewart in his February 2015 testimony to Congress said, "[China has] more than 1,200 conventional short-range ballistic missiles deployed opposite Taiwan . . ." According to the Taiwan Ministry of National Defense's (MND) August 2015 report on China's military power for the Legislative Yuan, China increased its ballistic and cruise missile force from 1,600 to 1,700 over the past year and increased the number of missiles deployed against Taiwan from 1,400 to 1,500. H.H. Lu and Lillian Lin, "MND Reports China Deploying More Missiles Against Taiwan," Focus Taiwan, August 31, 2015; Senate Armed Services Committee, *Hearing on Worldwide Threats*, oral testimony of Vincent R. Stewart, February 26, 2015.

China could quickly conduct SRBM and LACM attacks against Taiwan's key defense nodes, including its air defense systems, air bases, naval ports, and command and control infrastructure.⁹⁷ (For more information on China's missile forces, see Chapter 2, Section 3, "China's Offensive Missile Forces.")

- The People's Liberation Army (PLA) Air Force and Navy have about 2,100 combat aircraft, 330 of which operate from permanent bases in the eastern half of China, allowing them to conduct operations around Taiwan without aerial refueling.* About 600 of China's combat aircraft are modern,† while fewer than 330 of Taiwan's combat aircraft are modern.⁹⁸ In addition, Russia in April 2015 confirmed the sale of four to six Russian S-400 surface-to-air missile systems to China and plans to deliver them in 2017.⁹⁹ The S-400 will increase the range of China's surface-to-air missile force from 300 km (approximately 186 mi) to 400 km (approximately 249 mi)—enough to cover all of Taiwan ‡—and likely will feature an improved ballistic missile defense capability over China's existing surface-to-air missile systems, though the platform has yet to demonstrate such a capability.¹⁰⁰ As China pursues the S-400, it also is developing its next-generation indigenous surface-to-air missile, the HQ-19, which likely will have features and range similar to the S-400.¹⁰¹
- The PLA Navy has more than 300 surface combatants, submarines, and missile-armed patrol craft.¹⁰² As China's naval modernization continues, an increasing percentage of these ships will be modern § and feature advanced weaponry. Taiwan, on the other hand, has 92 naval combatants, comprised of 4 submarines and 88 surface ships.¹⁰³ Taiwan's submarine

*Moreover, China—using its robust military, civilian, and reserve airfield network—could forward deploy hundreds of additional combat aircraft on short notice in a conflict scenario. U.S. Department of Defense, *Annual Report to Congress: Military and Security Developments Involving the People's Republic of China 2015*, May 2015, 80; U.S. Department of Defense, *Annual Report to Congress: Military and Security Developments Involving the People's Republic of China 2014*, June 2014, 78; and U.S.-China Economic and Security Review Commission, *Hearing on China's Military Modernization and Its Implications for the United States*, written testimony of Lee Fuell, January 30, 2014.

†“Modern” combat aircraft are defined as possessing advanced avionics and weapons systems. These aircraft include the J-10, J-11, JH-7, Su-27, and Su-30. For more information on the Commission's definition of “modern” combat aircraft, see U.S.-China Economic and Security Review Commission, *2014 Annual Report to Congress*, November 2014, 309.

‡China would have to deploy the battalions opposite Taiwan to have the range necessary to cover Taiwan. It is unclear whether the sale included the missiles themselves, and if so, what their capabilities are. J. Michael Cole, “Alarm over China's S-400 Acquisition is Premature,” *Diplomat*, April 22, 2015; Zackary Keck, “Putin Approves Sale of S-400 to China,” *Diplomat*, April 11, 2014; Wendell Minnick, “China's New Jet, Radar Complicate U.S. Posture,” *Defense News*, July 6, 2013; and Wendell Minnick, “Time Running Out for Taiwan if Russia Releases S-400 SAM,” *Defense News*, May 25, 2013.

§ In reference to China's submarine force, the term “modern” is used in this Report to describe a second-generation submarine that is capable of employing antiship cruise missiles or submarine-launched intercontinental ballistic missiles. These include the SHANG nuclear attack submarine (SSN), YUAN SSN, SONG diesel attack submarine (SS), KILO 636 SS, and JIN nuclear ballistic missile submarine (SSBN). In reference to China's surface force, the term “modern” is used to describe a surface ship that possesses a multi-mission capability, is armed with more than a short-range air defense capability, and has the ability to embark a helicopter. These include the following: LUHU destroyer (DD), LUHAI DD, LUZHOU guided missile destroyer (DDG), LUYANG I/II/III DDG, Sovremenny I/II DDG, JIANGWEI I/II frigate (FF), JIANGKAI I FF, and JIANGKAI II guided missile frigate. For more information on the Commission's definition of “modern” submarines and surface ships, see U.S.-China Economic and Security Review Commission, *2014 Annual Report to Congress*, November 2014, 300.

fleet is particularly weak compared to that of China;* it includes two former U.S. boats that were built in the 1940s and transferred to Taiwan in the 1970s. In a military contingency with Taiwan, China could use its more numerous and advanced platforms to conduct a range of military courses of action, including a maritime blockade or quarantine, air and missile attacks, and amphibious invasions of Taiwan-held islands in the Taiwan Strait and South China Sea. China is actively pursuing amphibious capabilities, but does not have the necessary platforms needed to conduct a large-scale amphibious invasion of Taiwan.¹⁰⁴

China continues to prepare for a Taiwan contingency through a variety of exercises involving amphibious platforms, missiles fired into Taiwan's nearby waters, and combat aircraft flying close to Taiwan's airspace.¹⁰⁵ In July 2015, one exercise involved PLA soldiers raiding a building similar in appearance to Taiwan's presidential palace.¹⁰⁶ In addition to a formal protest by the Taiwan government, a Taiwan Ministry of National Defense (MND) spokesperson said, "[The exercise was] unacceptable for the Taiwanese public and the international community."¹⁰⁷ J. Michael Cole, editor-in-chief of *Thinking Taiwan*, said that the exercise

*strikes at the heart of what is recognizable to ordinary Taiwanese—downtown Taipei. . . . By making the threat more recognizable and immediate than missiles fired off Taiwan's northern and southern tips, or drills simulating an amphibious assault, Beijing may hope to engage ordinary Taiwanese not at the intellectual and abstract level, but on an emotional one.*¹⁰⁸

Despite its growing military disadvantage relative to China, Taiwan's defense budget has stagnated. Over the last decade, China has boosted its defense budget in nominal terms by double digits almost every year,[†] increasing the official defense spending gap between Taiwan and China in 2015 to more than \$132 billion (see Figure 2).[‡] Taiwan's announced 2015 defense budget increased, albeit slightly, for the first time since 2012. From 2009 to 2014, Taiwan's defense budget declined by an average of 1.6 percent annually.[§]¹⁰⁹ Despite a further increase in Taiwan's announced 2016 defense budget, spending on the military is projected to fall to 1.8 percent of GDP, the lowest such level in over a decade.¹¹⁰ This stagnation is due to a number of factors, including warming cross-

*For more information on Taiwan's submarine fleet and indigenous production plans, see additional discussion later in this section.

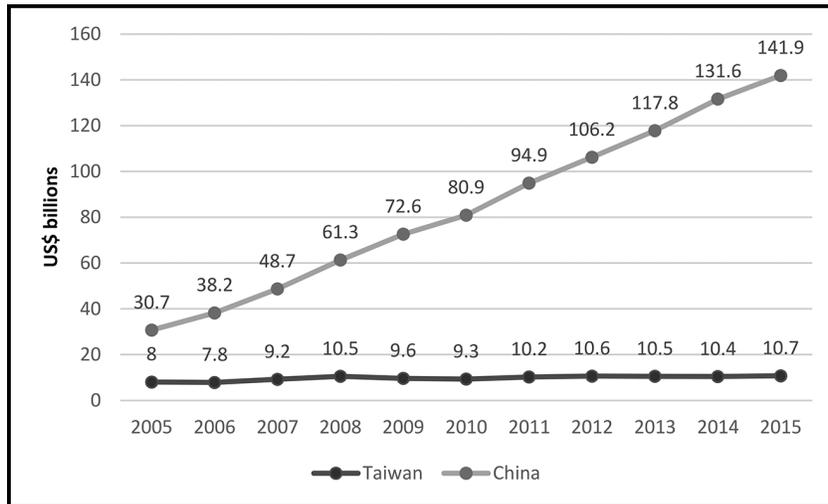
†This measurement is according to China's announced defense budgets, not actual aggregate spending. China's announced budget omits major defense-related expenditures such as purchases of advanced weapons, research and development programs, and local government support to the PLA. For more information, see Chapter 2, Section 1, "Year in Review: Security and Foreign Affairs."

‡China's announced defense budget in 2015 was RMB 886.9 billion (\$141.9 billion) compared to Taiwan's budget of NTD (New Taiwan dollars) 319.3 billion (\$10.7 billion). Xinhua (English edition), "China 2015 Defense Budget to Grow 10.1 Pct., Lowest in 5 Years," March 5, 2015; *China Post* (Taiwan), "Taiwan's Proposed Defense Budget for 2015 Sees \$330 Million Increase," August 30, 2014.

§According to Mr. Easton, Taiwan's defense budget, like China's, is significantly underreported. However, unlike China's defense budget, there are no outside estimates of Taiwan's real defense budget. Ian Easton (Research Fellow, Project 2049 Institute), interview with Commission staff, August 11, 2015.

Strait ties that have reduced public perceptions of China's military threat to Taiwan; growing competition for government resources, particularly from social welfare programs; increasing government debt; partisan political wrangling; and uncertainty about the future of U.S. arms sales to Taiwan, particularly requested sales that Taiwan factors into its budgets but are not completed due to delays resulting from unresolved issues on both sides.¹¹¹

Figure 2: Gap between Announced Defense Budgets of China and Taiwan (2005–2015)



Note: These numbers represent both China's and Taiwan's announced official defense budgets, not actual aggregate defense spending. China's figures are converted from RMB into U.S. dollars based on China's year-end nominal exchange rate.

Source: The following sources were used to calculate China's defense budget: China's Ministry of Finance; Xinhua (English edition), "China 2015 Defense Budget to Grow 10.1 Pct, Lowest in 5 Years," March 5, 2015; Xinhua (English edition), "China Defense Budget to Increase 12.2 Pct in 2014," March 5, 2014; Xinhua (English edition), "China Defense Budget to Increase 10.7 Pct in 2013: Report," March 5, 2013; and Dennis J. Blasko, et al., "Defense-Related Spending in China: A Preliminary Analysis and Comparison with American Equivalents," *United States-China Policy Foundation*, November 2006, 19. The following sources were used to calculate Taiwan's defense budget: *China Post* (Taiwan), "Taiwan's Proposed Defense Budget for 2015 Sees \$330 Million Increase," August 30, 2014; Shirley Kan, "Taiwan: Major U.S. Arms Sales since 1990," *Congressional Research Service*, August 29, 2014, 34.

Furthermore, Taiwan's unique status and China's insistence on the "one China" principle make it difficult for Taiwan to procure arms from most producers. Taiwan also lacks the ability to indigenously design and produce certain weapons systems.¹¹² Under such constraints, Taiwan has mainly relied on the United States for arms and military equipment.

Nevertheless, Taiwan has sought to improve its position vis-à-vis China in recent years by producing or acquiring military platforms and weapon systems. Major indigenous programs under development or recently completed include the following:

- *Surface-to-Air Missiles:* In December 2014, Taiwan's Chung-Shan Institute of Science and Technology confirmed it will upgrade the Tien Kung III, the third-generation of its family of

indigenous surface-to-air missiles, to extend the missile's range from 150 km (approximately 93 mi) to over 200 km (approximately 124 mi), potentially reaching mainland China.¹¹³ Production of the missile, which is capable of defending against short- and medium-range ballistic missiles, is scheduled to occur from 2015 through 2024.¹¹⁴ The Tien Kung III will complement Patriot missile systems, which Taiwan acquired from the United States to defend Taiwan's air space, providing Taiwan greater air coverage in a potential cross-Strait conflict.¹¹⁵

- *Combat Support Ships*: In January 2015, the Taiwan Navy commissioned its second supply vessel, the Panshih. The ship has improved functionality and versatility over Taiwan's other supply ship, including its advanced medical equipment that could be used for humanitarian assistance and disaster relief missions. In a cross-Strait military conflict, this ship would enable Taiwan to better replenish its frigates and destroyers with ammunition, fuel, and other supplies.¹¹⁶
- *Missile Corvette*: In March 2015, the Taiwan Navy commissioned the TUO JIANG, its first ship in a new class of catamaran-style missile corvettes. Taiwan may build up to 11 more of these ships. The new corvette has better range, endurance, and sea-keeping ability than Taiwan's other patrol ships, and is equipped with 16 antiship cruise missiles. The ship enhances the survivability and lethality of Taiwan's antisurface force in a potential cross-Strait conflict and increases the Taiwan Navy's ability to patrol the East and South China seas.¹¹⁷
- *Coast Guard Cutters*: In June 2015, the Taiwan Coast Guard Administration commissioned two helicopter-capable cutters. These ships are the largest of Taiwan's eight-ship Coast Guard fleet, and each is armed with one 40 millimeter gun, two 20 millimeter guns, and a water cannon.¹¹⁸ The cutters will enhance the Coast Guard's maritime patrol capabilities with the range necessary to conduct missions in the East and South China seas.¹¹⁹
- *Unmanned Aerial Vehicles (UAVs)*: In August 2015 at the biennial Taipei Aerospace and Defense Technology Exhibition, Taiwan's Chung-Shan Institute of Science and Technology unveiled a prototype of its largest UAV to date—more than double the size of any model in service.¹²⁰ Although its specific technical details were not disclosed, the UAV has a medium range and long endurance; can carry multiple payloads; and is designed for intelligence, surveillance, and reconnaissance (ISR) missions. When it enters service, the UAV will complement Taiwan's operational fleet of 32 UAVs and will enhance Taiwan's ISR capabilities.¹²¹

Select military equipment Taiwan is acquiring or seeking to acquire from the United States includes the following (see also the discussion on arms sales, military-to-military contact, and U.S.-Taiwan defense relations in "U.S.-Taiwan Relations," later in this section):

- *Black Hawk Helicopters*: Between December 2014 and May 2015, Taiwan received eight UH-60 Black Hawk helicopters, the first shipments of a U.S. arms package worth \$3.1 billion announced in 2010. A total of 60 helicopters are set to be transferred in eight subsequent batches with the final delivery set for 2019.¹²² The helicopters reportedly will be equipped with radar warning receivers, infrared countermeasure sets, missile warning systems, Gatling-type guns, and data link systems.¹²³ According to a Taiwan Army official, the UH-60s will replace the aging UH-1H helicopter fleet and will be used primarily to transport supplies and personnel. Taiwan's National Airborne Service Corps reportedly will use 15 of the Black Hawks for humanitarian assistance and disaster relief missions.¹²⁴ In a potential PLA invasion of Taiwan territory, the helicopters could be used to counter a PLA landing force and coordinate command and control and special operations missions.¹²⁵
- *OLIVER HAZARD PERRY-Class Guided-Missile Frigates*: In December 2014, U.S. President Barack Obama signed legislation authorizing the sale of four decommissioned and unarmed PERRY-class frigates to Taiwan, but the Administration has not formally notified Congress of the sale as of the writing of this Report.¹²⁶ Taiwan in April 2014 announced that it would only buy two ships due to budget constraints.¹²⁷ The ships, scheduled to arrive in Taiwan starting in 2016, will modernize and supplement Taiwan's fleet of six KNOX-class frigates. They will also help offset the retirement of two KNOX-class frigates and the eventual decommissioning of all KNOX-class frigates.¹²⁸ The PERRY-class frigates, depending on the equipment and arms with which they are outfitted,* could be used for antisubmarine, antisurface, and limited antiaircraft warfare in a conflict.¹²⁹
- *F-16 Fighter Upgrade*: Over the past year, the United States and Taiwan have moved forward with the planned mid-life upgrade of Taiwan's existing fleet of 145 F-16 A/B fighter aircraft. In December 2014, the United States awarded Lockheed Martin a \$308 million contract to supply active electronically scanned array radars for Taiwan's F-16s.¹³⁰ According to the development plan, the Taiwan Air Force will send two F-16s to Lockheed Martin to install and test the radar before upgrading the rest of Taiwan's fleet in Taiwan over the second half of 2016.¹³¹ With these upgrades, Taiwan's F-16 fleet will be better able to track China's advanced combat aircraft and ground-based targets.¹³²
- *Submarines*: In March 2015, President Ma reiterated his support for Taiwan to pursue an indigenous submarine program, following more than a decade of attempts to acquire diesel-elec-

*The Taiwan Navy will probably outfit the ships with a combination of indigenous and foreign weapons systems, including surface to air missile systems, antiship missiles, and artillery. Notably, five of Taiwan's eight domestically built CHENG KUNG-class frigates, based on PERRY-class frigates, already carry advanced Hsiung Feng III antiship cruise missiles that reportedly have a range of 81 nm. *IHS Jane's*, "Jane's World Navies—Taiwan," June 18, 2015, 20; Charles Au, "Taiwan Releases First Firing Footage of HF-3 'Carrier Killer,'" *IHS Jane's*, December 8, 2014.

tric submarines from abroad.* The indigenous submarine program enters its three-year project design phase in 2016, but Taiwan has already identified over 20 U.S. and European companies interested in assisting Taiwan shipbuilding companies.¹³³ As mentioned previously, Taiwan has four submarines; two are decommissioned U.S. Navy GUPPY-class submarines (they have undergone upgrades since the 1940s) used only for training.¹³⁴ The Taiwan Navy's already limited ability to conduct undersea warfare against China's expanding fleet of modern surface ships and submarines will continue to erode as Taiwan's submarine force ages.

- *P-3C Orion Maritime Patrol Aircraft*: Taiwan is scheduled to accept its final delivery of four P-3C antisubmarine aircraft by the end of 2015, which follows its first shipment of eight that arrived in 2013. Originally purchased from the United States in 2007, the P-3Cs will replace the Taiwan Air Force's fleet of 11 S-2T antisubmarine aircraft that have been in service for over 40 years.¹³⁵ The P-3C will increase the capabilities and endurance of the military's fixed-wing maritime patrol aircraft force, improving Taiwan's ability to perform antisubmarine warfare and ISR missions.¹³⁶

Status of Taiwan's Defense Reforms

As part of its military modernization effort, Taiwan is transitioning its conscripted military force to an all-volunteer army by 2017.† The goal of this effort is to create a "small but smart and strong force" in response to "the requirement for high quality manpower under advanced technological conditions and economic and social changes."¹³⁷ Taiwan's transition has been far more costly than expected, increasing budgetary pressure on research and development (R&D) as well as operations and maintenance.¹³⁸ To find additional savings, Taiwan in 2013 decided to reduce its active duty force from 275,000 to 215,000 by 2015,¹³⁹ and now plans to reduce the force to 170,000 by the end of 2019.¹⁴⁰

Reversing the trend of missing recruitment goals for its active duty force by wide margins from 2011 to 2013,¹⁴¹ Taiwan in 2014 recruited over 15,000 men and women, exceeding its target of about 10,500. Yet, Taiwan will still need to exceed goals through 2017 to meet the already reduced active duty target of 170,000.¹⁴² To encourage enrollment and retention, Taiwan has announced a variety of new incentives, such as increased wages, service-extending stipends, and expanded base privileges.¹⁴³ Although these new benefits show promise in reaching recruitment goals, they could also further increase the financial burden of the all-volunteer force by

* In 2001, then U.S. President George W. Bush proposed to help Taiwan acquire eight diesel-electric submarines, but the proposal has been delayed due to political and cost disagreements on both sides. The United States also has not built a conventional submarine in over 40 years. *Taiwan Today*, "Ma Pledges Support for Homegrown Naval Vessels," April 1, 2015; Agence France-Presse, "Taiwan Kicks Off Plan to Build Its Own Submarines," December 29, 2014.

† Taiwan had originally planned to complete the transition at the end of 2014, but shifted the timeline to 2017 due to lower than anticipated recruitment numbers. As part of the transition, men born after 1994 are now required to undergo four months of active duty military service and then enter Taiwan's reserve system. Previously, Taiwan conscripts served one year as active duty. Ministry of National Defense (Taiwan), *National Defense Report 2013*, October 2013, 95–96; Chris Wang, "Date for All Volunteer Military Delayed," *Taipei Times*, September 13, 2013.

comprising a larger percentage of the overall defense budget. In a setback to Taiwan's planned transition, the MND in August 2015 announced it would be unable to end conscription in 2016 for men born before 1994, as previously announced. The ministry said that recruitment goals fell short for voluntary enlistees in 2015 and therefore decided to conscript in 2016 approximately 23,100 men for one year of compulsory active duty service to meet defense needs.¹⁴⁴

The DPP Unveils Its Defense Reform Strategy in Defense Policy Blue Papers

In May 2015, the New Frontier Foundation, a think tank established by the DPP, released four new defense policy blue papers* articulating the DPP's views on Taiwan defense reform. The blue papers, along with eight others released since June 2013, outline a defense strategy that focuses on revitalizing Taiwan's indigenous defense industry, supporting the all-volunteer force transition with increased funding, and building and acquiring asymmetric platforms.¹⁴⁵ The DPP particularly emphasizes the need to invest in R&D to upgrade Taiwan's military equipment. Complementing its pledge of restoring defense spending to 3 percent of GDP annually,[†] the DPP advocates for 70 percent of all new defense spending to go toward "military investments," including procurement of weapons and equipment, defense construction, and R&D.¹⁴⁶

The DPP by 2020 aims to have no less than 60 percent of these "military investments" spent on indigenous R&D.¹⁴⁷ Like the KMT, development of the indigenous submarine program is the DPP's top priority for the defense industry; the DPP has outlined a 23-year development plan.¹⁴⁸ In addition, the DPP prioritizes other indigenous solutions, such as unmanned aerial vehicles, unmanned underwater vehicles, and short take-off and vertical landing fighter aircraft.¹⁴⁹

To strengthen Taiwan's asymmetric capabilities, the DPP supports creating a new cybersecurity service for the military; bolstering missile defense capacity; building improved combat survivability against missile strikes; restructuring the ground force into specialized rapid response units; and maintaining capabilities in air and sea control.¹⁵⁰ Should the DPP win the January 2016 presidential election, it plans to initiate an open defense policy discussion and issue its own quadrennial defense review within a year.¹⁵¹

*The four defense blue papers cover Taiwan's military capabilities, defense information security, veteran's affairs, and the indigenous defense industry. New Frontier Foundation, "Press Conference Announcing the Publication of Defense Policy Blue Papers No. 9-12," May 25, 2015. Staff translation.

†This pledge restates the DPP's commitment outlined in its first blue paper in June 2013. The KMT similarly pledged to raise defense spending to three percent of GDP prior to the 2008 election, but did not fulfill its promise. New Frontier Foundation, *Defense Blue Paper #1: DPP's Defense Agenda*, June 2013, 19; Ralph Jennings, "Taiwan's Ma Wins Election," Reuters, March 22, 2008.

Taiwan Military Training and Activities

The Taiwan military routinely conducts a range of exercises to maintain combat readiness; integrate new weapons systems and tactics; test and improve its capabilities; and demonstrate to the Taiwan people, China, and others that it has a credible deterrence capability. In 2015, select major exercises and activities included the following:

- *Naval Combat Readiness Exercise*: On January 1–2, Taiwan conducted an exercise with 13 vessels and 2 attack helicopters off its southwest coast primarily to test its new TUO JIANG-class stealth missile corvette that had been commissioned into service just one week before the exercise.¹⁵² The exercise simulated countering invading enemy naval forces, such as submarines and attack boats.¹⁵³
- *Planned Air Surveillance Patrols*: According to Taiwan’s MND, P–3C antisubmarine aircraft currently conduct ISR missions close to Taiwan’s coast and in airspace within its air defense identification zone.* In April, the MND for the first time confirmed P–3C antisubmarine aircraft patrols would eventually extend to areas in the South China Sea without providing a specific timeline. The expanded mission would enhance Taiwan’s ability to monitor Chinese naval activity in the South China Sea.¹⁵⁴
- *Han Kuang Exercises*: Han Kuang is Taiwan’s most important set of joint exercises; they have been held annually at the national level since 1984.¹⁵⁵ For the first phase of the exercise in May, the Taiwan military simulated rapid battle preparation, electronic warfare, and cyber attacks.¹⁵⁶ In the second phase of the exercise in September, Taiwan conducted live-fire drills simulating countering a Chinese invasion. The drills included an anti-amphibious landing exercise and tested Taiwan’s most advanced platforms.¹⁵⁷ According to a senior MND official, the ministry signed a five-year contract with the United States worth \$3.1 million, paying for the services of the U.S. military to advise the Han Kuang exercises from 2015 through 2019.¹⁵⁸ Previously, U.S. military representatives only observed the exercises. The senior MND official said, “The U.S. will advise in strategic planning and operational development of combat units for Taiwan’s defense against hostile actions in the Taiwan Strait.”¹⁵⁹

Cross-Strait Espionage

Expanding cross-Strait ties promote not only increasing economic cooperation with China but also increase Taiwan’s vulnerability to Chinese espionage. Increased travel between Taiwan and China

*An air defense identification zone is a publicly-declared area established in international airspace adjacent to a state’s national airspace, in which civil aircraft must be prepared to submit to local air traffic control and provide aircraft identifiers and location. Its purpose is to allow a state the time and space to identify the nature of approaching aircraft prior to entering national airspace in order to prepare for defensive measures if necessary. U.S. Code of Federal Regulations, 14 C.F.R. §99.3 (2013); U.S. Department of Defense, “2.7.2.3 Air Defense Identification Zones in International Airspace,” in *The Commander’s Handbook on the Law of Naval Operations* (July 2007), p. 2-13; and Ruwantissa Abeyratne, “In Search of Theoretical Justification for Air Defence Identification Zones,” *Journal of Transportation Security* (September 2011).

heightens the risk of Taiwan defense secrets being compromised, as China has improved access to Taiwan with better opportunities to conduct intelligence operations against Taiwan citizens both in Taiwan and China.*

After 15 cases of alleged spying in 2014, nearly all involving active or retired Taiwan military officers, espionage continues to proliferate.¹⁶⁰ The September 2014 arrest of retired PLA captain and intelligence officer Zhen Xiaojiang—the first mainland Chinese spy to be apprehended in Taiwan in decades—uncovered the largest cross-Strait spy ring in years.¹⁶¹ In September 2015, Mr. Zhen received a four-year prison sentence, while five retired Taiwan military officers recruited by Mr. Zhen to spy for the Mainland were handed more lenient sentences.¹⁶² Since 2005, Mr. Zhen allegedly acquired classified information on Taiwan's Mirage 2000 aircraft, ultra-high frequency radar systems, and other weapons platforms.¹⁶³ In another case, a retired vice admiral and deputy commander of the Taiwan Navy Ko Cheng-sheng was found guilty of espionage and sentenced in October 2014 to 14 months in prison. Vice Admiral Ko was one of the highest-ranking retired Taiwan military officers to be caught spying for China.¹⁶⁴

China's increased efforts to acquire Taiwan defense secrets have significant implications for Taiwan's security. In January 2015, Taiwan Defense Minister Kao Kuang-chi said, "[T]he military [should] heighten its guard against spies, as China has not relented in its efforts to infiltrate Taiwan's military as exchanges across the Taiwan Strait increase."¹⁶⁵ As noted by retired Vice Minister of National Defense Lin Chong-pin, exposure of Beijing's successful infiltration of Taiwan defense systems supplied or marketed by the United States could give pause to U.S. defense officials regarding future arms sales to the island.¹⁶⁶ Aside from traditional reasons for espionage, China also seeks to weaken the morale of the Taiwan military. Each spy case revealed by Taiwan has the potential to achieve psychological benefits for Beijing, creating an environment where China's capture of Taiwan's defense secrets could be perceived as an inevitability.¹⁶⁷

Computer Network Security

Taiwan faces a growing problem of cyber attacks—increasingly from China—that threaten the security of sensitive information. According to U.S. cybersecurity firm FireEye, Taiwan in 2014 was the third most targeted country in the Asia Pacific region in terms of hacking attempts to steal data.† In March 2015, senior Taiwan intelligence officials publicly identified what appears to be a PLA cyberespionage unit based at China's Wuhan University responsible for cyber activities against Taiwan. The unit is reportedly part of the Sixth Bureau of the PLA General Staff Department's Third Department, one of the 12 bureaus under the Third Depart-

* In 2014, nearly four million people from mainland China traveled to Taiwan, up from approximately three million visitors in 2013. Tourism Bureau (Taiwan), "Visitors by Residence, 2014." August 17, 2015; Wendell Minnick, "Chinese Spies Expand Operations in Taiwan," *Defense News*, January 24, 2015; and J. Michael Cole, "Why Spy on Taiwan when Taiwan Gives Information Away for Free?" *Diplomat*, March 12, 2014.

† Only South Korea and Hong Kong faced a higher volume of attempted cyber intrusions in 2014. *Want China Times* (Taiwan), "Taiwan Third Most Targeted Country by Cyber Attacks in Asia," April 3, 2015.

ment whose mission is technical reconnaissance and digital information warfare.¹⁶⁸ According to the National Security Bureau, one of Taiwan's major intelligence agencies, cyber attacks linked to China in 2013 alone targeted the agency over seven million times and the MND over one million times. This marked a significant increase in volume from previous years.¹⁶⁹

In response, Taiwan is working to improve its defenses by creating a new cybersecurity department responsible for securing the government's information security and key network infrastructure that would also have authority over military cyber defense.¹⁷⁰ Moreover, Taiwan has asked to join U.S.-led Cyber Storm, a multilateral cybersecurity exercise held every two years. Taiwan Vice Premier Simon Chang in a March 2015 interview noted that Taiwan's participation could help improve its ability to protect against Chinese cyber intrusions.¹⁷¹ The first Cyber Storm exercise in 2006 involved only U.S. government and private sector participants, but it has since expanded in size and scope to become the most extensive government-sponsored cybersecurity exercise of its kind. In Cyber Storm IV, the most recent exercise held in several stages between 2011 and 2014, participants aimed to "assess and strengthen cyber preparedness, examine incident response processes in response to ever-evolving threats, and enhance information sharing among federal, state, international, and private sector partners."¹⁷² The exercise involved 11 countries that are all members of the International Watch and Warning Network (a framework for cooperation on cyber situational awareness and incident response), of which Taiwan is not a member.*

U.S.-Taiwan Relations

Diplomatic Affairs

The U.S. and Taiwan governments continue to make progress on bilateral initiatives and areas of mutual interest. In February 2015, the United States issued new license plates to Taiwan's representatives in the United States similar to those granted to foreign diplomats, as a follow-on to an agreement reached in 2013. The license plates provide previously unavailable immunity privileges to Taiwan representatives.¹⁷³ U.S. and Taiwan officials in June 2015 signed a memorandum of understanding to increase cooperation in international public health, humanitarian assistance, and other global issues.¹⁷⁴ The United States also hosted DPP Chairperson Tsai on her June 2015 U.S. visit, and the U.S. government has said it would welcome other candidates if they visit the United States.¹⁷⁵ In addition to meeting with senior members of Congress, Chairperson Tsai visited the White House and U.S. Department of State for a series of "very successful, very positive" closed-door meetings.[†]¹⁷⁶ In response to the visit, a spokesperson

*Participants included Australia, Canada, France, Germany, Hungary, Japan, the Netherlands, Norway, Sweden, Switzerland, and the United States. U.S. Department of Homeland Security, "Cyber Storm: Securing Cyber Space," June 17, 2015; UN Terminology Database, "International Watch and Warning Network."

†Due to the unofficial nature of the U.S.-Taiwan relationship, the U.S. government limits contacts between U.S. and Taiwan officials at certain levels (for example, the United States rarely sends cabinet-level officials to Taiwan, and the Commission has been told that some senior level U.S. government officials are unable to visit Twin Oaks, Taiwan's de facto embassy in Washington, DC).

for China's Taiwan Affairs Office said, "The [meetings] went against the peace and stability of the Taiwan Strait and harmed peaceful development of cross-Strait ties. [They] sent a wrong signal to the island's separatist forces."¹⁷⁷ Beijing's response demonstrated its uneasiness regarding the DPP.

Economic and Trade Relations

In 2014, U.S.-Taiwan trade reached a record high, increasing by 6 percent to \$67.4 billion.¹⁷⁸ Also in 2014, Taiwan became the tenth largest trading partner of the United States, passing both India and Saudi Arabia. In addition, the United States moved ahead of Japan to become Taiwan's second largest trading partner.¹⁷⁹ Taiwan exports to the United States mostly consist of manufactured parts and accessories, including cell phones, motor vehicle parts and accessories, and office machine parts and accessories. By contrast, U.S. exports to Taiwan are diversified across a number of sectors; they mainly include machinery to manufacture semiconductors and liquid crystal display (LCD) panels; agriculture; and arms sales.¹⁸⁰ (For more information on arms sales, see "Military and Security Relations" below.)

Although U.S.-Taiwan economic ties remain strong, substantive progress on ongoing trade and investment negotiations has slowed.¹⁸¹ In the absence of official relations, both sides discuss bilateral economic issues through the Trade and Investment Framework Agreement (TIFA), a framework established in 1994. Taiwan Economic Affairs Minister John Deng said the U.S. focus on completing TPP and trade promotion authority negotiations postponed the TIFA meeting scheduled for April 2015.¹⁸² Nevertheless, Assistant Secretary of State for Economic and Business Affairs Charles Rivkin, the most senior State Department official to visit Taiwan since his predecessor visited in 2012, said in a June 2015 visit to Taipei that unofficial talks about how to enhance bilateral economic cooperation occur daily.¹⁸³ TIFA talks had been on hold from 2007 to 2012 due to Taiwan's refusal to import U.S. beef containing ractopamine, a common feed additive, but resumed in 2013 when the Taiwan legislature partially lifted restrictions.¹⁸⁴

In October 2015, U.S. and Taiwan officials held a TIFA meeting in Taipei, which included discussions on a range of bilateral economic issues, including agriculture, pharmaceuticals and medical devices, intellectual property rights, trade barriers, and investment.¹⁸⁵ In addition to these issues, the talks also covered a potential bilateral investment agreement and Taiwan's aspirations to join TPP. The meeting reportedly did not include a discussion about Taiwan's restrictions on U.S. pork imports, which remains a contentious area in ongoing negotiations.¹⁸⁶ Although Taiwan loosened some restrictions on residual levels of ractopamine in U.S. beef imports, it maintains these restrictions on pork imports. Since 2012, members of Congress have raised concerns about Taiwan restrictions on U.S. pork. Several key roadblocks to overturning restrictions include pressure from Taiwan's pork industry and Taiwan citizens' aversion to the use of ractopamine in pork production.¹⁸⁷ Progress on TIFA negotiations could be further constrained by Congressional demands for the removal of Taiwan's pork restrictions.

Military and Security Relations

Taiwan continues to be one of the world's largest buyers of U.S. defense exports. Over the last decade, Taiwan has agreed to buy U.S. arms worth approximately \$22.7 billion (see Table 1). However, the Obama Administration has not notified Congress of any arms sales to Taiwan since 2011. In December 2014, President Obama signed legislation authorizing the transfer of four PERRY-class frigates to Taiwan, but as of the writing of this Report, the Administration has yet to notify Congress and, per Taiwan's request, complete the sale of two of the frigates worth approximately \$179 million.¹⁸⁸

Table 1: U.S. Arms Sales to Taiwan (2005–2015)

Year of Notification to Congress	Weapon, Item, or Service*	Projected Value (US\$ millions)†	Status‡	Delivery
2005	10 AIM–9M Sidewinder and 5 AIM–7M Sparrow air-to-air missiles; continued pilot training and logistical support for F–16 fighters at Luke Air Force Base	280	Delivered	2006–2007
2007	218 AMRAAMs and 235 Maverick air-to-ground missiles for F–16 fighters	421	Delivered	2012
2007	60 AGM–84L Harpoon Block II antiship missiles	125	Delivered	2010–2012
2007	144 SM–2 Block IIIA Standard air-defense missiles for KIDD-class destroyers	272	Delivered	2010–2012
2007	12 P–3C maritime patrol/antisubmarine warfare aircraft	1,960	In progress	2012–2015 ¹⁸⁹
2007	Patriot configuration 2 ground systems upgrade	939	Unknown	Unknown
2008	330 PAC–3 missiles and firing units	3,100	In progress	Began in 2014 ¹⁹⁰
2008	32 UGM–84L sub-launched Harpoon Block II antiship missiles	200	Delivered	2013 ¹⁹¹
2008	Spare parts for F–5E/F C–130H, F–16A/B, and Indigenous Defense Fighter aircraft	334	In progress	N/A

*These are the weapons, items, and services as presented to Congress at the time of notification, which may differ from the actual weapons, items and services that the United States ultimately sells to Taiwan.

†These values represent amounts as presented to Congress at the time of notification, which may differ from the actual amount Taiwan pays for the weapon, item, or service.

‡This indicates the most current status as notified to Congress or indicated in media reports, which may differ from the actual status of the sale.

Table 1: U.S. Arms Sales to Taiwan (2005–2015)—Continued

Year of Notification to Congress	Weapon, Item, or Service*	Projected Value (US\$ millions)†	Status‡	Delivery
2008	182 Javelin missiles and command launch units	47	Delivered	2011
2008	Four E–2T aircraft refurbishment and upgrades	250	Delivered	2011–2013 ¹⁹²
2008	30 AH–64 Apache helicopters and related ordnance	2,532	Six delivered	2013
2010	114 PAC–3 missiles and firing units	2,810	In progress	Began in 2014 ¹⁹³
2010	60 UH–60M Black Hawk utility helicopters	3,100	In progress	2014–2019 ¹⁹⁴
2010	12 ATM–84L and RTM–84L Harpoon Block II antiship telemetry missiles	37	Unknown	Unknown
2010	60 MIDS/LVT–1 terminals to improve F–16A/B C4ISR § systems	340	Unknown	Unknown
2010	2 OSPREY-class mine hunting ships (refurbishment and upgrades)	105	Delivered	2012 ¹⁹⁵
2011	145 F–16AB aircraft refurbishment and upgrades	5,300	Not delivered	2016–2017
2011	F–16 pilot training	500	In progress	N/A
2011	Spare parts for F–16A/B, F–5E/F, C–130H, and IDF aircraft	52	In progress	N/A

*These are the weapons, items, and services as presented to Congress at the time of notification, which may differ from the actual weapons, items and services that the United States ultimately sells to Taiwan.

†These values represent amounts as presented to Congress at the time of notification, which may differ from the actual amount Taiwan pays for the weapon, item, or service.

‡This indicates the most current status as notified to Congress or indicated in media reports, which may differ from the actual status of the sale.

§C4ISR refers to command, control, communications, computers, intelligence, surveillance, and reconnaissance.

Source: Except where indicated, this information is compiled from the following sources: Shirley Kan, “Taiwan’s Major U.S. Arms Sales since 1990,” *Congressional Research Service*, August 29, 2014, 58–59; Piin-Fen Kok and David J. Firestein, “Threading the Needle: Proposals for U.S. And Chinese Actions on Arms Sales to Taiwan,” *East West Institute*, September 2013, 78–79; and U.S.-Taiwan Business Council and Project 2049 Institute, “Chinese Reactions to Taiwan Arms Sales,” March 2012, 26–28.

In 2014, military collaboration between the United States and Taiwan continued to increase. More than 3,000 U.S. Department of Defense personnel visited Taiwan in 2014,¹⁹⁶ a 50 percent increase over 2013. In 2012, only 1,500 officers conducted visits to Taiwan.¹⁹⁷ However, as Russell Hsiao, former non-resident senior fellow at the Project 2049 Institute, points out,

*Unfortunately, few U.S. military officers conduct in-country training in Taiwan, and there are no known [U.S. military officers] attending Taiwan's National Defense University or other intermediate and senior service schools. More educational exchanges between the two defense establishments are warranted, particularly for junior and noncommissioned officers.*¹⁹⁸

Nevertheless, momentum on increased military cooperation continued over the past year. As of September 2015, nearly 2,000 U.S. defense personnel conducted visits to Taiwan, on pace with 2014 numbers.¹⁹⁹ In addition to visits, the U.S. military in June 2015 established two “sister units” to increase exchanges between units in the U.S. military and their counterparts in the Taiwan military.²⁰⁰

Some observers assert the United States could do more to support Taiwan's defense in order to fulfill U.S. obligations under the Taiwan Relations Act, which requires the United States to provide “defense articles and defense services in such quantity as may be necessary to enable Taiwan to maintain sufficient self-defense capabilities.”²⁰¹ For example, Van Jackson, visiting fellow at the Center for a New American Security, proposed shifting U.S. arms sales from F-16 upgrades and similar platforms to weapons that enable antiaccess/area denial capabilities,* such as undersea mines, air and missile defense, and land-based antiship cruise missiles. According to Mr. Jackson, this would be relatively inexpensive for Taiwan; have a lower profile, which would be less likely to anger China; and provide Taipei with more effective options to impose costs on China in a potential conflict.²⁰² Aside from arms sales, Randall Schriver, president and chief executive officer of the Project 2049 Institute, and Ian Easton, research fellow at the Project 2049 Institute, argue that the United States should increase its defense engagement with Taiwan by taking a range of actions, such as supporting Taiwan's indigenous submarine program by signaling its intentions to approve licenses for potential U.S. defense industry participants; inviting Taiwan to the biannual multinational Rim of the Pacific Exercise (RIMPAC) and other bilateral and multilateral exercises; and sending high-level military officials to visit their counterparts in Taiwan.²⁰³

The Role of Taiwan in the U.S. Rebalance to Asia

In response to written questions from the House Foreign Affairs Committee in March 2015 on the 36th anniversary of the Taiwan Relations Act, U.S. Secretary of State John Kerry described Taiwan as “a key component of U.S.-Asia Pacific policies, including the Asia rebalance.”²⁰⁴ Since the Obama Administration announced its rebalance to Asia strategy in 2011, other U.S. officials have mentioned Taiwan's role in the rebalance but have not detailed how

* According to the U.S. Department of Defense, “antiaccess” actions are intended to slow the deployment of an adversary's forces into a theater or cause them to operate at distances farther from the conflict than they would prefer. “Area denial” actions affect maneuvers within a theater, and are intended to impede an adversary's operations within areas where friendly forces cannot or will not prevent access. China, however, uses the term “counterintervention,” reflecting its perception that such operations are reactive. U.S. Department of Defense, *Air Sea Battle: Service Collaboration to Address Anti-Access & Area Denial Challenges*, May 2013, 2; U.S. Department of Defense, *Military and Security Developments Involving the People's Republic of China 2013*, 2013, 1, 32, 33.

Taiwan fits into the strategy. This lack of clarity could be due to concerns about how China would perceive U.S. officials' calls for increased U.S. engagement with Taiwan, particularly on military issues. The Obama Administration may feel constrained by the unofficial nature of U.S.-Taiwan relations and concerned about the impact on U.S.-China relations of openly emphasizing Taiwan in the rebalance policy.

Some analysts and security experts in the United States and Taiwan argue the United States is not fully leveraging Taiwan's strengths in the rebalance and could benefit from further cooperation. According to Mr. Easton and Mr. Schriver, Taiwan can play an important maritime role in the rebalance:

*Large numbers of maritime domain awareness capabilities fielded by Taiwan have the potential to contribute important [indications and warning] information. However, it is not clear how closely Taiwan's capabilities are linked to, and integrated with, U.S. Navy and other allies' systems in the Western Pacific. . . . Taiwan's ISR could drastically improve U.S. and other allied nations' situational awareness in the Taiwan Strait and South China Sea where their capabilities are constrained by distance and basing limitations . . . [but] there are significant shortcomings when it comes to human "software" components*²⁰⁵

In addition to improving maritime cooperation, the United States can tap Taiwan's strengths by reimagining U.S.-Taiwan defense policy coordination, according to Andrew Yang, Taiwan deputy minister of defense from 2009 to 2013 and minister of national defense briefly in 2013. Mr. Yang outlines three levels of his proposed new military-to-military coordination dialogue: (1) policy-level: developing shared views of the security environment and identifying policy guidelines to deal with the evolving security situation; (2) planning-level: based on Taiwan's 2013 quadrennial defense review, evaluating Taiwan's defense needs and, if needed, planning for U.S. assistance; and (3) service-level: focus on jointness between the U.S. and Taiwan militaries with particular emphasis on Taiwan's role in participating in regional humanitarian assistance and disaster relief operations.²⁰⁶

Together with defense cooperation, increasing U.S. trade and investment in the Asia Pacific is an important piece of the rebalance strategy. President Ma has called for Taiwan to join TPP by 2020, but has not provided a detailed roadmap to achieve that goal.²⁰⁷ Although senior U.S. officials said they welcome Taiwan to join TPP,²⁰⁸ potential roadblocks could impede Taiwan's entry as a member. Taiwan would probably face Chinese opposition, complicating Taiwan's entry.²⁰⁹ While Taiwan has made significant progress reforming its economy in recent years, Taiwan's economy would likely need to further reform and open to accommodate the trade terms of TPP. The U.S. Chamber of Commerce in Taipei's "2015 Taiwan White Paper" cites problems in Taiwan's regulatory process, including rules that deviate from standard global business practices and a lack of transparency, that still require reform.²¹⁰

Implications for the United States

The U.S.-Taiwan relationship remains robust, despite the limitations posed by the lack of formal relations between the two governments. It is built on common democratic values, strong commercial ties, and a U.S. commitment under the Taiwan Relations Act to aid in Taiwan's defense. Taiwan remains vital to U.S. geopolitical interests in Asia and important for regional security. For example, the United States relies on Taiwan as a bastion of democracy in East Asia and as a like-minded force for peace and security. From providing humanitarian assistance and disaster relief resources in a region that often faces natural disasters to peacefully managing its maritime disputes in the East and South China seas, Taiwan contributes to regional security and the maintenance of peace and prosperity in the Asia Pacific.

Since 2008, Taipei and Beijing have taken steps to reduce cross-Strait tension and increase economic, cultural, and educational ties. Seven years of cross-Strait rapprochement have been beneficial to the United States by reducing cross-Strait tensions and allowing U.S. policymakers to address other priorities in the U.S.-China and U.S.-Taiwan relationships.

Two factors could change cross-Strait ties, however, complicating U.S. interests, its important security ties with Taiwan, and its relationship with China.

- The inherent uncertainty surrounding the transition to a new administration in Taiwan makes China uneasy, and it is unclear how Beijing would approach relations with Taipei if the DPP wins the upcoming presidential election. Should the DPP win, it is unclear how it might pursue cross-Strait relations differently from the current KMT government. According to Ms. Glaser and Ms. Vitello, "All of [DPP Chairperson Tsai's] statements indicate that she is unlikely to pursue provocative policies. . . . She has made a concerted effort to articulate a strategy aimed at maintaining the status quo."²¹¹ Chairperson Tsai's comments suggest a pragmatic approach that, in a departure from the last DPP president, would not seek to overtly promote pro-independence policies. On the other hand, Alan Romberg of the Stimson Center argued that "[Chairperson Tsai] will not embrace the '1992 Consensus' (or any other explicit form of 'one China') and will not oppose Taiwan independence, as Beijing insists." He noted that, "In this circumstance, Beijing's anxiety regarding a Tsai government could result in a measured approach continuing to support [certain] people-to-people aspects of cross-Strait ties while [simultaneously] taking a hardline approach reducing government-level cross-Strait interactions."²¹²
- China's modernizing military presents a significant challenge to Taiwan's ability to defend itself and to the U.S. military's ability to effectively intervene in a cross-Strait conflict should it decide to do so. With the cross-Strait military balance of power continuing to shift in Beijing's favor, Taipei's stagnating defense budget and capabilities, and China's improving antiaccess/area denial capabilities threatening to keep U.S.

forces farther from China's shores, Beijing has increasing advantages in a Taiwan contingency, raising the cost for the United States to intervene in a crisis or conflict.

Conclusions

- Taiwan and China have enjoyed seven years of increased economic and trade ties, but fears among Taiwan citizens about economic coercion and China's political encroachment over Taiwan are more widespread than in the past.
- The younger generation of Taiwan citizens appears to view itself increasingly as Taiwanese rather than Chinese, and to be willing to take visible and substantial steps to assert their national identity. This has the potential to disrupt the diplomatic narrative that has allowed China and Taiwan to coexist without armed conflict. At the same time, Taiwan may not have the will or ability to counterbalance the growing Chinese military advantage. In view of China's growing power in the region as a whole, these trends have the potential to create stress on the ability of the United States to meet its obligations to Taiwan under the Taiwan Relations Act.
- Although China restricts Taiwan's ability to join multilateral institutions, Taiwan continues to make some progress on issues affecting its international space. Were Taiwan to succeed in its efforts to participate in emerging regional economic mechanisms like the Asian Infrastructure Investment Bank, Regional Comprehensive Economic Partnership, and Trans-Pacific Partnership, its integration in the region and ability to make a positive contribution to the international community would increase further.
- In response to China's increasingly assertive actions in the East and South China seas, Taiwan has initiated diplomatic frameworks and signed agreements with claimants to encourage the shelving of territorial disputes and promotion of joint resource development. Through an updated fisheries agreement with Japan and steps taken to clarify its claims in the South China Sea over the past year, Taiwan continues to play a role in helping preserve regional stability.
- The United States and Taiwan share a close relationship based on common democratic values, strong commercial ties, and a U.S. commitment to aid in Taiwan's defense. U.S.-Taiwan trade is at a record high, underlying Taiwan's increasing importance as a close economic partner. Furthermore, the United States continues to support Taiwan's defense through increasing military-to-military contact and other discreet defense cooperation.
- China's military modernization continues to focus on its ability to conduct military operations against Taiwan and deter the United States from defending Taiwan in a potential conflict. Although Taiwan has improved its defense capabilities through a combination of domestic production and acquisition of arms from the United States, the cross-Strait military balance of power continues to shift strongly in China's favor.

ENDNOTES FOR SECTION 3

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