

CUSTOMS & ECONOMIC DEVELOPMENT  
—REFLECTIONS ON TRADE, STATE AND INSTITUTION

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**Abstract**

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To serve the economic development and social progress in a constantly changing world, Customs needs to be sensitive, open-minded and adaptable. Particularly, Customs should be able to acquaint itself with the advances in technology, deepen its understanding of various economic phenomena, and stay alert to the evolution of trade pattern. Supported by empirical evidence, this article attempts to depict a committed government agency in its quest for creatively accomplishing the missions imposed by the state and the public, especially its initiatives and innovations in dealing with economic downturn, fostering institutions in favor of economic development, and facilitating the development of national industries.

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For most economies in the world, 2009 will undoubtedly be a year of reflection and adjustment. Following a series of efforts by central banks and governments to resolve the growing crisis through liquidity injections and various ad hoc measures such as the trillions of dollars in rescue plans, policy makers have now recognized the necessity to address the issue in a more comprehensive and fundamental way. In addition to the monetary and fiscal policies of counter-cyclical nature, structural and institutional changes are proposed to enhance the stability and sustainability of economic development in a long-term.

When one looks at the more recent trends in development thinking, the areas that dominate the growth literature are the role of trade, state, and institutions as pieces that collectively and collaboratively fit together to allow the development story to be comprehended (Grabowski, et al. 2007). Customs, as a government agency with law enforcement power, is in charge of import & export, controls and regulates the cross-border movement of goods and their means of transport. Pursuant to its statutory and regulatory authority, Customs is deeply concerned with trade compliance, trade regulation, trade security and facilitation, and many other trade related issues. Customs institutions, such as that of Customs control, classification and valuation, rules of origin, risk management etc., have direct and profound impact on international trade. There is no other organization that is more typical than Customs whose operation necessitates a systemic perception of trade, state and institutions.

**1. Processing Trade**

China is already the world's second largest economy and is the second largest exporter. It has by far the world's largest current account surplus and foreign exchange reserves. Growth has averaged 10 percent for the past 30 years, the most stunning record in history. The economic prosperity of China is based primarily on the combination of domestic production and foreign consumption, or export-led growth in other words. To achieve the policy goals, two conditions must be met. One is the sufficient supply of capital and technology necessary for the start-up of industrialization. The other is the reliable demand for the output to sustain the process over long-term. Since neither of the conditions can be guaranteed under ordinary trade, processing trade fits in as a special trade pattern.

Different from ordinary trade, of which the buyer and the seller are separate and take their risks respectively, enterprises engaged in processing trade minimize their risks by sheltering their production under someone else's label and deliberately avoid the risky processes like R&D, marketing, sales and distribution. Under the pattern, foreign markets are both the sources of the raw materials and the destinations of the final products.

### *History and development*

Under processing trade, China provides labor, land, infrastructure and sometimes facilities for the production while it harvests processing fees, taxes, technologies, managerial know-how and equipments brought with the production. The development of processing trade in China has experienced three phases.

The first phase (1978-1987) was characterized by the dominance of labor-intensive assembly lines and the uneven geographic distribution. For the sufficient employment of unskilled labor, most developing countries had to start processing trade with labor-intensive industries. At that period of time, tapping the cost-effective labor were also the major concern of foreign contractors or investors. Both internal and external factors led to the prominence of labor-intensive industries at the phase. The processing factories originated and concentrated in southern coast area because the opening-up policy was first tested in that area and processing trade naturally required proximity to international market.

The second phase (1988-1995) witnessed the boom and rapid development of processing trade. After the rosy foretaste, processing trade embraced its booming time. Enterprises engaged in the business proliferated and expanded from coast area to inland area. Parallel to the labor-intensive assembly lines, capital and technology intensive processing industries started to take their forms.

The third phase (1996-now), the developed and well deployed manufacturing capacity began to flex its muscles. In 1996, the proportion of processing trade exceeded, for the first time, half of the aggregate trade volume. The high proportion has been maintained since then. In 2008, China's total import and export amounted to US\$2,561.6 billion, and the processing trade took a share of 41 percent, at US\$1,053.6 billion.<sup>1</sup>

### *Strategic impact*

The overall impact of processing trade has already left its mark on businesses throughout the world. China is by now the dominant global player. China-based factories make 70 percent of the world's toys, 60 percent of its bicycles, and half its shoes. The world factory also builds half of the world's microwave ovens, one-third of its television sets and air conditioners, a quarter of its washers, and one-fifth of its refrigerators. Manufacturers in other countries increasingly rely on Chinese components or subassemblies to stay competitive (Shenkar, 2005). China's cost advantage is increasingly associated with high productivity, scale economies, supporting industries, and advanced manufacturing technologies rather than merely with low wages.

With the global business process outsourcing (BPO) and IT outsourcing (ITO) markets now

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<sup>1</sup> Source: National Bureau of Statistics of China. <http://www.stats.gov.cn>

multi-billion dollar industries and growing rapidly, outsourcing industry has been identified by Chinese government as a new strategic opportunity. Because outsourcing and processing trade root in the same rationale—division & specialization, the successful experience of developing processing trade has been applied immediately to fostering the outsourcing industries. This time, China's huge population, cost effective labor and emphasis on education collectively present the world an essential sourcing destination. In 2005, the 2,273 operating universities accommodated 23 million students in sum. That year, they graduated more than 640,000 engineering students while U.S. universities issued 137,437 bachelor's degrees in engineering, and India, 112,000 (Eltschinger, 2007). Catalyzed by global sourcing, changing external perception about China, investment flow, inherent advantages of a low-cost and skilled labor pool, and strong government support, the country's IT services export grows rapidly.

Beyond the goods and services that are transacted on the markets, the boom of processing trade also challenges the principles, norms, standards and other institutions underpinning the markets. In fact, the world has already seen the alteration of basic assumptions regarding the competitiveness of nation and business, the value of geographic proximity, and the cost of market entry and exit. For instance, the Chinese edge in terms of cheaper labor cost, a modern infrastructure, and the benefits of scale and agglomeration is now often sufficient to erase the proximity advantage of countries like Mexico, who have been counting on the combination of geography and NAFTA as a sort of insurance policy in the U.S. market. They are now finding out that payout is not guaranteed (Shenkar, 2005). Moreover, driven by technological improvements and managerial efficiencies, the cost of logistics has been on a downward trend for two decades, and in some cases is down by two-thirds from its level a decade or two ago. Firms initially protected from Chinese competition by high transportation costs find themselves on the firing line as logistic costs decline and as productivity rises on the Chinese side. Chinese ambassador ever said to the World Trade Organization during China's negotiations to enter the institution "We know we have to play the game your way now but in ten years we will set the rules!"

The dilution or decline of brand is another noteworthy effect of processing trade. Since brand and reputation are abstract notions and difficult to quantify, their strength is determined, to a large extent, by the subjective perception of consumers, the value of a brand and the consumer loyalty to it decline if the origin of the products bearing the brand is diversified or if its market is eroded by ubiquitous counterfeits. America's Research Group found that, between 2000 and 2003, the percentage of shoppers who said that brands were extremely important in their purchase decision declined from 48 to 32 percent (Shenkar, 2005). Moreover, the technology dissemination has dramatically enlarged the product lines of imitators. Actually, it is very difficult to find a product that is immune to counterfeit or piracy today. Consequently, the focus of popular consumption is shifted from brands to the appearance and functions of commodities, and the trend is reinforced by the surge of Shan Zhai products, which defy the brand notion completely and put the innovation of appearance and combination of functions to an extreme. Benefiting from the standardization and compatibility of components, my desktop is a product of DIY. There is nothing wrong here because it is a personal behavior for personal use. But the Shan Zhai phenomenon is an

application of DIY at commercial scale. Unlike counterfeits using trademarks that are identical or confusingly similar to those of genuine products, Shan Zhai products prefer to use their own brands or don't use any identification mark at all. The consumers will be explicitly notified that they are buying a Shan Zhai product, and there is no quality guarantee, neither after sale service. But they can get something with good appearance as fashionable as the famous brands, stronger functions, and extremely competitive prices. Its impact can never be overstated if we take into consideration the size of Chinese population and its poor average income. The favor granted by the market to Shan Zhai products can even incubate championship in adversity (See Box 1).

#### Box 1. Success from China phones

Taiwan's MediaTek did not attract a lot of international attention when it became one of the biggest chip suppliers for optical disc drives in personal computers in 2002, nor when it achieved the same dominance in DVD players a year later. It took MediaTek's recent success with supplying mobile phone chips to Chinese manufacturers to catapult it to prominence as the world's fourth-largest "fabless" chip company – fabless chipmakers do not own their own production facilities but outsource the work.

China's burgeoning mobile phone industry has also made Taiwan's biggest chip design company a rare winner in the economic downturn. While sales by Taiwanese chip vendors fell 8.7 percent in 2008, MediaTek's revenue grew by 17 percent, according to Gartner, the research company. Sales in the first half of 2009 were up 25 percent from a year ago. Yu Ming-to, chief financial officer, said there had been "almost no slowdown" from the global economic crisis.

MediaTek's strategy, in both DVD players and mobile phone chips, was to help hordes of new Chinese manufacturers easily enter the market by providing them with complete chip sets that came ready-made with a variety of functions. This led to the rise of low-cost Chinese manufacturers with little-known brands – so-called "whitebox" manufacturers.

MediaTek is looking for a similar feat with more complicated smartphones and will launch its first smartphone chipset this year. The company is also looking to become a supplier to global brands such as Nokia. Tsai Ming-kai, MediaTek chairman, sums up his company's ambitions as: "Whitebox today, mainstream tomorrow."

*Source: www.ftchinese.com*

Encouraging it or prohibiting it, as what kind of attitude should be adopted towards Shan Zhai products is hotly debated in China because despite a lot of problems associated with it, like public health, consumer rights, and IPR protection etc., some positive elements such as the spirits of innovation, customization and pricing in favor of grass-roots consumers are recognized. It is expected that most brands will degenerate into labels as processing trade transforms their products into commodities.

## 2. Responsive Customs

According to the government structure of China, the State Council is the highest executive body of state administration. It exercises unified leadership over local state administrative organs at various levels throughout the country, regulates the specific division of power and

functions of the state administrative organs at the central level and at the provincial, autonomous regional and municipal levels. The State Council operates through 28 ministries and state commissions, it also directly controls 8 other key national institutions including the General Administration of Customs. Such a deployment makes China Customs next to the nation's highest executive body and enables it to secure a better understanding of the national interests and an agile support from the state leaders. Nobody doubts the importance of Customs as the guardian of national borders, the collector of state revenues, and the regulator of import and export. But the common perception of its importance does not necessarily accord Customs the same position in state architecture. A few Customs Administrations in the world enjoys the same status as China Customs. The underlying rationale is simple—structure determines function. If the Customs is supposed to make greater contributions to the state, appropriate authority and social status should be granted correspondingly.

### *The Headwind*

What began in August 2007 as financial difficulties in the United States tied to subprime mortgage-based securities had turned into a global financial crisis as of October 2008. In East Asia, equity markets were hard hit, exchange rates depreciated rapidly, and gross capital flows to the region fell by half during the first 9 months of 2008. Slower investment growth in East Asia is now expected to spill over into still weaker production, employment, household spending, and GDP growth (World Bank, 2009). Because of the sheer size of its economy and the unusually high degree of openness to the world economy—foreign trade accounts for more than 60 percent of its GDP, China is undoubtedly one of those who have the strongest risk perceptions towards the crisis.

According to Shanghai Customs, the total value of imports & exports of the District was US\$45.4 billion in November 2008, decreased 9.7 percent compared with the same period of last year, a new record of monthly decrease since China's accession to WTO. It also terminated the miracle that Shanghai Customs District has held for seven months, with imports & exports exceeding US\$50 billion in a single month. More specific, the exports of US\$31.42 billion shifted from a growth of 20.8 percent in last month to a decline of 2.4 percent; the imports of US\$13.98 billion created the nadir of previous 21 months, changed from an increase of 7 percent in October to a decrease of 22.8 percent in November. Last time it was in December 2001 when the import and export dropped simultaneously in one month.

Man ZhouLi Customs District, the top railway entry of port in China, reported that the imports dropped to 1.19 million tons in January 2009, decreased 32.27 percent compared with the same period of last year. It was even worse in February 2009, the imports of 1.21 million tons declined 50.4 percent compared with the same period of last year.

At national level, the aggregate value of import and export was \$189.89 billion in November 2008, declined 9 percent compared with the same period of last year, a negative growth for the first time in past seven years.

### *Initiatives and innovations*

Jack Gottschalk (2002) argued in his 'Crisis Management' that the need to be ready to communicate when things go wrong, to engage in crisis management, will continue to be an

ever-increasing part of management's responsibility during the twenty-first century. China's rapid response to the crisis was reflected in the Central Economic Working Conference held in Beijing December 8-10, 2008, which summarized the situation and made a national call for concerted efforts to defend the economy.

Starting from July of 2008 the Ministry of Finance has raised the rates of tax rebate for exports several times to subsidize the exporters primarily of labor-intensive products like textiles, garments and toys etc. The State Council decided at a routine meeting on November 12 to eliminate the export duties on some industrial and agricultural products (Ming, 2008). All in all, more than a dozen tax reduction packages have been devised and promulgated by the Ministry of Finance since the end of 2008, with an estimated scale of RMB 300 billion Yuan (Wu, 2009). The General Administration of Customs (GAC) presented its "Ten Measures for Stimulating Domestic Demand and Promoting Economic Development".

### *Liquidity Injection*

On November 21, the Ministry of Commerce and the GAC jointly proclaimed significant changes of regulatory policy concerning processing trade, removed the restriction on the export of some goods covered by 1,853 headings of Customs nomenclature, shifted 272 headings from real transfer treatment to nominal transfer treatment. Different from the tax rebate, which is a general benefit enjoyed by all exporters, the cash deposit guarantee is a mechanism specially designed for processing trade, in which enterprises engaged in processing trade have to make cash deposit guarantee for the bonded imports of raw materials. According to the extent of their credibility, enterprises are classified into five categories, namely AA, A, B, C, and D<sup>2</sup>. Generally, for categories C and D, enterprises must have real deposits in a designated bank account as security for the bonded imports of processing materials, and the phrase "real transfer" means they really transfer money from their deposit account to the security account. While for categories B and above, nominal transfer is exercised, the transferred are documents instead of real money. The new policy is thus expected to save current fund of RMB 18.5 billion Yuan for processing trade (Shanghai Customs, 2008), a remarkable injection of liquidity that may help enterprises survive the recession.

### *Data mining*

For a long period in the past, the primary users of Customs statistics were government agencies and the social utility was poor especially compared with the high cost of obtaining the data. The rapid development of computer and information technology in the last 20 years has fundamentally changed almost every field in our society. The digitization of Customs statistics has been transforming many disciplines from data-poor to increasingly data-rich, and calling for the development of new, data-intensive methods to conduct research in trade pattern and tendency. The persistent endeavor of China Customs in this regard has produced a number of useful applications in this regard, such as the enforcement assessment system, the control system on trade statistics quality, the system of control & analysis on goods declarations, the pre-warning and monitoring system on import & export etc. In addition to

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<sup>2</sup> One of the criteria that distinguish categories C and D from B and above is that both C and D have violation records under Customs control, with D's violation is more serious in quality or quantity.

the contributions to enhancing the accuracy and standardization of statistic data, these innovations enable Customs to diversify and extend their services for the public. For example, Tai Zhou Customs, a subordinate body of Hang Zhou Customs, notifies local enterprises of the trade pre-warning information through mobile phone text messages. The instant and customized service is embraced by exporters because it helps them make informed production decisions and respond swiftly to trade risks. On this point, Data mining offers three major advantages to the enterprise: (1) it provides information about business processes, the customer, and market behavior; (2) it takes advantage of data that may already be available in operational data collections, data marts, and the data warehouse; (3) it provides patterns of behavior that is reflected in data and able to drive the accumulation of business knowledge and the ability to foresee and shape future events (Ville, 2001). The extensive applications of data mining can also enhance Customs performance. Since the risk management has been assimilated into all kinds of operations of China Customs, data mining starts to show its usefulness in supporting risk analysis, profiling and targeting. Take fraud detection as an example, because fraudsters often have measured values that do not fit a common pattern, trend, or known long-memory stochastic process, Customs can use data mining to detect money laundering, tied transaction, fraudulent declarations etc.

#### *Business integration*

To meet the economic integration with the integration of Customs operations is an important strategy adopted by China Customs. The ever increasing scale and complexity of production have amplified the flows of goods and services across border, urging China Customs to constantly simplify its formalities and smooth the movement of consignments. A new clearance mode—local declaration & port release—has just been popularized to help enterprises relieve the impact of economic crisis.

Moving goods from one place to another is a basic commercial practice and transit procedures are developed especially for the movement of consignments with unfulfilled Customs obligations. China Customs classifies national transit into three types, namely, transit at importation—from the Customs at port of entry to the Customs at inland; transit at exportation—from the Customs at inland to the Customs at port of exit; and internal transit—from one Customs at inland to another. Prerequisites for initiating the transit procedure include the existence of Customs establishment at each end of the transit, the competent vehicles to which Customs seals and other control measures can be applied, and the authorized carrier by Customs. As a summary of practice, inconveniences have been reported in the following aspects. First, enterprises have to declare or register twice for the same consignment, that is, at the opening and termination of transit respectively. That results in extra burden of Customs formalities and prolonged clearance time. Second, the entry barrier to carriers who want to be involved in transit transport is high, for instance with registered capital no less than RMB 2 million Yuan is one of the requirements. Moreover, mixed transport is prohibited, which means the commodities in free circulation cannot share vehicles with the goods in transit, inevitably leading to the high cost of transit logistics. Given the same route, freight charged for transit transport is at least 20% higher than that for ordinary goods. Last, the delayed tax refund hampers enterprises' cash flow. Because the tax refund on exports is based on the fact that the transaction is real and the goods has left

Chinese territory, inland Customs usually have to hold issuing export certificates, which are essential for applying to tax bureaus for tax refund, until they receive the verification from port Customs concerning the exit of consignments. Most often, it takes enterprises one week to get the refund after exportation. But it is explicitly stated in legislation that enterprises can choose at will port Customs or inland Customs to clear the consignments, so why don't the importers and exporters just put an end to their Customs obligations at the port of entry or exit? As we know the duties and taxes will be collected by port Customs if consignments are cleared there while that revenue is also desired by inland Customs because the revenue contribution is currently the foremost indicator when measuring the performance of a Customs unit. Disappointing inland Customs on this point is absolutely inadvisable because the registration of enterprises, review and approval of processing trade contracts, and tax refund are all under the control of local Customs. Consequently, most enterprises have to transit against their true will. Under the new clearance mode, enterprises lodge declarations and pay duties and taxes to local Customs while their consignments will be (examined if necessary and) released by Customs at the port of entry or exit. Compared with transit mode, major advantages include that: (1) formalities like declaration, examination and release are reduced from twice to once. According to the estimation of Zhuo Li Group, a conglomerate in Zhe Jiang province, by applying the new clearance mode the annual cut in the cost of declaration lodgment may approach RMB 1 million Yuan; (2) financial transactions are more express and safer because the tax payment and the repayment are all done locally; (3) logistic cost has been cut significantly because cleared consignments can be transported with ordinary vehicles and with more flexibility in route and time; (4) it also serves as a great incentive for trade compliance because only the enterprises of grade A and above can enjoy this facilitation.

The new mode also challenges the traditions of China Customs by dividing and redistributing Customs authority across different Customs districts so that the seamless coordination and cross-functional cooperation of several Customs establishments becomes essential for the accomplishment of Customs missions. China Customs runs a vertical leading system, in which the GAC delegates its power to a number of Customs districts that are established generally in line with the provincial compartment. The Customs districts compete with each other in the fields of revenue collection, anti-smuggling, trade compliance and supporting local economic development etc. Because of the competitive relation and the bureaucratic legacy, the communication and cooperation of these relatively independent Customs districts has been a prolonged problem. For instance, a deeply rooted prejudice argued that a competent Customs establishment should be self-sufficient in exercising all kinds of authority and the absence or outsourcing of particular enforcement power would inevitably weaken its discretion and deterrence hence should be prevented at all cost. Now as the economic development breaks and blurs the district boundaries, Customs districts start to learn how to cooperate and function as an organic whole. In 2006, promoted by the GAC, the Customs districts in northeast China<sup>3</sup> met to discuss the reforms on the clearance modes for sea transport and land transport. As a result of the meeting, the Northeast Agreement on the Reform of Regional Customs Clearance has been signed. December of that year, in Hei LongJiang Province the first importation under the new mode accomplished its clearance

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<sup>3</sup> Represented by Shen Yang Customs, Chang Chun Customs, Haer Bin Customs, and Man ZhouLi Customs etc.



formality in thirty minutes after lodging its declaration to Haer Bin Customs. Hundreds miles away at the port of entry, Da Lian Customs successfully examined the consignment and released it to the consignee in just a few hours. This represents a remarkable lift in the capacity of China Customs to integrate, both institutionally and technologically, its operations across the vast territory, and makes its support to economic development sustainable.

### *Trade Facilitation*

In general, trade facilitation refers to simplification, standardization and harmonization of trade processes, procedures and related information flows. In a narrow sense, trade facilitation relates to streamlining the customs and other border agencies procedures and related documentary requirements. Recently, the focus has shifted from enforcement to trade facilitation with the use of pre-arrival clearances, the authorized operators concept, green lanes and post-clearance audits, increasingly employing ICT applications and advanced cargo information (UNESCAP, 2006). Responding to the call of GAC, local Customs come up with measures of different focuses and depth, which can be sorted as:

Measures to extend service time: the practice of appointed clearance enables most Customs to extend their service time to weekends and holidays. Several Customs even set up hotlines to ensure the availability of Customs services around the clock. October 24, 2008, the Fang Lu Tea Company had 36 containers of tea returned from US, contract value US\$ 290 thousand, to which protective measures should be applied as soon as possible. Acquainted with the situation, officers of Hu Zhou Customs dedicated their weekends to clearing the consignment, and the timely clearance helped the company prevent further loss.

Measures to extend service space: Man ZhouLi Customs grants freedom of choice to the exporters of fruits, vegetables, and other perishable products. The exporters may choose domiciliary clearance or clearance at the Customs establishment at their convenience. Some of them are even allowed to substitute commercial seals for Customs seals in transit procedures.

Measures to widen the application of ICT: Shanghai Customs has been piloting paperless clearance among its 37 enterprises of grade AA, positive results encourage the Customs to spread the paperless mode to all the enterprises of grades AA and A. Supervision through intranet has been applied to more enterprises engaged in processing trade by Jia Xing Customs. Hu HaiMei, a Customs broker of Posk-CPPC, said “I had to visit the Customs office several times a month to lodge the goods declarations, benefited from the intranet supervision system, now I can handle all of them in my office and the monthly summary can be finished in one day.”

Measures to refine institutions: China Customs has accepted and implemented the notion of authorized economic operators (AEOs) but the smooth running of the mechanism depends, to a large extent, on the effectiveness of various incentives provided to the AEOs by Customs. A common practice is that in addition to the many priorities in clearance procedures, enterprises of Grade AA usually enjoy a designated Customs liaison that is instantly available to render one-to-one services, and at most time can navigate them through the maze of Customs formalities when emergencies arise. More publicity, training and regular meetings with

exporters on the clearance process can also make a difference. To encourage voluntary compliance, enterprises with low error rates in lodging declarations are rewarded with access to fast-track clearance procedures, while those with high error rates face more scrutiny. Consequently, a more serious attitude is assumed when enterprises examine their declarations for conformity to Customs requirements before lodgment.

The measures constitute the kind of forceful and credible action that has been needed. The exports that have fallen substantially begin to greet these measures favorably. At US\$ 95.4 billion in June, the highest monthly tally since December, Chinese exports rose 7.5 percent from May.

### **3. Evolving Institutions**

It has been a decade since the GAC embarked on its expedition in 1998 to modernize and streamline the operations and structure of China Customs, over the period of time, the organization has experienced significant changes that were unprecedented in history to its present structure and management approaches. Aiming to establish a modern Customs administration, the strategic development was scheduled to be accomplished in two steps.

#### *Stage One (1998-2003): The rise of rule of law*

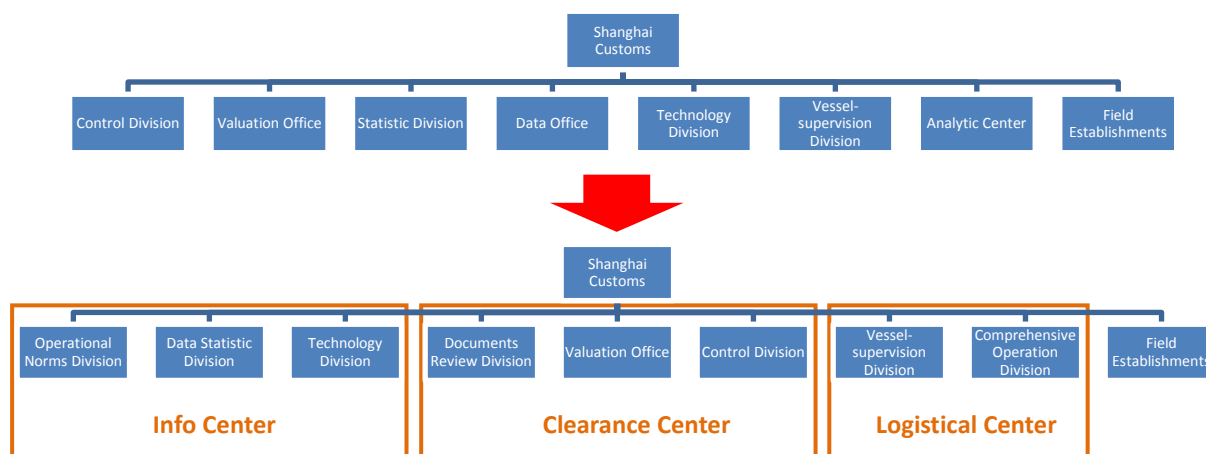
At the first stage, the main objectives were to modernize the thought, the institutions, the methods and the measures of Customs management. A quantitative description of these objectives specified the formation of eight systems with modern Customs features, namely the legal system, the trade compliance system, the information system, the clearance system, the logistic supervision and control system, the investigative system, the administrative system, and the public relation system.

In 1999, the Third Amendment to the Chinese Constitution incorporated for the first time in the history of China the concept of rule of law into the Constitution, in which it stipulates that "the People's Republic of China implements law to govern the State and construct the socialist country with the rule of law". The revolutionary alteration triggered chain reactions in many social aspects but the most important and profoundest one is the enhanced legal awareness and respect for institutions in Chinese community. The State Council appealed governments at all levels and its subordinate departments to strengthen institutional building, tighten administrative law enforcement, strengthen supervision for administrative law enforcement, and heighten the capability of administration in accordance with law. The GAC grasped the golden opportunity to initiate bold and resolute reforms on Customs institutions, and special attention had been attached to its legal framework as demonstrated in the GAC's perception about modern Customs features—the legal system preceded other systems. A remarkable breakthrough came on July 8, 2000. After 20 months of intensive efforts, the revised Customs Law was promulgated on that day. The revision occurred mainly in five aspects: the new Customs Law (1) clarified the legal status of anti-smuggling police in legislation and amplified its institutions; (2) toughened the penalties for smuggling crimes and enriched the enforcement measures; (3) created, adjusted or refined some Customs formalities and procedures to facilitate trade and increase clearance efficiency with reference to particular WTO rules; (4) improved the protection for interested parties with reference to international

conventions and best practice; (5) particularized the requirements for Customs enforcement supervision, stressed that enforcement shall be strictly pursuant to its statutory and regulatory authorities in both procedural and substantive terms, and is subject to the supervision of the public and other agencies.

Drastic changes were not limited to the legislation, the structural re-engineering was also unprecedented in the history of China Customs. Back to 1994, the GAC instituted a number of research groups to explore various issues related to the strategic development of China Customs. Over the next four years, plenty of field surveys, seminars, and academic discussions had been organized at both national and international levels. Thousands of Customs professionals contributed their ideas and expertise to the formation of the blueprint. The studies focused our attention on the following problems and deficiencies: (1) an obsolete organizational structure characterized by layers and internal barriers; (2) a lack of uniformity in Customs application of laws, policies and procedures; (3) a persistent occurrence of intra-department turf war and destructive internal competition; (4) a widespread concern that the allocation of our workforce does not meet the workload requirements effectively. Although remedial actions are constantly under way to tackle some practical issues, in many cases the existing structure, our mindset and approaches to management is ineffective. For them, more fundamental and comprehensive solutions are required, so the structural re-engineering moved in. Take Shanghai Customs as an example, Exhibit 1 confronts the structures before and after the re-engineering. It is very clear that (1) the reformed architecture broke down the walls that had isolated the various functional departments and helped the incubation of individualism among them; (2) it normalized and standardized Customs formalities and procedures by utilizing electronic declaration and centralized mechanism for declaration review; (3) by combining the functional departments into a organic process, it emphasizes the cross-functional teams as a routine approach to Customs operations; (4) based on the notions of risk management, it started to differentiate consignments of different risk so that a more effective balance between workload and workforce could be established, for instance, the division of office duties and field duties became possible under the new mode, which is favorable to specialization and efficiency improvement.

**Exhibit 1. Structural Change of Shanghai Customs**



Source: Shanghai Customs

*Stage Two (2004-2010): From control to service*

If the whole Customs can be viewed as a machine and the first stage was characterized by structural and institutional construction, the second stage is intended to foster intelligence and humanity out of it. Recognizing that the government role has evolved dramatically, from the owner of enterprises to the supervisor of them, then the facilitator, and now their partner, the GAC has concluded that it is now the right time to rebuild the organizational culture and the attitude of its members in order to transform China Customs from a control-type agency to a service-type one. Based on the SWOT matches, the GAC derived the following priorities: (1) the vision of China Customs needs to be refined to match its mission and capabilities against the dynamic needs of the nation and society. The process will take into consideration the core business of China Customs, the interests and the needs of its staff and customers, a system of metrics to evaluate outcomes and efficiency, and the improvement efforts; (2) the risk management has proved an effective mechanism for resource allocation and performance enhancement. Our staff should be acquainted with the knowledge of risk management and risk awareness will be reflected in all Customs operations. Under the principles of “scientific methods, advanced measures, accurate identification, agile response, close cooperation, and effective management”, China Customs will constantly refine its risk management applications, optimize the risk indicators in various Customs procedures, and enrich the instruments for risk avoidance, transfer, and mitigation etc.; (3) China Customs will shift its emphasis from enforcement and required compliance to partnership-building and voluntary compliance. Establishing partnership means recognizing our customers and stakeholders, understanding their needs, devising strategies responsive to their requirements, and measuring our performance against the extent of their satisfaction. Our predominant method of operation will be to work effectively with the business community and other government agencies to enable people and commerce to voluntarily comply with the statutory and regulatory requirements of China Customs so that a high compliance rate can be reached. Customer satisfaction will be integrated into our organizational goals and customer feedback will be incorporated into our system of performance measurement; (4) to bravely explore new business management techniques and measurement systems and their application to Customs operations. To master these techniques, organizational learning will be a continuing process; (5) an effective organization must have a shared understanding of its mission and vision, and this can only be done by well designed and delivered trainings. Trainings in a variety of forms will increase their availability to our staff, some of them are designed to foster a better understanding of the organizational goals and the role that each of them plays in achieving these goals while the others aim to improve their performance in technical and supervisory perspectives. Both types should be delivered just in time; (6) the leadership is dedicated to create a better working environment, in which our staff can make their maximum contribution to the goals of our agency and the government, free from fear, harassment, and bias. Personnel system will be reformed to establish more flexible performance management and reward systems, during the process, people should be involved in process improvement efforts and management techniques should be utilized to explain their values and clarify their roles in the organization.

Sticking to these initiatives is neither an easy nor a one-time task, China Customs should

serve as a role model for border agencies throughout the world with its responsiveness, innovation and adaptability. Through collective and persistent endeavor, the GAC anticipates the successful transformation of China Customs from a control-type Customs to a service-type Customs that will be the most facilitative Customs in the world.

#### **4. Conclusion**

So far, we have witnessed the development of processing trade, its great contribution to national economy, and its significant impact on international economic order. We also understand how China Customs, as a committed, responsive and modern government agency, keeps adapting itself to the dynamic economic development, defend and support the national strategies through its timely initiatives and innovations. The interaction between trade and institutions, particularly the evolution of Customs institutions to accommodate the new requirements and functions imposed by the public and the state, has demonstrated that institutions are important for initiating and maintaining economic growth.

Besides the points that have been explicitly discussed in the text, a few more noteworthy implications include: (1) trade is important but pattern is decisive. Once the pattern is identified, Customs policies and operations should be aligned with its characteristics and foster a favorable environment for its development; (2) a correct attitude towards change is essential. Organizations won't be able to approach their goals at full speed unless all the members are convinced of the reasons and the effect of changes. The Customs Administrations engaged in modernization, process re-engineering, and any other form of changes are suggested to attach at least the same emphasis on cultivating the right attitude out of their staff as on equipping them with technical skills; (3) look before you leap. The development of economies frequently necessitates the transformation of social institutions such as the change of government functions, the alteration of government structure, and the reform of administrative manners etc. Customs Administrations are recommended to deepen their understanding of economic fundamentals and build a profound insight into the tendency and complexity of realities before diving for changes; (4) development projects must be planned under real-world conditions. After exploring many developed Administrations for best practice, China Customs has concluded that to improve governance systems the developing community is not lacking the tools needed for technical solutions to governance challenges. The toolbox is overflowing, best practice manuals in various areas of interest tumble out of seminars and workshops. However, difficulties arise when attempts are made to apply what are often excellent technical solutions under real-world conditions. Therefore, the Customs community, in order to meet those challenges, is required to foster a broad vision going far beyond Customs operations to incorporate political sense, business acumen, and enduring adaptability. It is very nice to know that the WCO is strengthening its efforts in strategic research, the organization is thus expected to serve a role model for other international organizations in combining more social, cultural, and political dimensions of development into its future efforts for assisting member Administrations in the fields of Customs modernization, trade security and facilitation, revenue collections and capacity building etc.; (5) closer academic relationships among Customs institutions are increasingly important. The rapid growth in INCU membership and the finalization of PICARD Professional Standards indicate that strengthening international cooperation is now a

consensus of world Customs academia. An important characteristic of Customs work is that it “acts locally but impacts globally.” To cultivate our officers, helping them forge global visions in their work, is particularly urgent at a time of globalization and integration. To accomplish this mission, there is nothing better than a global team of Customs universities because it has inherent cross-culture and cross-discipline qualities that best match the nature of Customs jobs. The membership and the Standards thus should function as stepping stones for deep cooperation of Customs institutions, facilitating the joint efforts in detailed projects such as compiling an encyclopedia of modern Customs, developing textbooks and training materials for Administrations involved in particular trade agreements, and exploring new trade patterns for closer economic partnership etc. Differences are expected to be made as the PICARD program and many other endeavors eventually trigger the quantum leaps in this regard.

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