

## **A Study on Hindrance of Customs Procedures to Taiwan's Development of Free Trade Zones**

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## Abstract

This study investigated the hindrance of customs procedures to the development of free trade zones in Taiwan, attempted to identify the hindrances and proposed solutions through literature reviews and field research. Through literature reviews and field research, this study found that: a. customs procedures impede the liberalization of international logistics in free trade zones., b. the coexistence of business in existing development areas and same business in free trade zones impedes customs management; c. customs is inflexible in thinking and rules and is not easily subject to autonomous management; d. unsimplified customs procedures are one of the major obstacles to the development of free trade zone in Taiwan; e. the Customs Administration, the Ministry of Transportation and Communications, and non-governmental enterprises have different attitudes towards autonomous management of security guards and audit mechanism.

**Keyword:** Customs Procedures; Free Trade Zones; Taiwan

## 1. Introduction

Free trade zones in Taiwan are designated areas where special Acts are legislated for the adjustment of customs administration and taxation, and they are granted the most open economic zones or even areas outside customs territory to accommodate trade, processing and

technological development with the benefit of highly efficient storage, transportation and in-depth local value added for the purpose of meeting the needs of just-in-time goods and international supply chain. For a free trade zone to be run successfully in a country, the customs administration and taxes must be adjusted to comply with its development. Some researchers have stressed that customs procedures have a crucial impact on Taiwan's development of free trade zones (Tseng et al., 2004).

With the increasing demand of international trade for just-in-time goods and solutions needed for removing limitations within international trade regulations, relieving tax burden, and ameliorating timely transportation among countries, Taiwan government passed the Act for the Establishment and Management of Free Trade Zones in 2002, which was to initiate free trade zones for congregating trade, processing, storage and forwarding business in specific areas. Currently, there are free trade zones established in or near one airport and six harbors in Taiwan to help Taiwanese enterprises develop global logistics management.

Ballou (1987) suggested that a free trade zone must have the following advantages: a. imported goods can be forwarded to other countries without passing customs clearance; b. customs duties are paid on foreign goods only when those goods are transported from a free trade zone to a customs territory; c. if foreign goods are requested to have specific labels when they enter domestic area, the labeling work can be done in the zone to avoid penalty; d. if the number of goods are diminished due to spoilage, evaporation or damage, these goods shall not be tariffed; e. if an importer is granted preferential tariff treatment, there shall be tariff standstill; f. only when goods that use imported raw materials or components enter a domestic area will tariff be imposed. Lin and Lin (2012) and Shen (2013) classified main advantages of free trade zones under four categories: service, efficiency, cost and operation. Efficiency is that cargo is released without the review of written documents, physical examination, or escort, but with monthly

summary of clearance notices so that goods can be freely circulated within a free trade zone. In this case, customs clearance is one of the most important elements leading to success of the development of free trade zones in Taiwan. However, other researchers (Tseng et al., 2004; Lin 2008) have found that many customs procedures are obstacles to the development of free trade zones: customs verification and inspection of businesses in the zones, the establishment of depots in the zones and conflicts between previously existing businesses and newly established businesses in the zones. All of these have reduced liberalization of international logistics and caused great inconvenience to customs management. On the whole, the openness of customs procedures is one of the most influential factors in the development of free trade zones in Taiwan.

With regards to the importance of customs procedures to the development of free trade zones in Taiwan, this study aimed to investigate the influences of customs on the development of free trade zones by employing documentary analysis (the year of domestic documents started from 2003) and explore unsolved problems that the development of free trade zones in Taiwan may have during customs clearance by conducting exploratory research on some countries' experience of developing their free trade zones, and propose solutions.

## **2. The Development Status and Analysis of Free Trade Zones in Taiwan and Other Asian Countries**

Trade liberalization is the key to success of a nation's economic development. Discussion on customs procedures and preferential treatment in Taiwan and other Asian countries is presented as follows:

### **Singapore<sup>1</sup>**

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<sup>1</sup>Tseng, K. S., Tseng, W. J., & Kuo, K. L. (2004). The Study on Cargo Customs System of Taiwan's Free Port Zone. *Maritime Quarterly*, 13 (1), 57-74.

Free entrepot trade has been Singapore's main economic activity since the establishment of its first free trade zone "Jurong Port" in 1969 (Tseng et al., 2004). With the deepening of international division of labor and Singapore's opening of its import policy, now, Singapore has 7 free trade zones. Changi Airfreight Center is located near Singapore Changi Airport, and the rest 6 are located near ports. The Ministry of Transport of Singapore appoints the Free Trade Zone Advisory Committee. Some free trade zones are governed by the Port of Singapore Authority Corporation Limited under the administration of the Maritime and Port Authority of Singapore. Singapore Customs— a department under the Ministry of Finance, has responsibility of issuing Import Certificates, endorsing Export Permits, collecting customs duties and Goods and Services Tax, processing bonded warehouses license applications, processing permit applications and customs clearance in the free trade zones, and upholding employee training. The primary function of the free trade zones in Singapore is to encourage entrepot trading. The free trade zones operate and facilitate goods that are transported from overseas to the zones, from customs territory to the zones, from the zones to overseas, from the zones to customs territory, or from one free trade zone to another. Cargo clearance in the free trade zones is processed on TradeNet which integrates import, export and transshipment documentation processing procedures and expedites the clearance of cargo within 15 min.

### **Hong Kong<sup>2</sup>**

Hong Kong pursues a free trade policy, and a free economic policy of laissez-faire has been the practice. No tariff is charged on imported or exported goods. There is neither tariff quota, surtax, value-added tax, nor services tax. According to Chapter 60 of the Import and Export Regulations, anyone who imports or exports any article other than an exempted article is

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<sup>2</sup> Yang, Y. C. (2017). The implications of neighboring Asian countries for free trade port zone in Kaohsiung port.

Available at: <http://web.idv.nkmu.edu.tw/~hgyang/lm013.pdf> (accessed 17 June, 2017).

required to lodge with the Commissioner of Customs and Excise, an accurate and complete import or export declaration within 14 days after the importation or exportation of the article. Prosecution may be initiated against anyone who fails to lodge the required declaration, or knowingly or recklessly lodges any declaration that is inaccurate in any material particular. Customs clearance procedures are easy in Hong Kong. No prior applications are required for importing or exporting goods. Traders can complete customs declaration within 14 days after the importation or exportation of the goods.

## **China**

Kuo (2013) reported that China set out the framework plan to run pilot free trade zones in Qingdao, Tianjin, Shenzhen and Shanghai in 2011. The following is a sketch of Shanghai free trade zone<sup>3</sup>.

Shanghai sits in the middle part of East China coast. It merges bonded areas such as Waigaoqiao Free Trade Zone and Pudong Airport Free Trade Zone. Businesses in the zone comprise international trade, logistics center and processing. In bonded areas, all trades are subject to customs inspection and traders can transmit cargo clearance information to the customs by means of electronic data transmission. Traders have to apply to the customs for file recording of foreign goods which enter and exit free trade zones. Traders have to submit customs declaration for goods which enter and exit free trade zones and customs territory. Shanghai free trade zone has done pilot test on operations of “Three-Once” Program: one application, one inspection and one clearance to simplify the customs procedures. In addition, Shanghai Waigaoqiao Bonded Logistics Park provides a time-saving and cost-effective one-stop-shop service with partial distribution.

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<sup>3</sup> Kuo, C. S. (2013). The study on free trade zone in Taiwan – A case study of Farglory free trade zone. Unpublished master dissertation, Department of Business Administration, China University of Technology, Taipei.

## Taiwan

Free trade zones in Taiwan are designated areas where special Acts are legislated for the adjustment of customs administration and taxation and to grant them the most open economic zones or even areas outside customs territory to accommodate trade, processing and technological development with the benefit of highly efficient storage, transportation and in-depth local value added for the purpose of meeting the need of just-in-time goods and international supply chain (Tseng et al., 2004). There are now 6 free trade zones in Taiwan which are single window, industrial cluster (affected by introducing industry classification), free capital flow, tax preference, expedited cargo release and autonomous management of enterprises. Whether all these features can satisfy enterprises' needs has been a critical factor for Taiwan to succeed in developing free trade zones (Chang, 2006).

### **4. Current status and problems of customs procedures in Taiwan's free trade zones**

Free trade zones in Taiwan are areas within national territory but outside customs territory. Cargo that enters or exits free trade zones is concerned with clearance procedures inside or outside customs territory. To accelerate circulation efficiency of goods, Taiwan government promulgated Articles 17 and 18 of the Act for the Establishment and Management of Free trade zones and the Regulations Governing Customs Clearance for Goods in Free Trade Zones (Ministry of Finance, ROC, 2017) for enterprises to deliver goods in accordance with customs procedures. Customs procedures for the entry and exit of goods in free trade zones include report and customs clearance. In November, 2005, an amendment of the Regulations Governing Customs Clearance for Goods in Free Trade Zones set out that consolidated monthly customs clearance declaration can be adopted by enterprises in free trade zones upon approval of the Customs (Ministry of Finance, ROC, 2015). Enterprises can report goods, machines and equipment that are to be used in free trade zones, to the customs without proceeding customs

clearance. Goods to be transported from a tax area to a free trade zone shall be considered export. Cargo, exclusive of goods related to national security or environmental concerns, to be transported among free trade zones shall be autonomously managed by enterprises in a manner of high-tech cargo tracking system (Chang et al., 2014).

Problems that Taiwan has encountered during the development of special economic zones in the past years include cross-strait political disparity and insufficient liberalization of investment environment and unsatisfactory efficiency. With regards to the planning of free trade zones, investment environment of software and tax preference were ameliorated. But from the perspective of liberalization and internationalization, the Act for the Establishment and Management of Free trade zones and relevant regulations still have many problems which need further discussion, especially problems of customs clearance of cargo and movement of goods into and out of free trade zones (Tseng et al., 2004). Many researches indicated that customs procedures are one of the major hindrances to Taiwan's development of free trade zones. For example, Yang (2008) observed that successful factors in developing free trade zones can be ranked in important order: the integration between customs clearance and port logistics information system, port operational efficiency, goods in free trade zones which are exempted from tariff and value-added tax, and facilitation of customs clearance. On the other hand, he found that incomplete liberalization of customs procedures has impeded the development of free trade zones. Another researcher, Chen (2010) discovered in his study on measures taken by customs to cope with customs formalities in free trade zones, that main complaints from enterprises against customs formalities are: customs do not simplify their procedures, and it is difficult for customs to loosen their control, change their original way of thinking, practice autonomous management and apply regulations flexibly. Moreover, Yang and Shi (2015) noted that the smoothness of customs clearance is often subject to customs policies and complex



personnel.

From relevant researches, it is obvious that regulations governing foreign goods' entry into and exit from free trade zones still have some problems with limitations on circulation of goods and customs' control. The spirit of free circulation of goods cannot be embodied. There is still hindrance to Taiwan's development of free trade zones.

## **5. Conclusions and Suggestions**

### **5.1 Conclusions**

After reviewing several researches, this study concluded that customs' inspection of businesses in free trade zones has confined the liberalization of international logistics. The spirit of establishing free trade zones is to eliminate unnecessary governmental controls, to emphasize the concept of "within national territory but outside customs territory," to exempt goods in free trade zones from customs duties and sales tax, and to permit enterprises performing limited business activities. Nevertheless, Article 19 of Taiwan's Act for the Establishment and Management of Free trade zones stipulated that the customs office may team up a combined audit taskforce to irregularly conduct on-line computerized inspection and physical inventory of the goods. These inspections in principle are to prevent enterprises from smuggling. But since circulation of goods is within national territory but outside customs territory, and there is an on-line computerized customs declaration system, how can smuggling occur when cargo has not gone through customs clearance? Furthermore, irregular physical inventory of the goods has affected the circulation efficiency and has contradicted the liberal spirit of the concept "within national territory but outside customs territory" (Tseng et al., 2004).

The establishment of depots in the zones also impedes the spirit of free circulation of goods. The purpose of setting up free trade zones is to simplify trade procedures and allow free circulation of goods by exempting businesses in the zones from customs administration and

clearance procedures. Not only highly liberalized circulation of goods but also least governmental intervention is required for successful development of free trade zones. However, in the Regulations Governing Customs Clearance for Goods in Free Trade Zones, depots shall be built in the zones for customs inspection of goods entering and leaving the zones. If exported goods and goods to be transported to another free trade zone comply with the Guidelines for Examination and Inspection of Import and/or Export Goods, enterprises can apply to the customs for cargo to be examined and released alongside a ship; otherwise, cargo must be stored in a depot prior to export. These regulations complicate customs control formalities and impact greatly on circulation efficiency of goods.

Coexistence of business in existing development areas and same business in free trade zones impedes customs management. The initiation of free trade zones is supposed to create an entirely free economic environment so that businesses in the zones are exempted from customs duties to accelerate the circulation efficiency of goods. If business outside the zones, similar to the one in the zones is allowed to run within the zones, the influence on existing enterprises may not be severe, but for authorities of the zones, how to manage circulation of goods effectively may be a problem. More complicated customs controls may cause chaos and inconveniences to the circulation of goods in the zones and affect the efficiency of international logistics (Tseng et al., 2004).

Difficulties that enterprises in free trade zones often encounter with regards to customs procedures and clearance are: customs do not simplify customs procedures, it is difficult for customs to change their original way of thinking, to practice autonomous management, and to apply regulations flexibly (Chen, 2010). Indeed, unsimplified customs procedures are one of the major hindrances to Taiwan's development of free trade zones. Taking customs declaration for goods in free trade zones as example, an enterprise shall declare foreign goods incoming to a free

trade zone for storage by using “F1” declaration sheet, declare goods stored in a free trade zone leaving for a foreign country by using “F5” declaration sheet, but declare goods traded in the zones by using “F3” declaration sheet. All kinds of customs procedures seemed to be qualified for the concept of innovation management, but in fact, they all have to be simplified (Shen, 2013). Besides, the Customs Administration, the Ministry of Transportation and Communications, and non-governmental enterprises have different attitudes towards autonomous management of security guards and audit mechanism. This has been another issue regarding cross-organizational coordination (Chang et al., 2014).

## 5.2 Suggestions

From the above literature reviews and analyses, difficulties related to customs procedures shall be preceding issues to settle for the development of free trade zones in Taiwan. The actual operation of a free trade zone includes movement and transportation of cargo and customs clearance of cargo. The customs conduct procedures for the above operation and oversee management by security guards involving cargo entering and leaving a free trade zone. An enterprise usually needs to coordinate with the customs on its activities in the zone. As for the Ministry of Transportation and Communications, there are still many issues regarding the planning of business operation and cross-departmental coordination (Chang, et al., 2014).

First of all, this study suggests that some regulations for storage of cargo in a depot shall be removed. As Tseng et al. (2004) proposed, when cargo enters a free trade zone after security check, it shall be an enterprise’s decision whether to store it in a depot or not under consideration of its storage capacity and circulation efficiency. Storage in a depot shall not be compulsory since it is of enterprise’s own free will. To carry out free circulation of goods “within national territory but outside customs territory” and the exemption of customs intervention, Taiwan’s customs shall loosen their control more or shall be completely out of free trade zones.

All the customs need to do is to prevent cargo which is not declared to or cleared by the customs from moving in or out of a free trade zone. Facilitation of customs clearance and service of prompt handling can be attained by autonomous and liberalized circulation of goods whether they are to be declared to or cleared by the customs. Tseng et al. (2004) found that there is still high degree of customs control over Taiwan's free trade zones. The regulations— cargo must be stored in a depot, and the customs office may team up a combined audit taskforce to conduct on-line computerized inspection and physical inventory of the goods— seem to apply the autonomous management concept of “within national territory but outside customs territory” to enterprises that do not need customs control in the zones. Customs shall adopt risk management to exempt cargo from customs clearance except cargo which enters a tax area or a bonded area or cargo which enters a free trade zone from a tax area or a bonded area shall be subject to the Regulations Governing Import/Export of Commodities. This study also suggests that some amendment shall be made to the Act for the Establishment and Management of Free trade zones. Some researchers have stated that a legalized dedicated-unit shall be set up in a free trade zone as a science and industrial park in Taiwan so that a single-window combining administration and management and the division of authority powers and responsibilities can be actualized; for example, the customs can issue approved documents for cargo clearance within 24 h (Chang et al., 2014). A researcher has indicated that a free trade zone can accelerate the integration of its information system into customs' computers and enterprises' information platform to assure enterprises' rights and interests (Shen, 2013). Another researcher pointed out that customs procedures shall be simplified, customs clearance shall be facilitated, customs service fees shall be reduced, and customs declaration and clearance mechanism within or outside a free trade zone shall be clearly divided (Chen, 2008).

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