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ALERT

NY Fed Finds Apparent Narrowing of U.S.-China Trade Deficit Largely Attributable to $10 Billion of Duty Evasion

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Tariff evasion has been a growing problem for years, but the scale of the problem has reached unprecedented levels. Economists at the Federal Reserve Bank of New York and Board of Governors of the Federal Reserve System recently found that "much of the decline" in the U.S.-China trade deficit was due to duty evasion schemes. While U.S. trade data appeared to show a narrowing of trade volume between China and the United States, the analysis proposes that this narrowing is overstated due to U.S. importers underreporting Chinese imports and, to a lesser extent, Chinese exporters reporting higher exports to take advantage of new Chinese tax incentives. According to these findings, the United States lost approximately $10 billion in tariff revenue due to U.S. companies' underreporting.

The article's authors, Hunter Clark and Anna Wong, noted that the discrepancies between Chinese- and U.S.-reported trade statistics indicated that evasion was likely occurring. U.S. trade statistics showed a significant decrease in 2018-2020 imports from China. The decline coincides with the imposition of Section 301 duties on hundreds of billions of dollars of Chinese imports during the Trump Administration. However, after initially reflecting a decline in exports from 2018-2019, the Chinese trade statistics showed an increase in exports to the United States from 2019-2020.

Although it is illegal to do so, some U.S. companies importing goods from China have incentives to misreport their imports, due to the substantial tariffs on these products. According to the findings, importers are likely reporting import prices to U.S. Customs and Border Protection (Customs or CBP) based on "low-ball" invoiced

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prices, which would decrease the amount of duties collected but not reflect the actual cost of the imported merchandise. Other common evasion techniques may also contribute to the exaggerated decline in the trade deficit, including mislabeling the country of origin, misclassifying imported products, or misidentifying sales through affiliated companies.

The researchers' conclusions are consistent with an increase in the number of trade remedy evasion findings made by CBP, the agency responsible for collecting all customs duties and investigating allegations of duty evasion, misclassification, and undervaluation. While Customs carefully analyzes trade data to detect potential instances of fraud, it also relies heavily on allegations from U.S. producers and importers harmed by unfair trade practices.

Evasion schemes not only deprive the U.S. Treasury of duties, they harm U.S. producers and importers that comply with U.S. trade laws, as they may lose billions in sales each year to competitors engaging in duty evasion. Wiley has a robust Customs Law and Compliance practice, as well as unparalleled experience and expertise in International Trade, Trade Analytics, and Supply Chains and can help clients navigate evolving developments in these areas.

Should you have questions on tariff relief, evasion investigations, import/export trends, or international trade generally, please contact one of the authors listed on this alert.