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## THE NEED TO REDUCE TARIFFS ON NON-LEATHER GOODS

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### INTRODUCTION

Since World War II, tariffs and other barriers to trade have fallen dramatically as the United States and its economic partners have liberalized the trade of goods and services across borders.<sup>1</sup> On net, these changes have produced tremendous gains for the average citizen.<sup>2</sup> One analysis estimates that between 1950 and 2016, trade liberalization and globalization more broadly has produced approximately \$2.1 trillion dollars in additional gross domestic product (GDP), adjusted for inflation.<sup>3</sup> Likewise, it is estimated that U.S. “GDP per capita and GDP per household . . . increased by \$7,016 and \$18,131” (adjusted for inflation) and that “disproportionate gains probably accrue to poorer households.”<sup>4</sup> However, not all of the gains from globalization have been shared equitably.

In 2016, a now-famous paper, colloquially known as the “China Shock,” found that admitting China into the World Trade Organization in 2001 led to a flood of imports from the country, which displaced up to approximately 2 million domestic manufacturing jobs over a 10 year period.<sup>5</sup> There was plenty of pushback on the China Shock, but the paper added intellectual fuel to the anti-globalization fire.<sup>6</sup> For example, the Trump administration used the paper’s find-

ings, in part, to justify its trade war with Beijing.<sup>7</sup> Yet even the authors of the China Shock do not blame trade liberalization per se for legitimate problems; rather, they see this as a larger story about how certain labor markets in concentrated areas did not adjust as quickly or efficiently as economists believed they would.<sup>8</sup> In fact, the authors are skeptical that erecting new tariffs or trade restrictions would do much to revive domestic manufacturing; in an update to their original findings, the economists note: “We are aware of no research that would justify ex-post protectionist trade measures as a means of helping workers hurt by past import competition.”<sup>9</sup>

On net, though, globalization has withstood the test of time, proving itself to be overwhelmingly beneficial for society. A recent study that surveyed economists found strong consensus in favor of trade liberalization and skepticism of trade barriers.<sup>10</sup>

While tariffs and trade barriers have generally fallen in the United States, persistently high tariffs on a small number of products and services exist, all of which can have detrimental social effects. For example, in 2012, the United States Department of Commerce imposed heavy anti-dumping duties on solar cells imported from China.<sup>11</sup> In 2018, the United States again imposed heavy tariffs on imported solar from basically every country.<sup>12</sup> In both of these instances, the U.S. government was responding to domestic complaints about import competition from foreign solar producers. These policy choices may help bolster the domestic solar manufacturing industry, but they raise prices for consumers, which in turn slows the deployment of clean energy.<sup>13</sup> Intentionally increasing the price of solar products hinders efforts to aggressively confront climate change.

This is just one example of tariffs and trade policies that cause negative externalities for society—beyond the simple economics of the product in question—but there are myriad examples. This policy brief will present a case study of another example.

### BRIEF CASE STUDY: LEATHER APPAREL AND FOOTWEAR

Minute distinctions in the tariff code have serious consequences, which guide the commercial decisions of many American companies. This is especially true in certain industries—like apparel and footwear—that are both highly import-dependent and face dramatic swings in tariff rates for minor product differences.

These industries actively engage in “tariff engineering” wherein they consider the tariff code when designing a product. In 2019, *Marketplace*, a weekday radio show on National Public Radio (NPR), profiled Columbia Sportswear’s efforts to design clothing based on tariff differences.<sup>14</sup> By way of

example, *Marketplace* explained:

Women's or girls' blouses, shirts and shirt-blouses of man-made fibers imported from other countries can get tariffed as high as 26.9% . . . But here's a little loophole: If the garments have "pockets below the waist, a ribbed waistband or other means of tightening at the bottom of the garment," they get to be excluded from this category. So if you took that same type of blouse with a 26.9% duty rate and added a pocket or two below the waist, it would instead get tariffed at a rate of 16%.<sup>15</sup>

Another high-profile example of this phenomenon is the existence of felt on the bottom of Converse All Star shoes. Shoes with "outer soles of rubber ... and uppers of textile materials" face tariffs ranging from 20-48 percent. But with a little felt covering the outside of the shoe's sole, the shoe becomes classified as a "slipper" for purposes of the tariff code, "which guarantees the rate of 3 percent."<sup>16</sup> These types of seemingly random distinctions occur all throughout the tariff code, which may explain why one sportswear executive ironically told *Marketplace*, "the real designers of apparel and footwear in this country live on Capitol Hill."<sup>17</sup>

### Leather-Based Tariff Differences

There are numerous products that face significantly lower tariffs if they are made of leather as opposed to other materials. Consider handbags. Generally speaking, if a purse is valued over \$20 and has an "outer surface of leather," it will enter the United States under tariff line 4202.21.90 of the Harmonized Tariff Schedule (HTS) with a duty of 9 percent.<sup>18</sup> If a leather purse valued over \$20 comes from a country the United States has a free trade agreement (FTA) with—Australia, Bahrain, Canada, Chile, Colombia, Israel, Jordan, South Korea, Morocco, Mexico, Oman, Panama, Peru, Singapore, Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, Nicaragua—or from a country with preferential market access established by Congress, such as the African Growth and Opportunity Act (AGOA) bloc, the purse enters the country duty free.<sup>19</sup> If that same bag instead has an "outer surface of sheeting of plastics," it enters under a different tariff line—4202.22.1500—of the HTU with a tariff rate of 16 percent.<sup>20</sup> With this composition, the bag would enter the United States with a zero percent tariff if it originated in the countries with which the United States has an FTA or the AGOA countries.<sup>21</sup> If the bag had an outer surface that is mostly composed of "man-made fibers," the tariff rises to 17.6 percent under HTU 4202.22.81, and again, enters the country duty-free if it originates from in a country with which the United States has an FTA or an AGOA country.<sup>22</sup>

The difference is even more dramatic for footwear. A pair of men's shoes made mostly of leather with a rubber sole could enter the United States under HTU 6403.99.60 with a tar-

iff of 8.5 percent.<sup>23</sup> The same shoes would enter the United States tariff-free if they originated from certain countries with which the United States has an FTA, though such shoes are not part of the AGOA.<sup>24</sup> Change the leather in the shoe to some other fabric like cotton and the tariff rises to 37.5 percent.<sup>25</sup>

This is not unique to handbags and footwear. Similar tariff differences exist between leather and non-leather for winter coats, vests, wallets, suitcases and other products.<sup>26</sup> In other words, Congress, through the HTS, has established lower tariffs, generally, on leather products versus similar products made from other materials.

### Externalities

Such differences matter beyond the simple economics involved in leather because of something economists recognize as "externalities," which are "situations when the effect of production or consumption of goods and services imposes costs or benefits on others which are not reflected in the prices charged for the goods and services being provided."<sup>27</sup> Externalities can be either positive or negative for third parties not involved in the transaction. In the case of leather, the true costs of production are not borne entirely by consumers, but rather by society at large.

Most leather products come from cattle, which are the top agricultural source of greenhouse gases.<sup>28</sup> As an air quality specialist recently put it: "Each year a single cow will belch about 220 pounds of methane. Methane is shorter lived than carbon dioxide but 29 times more potent in warming the atmosphere."<sup>29</sup> Likewise, leather is tanned often using various chemicals including chromium.<sup>30</sup> Though beyond the scope of this policy brief, such chemicals can cause a number of environmental problems—another externality.<sup>31</sup>

### RECOMMENDATIONS

Where clear externalities exist, R Street has been supportive of efforts to tax such transactions. This is the textbook way to deal with externalities so that producers and consumers internalize the costs of certain transactions. That is the guiding principle behind our support of a carbon tax in the case of global warming, for example.<sup>32</sup> In this case, the federal government could levy a tax on leather in order to discourage its production and consumption. In order to maintain consistency with basic World Trade Organization rules, such a tax would have to be applied to both imported leather and domestically produced leather. Given the political economy involved and the strength of various lobbies involved, this is probably a nonstarter.

The smarter, more politically realistic response would be to at least stop essentially subsidizing leather by lowering

tariffs on similar products made with materials other than leather. There is simply no good reason for the various tariff differences described above. To be clear, this is not an argument in favor of raising leather tariffs. Rather, policymakers should lower—or at least equalize—tariffs on non-leather products that directly compete with leather products.

Over the long term, policymakers should create a commission—or task the International Trade Commission—to study other perverse incentives and externalities created by various tariff disparities. Focus should be on environmental and health externalities. If policymakers are serious about addressing climate change, it simply belies common sense to impose much higher tariffs on products with lower societal impact.

## CONCLUSION

On net, trade liberalization has been overwhelmingly positive for the United States and people around the world. However, there are still perverse incentives created by various tariff differences between like-products that create externalities for society at large. In an ideal world, policymakers would simply unilaterally eliminate all existing tariffs since they are regressive sales taxes borne by consumers, but history and political economy demonstrate that such actions are almost impossible politically. Policymakers should lower tariffs on socially beneficial products such as leather substitutes and be more mindful of potential social harms they may be unintentionally creating by establishing various tariff disparities.

## ABOUT THE AUTHORS

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