

**Testimony before the U.S.-China Economic and Security Review Commission,
U.S.-China Relations in 2021: Emerging Risks**

U.S. Trade with Hong Kong and the Potential for Duty Evasion, September 8, 2021

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I. Introduction

This testimony focuses on the how the United States' import trade with Hong Kong has shifted in recent years, and the extent to which recent trade flows suggest evasion of U.S. import duties, particularly duties applicable to Chinese-origin merchandise under Section 301 of the Trade Act of 1974.

I begin with a background discussion of recent developments in the United States' treatment of imports from Hong Kong, including the suspension of certain special treatment accorded to Hong Kong under the United States-Hong Kong Policy Act of 1992. I also discuss the imposition of Section 301 duties on goods of China, and how this has incentivized Chinese producers and exporters, and unscrupulous U.S. importers, to engage in duty evasion schemes.

Next, I review historical and recent trends in imports into the United States from Hong Kong, focusing on how trade flows from Hong Kong have shifted since Section 301 duties were first imposed on Chinese-origin goods. I discuss the extent to which these data suggest that goods of Chinese origin are being transshipped through Hong Kong and other Southeast Asian countries, in a bid to conceal their origin and avoid lawful U.S. import duties. While these data do not suggest – yet – that Hong Kong is a major transshipment hub, the territory has been used as a transshipment hub in the past, particularly with respect to textiles. Further, transshipment writ large is a substantial problem, with Chinese companies going to great lengths to conceal the origin of their goods by transshipping them through countries like Vietnam.

To combat existing and future transshipment, the United States should consider at least three strategies. These include (1) increased funding for transshipment-focused targeting and enforcement; (2) expanding the reach of the Enforce and Protect Act (EAPA) to cover action to evade Section 301 duties; and (3) implementing new legislation similar to the existing 19 U.S.C. § 1592a, to “name-and-shame” transshippers and raise awareness in the trade community as to the companies engaging in the practice.

¹ This testimony reflects the personal views of the author and not necessarily the views of her firm or the firm's clients.

II. Recent Developments in the United States' Trade and Tariff Treatment of Hong Kong

In 1992, five years in advance of the return of Hong Kong to Chinese sovereignty, Congress enacted the United States-Hong Kong Policy Act.² The Act reflected Congress's position that the United States should continue to "respect Hong Kong's status a separate customs territory" and a signatory in its own right to the General Agreement on Tariffs on Trade, which forms the backbone of the World Trade Organization agreements.³ However, the Act also provided the President of the United States with authority to declare, at any time on or after July 1, 1997, that Hong Kong was no longer sufficiently autonomous to justify special treatment under a particular U.S. law, and to suspend such treatment.⁴ In 2019, the Act was amended to require the Secretary of State to report annually to Congress regarding Hong Kong's autonomy and status.⁵

On May 28, 2020, then-Secretary of State Mike Pompeo released the annual Hong Kong Policy Act Report for 2020.⁶ In that report, the Secretary stated that he could "no longer certify that Hong Kong continues to warrant" treatment different from China under U.S. law.⁷ Secretary Pompeo pointed specifically to the erosion of political liberties in the territory, as well the Chinese government's May 22, 2020 announcement that it would soon impose new national security legislation on Hong Kong.⁸ On the same day that Secretary Pompeo issued his report, China's National People's Congress approved the enactment of this national security legislation.⁹

On July 16, 2020, then-President Trump issued Executive Order 13936, titled "The President's Executive Order on Hong Kong Normalization."¹⁰ In that order, the President declared that Hong Kong was no longer sufficiently autonomous to warrant treatment distinct from that of China for certain purposes.¹¹ He stated that the United States' policy, going forward, "shall be to suspend or eliminate differential and preferential treatment for Hong Kong to the extent permitted by law."¹² In the Executive Order, the

² United States-Hong Kong Policy Act, Public Law 102-383 (Oct 5, 1992), 106 Stat. 1448.

³ *Id.* at Section 102.

⁴ *Id.* at Section 202.

⁵ Hong Kong Human Rights and Democracy Act of 2019, Public Law 116-76 (Nov. 27, 2019).

⁶ U.S. Department of State, *2020 Hong Kong Policy Act Report* (May 28, 2020), available at <https://www.state.gov/2020-hong-kong-policy-act-report/>.

⁷ *Id.*

⁸ *Id.*

⁹ Congressional Research Service, *Revoking Hong Kong's Preferential Trade Status: Legal Framework and Implications* (Apr. 2, 2021) at 1, available at <https://fas.org/sgp/crs/row/LSB10488.pdf>.

¹⁰ *The President's Executive Order on Hong Kong Normalization*, E.O. 13936, 85 Fed. Reg. 43,413 (July 14, 2020) ("Executive Order 13936").

¹¹ *Id.* at 43,413.

¹² *Id.* at 43,414.

President specifically suspended special treatment for Hong Kong under 19 U.S.C. § 1304,¹³ a statute that requires goods imported into the United States to be marked with their country of origin.¹⁴ However, the Executive Order did not require Hong Kong to be treated equivalently with China for purposes of special import duties, such as the duties imposed on Chinese-origin products under Section 301 of the Trade Act of 1974.¹⁵

U.S. Customs and Border Protection (“CBP”) subsequently issued Cargo Systems Message 43633414 on August 11, 2020.¹⁶ The agency stated that it would provide importers with a transition period lasting until September 25, 2020 in which to adjust the marking of goods produced in Hong Kong to reflect China as the country of origin.¹⁷ CBP’s message did not indicate that products of Hong Kong would be treated as Chinese for purposes of Section 301 duties.¹⁸ CBP later posted guidance to its website confirming that Section 301 duties were not applicable to goods produced in Hong Kong.¹⁹

Hong Kong subsequently filed a complaint against the new marking requirements with the World Trade Organization.²⁰

III. The Imposition of Section 301 Duties on Chinese-Origin Goods

On August 24, 2017, at the request of the President, the Office of the U.S. Trade Representative (“USTR”) initiated an investigation under Section 301 of the Trade Act of 1974 into the Government of China’s acts, policies, and practices related to technology transfer, intellectual property, and innovation.²¹ Consistently with Section 301, the investigation sought to determine whether the investigated practices were unreasonable or discriminatory, such that they burdened or restricted U.S. commerce.²² After

¹³ *Id.*

¹⁴ 19 U.S.C. § 1304.

¹⁵ See Executive Order 13936.

¹⁶ CSMS # 43633412 – GUIDANCE: New Marking Rules for Goods Made in Hong Kong – Executive Order 13936 (August 11, 2020), *available at* <https://content.govdelivery.com/accounts/USDHSCBP/bulletins/299cb04>.

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ U.S. Customs & Border Protection, “Section 301 Trade Remedies Frequently Asked Questions,” *available at* <https://www.cbp.gov/trade/programs-administration/entry-summary/section-301-trade-remedies/faqs>.

²⁰ See, e.g., *WTO Dispute Settlement Proceeding Regarding United States – Origin Marking Requirement (Hong Kong, China)*, 86 Fed. Reg. 13,960 (USTR Mar. 11, 2021). Hong Kong alleges that the marking requirement violates various articles of the General Agreement on Tariffs and Trade, the Agreement on Rules of Origin, and the Agreement on Technical Barriers to Trade. The WTO’s Dispute Settlement Body established a panel to consider the complaint on April 30, 2021.

²¹ *China’s Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation* (82 Fed. Reg. 40,213 (USTR Aug. 24, 2017)) (initiation of Section 301 investigation).

²² *Id.*

collecting written comments and holding a hearing, USTR issued a report on March 22, 2018, in which it found a variety of Chinese policies and practices to be unfair and burdensome.²³ On April 6, 2018, USTR published a notice of its determination in the *Federal Register*, and indicated that it proposed to take action by imposing additional duties on a range of Chinese goods.²⁴

Ultimately, duties were applied in four stages. For each stage, duties were applied to specific goods based on tariff line – that is, the eight-digit classification of specific goods under the Harmonized Tariff Schedule of the United States (“HTSUS”).²⁵ The first stage, often termed “Tranche 1,” covered tariff lines accounting for approximately \$34 billion in yearly imports from China.²⁶ Duties became effective at a rate of 25% as to Tranche 1’s tariff lines on July 6, 2018.²⁷ The tariff lines covered by Tranche 1 were primarily located in Chapters 84 and 85 of the United States’ tariff schedule, covering machinery and electronics.²⁸ The “Tranche 2” duties, covering additional tariff lines accounting for approximately \$16 billion in yearly imports of Chinese goods, went into effect at a duty rate of 25% on August 23, 2018.²⁹ This tranche included tariff lines associated with additional machinery, plastics, certain vehicles, and optical and measuring devices.³⁰ The “Tranche 3” duties, covering additional tariff lines accounting for approximately \$200 billion in annual imports, went into effect on September 24, 2018, at a duty rate of 10%.³¹ This tranche covered a broad range of goods including foods, chemicals, wood products, leather, certain textiles, metals and metal products, but did not cover apparel or footwear.³² Duties were raised on goods subject to this tranche effective May 10, 2019, with a short grace period for goods that had already been exported from China by May 10.³³ The fourth tranche of duties covered a similarly broad range of goods,

²³ Office of the United States Trade Representative, *Findings of the Investigation into China’s Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation Under Section 301 of the Trade Act of 1974* (Mar. 22, 2018), available at <https://ustr.gov/sites/default/files/Section%20301%20FINAL.PDF>.

²⁴ *China’s Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation* (83 Fed. Reg. 14,906 (USTR Apr. 6, 2018) (notice of determination and request for public comment concerning proposed determination of action pursuant to Section 301).

²⁵ See, e.g., *China’s Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation* (83 Fed. Reg. 28,710 (USTR June 20, 2018) (notice of action and request for public comment concerning proposed determination of action pursuant to Section 301).

²⁶ *Id.*

²⁷ *Id.*

²⁸ *Id.*

²⁹ *China’s Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation* (83 Fed. Reg. 40,823 (USTR Aug. 16, 2018) (notice of action pursuant to Section 301).

³⁰ *Id.*

³¹ *China’s Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation* (83 Fed. Reg. 47,974 (USTR Sept. 21, 2018) (notice of modification of Section 301 action).

³² *Id.*

³³ *China’s Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation* (84 Fed. Reg. 21,892 (USTR May 15, 2019) (implementing modification of Section 301 action);

including certain apparel and footwear.³⁴ These duties went into place on September 1, 2019, at a rate of 15%.³⁵ The Tranche 4 duties were halved to 7.5% effective February 14, 2020.³⁶ Since then, no additional tranches of duties have been imposed; nor have any of the existing tranches been modified.

IV. Historical and Recent Trends in U.S. Imports from Hong Kong

Since 1990, U.S. imports from Hong Kong have remained under \$12 billion each year. By comparison, the value of imports from china in January of this year alone was more than \$39 billion.³⁷

During the 1990s, the annual value of U.S. imports from Hong Kong rose gradually, from just under \$10 billion in 1990 to a highwater mark of just under \$11.5 billion in 2000, the year before China joined the World Trade Organization.³⁸ From 2001 through 2008, import volumes from Hong Kong fell gradually from \$10.5 billion to \$6.5 billion.³⁹ In 2009, as the global recession deepened, imports into the United States from Hong Kong fell to \$3.6 billion.⁴⁰ From 2010 – 2017, as the effects of the recession diminished, they gradually returned to pre-precession levels, rising to \$7.4 billion in 2017, the year before Section 301 tariffs began to be imposed on goods from China.⁴¹

Section 301 duties were first imposed on Chinese-origin goods on July 6, 2018, and by September 24, 2018, duties had been imposed on tariff lines accounting for \$250 billion

China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation (84 Fed. Reg. 20,459 (USTR May 9, 2019) (notice of modification of Section 301 action).

³⁴ *China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation* (83 Fed. Reg. 45,821 (USTR Aug. 30, 2019) (notice of modification of Section 301 action). The fourth tranche covered tariff lines accounting for approximately \$300 billion in annual imports from China. However, it was divided into two sub-tranches, Tranche 4A and 4B. Duties were ultimately imposed only on tariff lines included in Tranche 4A. While duties were originally intended to go into effect on Tranche 4B tariff lines on December 15, 2019, the imposition of such tariffs was indefinitely suspended in the wake of "Phase 1" trade agreement between the United States and China. *China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation* (83 Fed. Reg. 69,447 (USTR Dec. 18, 2019) (notice of modification of Section 301 action).

³⁵ *Id.*

³⁶ *China's Acts, Policies, and Practices Related to Technology Transfer, Intellectual Property, and Innovation* (84 Fed. Reg. 3,741 (USTR Jan. 22, 2020) (notice of modification of Section 301 action).

³⁷ U.S. Census Bureau, Trade in Goods with Hong Kong, *available at* <https://www.census.gov/foreign-trade/balance/c5820.html>; U.S. Census Bureau, Trade in Goods with China, *available at* <https://www.census.gov/foreign-trade/balance/c5700.html>.

³⁸ U.S. Census Bureau, Trade in Goods with Hong Kong, *available at* <https://www.census.gov/foreign-trade/balance/c5820.html>.

³⁹ *Id.*

⁴⁰ *Id.*

⁴¹ *Id.*

in annual imports from China.⁴² Additional tariff lines were subjected to duties starting on September 1, 2019.⁴³

To evaluate the impact of the Section 301 duties on imports into the United States from Hong Kong – and particularly to examine whether Chinese goods may have been re-routed through Hong Kong and subsequently imported into the United States as duty-exempt goods of Hong Kong, I reviewed official import statistics for annual and quarterly imports from Hong Kong from 2016-2020.

The United States' tariff schedule is divided into sections according to the general nature of imported goods, and further divided into tariff chapters, headings, subheadings, etc.⁴⁴ Based on a review of import statistics collected by the U.S. International Trade Commission, prior to the imposition of Section 301 tariffs, the vast majority of U.S. imports from Hong Kong consisted of miscellaneous articles (including optical equipment, works of art, furniture, toys, and goods classified in special provisions for articles reimported after export from the United States, etc.),⁴⁵ machinery and equipment, and precious metals/jewelry.⁴⁶ In 2017, goods in these categories accounted for 86.6% of U.S. imports from Hong Kong.⁴⁷ Between 2018-2020, the percentage of U.S. imports from Hong Kong accounted for by goods in these categories grew from 85.7% to 93.9%.⁴⁸

In 2017, U.S. imports from Hong Kong totaled \$6.8 billion.⁴⁹ In 2018, U.S. imports of Hong Kong fell to just over \$6.1 billion.⁵⁰ The vast majority of this decrease was due to a decline in imports of precious metals and jewelry, which fell by 11%, from \$1.26 billion in 2017 to just under \$800,000 in 2018.⁵¹ The year 2019, the first full year in which Section 301 duties were in effect, saw a more precipitous overall drop in imports, from \$6.1 billion in 2018 to \$4.6 billion.⁵² The majority of this year-on-year decrease was

⁴² See discussion at 4-5, *supra*.

⁴³ *Id.*

⁴⁴ Harmonized Tariff Schedule of the United States, *available at* <https://hts.usitc.gov/current>.

⁴⁵ A substantial percentage of U.S. imports from Hong Kong of “miscellaneous” items enter under tariff line 9801.00.10, applicable to U.S.-origin articles and previously-imported articles exported and then returned without being advanced in value. \$2.2 billion in such products entered the United States in 2016. In 2018, the year in which Section 301 duties started to take hold on goods of China, the level of imports from Hong Kong under this tariff line equaled \$2.5 billion. By 2020, the number fell to \$1.2 billion. U.S. International Trade Commission, Dataweb, U.S. Imports for Consumption from Hong Kong under tariff heading 9801 and tariff line 9801.00.10, 2016-2021.

⁴⁶ U.S. International Trade Commission, Dataweb, U.S. Imports for Consumption from Hong Kong, 2016-2021.

⁴⁷ *Id.*

⁴⁸ *Id.*

⁴⁹ *Id.*

⁵⁰ *Id.*

⁵¹ *Id.*

⁵² *Id.*

attributable to a steep decline in imports of machinery and equipment, from \$1.3 billion in 2018 to less than \$600,000 in 2019.⁵³

2020 was notable for a spike in imports from Hong Kong. Overall import value rose from \$4.6 billion in 2019 to \$7.9 billion in 2020, an amount higher than any year since 2006.⁵⁴ Nearly all of this increase was attributable to a sudden jump in imports of precious metal and jewelry.⁵⁵ Nearly \$5.5 billion in precious metal and jewelry entered the United States from Hong Kong in 2020.⁵⁶ Notably, the vast majority of these imports entered the United States in just two months – April and May of 2020.⁵⁷

Looking closer at this import spike, the importers were clustered in just two tariff headings, 7115 and 7108.⁵⁸ These cover articles of precious metal or metal clad with precious metal (heading 7115) and gold, including platinum-plated gold, in unwrought or semi-manufactured forms.⁵⁹ These headings would cover, for example, gold or silver bars, blanks for gold coins, or gold flakes. The vast majority of these imports (\$5.2 billion), entered the United States through the Port of New York.⁶⁰

After spiking in the second quarter of 2020, imports under these tariff headings, and under tariff codes generally applicable to precious metals and jewelry, fell back to levels consistent with prior years' quarterly import levels, of approximately \$165 million - \$300 million per quarter.⁶¹

To put these figures into context, U.S. imports of goods under headings 7115 and 7108 increased from all countries increased significantly starting in March of 2020.⁶² In January of 2020, total U.S. imports under these headings were approximately \$800 million.⁶³ In March, this rose to \$4.3 billion, and peaked at \$14.8 billion in June of 2018.⁶⁴ U.S. imports of gold have remained elevated, compared to historical levels,

⁵³ *Id.*

⁵⁴ *Id.*

⁵⁵ *Id.*

⁵⁶ *Id.*

⁵⁷ *Id.*

⁵⁸ U.S. International Trade Commission, Dataweb, U.S. Imports for Consumption from Hong Kong under tariff chapter 71, 2016-2021.

⁵⁹ Chapter 71, Harmonized Tariff Schedule of the United States, *available at* <https://hts.usitc.gov/current>.

⁶⁰ U.S. International Trade Commission, Dataweb, U.S. Imports for Consumption from Hong Kong under tariff chapter 71, 2016-2021.

⁶¹ *Id.*

⁶² U.S. International Trade Commission, Dataweb, U.S. Imports for Consumption under tariff chapter 71, 2016-2021.

⁶³ *Id.*

⁶⁴ *Id.*

since the global coronavirus took hold.⁶⁵ This is not surprising, given that imports of gold tend to increase during times of economic uncertainty.

During March-June of 2020, imports of gold spiked not just from Hong Kong, but from other territories known as financial and banking hubs, like Switzerland and Switzerland. For example, imports into the United States from Switzerland under tariff headings 7108 and 7115 rose from \$67 million in January 2020 to nearly \$8.5 billion in May of 2020.⁶⁶ Imports into the United States from Singapore under the same tariff headings rose from \$1.3 million in January 2020 to \$1.4 billion in May 2020.⁶⁷

From January-June 2021, the value of U.S. imports from Hong Kong equaled \$1.8 billion.⁶⁸ On an annualized basis, imports in 2021 are projected to be lower than in at any time since 2009, when they equaled \$3.6 billion.⁶⁹

V. Hong Kong and Transshipment of Chinese Goods

With the imposition of Section 301 duties on Chinese goods, companies importing Chinese-origin goods had an incentive to take actions to avoid the impact of the duties. Some of these actions were fully legal – such as moving production operations, in whole or in part, outside of China, so that their goods would no longer have Chinese origin under the test used by U.S. CBP to determine origin for duty purposes.⁷⁰

However, shifts in trade flows, as well as customs inspections, indicate that certain Chinese exporters, and/or the importers of their goods into the United States, have engaged in unlawful means of avoiding duties.⁷¹ One common scheme for avoiding increased duties on goods of a specific country is transshipment. In a transshipment

⁶⁵ *Id.*

⁶⁶ *Id.*

⁶⁷ *Id.*

⁶⁸ U.S. Census Bureau, Trade in Goods with Hong Kong, *available at* <https://www.census.gov/foreign-trade/balance/c5820.html>.

⁶⁹ *Id.*

⁷⁰ This test, known as the “substantial transformation test,” was developed by the federal courts in the wake of Congress’s enactment of 19 U.S.C. § 1304, the federal origin marking statute. The test defines origin based on the last country in which a product underwent a “substantial transformation” prior to importation, and defines a substantial transformation as occurring “when an article emerges from a manufacturing process with a name, character, and use that differs from the original material subjected to the processing.” *See United States v. Gibson-Thomsen Co.*, 27 C.C.P.A. 267 (C.A.D. 98) (1940). There, the Court of Customs and Patent Appeals found that “[a] substantial transformation occurs when an article emerges from a manufacturing process with a name, character, and use that differs from the original material subjected to the processing.” In practice, the test is highly fact-specific and often requires in-depth analysis of components and manufacturing processes.

⁷¹ *See, e.g.*, Chui-Wei Yap, “American Tariffs on China re Being Blunted by Trade Cheats,” *The Wall Street Journal* (June 26, 2019); “Vietnam to crack down on Chinese goods relabeled to beat U.S. tariffs,” *Reuters* (June 10, 2019).

operation, goods are routed through a third country so as to disguise their true origin. In the third country, they are generally relabeled or repacked with markings that indicate that they were produced there, rather than in the actual country of manufacture.

To the extent that Chinese companies chose to use Hong Kong as a transshipment hub for evading Section 301 duties, one would expect increased exports from Hong Kong coinciding with the imposition of Section 301 duties on particular product lines. For example, one might expect to see increased exports of machinery from Hong Kong in the third and fourth quarters of 2018, concurrently with the imposition of the first three tranches of Section 301 duties. However, U.S. imports of machinery from Hong Kong grew by only 2% from 2017-2018; the value of imports in this category fell sharply in 2019 from 2018 levels and remain depressed.⁷² Even when one considers machinery imports at a more granular level (for example, by reviewing imports of goods under the individual four-digit tariff headings of Chapters 84 and 85), the tariff headings do not reveal substantial increases after Section 301 duties were put into effect. Rather, the trend even at this level is one of substantial declines in imports, particularly between 2018-2019, and into 2020.⁷³

For example, in 2018, the United States imported \$109 million in goods from Hong Kong of tariff heading 8471, covering automatic data processing machines (computers) and parts thereof.⁷⁴ This fell to \$53 million in 2019, and \$31 million in 2020.⁷⁵ Likewise, in 2018, the United States imported from Hong Kong \$335 million in goods of tariff heading 8517, covering telephones (including cell/smartphones) and communication equipment such as routers and certain Bluetooth devices.⁷⁶ In 2020, this fell to \$175 million.⁷⁷

The lack of import growth suggests that China did not turn to Hong Kong as a transshipment hub for machinery,⁷⁸ but the severe drop-off in imports is harder to explain. After all, machinery produced in Hong Kong was, and remains, legitimately free of Section 301 duty liability. One possibility might be that while China did not seek to

⁷² U.S. International Trade Commission, Dataweb, U.S. Imports for Consumption from Hong Kong under tariff chapters 84 and 85, 2016-2021.

⁷³ *Id.*

⁷⁴ U.S. International Trade Commission, Dataweb, U.S. Imports for Consumption from Hong Kong under tariff heading 8471, 2016-2021.

⁷⁵ *Id.*

⁷⁶ U.S. International Trade Commission, Dataweb, U.S. Imports for Consumption from Hong Kong under tariff heading 8517, 2016-2021.

⁷⁷ *Id.*

⁷⁸ It also suggests that U.S. importers did not turn to Hong Kong as a place to legitimately move certain manufacturing operations so that the resulting products would be considered Hong Kong products under U.S. law. This may have been due to a lack of available capacity there, or because the imposition of Section 301 duties on Chinese goods led certain importers to be wary of production operations conducted anywhere under China's control.

use Hong Kong as a specific transshipment hub after the imposition of the Section 301 duties, the imposition of the duties led importers to realize that goods that they had previously imported as products of Hong Kong were actually of Chinese origin, and to reduce their import volumes accordingly.

Prior to the imposition of Section 301 duties, there were generally no duty differences between goods of Hong Kong and goods of China. This meant that, at least from a duty savings perspective, there was no reason to improperly import Chinese goods as goods of Hong Kong. This lack of duty risk may have led certain importers to pay less attention to the manufacturing processes and locations for their goods than would be ideal. Imposition of duties on Chinese products, however, provided importers with good reason to inquire closely into the manufacturing location of goods purchased from Hong Kong sellers, and otherwise to conduct the detailed, fact-specific analyses required to determine origin under the substantial transformation test. The results of these inquiries and analyses may have led importers to reduce imports, or otherwise to shift their sourcing patterns.⁷⁹

VI. Recommendations

While the import data that I have reviewed does not appear to reflect increased transshipment through Hong Kong in the wake of the Section 301 duties, the territory was a known transshipment hub in the past – particularly for textiles.⁸⁰ And transshipment of Chinese-origin goods to avoid Section 301 duties, as well as antidumping and countervailing duties, is a significant problem in countries like Vietnam.⁸¹ Indeed, U.S. imports from Vietnam grew by 26.5% from 2018-2019, and grew by an additional 20.9% in 2020, despite the trade-depressing effects of the

⁷⁹ The volume of U.S. goods imported from China did not fall immediately in the wake of the imposition of Section 301 duties. Indeed, by value, imports from China in the fourth quarter of 2018, when the first three tranches of Section 301 duties were newly in effect, increased slightly from \$141 billion in fourth quarter 2017 to just over \$144 billion. In 2019, imports from China fell significantly from 2018 levels, from \$538 billion to \$450 billion, a level slightly lower than the \$462 billion in imports seen in 2016. See U.S. Census Bureau, Trade in Goods with China, *available at* <https://www.census.gov/foreign-trade/balance/c5700.html>.

⁸⁰ See, e.g., Patrick Conway, “How transshipment may undercut Trump’s tariffs,” *The Conversation* (Apr. 26, 2018); “U.S. Customs Lists Textile Transshipment, Origin Rule Violators,” *American Shipper* (Oct. 10, 2001).

⁸¹ See, e.g., U.S. Customs & Border Protection, Notice of Action in EAPA Investigation 7250 (Aug. 10, 2021); Chuin-Wei Yap, “American Tariffs on China re Being Blunted by Trade Cheats,” *The Wall Street Journal* (June 26, 2019); “Prak Chan Thul, “U.S. fines firms transshipping via Cambodia to dodge Trump’s China tariffs,” *Reuters* (June 19, 2019); “Vietnam to crack down on Chinese goods relabeled to beat U.S. tariffs,” *Reuters* (June 10, 2019).

coronavirus pandemic.⁸² In the first six months of 2021, imports from Vietnam have grown by 46% compared with the same period in 2020.⁸³

Vietnam is far from alone in this regard. Trade data also shows significant growth in imports declared as originating in countries such as Thailand, Malaysia, and Taiwan, even as imports from China have fallen.⁸⁴ Some of this increase is likely due to lawful trade shifts, with companies moving meaningful aspects of their production operations out of China. But so long as duty differences exist between products produced in different countries, unscrupulous companies will have an incentive for unlawful duty evasion.

To combat transshipment and related practices both today and in the future, the United States should consider several actions, all of which would require Congressional action.

First, CBP should receive increased funding for investigating and addressing transshipment. CBP already has the authority to investigate transshipment and to penalize importers of transshipped goods under 19 U.S.C. § 1592(d), the general customs fraud statute. However, limited resources mean that the agency must triage its enforcement activities. Transshipment is a substantial enough problem to deserve additional, specific funding.

The United States should also consider expanding the reach of the Enforce and Protect Act, or EAPA. Passed as part of the Trade Facilitation and Trade Enforcement Act of 2015, EAPA authorized provided CBP with enhanced authority to combat the evasion of antidumping and countervailing duties.⁸⁵ Since the law's enactment, CBP has conducted more than 130 investigations into evasion of antidumping and countervailing duties, and identified more than \$600 million in duties owed.⁸⁶ Notably, many EAPA investigations involve transshipment of Chinese goods through third countries.⁸⁷

⁸² U.S. International Trade Commission, Dataweb, U.S. Imports for Consumption from Vietnam, 2016-2021.

⁸³ *Id.*

⁸⁴ U.S. International Trade Commission, Dataweb, U.S. Imports for Consumption from Malaysia, Taiwan, and Thailand, 2016-2021.

⁸⁵ Trade Facilitation and Trade Enforcement Act of 2015, Public Law 114-125 (Feb. 24, 2016), Title IV, Sec. 421.

⁸⁶ U.S. Customs & Border Protection, "Enforce and Protect Act (EAPA)", *available at* <https://www.cbp.gov/trade/trade-enforcement/tftea/eapa>.

⁸⁷ See, e.g., U.S. Customs & Border Protection, Notice of Action in EAPA Investigation 7250 (Aug. 10, 2021) (Chinese diamond sawblades transshipped through Thailand); U.S. Customs & Border Protection, Notice of Action in EAPA Investigation 7430 (Feb. 23, 2021) (Chinese activated carbon transshipped through Indonesia); Notice of Action in EAPA Investigation 7379 (Sept. 23, 2020) (Chinese wire garment hangers transshipped through India); Notice of Action in EAPA Investigation 7430 (Mar. 9, 2020) (Chinese xanthan gum transshipped through India); Notice of Action in EAPA Investigation 7270 (Sept. 25, 2019) (Chinese glycine transshipped through Thailand); Notice of Action in EAPA Investigation

CBP's successful use of EAPA to combat transshipment in the antidumping and countervailing duty context indicates that the EAPA process could be successfully used to combat evasion of other kinds of special duties, such as Section 301 duties. The process's timelines ensure that action is taken where information available to CBP reasonably suggests that transshipment is taking place.⁸⁸ This, in turn, allows the agency to quickly shut down illegal and distortive transshipment operations, and to collect lawful duties on goods previously imported through transshipment. The EAPA process also provides enhanced public visibility into the identities of bad actors, and complicates their ability to simply alter, rather than halt, their transshipment schemes.

Finally, the United States should consider enacting a statute similar to 19 U.S.C. § 1592a, a statute passed in the early 1990s, at a time when the United States still maintained a country-specific quotas on imports.⁸⁹ Among other things, this statutory provision requires CBP to publish, at least twice a year, the names of foreign entities and persons who have been issued penalties under the agency's general fraud statute for "engaging in practices which aid or abet the transshipment, through a country other than the country of origin" of textile products.⁹⁰ The statute also places a heightened requirement of "reasonable care" on importers that enter goods supplied by such persons or entities.

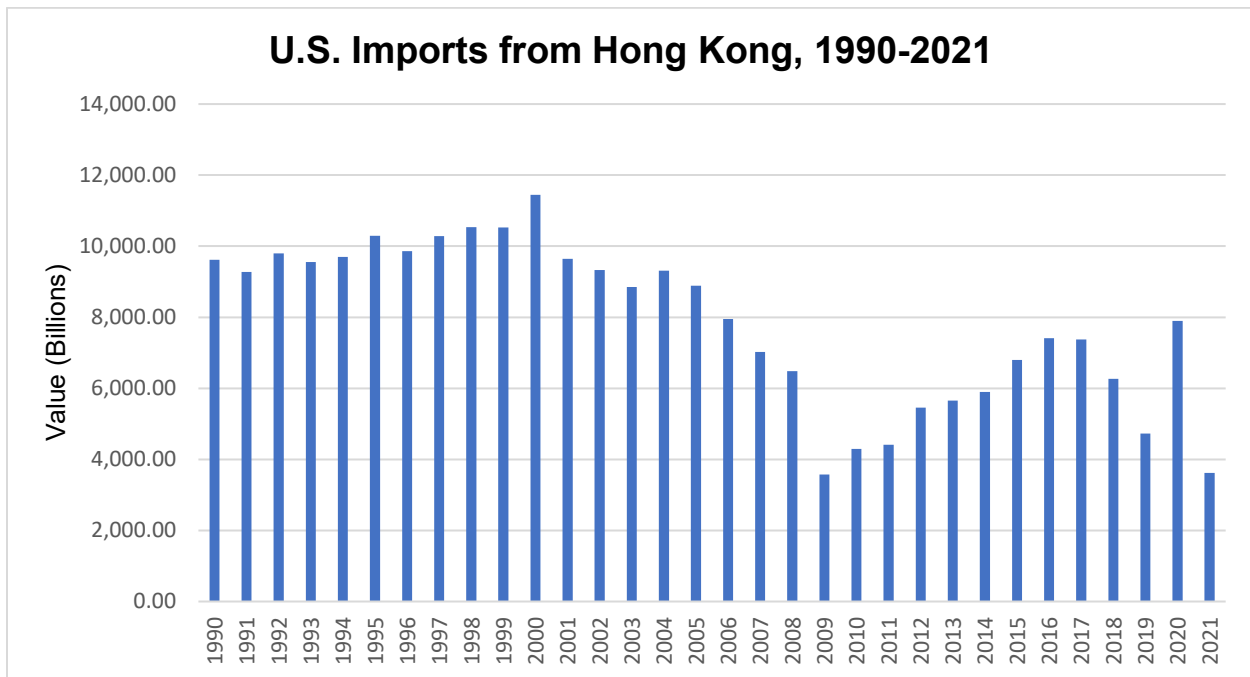
While 19 U.S.C. § 1592a applies only to transshipped textile products, it provides a model that could be used with respect to transshipment more broadly. Public naming and shaming of bad actors would bring heightened visibility to the problem of transshipment in the trade community. It would also provide useful information to importers that might otherwise believe that they were legitimately purchasing non-Chinese-origin goods.

7232 (Mar. 20, 2019) (Chinese aluminum products transshipped through Vietnam); Notice of Action in EAPA Investigation 7191 (Mar. 15, 2018) (Chinese wire garment hangers transshipped through Malaysia).

⁸⁸ 19 U.S.C. § 1517.

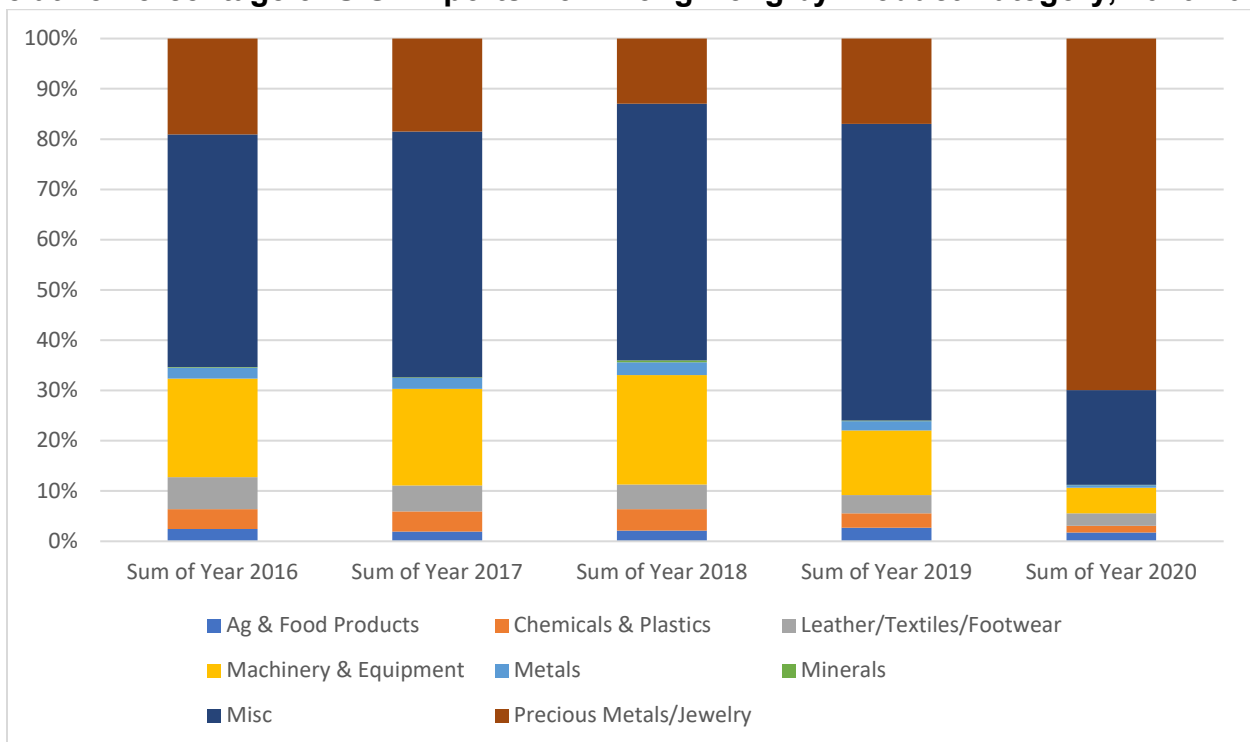
⁸⁹ The United States fully removed this quota system in 2005.

⁹⁰ 19 U.S.C. § 1592a.



Source: U.S. Census Bureau, Trade in Goods with Hong Kong⁹¹

Relative Percentage of U.S. Imports from Hong Kong by Product Category, 2016-2020



Source: U.S. International Trade Commission, Dataweb

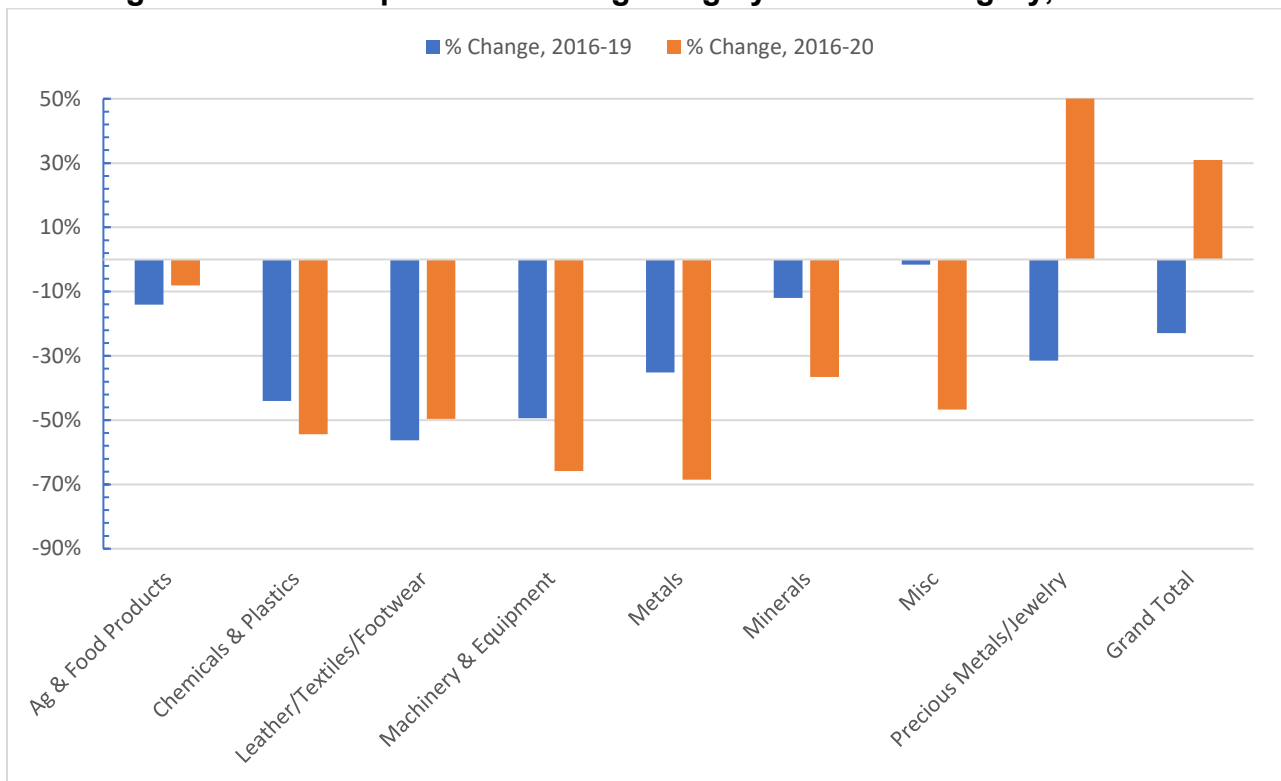
⁹¹ 2021 data have been annualized. From January-June 2021, U.S. import from Hong Kong were \$1.8. billion.

Year-on-Year Change in Value of Imports from Hong Kong by Product Category

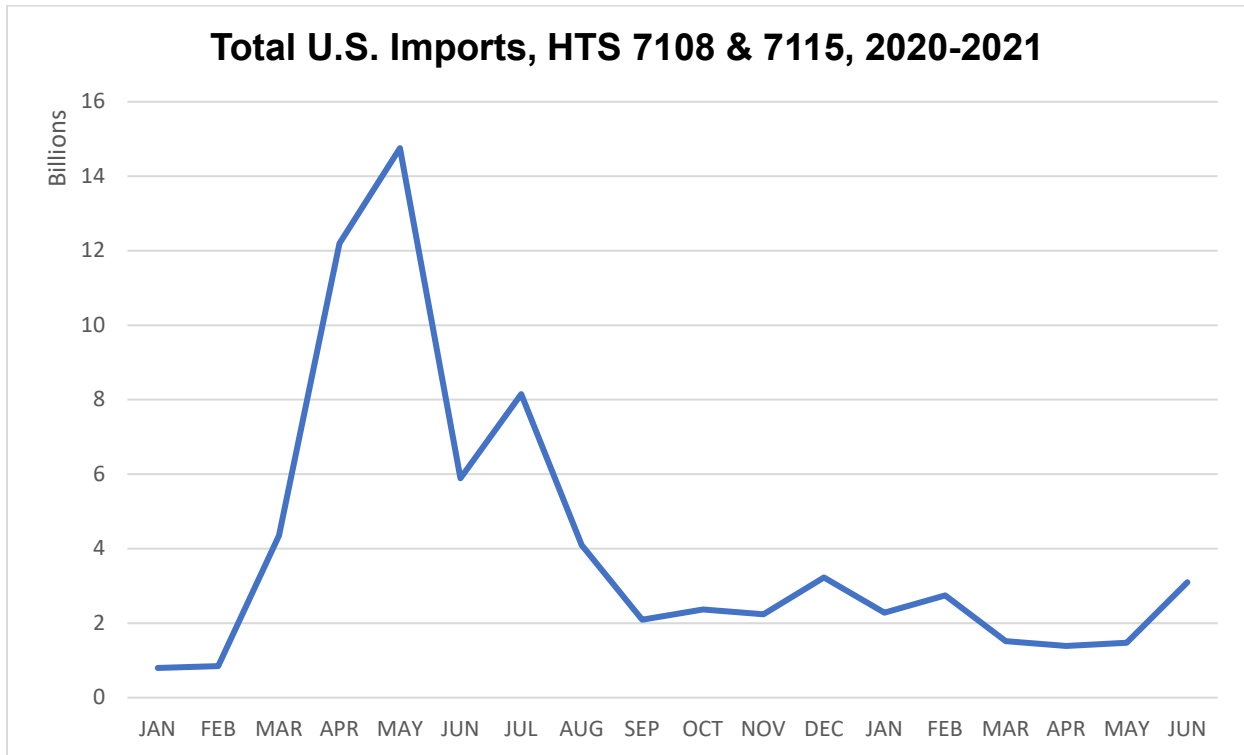
	<u>16-17</u>	<u>17-18</u>	<u>18-19</u>	<u>19-20</u>
Ag & Food Products	-11%	2%	-5%	7%
Chemicals & Plastics	17%	-5%	-50%	-18%
Leather/Textiles/Footwear	-8%	-14%	-45%	15%
Machinery & Equipment	12%	2%	-56%	-32%
Metals	11%	9%	-46%	-51%
Minerals	97%	80%	-75%	-28%
Misc	20%	-6%	-13%	-46%
Precious Metals/Jewelry	11%	-37%	-2%	600%
All	14%	-10%	-25%	70%

Source: U.S. International Trade Commission, Dataweb

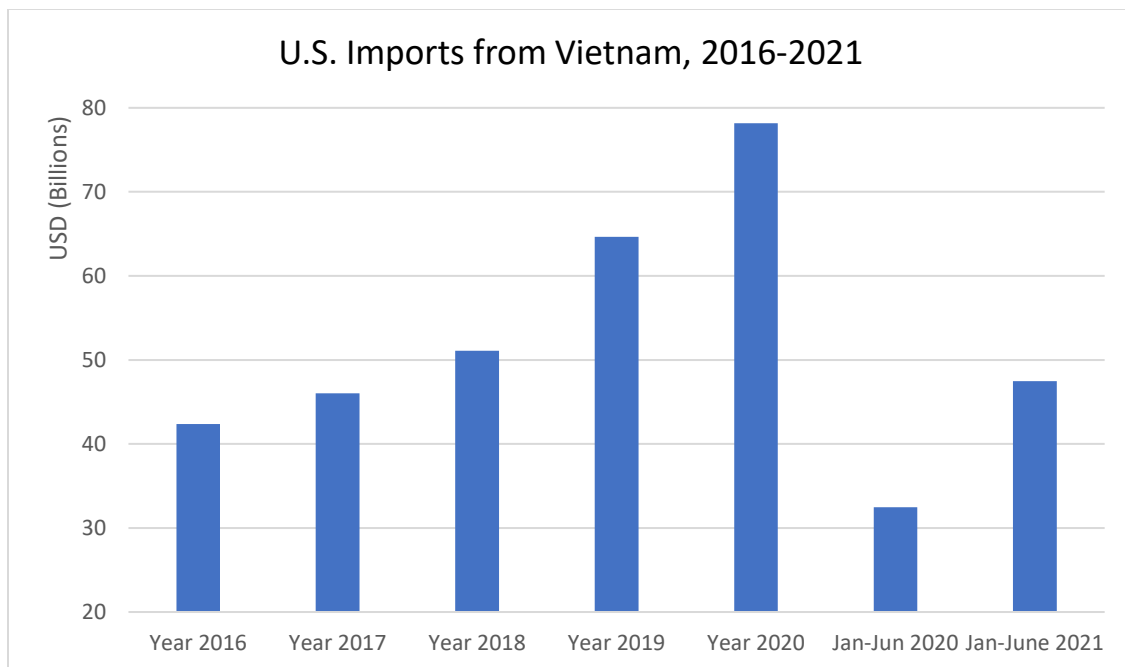
Change in Value of Imports from Hong Kong by Product Category, 2016-2020



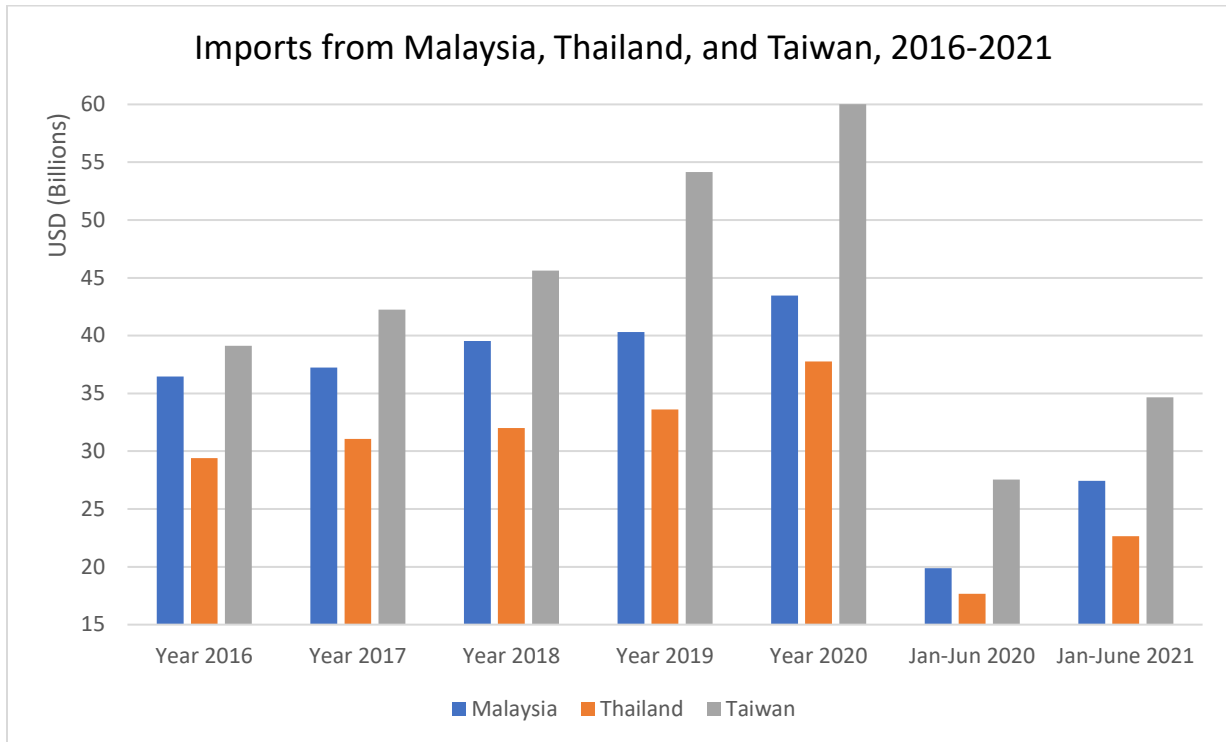
Source: U.S. International Trade Commission, Dataweb



Source: U.S. International Trade Commission, Dataweb



Source: U.S. International Trade Commission, Dataweb



Source: U.S. International Trade Commission, Dataweb