Abstract
Since the late 1990s, reported U.S. imports from China and Hong Kong have regularly and increasingly exceeded reported exports of China and Hong Kong to the United States. This discrepancy, which is not caused by re-exporting through Hong Kong, varies by product categories, and in some cases takes the opposite sign. In this paper, we focus on China’s direct exports to the United States. Using a model that allows for simultaneous misreporting to two authorities, we find strong statistical evidence of under-reporting exports at the Chinese border to avoid paying value-added tax (VAT). The value of VAT avoided is estimated at $6.5 billion during 2002–2008, and the associated understatements account for approximately two-thirds of the discrepancy. We also provide evidence of tariff evasion at the U.S. border, in particular for related-party transactions, and indirect evidence of transfer pricing and evasion of Chinese capital
controls. An estimated $2 billion of U.S. tariff revenue is lost due to such evasion during 2002–2008, which reduces the apparent size of the statistical discrepancy.

Highlights
â–º We develop a simple misreporting model to explain trade data discrepancy. â–º We test the model using mirrored U.S.–China eastbound direct trade data. â–º We find strong evidence for under-reporting of Chinese exports to avoid paying VAT. â–º We also provide evidence of tariff evasion at the U.S. border. â–º There are also indirect evidence of transfer pricing for U.S. multi-nationals.

JEL classification
H26; F1

Keywords
Trade data discrepancy; Tax evasion; Export VAT rebates; Transfer pricing

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