the toy association
Inspiring Generations of Play

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May 10, 2018

The Honorable Robert E. Lighthizer
United States Trade Representative
600 17th Street, NW
Washington, DC 20508

Docket Number: USTR-2018-0005

Dear Ambassador Lighthizer:

The Toy Association™, Inc. represents more than 1,100 businesses – toy manufacturers, importers and retailers, as well as toy inventors, designers and testing labs – all involved in bringing safe, fun and educational toys and games for children to market. With an annual positive economic impact of $109.2 billion, the U.S. toy industry supports 683,933 U.S. jobs and generates $14.8 billion in state and federal tax revenue each year. Approximately 3 billion toys are sold in the U.S. each year, totaling $27 billion at retail, and our members account for approximately 90% of this market. Importantly, over 95% of toy manufacturers, wholesalers, distributors in the United States are small businesses.

We are strongly opposed to any tariffs being levied on toys, games and other toy-related imports due to the significant negative impact on the U.S. toy industry and American consumers. We appreciate your office's consideration of the harmful economic impact tariffs would have on toy consumers and U.S. toy companies and the subsequent decision not to include toys and games in the initial proposed list of products that would be subject to an additional tariff. The toy industry also wishes to express its appreciation for the Administration's efforts to address actions (or, in some cases, inaction) by the Chinese government that cause significant harm to U.S. intellectual property rights holders. In the toy sector, we have seen a growing number of counterfeit and IP infringing toys sold online originating from China and we pledge to continue working with the Administration as we seek solutions to address this concern.

Toys and toy-related products (such as educational items), however, are far outside the scope of the Administration's focus on the technologies and industries included in the "Made in China 2025" initiative that is central to the Section 301 investigation. In addition, including toys in the current or any future tariff retaliation against China would be singularly inappropriate for the following reasons:

- With China supplying 85% of all toys sold in the U.S. and with no alternative manufacturing capacity readily available elsewhere, tariffs on toys will cause substantial harm to consumers due to higher prices and fewer choices.
- Toy tariffs will lead to projected losses of tens of thousands of U.S. jobs at a time when the U.S. toy industry is already disrupted by the Toys 'R' Us bankruptcy and closure.

<u>Impact on U.S. Consumers</u>

With 85% of all toys sold in the United States imported from China, imposing a tariff on toys manufactured in China would have a major immediate impact on the U.S. toy market generally and on

U.S. consumers in particular. Production by U.S. toy companies is well entrenched in China, having developed over decades while companies have maintained product design and other functions here in the U.S. The efficiencies of this manufacturing arrangement have allowed U.S. toy companies to be among the most competitive in the world, providing consumers with a broad array of toys at highly competitive prices.

Given this entrenchment, U.S. toy companies could not switch to non-Chinese sources quickly or easily. One reason is that Chinese factories have adapted to the seasonal nature of the toy industry, often producing toys only six months of the year and other products during the other half of the year.

Of even greater importance to U.S. consumers, the U.S. toy industry has invested in ensuring that Chinese suppliers produce toys that comply with the strict U.S. safety standards that protect America's children and families while at play. Establishing a new manufacturing base elsewhere could thus force companies to move hastily (and at significant cost) to educate new manufacturers of these requirements and develop relationships with them to ensure that the toys are, in fact, compliant.

Given these factors – the proportion of toys sold in the U.S. that are produced in China and the absence of readily available and safe alternative sources – it is implausible to say that U.S. toy companies can source toys from another country in the near- to mid-term. Moreover, the inelasticity of the U.S. demand for toys means that the U.S. consumer will feel the burden of any tariffs. A tariff would simply add a major additional layer of cost that will ultimately be borne by consumers in the form of higher prices and product scarcity.

Impact on U.S. Toy Industry

Although low-level toy assembly typically occurs in China, the U.S. toy industry maintains essential corporate, design, marketing and distribution operations in the U.S. that would be significantly and negatively affected by tariffs on toys. More than $27 billion of toys are purchased by consumers in the U.S. each year – nearly a third of total global toy sales. Over 80% of those retail dollars remain in the country because of U.S. domestic operations (e.g., production plus wholesale and retail). The most important aspects of creating a toy – research and development, design (including safety considerations), as well as some component manufacturing – occur domestically. On average, about 65% of the more than $14.7 billion that toy companies invest annually in production (e.g., salaries, benefits and material costs) remains in the U.S. These are high-paying jobs that fuel the consumer-driven U.S. economy – exactly the ones we want to keep here.

As mentioned above, the U.S. toy industry supports over 680,000 American workers and accounts for approximately $110 billion in economic value. The viability of these American jobs would be significantly undermined by the imposition of tariffs. In fact, economic analysis has determined that a 25% tariff applied to toys and games would result in the loss of 68,014 U.S. jobs and $3.4 billion in lost wages. Overall, tariffs on the toy industry would reduce the economic impact of the toy industry on the U.S. economy by approximately 10%, or $10.8 billion[1].

We note that the imposition of tariffs would come at a historically inopportune time for our industry considering the bankruptcy of Toys 'R' Us. The liquidation of all 800 Toys 'R' Us stores and elimination of 30,000-plus U.S. jobs is already having a seriously disruptive impact on the toy industry

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[1] The Economic Impact of the Toy Industry in the United States (data cited as of August 2017), and the Economic Impact of a Potential 25% Tariff on Imported Toys from China (data cited as of April 2018), produced by John Dunham & Associates for The Toy Association.

in this country. Levying what is almost tantamount to an across-the-board 25% additional tax on U.S. toy companies at this time could be crippling.

Also, the impact of the tariffs would be disproportionately felt by small U.S. toy companies and toy stores and likely would favor Chinese toy companies that sell toys to consumers via e-commerce platforms. With the U.S. de minimis exemption raised to $800, toys imported under this exemption would not be subjected to tariffs. So, a Chinese toy company that sells directly to consumers would be able to price their products more affordably than a U.S. toy company that imports larger volumes to sell to local toy and hobby shops. Moreover, as many counterfeit and IP infringing toys are sold by foreign sellers through e-commerce platforms, the tariff may result in an *increase* of IP infringement as consumers seek out cheaper options.

Finally, though the primary Harmonized Tariff Schedule (HTS) codes for toys and games (9503 and 9504) were not included on the April 3 tariff list, our industry nevertheless continues to assess the negative impact of the proposed tariffs on component parts and other products critical to toy production in the U.S. such as: certain machinery, batteries, television screens, remote controls, hard drives, and printed circuit assemblies.[2] One toy company located in the Midwest reports that its cost for tooling planned for importation from China over the next several months would increase by $120,000:

> *Our domestic vendors have identified tools/molds with HTS 84807180 for manufacturing our products that would be impacted by the proposed tariffs. Considering that the intention of these tariffs is to promote U.S. manufacturing, it seems counterproductive to impose a tariff on the tooling that's required to manufacture here. This would increase the investment cost to move manufacturing back to the U.S. In fact, our vendors have scheduled several of these tools to be shipped from China in the next several months and the proposed 25% tariffs would cost them and us an extra $120,000 to bring them in. The $120,000 is additional tax due to the 25% tariff. Tools/molds can be sourced somewhere else including U.S.; however, it could drive the cost of product up. In fact, some of these items are also exported to other countries like Canada so these tariffs are not only hurting U.S. manufacturing but export business also if we decided not to continue manufacturing in U.S. due to the cost.*

Tariffs on Toys Will Not Advance Administration Goals

As a general matter, the imposition of tariffs on imports from China is unlikely to meet the Administration's goal of inflicting maximum pain on China and minimal pain on U.S. consumers. Tariffs are hidden, regressive taxes that will be paid by both U.S. businesses and consumers in the form of higher prices.

The imposition of tariffs on toys specifically is especially unlikely to advance the Administration's objectives, including the criteria set forth in USTR's *Federal Register* notice, for the following reasons:

- Toys are not relevant to the Administration's stated goal of targeting those products relevant to China's "Made in China 2025" plan;
- Imposing tariffs on toys would provide little leverage in helping eliminate China's offending practices as the country has placed little emphasis in promoting and developing its domestic toy industry given the high foreign value (typically U.S.) incorporated in most Chinese toys;
- Tariffs on toys would cause disproportionate harm to U.S. consumers for the reasons detailed above;

[2] Specifically, members have identified the following HTS codes as impactful on U.S. toy production and we request they be removed from the list: 7318, 7320, 8443, 8471, 8473, 8477, 8480, 8505, 8506, 8507, 8526, 8527, 8528, 8529.

- Tariffs on toys would cause disproportionate harm to U.S. toy companies, particularly small- or medium-size businesses;
- China provides full tariff reciprocity on toys (China agreed to eliminate its duties on toys and games as part of its WTO accession negotiation, a crucial step for the U.S. toy industry in building on the earlier Uruguay Round zero-for-zero agreement on toys); and
- President Trump has made it clear that he wishes to protect U.S. jobs, particularly those in manufacturing. Unfortunately, tariff imposition has a perverse negative impact on this goal; it forces U.S. manufacturers to pay more for raw materials and subcomponent inputs (even if these are sourced in the U.S.), leading to job loss to make up for the reduced margins realized on finished items.

In lieu of higher tariffs, we encourage the Administration to employ a strategic policy to address China's offending intellectual property practices in concert with other major trading partners who share U.S. concerns.

Conclusion

The U.S. toy industry strongly opposes any punitive tariffs on toy imports. As detailed above, imposing tariffs on toys and toy-related imports would have a significant negative impact on U.S. consumers, would be devastating to the U.S. toy industry, and would fail to advance the objectives set forth by the Administration.

We greatly appreciate the opportunity to submit these views and would welcome any questions you or others in the Administration may have regarding U.S. toy industry concerns on this matter.

Sincerely,

Steve Pasierb
President & CEO
The Toy Association