Tariffs 101: What they are, who pays them, and why they matter now

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The U.S. Supreme Court is currently reviewing a case to determine whether President Donald Trump's global tariffs are legal.

Until recently, tariffs rarely made headlines. Yet today, they play a major role in U.S. economic policy, affecting the prices of everything from groceries to autos to holiday gifts, as well as the outlook for unemployment, inflation and even recession.

I'm an economist who studies trade policy, and I've found that many people have questions about tariffs. This primer explains what they are, what effects they have, and why governments impose them.

What are tariffs, and who pays them?

Tariffs are taxes on imports of goods, usually for purposes of protecting particular domestic industries from import competition. When an American business imports goods, U.S. Customs and Border Protection sends it a tariff bill that the company must pay before the merchandise can enter the country.

Because tariffs raise costs for U.S. importers, those companies usually pass the expense on to their customers by raising prices. Sometimes, importers choose to absorb part of the tariff's cost so consumers don't switch to more affordable competing products. However, firms with low profit margins may risk going out of business if they do that for very long. In general, the longer tariffs are in place, the more likely companies are to pass the costs on to customers.

Importers can also ask foreign suppliers to absorb some of the tariff cost by lowering their export price. But exporters don't have an incentive to do that if they can sell to other countries at a higher price.

Studies of Trump's 2025 tariffs suggest that U.S. consumers and importers are already paying the price, with little evidence that foreign suppliers have borne any of the burden. After six months of the tariffs, importers are absorbing as much as 80% of the cost, which suggests that they believe the tariffs will be temporary. If the Supreme Court allows the Trump tariffs to continue, the burden on consumers will likely increase.

While tariffs apply only to imports, they tend to indirectly boost the prices of domestically produced goods, too. That's because tariffs reduce demand for imports, which in turn increases the demand for substitutes. This allows domestic producers to raise their prices as well.

A brief history of tariffs

The U.S. Constitution assigns all tariff- and tax-making power to Congress. Early in U.S. history, tariffs were used to finance the federal government. Especially after the Civil War, when U.S. manufacturing was growing rapidly, tariffs were used to shield U.S. industries from foreign competition.

The introduction of the individual income tax in 1913 displaced tariffs as the main source of U.S. tax revenue. The last major U.S. tariff law was the Smoot-Hawley Tariff Act of 1930, which established an average tariff rate of 20% on all imports by 1933.

Those tariffs sparked foreign retaliation and a global trade war during the Great Depression. After World War II, the U.S. led the formation of the General Agreement on Tariffs and Trade, or GATT, which promoted tariff reduction policies as the key to economic stability and growth. As a result, global average tariff rates dropped from around 40% in 1947 to 3.5% in 2024. The U.S. average tariff rate fell to 2.5% that year, while about 60% of all U.S. imports entered duty-free.

While Congress is officially responsible for tariffs, it can delegate emergency tariff power to the president for quick action as long as constitutional boundaries are followed. The current Supreme Court case involves Trump's use of the International Emergency Economic Powers Act, or IEEPA, to unilaterally change all U.S. general tariff rates and duration, country by country, by executive order. The controversy stems from the claim that Trump has overstepped his constitutional authority granted by that act, which does not mention tariffs or specifically authorize the president to impose them.

The pros and cons of tariffs

In my view, though, the bigger question is whether tariffs are good or bad policy. The disastrous experience of the tariff war during the Great Depression led to a broad global consensus favoring freer trade and lower tariffs. Research in economics and political science tends to back up this view, although tariffs have never disappeared as a policy tool, particularly for developing countries with limited sources of tax revenue and the desire to protect their fledgling industries from imports.

Yet Trump has resurrected tariffs not only as a protectionist device, but also as a source of government revenue for the world's largest economy. In fact, Trump insists that tariffs can replace individual income taxes, a view contested by most economists.

Most of Trump's tariffs have a protectionist purpose: to favor domestic industries by raising import prices and shifting demand to domestically produced goods. The aim is to increase domestic output and employment in tariff-protected industries, whose success is presumably more valuable to the economy than the open market allows. The success of this approach depends on labor, capital and long-term investment flowing into protected sectors in ways that improve their efficiency, growth and employment.

Critics argue that tariffs come with trade-offs: Favoring one set of industries necessarily disfavors others, and it raises prices for consumers. Manipulating prices and demand results in market inefficiency, as the U.S. economy produces more goods that are less efficiently made and fewer that are more efficiently made. In addition, U.S. tariffs have already resulted in foreign retaliatory trade actions, damaging U.S. exporters.

Trump's tariffs also carry an uncertainty cost because he is constantly threatening, changing, canceling and reinstating them. Companies and financiers tend to invest in protected industries only if tariff levels are predictable. But Trump's negotiating strategy has involved numerous reversals and new threats, making it difficult for investors to calculate the value of those commitments. One study estimates that such uncertainty has actually reduced U.S. investment by 4.4% in 2025.

A major, if underappreciated, cost of Trump's tariffs is that they have violated U.S. global trade agreements and GATT rules on nondiscrimination and tariff-binding. This has made the U.S. a less reliable trading partner. The U.S. had previously championed this system, which brought stability and cooperation to global trade relations. Now that the U.S. is conducting trade policy through unilateral tariff hikes and antagonistic rhetoric, its trading partners are already beginning to look for new, more stable and growing trade relationships.

So what's next? Trump has vowed to use other emergency tariff measures if the Supreme Court strikes down his IEEPA tariffs. So as long as Congress is unwilling to step in, it's likely that an aggressive U.S. tariff regime will continue, regardless of the court's judgment. That means public awareness of tariffs – and of who pays them and what they change – will remain crucial for understanding the direction of the U.S. economy.

Kent Jones does not work for, consult, own shares in or receive funding from any company or organization that would benefit from this article, and has disclosed no relevant affiliations beyond their academic appointment.