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## **Recent Rulings Affect Penalties**

by **Steven S. Weiser and Arthur W. Bodek**

When it comes to Customs penalty cases, things were much easier in the good old days. Then (and now), a penalty case would begin with Customs accusing an importer of committing a purportedly violative act and alleging a level of culpability. Traditionally, this would then be followed by an administrative process and sometimes a court battle largely focusing on the questions of whether the act occurred as alleged and whether the act violated a requirement embodied in the Customs laws. In the event that the case was pursued in the U.S. Court of International Trade, the court would typically be the final arbiter of all factual and legal issues and, based on its findings and conclusions, the issues of culpability and the penalty amount would be determined.

Two cases handed down by the court in the final quarter of 1999 have the potential of dramatically changing the landscape of how Customs penalty cases will be resolved in the future.

### **First for jury: Customs penalty claim**

The first case, which is significant on two fronts, is *U.S. v. Tri-State Hospital Supply Corp.* It represents perhaps the first instance in which a Customs penalty claim was resolved by a jury trial.

Secondly, it brought into question the long held Customs' position that misrepresentations as to the value of imported merchandise are per se material (as opposed to being a factual issue to be resolved at trial).

The Tri-State case involved allegations that an importer entered surgical instruments by means of false representations and omissions that caused the purchase price to be overstated. The overvaluation did not result in any loss of revenue in that the merchandise qualified for duty-free entry under the Generalized System of Preferences.

The government asserted a claim under the Customs commercial fraud statute which penalizes parties for negligently, gross negligently or fraudulently entering goods by means of material false statements or omissions (irrespective of whether the United States is deprived of revenue).

Central to the government's claim was the proposition that a false representation as to value is, by its very nature, always material. Underlying this proposition were government claims that the misstatements of value had the potential to affect the appraisement of the imported merchandise and the GSP status of the particular exporting country as well as interfering with the compilation of trade statistics.

In connection with a procedural motion filed by the government, the court overturned years of precedent by finding that the question of materiality is not purely a question of law. Rather, the question of materiality was concluded to be at least partially one of fact.

As such, in a virtually unprecedented action, the court ordered a jury trial in order to determine whether the importer's statements were "material" (i.e., having a practical effect on the administration of the Customs laws). Indeed, the court bristled at the government's

contention that no reasonable jury could possibly find that a value misstatement, even one involving a discrepancy as little as a one cent, could be immaterial for purposes of the commercial fraud statute.

Thus, the court observed that a statement made in connection with an importation could be both false and even negligent without being material. At trial, the jury ultimately delivered a verdict in favor of the importer.

After *Tri-State*, one thing seems clear, Customs will no longer be able to routinely rely on certain classes of entry misstatements (e.g., erroneous value declarations) as being per se “material”. Rather, the government will have to affirmatively persuade the trier of fact (which may very well be a jury) that a particular false statement, in a tangible way, actually had a capacity to influence an aspect of the administration of the Customs laws.

Where, as in *Tri-State*, a misstatement as to value results in no loss of revenue (or a loss of revenue which is de minimis), materiality will no longer be a foregone conclusion.

### **Case helped clarify standards for assessment**

The second recent case impacting the manner in which Customs penalty cases are to be resolved is *U.S. v. Complex Machine Works Co.*

While perhaps not as groundbreaking as the decision in *Tri-State*, it represents an important clarification of the standards to be applied in determining the amount of a penalty to be assessed under the Customs commercial fraud statute.

The *Complex Machine Works* case involved allegations against an importer for having imported machine parts without having made proper declarations to Customs in some instances and providing Customs with false information as to value in other instances. In earlier proceedings, the U.S. Court of International Trade found that the importer’s actions amounted to a fraudulent violation of the Customs laws.

In this case, the government pursued a claim against the importer in an amount representing the domestic value of the merchandise (the maximum amount authorized by statute).

The court began its analysis by affirming prior precedent to the effect that there is no presumption that the maximum authorized penalty is most appropriate or that the penalty amount assessed by the government is to be accorded any special weight.

The Court then observed that, while the penalty statute provides for penalty assessment ranges, it does not provide any factors to be applied in determining the particular penalty assessment in a given situation.

In addressing the question of the appropriate penalty amount to be assessed in the context of the facts before it, the court conducted a survey of the discretionary factors found in other penal statutes comparable to the Customs commercial fraud statute.

As a result of this exercise, the court developed a list of fourteen factors to be applied. Many of these factors differed from the list of mitigating and aggravating factors embodied in the Customs Service regulations.

Through a mechanical application of these factors, the court found it appropriate to reduce the penalty amount sought by Customs by approximately 42%.

### **Cases help resolve Customs penalty cases**

The *Tri-State* and *Complex Machine Works* cases represent significant new directions in the resolution of Customs penalty cases in the U.S. Court of International Trade.

Taken together, they hold that the issue of whether a false statement or omission is “material” is partially one of fact which may be decided by a jury and that the statutory maximum penalty amounts will not perfunctorily be regarded as appropriate. Rather the fourteen factors divined by the court are to be applied in arriving at the final penalty amount.

Thus, in the event that today’s mail brings with it a penalty notice from the U.S. Customs Service, it is important to be fully aware of the avenues of relief provided by recent judicial action. What effect will these developments ultimately have on penalties assessed by Customs in the future? The jury is still out.

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