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International Electronic Transactions: Ensuring Compliance With U.S. Customs And International Trade Laws

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This article examines the impact of U.S. customs and international trade laws on international electronic transactions and discusses the need for corporate compliance programs that address these laws. International e-transactions include a wide variety of corporate activities, ranging from intranet document-sharing systems to online purchases of physical goods. Like conventional international transactions, these activities are subject to regulation under U.S. customs and trade laws. As a result, companies should have compliance procedures in place to avoid disruption by regulatory agencies and to minimize potential liability for noncompliance.

Transferring Goods, Services and Information Across Borders in the New Economy

E-commerce allows buyers and sellers to import and export goods and services with unparalleled speed. For example, companies are increasingly relying upon business-to-business (B2B) software programs to buy and sell goods and services internationally. In addition, companies sell goods and services directly to end-users in other countries over the Internet, thereby bypassing normal distribution chains. Businesses also conduct much of their international communication through e-mail and company intranets. Nonetheless, companies may overlook the fact that U.S. regulatory agencies, particularly the U.S. Customs Service and the Bureau of Export Administration (BXA), apply the same customs and trade laws to these transactions as they do to those made through traditional channels. Three hypothetical examples illustrate this point.

Example I: Importing Tangible Goods and Services

Using a B2B application, U.S. Company A buys parts and supplies from Company B on an FOB basis. Company A intends to use the parts and supplies in the United States for further manufacturing. Company B is a multinational based in another country and produces merchandise in a number of countries. Occasionally, Company B will fulfill the online orders of Company A by referring them to Company B's foreign branches or subsidiaries. In many cases, the foreign branches or subsidiaries will ship the orders directly to Company A. Although Company B sends computer-generated e-mail shipment status reports to Company A, those e-mails do not identify the country from which the merchandise is being shipped.

In this situation, Company A has, perhaps unknowingly, become the importer for shipments of physical merchandise (i.e., tangible goods) from outside the United States. Because the terms of sale are FOB, Company A will have to arrange for importation into the United States. Unless another party becomes the importer of record for customs purposes, Company A will have to ensure that it complies with all customs laws and regulations that apply to imported merchandise. Accelerated Internet-based transactions can make compliance with some of these requirements, such as the duty to exercise "reasonable care," particularly difficult, thereby exposing Company A to significant monetary penalties. For instance, Company A must ensure that it understands Company B's branches or subsidiaries so that it can properly declare the country of origin of the parts and supplies. An improper declaration can result in penalties as high as the value of the parts and supplies.

Example II: Exporting Tangible Goods and Services

Company A also maintains a Web site from which visitors purchase products. A sophisticated exporter, Company A has procedures to comply with U.S. export laws for online sales, including the automatic rejection of shipments to countries subject to U.S. sanctions law. However, the company neither uses interdiction software nor performs manual checks to screen online orders for "specially designated nationals" or citizens of sanctioned countries if those persons or entities are not residing in a sanctioned country.

Consequently, Company A may inadvertently violate U.S. sanctions law by transacting business with those persons or entities. The Office of Foreign Assets Control (OFAC) publishes an annual list of persons or entities with which U.S. citizens are prohibited from doing business without a license. Under the old economy sales paradigm, Company A's system might have included time to review purchase requests by phone, fax or letter. However, the very advantage of Web site purchasing—frictionless ordering that can generate sales and shipping documents instantaneously and automatically—may not provide Company A with enough time and flexibility to comply with trade laws.

Example III: Exporting Intangible Goods and Services

The first two examples are not necessarily unique to the Internet, but, rather, represent issues in transitioning the sales and purchase of physical goods into a new medium. Conversely, the third example arises specifically out of the characteristics of the new medium. Assume that a research and development division at Company A includes foreign and domestic citizens working in the United States and abroad. Because the employees are in different offices, they frequently communicate by e-mail, often attaching documents containing product information and specifications. In addition, the division has created an intranet site—to which only members of the division have access—where information and projects can be posted, reviewed and edited by different members of the division. Finally, Company A has a documents management system whereby any member of the division can obtain access to any other member's computer files.

The Export Administration Regulations (EAR), in 15 C.F.R. § 730.5(c), specifically state that "electronic transmissions of non-public data that will be received abroad" are considered exports subject to the EAR. Because the EAR includes the international transfer of tangible and intangible goods (i.e., information or goods transferred electronically) within the scope of the term "exports," multinational companies such as Company A should ensure that international e-transmissions comply with the EAR, as well as other laws that govern export transactions (e.g., the International Traffic in Arms Regulations and OFAC sanctions programs). As information becomes more easily exchangeable across borders and nationalities, the problems of intangible transfers become increasingly significant with respect to compliance with the export control laws.

A Note on Importing Intangible Goods

It is important to point out that, although the above examples are illustrative and cannot address the vast and varied potential compliance problems, one type of e-transaction was intentionally excluded: imports of intangible goods (i.e., goods such as software in electronic form). Although these goods are subject to other laws enforced by the Customs Service, such as copyright infringement laws, they are not subject to duty and entry requirements when imported electronically. Thus, goods such as videos, compact discs, e-books and software that are dutiable and subject to entry requirements when imported in tangible form are not subject to those requirements when downloaded from the Internet.

The Prospect of Enforcement

Violators of U.S. laws governing imports and exports are subject to fines, penalties and possibly criminal prosecution. Moreover, goods may be delayed or prevented from entering or leaving the United States if the proper procedures are not followed. In the case of imports or exports of tangible goods purchased online, the potential for enforcement actions is no different than with imports or exports purchased using other media. Nonetheless, it is notable that the Customs Service has a dedicated CyberSmuggling unit, established in 1997, which is responsible for investigating international Internet-based criminal activity, including both illegal imports and exports.

Conversely, the difficulties associated with detecting potential export violations involving transfers of intangible goods may decrease the possibility of enforcement actions. It is noteworthy, however, that BXA and the Customs Service have committed resources to developing new research techniques and investigating possible violations in e-transmissions, and have already investigated cases involving illegal e-mail transfers of software. As a result, the prospect of enforcement actions involving e-transmissions is not negligible and will likely continue to increase.

Compliance Programs

The wide range of possible import and export violations, the risk of penalties, fines and imprisonment, and the potential disruption to commercial shipments are compelling reasons for companies to institute procedures to ensure that international e-transactions comply with U.S. trade laws. Moreover, they serve another well-known purpose: to mitigate liability in the event of an investigation by the Customs Service, BXA or other government agencies. Of course, the procedures instituted are largely dependent on the identification of the areas in which a company is most at risk and that company's characteristics, including its experience with importing and exporting, the type of business in which it is engaged, the physical location of its offices, and the nationalities of its employees. An experienced importer or exporter may simply need to make small adjustments to current Internet use or import-export policies to ensure an adequate level of protection, while other companies may require more significant changes to corporate policies and may benefit from outside assistance.

Nevertheless, several considerations are worth mentioning as companies formulate these procedures. First, in addressing tangible imports and exports, procedures should focus on obtaining sufficient information on the other parties involved and the nature of the transaction itself. Second, because the nature of the problem is different with intangible exports, procedures should emphasize protecting information from illegal release. Third, companies should focus on their areas of vulnerability, but should also make their policies as comprehensive and prospective as possible. Moreover, they should build flexibility into the policy that will allow it to evolve so that it can address future changes in that company's operations. Of course, it is not realistic to believe that a policy in this area can anticipate future changes in technology or how the law and government will respond to those changes, even in the near term. Thus, the final consideration is that companies should make educating employees on these issues and the identification of new problems by employees a high priority.

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