

# **The International Legal Environment of Business**

## **Chapter 21**



# **International Issues**

- **International law and business**
- **U.S. import policy**
- **Business structures in foreign markets**
- **Foreign Corrupt Practices Act and its restraints on competitiveness for U.S. firms**
- **International contracting**
- **Insuring losses**
- **Resolution of international disputes**

# The International Business Environment

- **Includes all business transactions that involve 2 or more countries**
  - **Movement of goods across national boundaries**
  - **Movement of services across national boundaries**
  - **Issues regarding capital**
  - **Issues regarding personnel**



# Risks of International Business Transactions



- Financial
- Political
- Regulatory
- These stem from differences in:
  - Currencies
  - Language
  - Business customs
  - Legal systems
  - Social philosophies
  - National goals



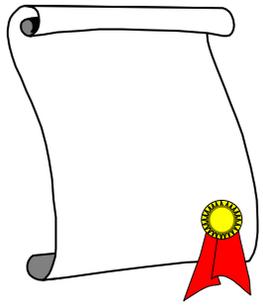
# The Foreign Corrupt Practices Act (FCPA) 1977

- ☞ Punishment of *payer* of bribe to *foreign officials*
- ☞ “Corrupt” person displays reckless or conscious disregard for consequences of one’s actions
- ☞ Payer *knows* payment will go to public official
  - “Any reasonable person would have realized”
  - “Consciously chose not to ask about what he/she had reason to believe would be discovered”
  - “Simple negligence” or “mere foolishness” exception
- ☞ Routine governmental action (Grease Payment) exception: “facilitation or expediting payment. . . the purpose of which is to expedite or secure the performance of a *routine governmental action.*” (i.e. visas, providing basic utilities, transportation services, etc.--*small amount and very limited usage*).

# Punishments Under FCPA

- **Individuals: Maximum of \$100,000 & 5 years in jail**
- **Corporation: Up to \$2,000,000/violation**
- **Exception: Dept. of Justice “pre-deal interpretation”**
- **Watch: “Slush funds” or “Salaries, commissions or fees” *disproportionate* to service provided**





# International Contracts

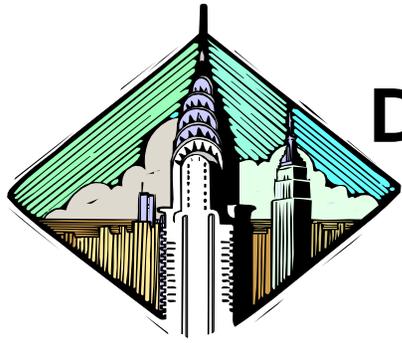
- **Cultural Aspects**
  - i.e. Asia, Europe, Latin America all have long-term approach to relationships
- **Payment Clauses & Exchange Rates**
- **Repatriation of Profits**
- **Choice of Language Clause**
- ***Force Majeure Clauses***
- **Forum Selection Clause**
  - *Selection of Court*
- **Choice-of-Law Clauses**
  - *Select law that applies*
- **Letters of Credit**
  - Assurance by bank of buyer to pay seller upon receipt of documents that prove goods were shipped and contract fulfilled
  - Revocable or Irrevocable



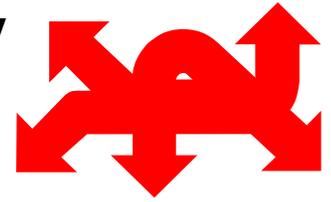
# Loss of Investment

(Political Upheavals, Unstable Monetary Systems, Changes in Laws)

- **Nationalization**: Gov't “nationalizes” foreign investment
  - Gov't may pay less than value
  - i.e. Iran, Cuba, England
- **Expropriation**: Taking foreign property in accordance with international law
- **Confiscation**: Taking is discriminatory
- **Insuring Against Risk of Loss**
  - Short-term private insurers
  - Major insurers (i.e. Lloyds of London)
  - Gov't agencies (i.e. Overseas Private Investment Corporation [OPIC]) insures investors who invest in less developed countries



# Doctrine of Sovereign Immunity and Doctrine of Act of State



- **Act of State**

- Court gives up right of jurisdiction over foreign country or representative
- Court will bar compensation because the acts were by a foreign government or representative

- **Sovereign Immunity**

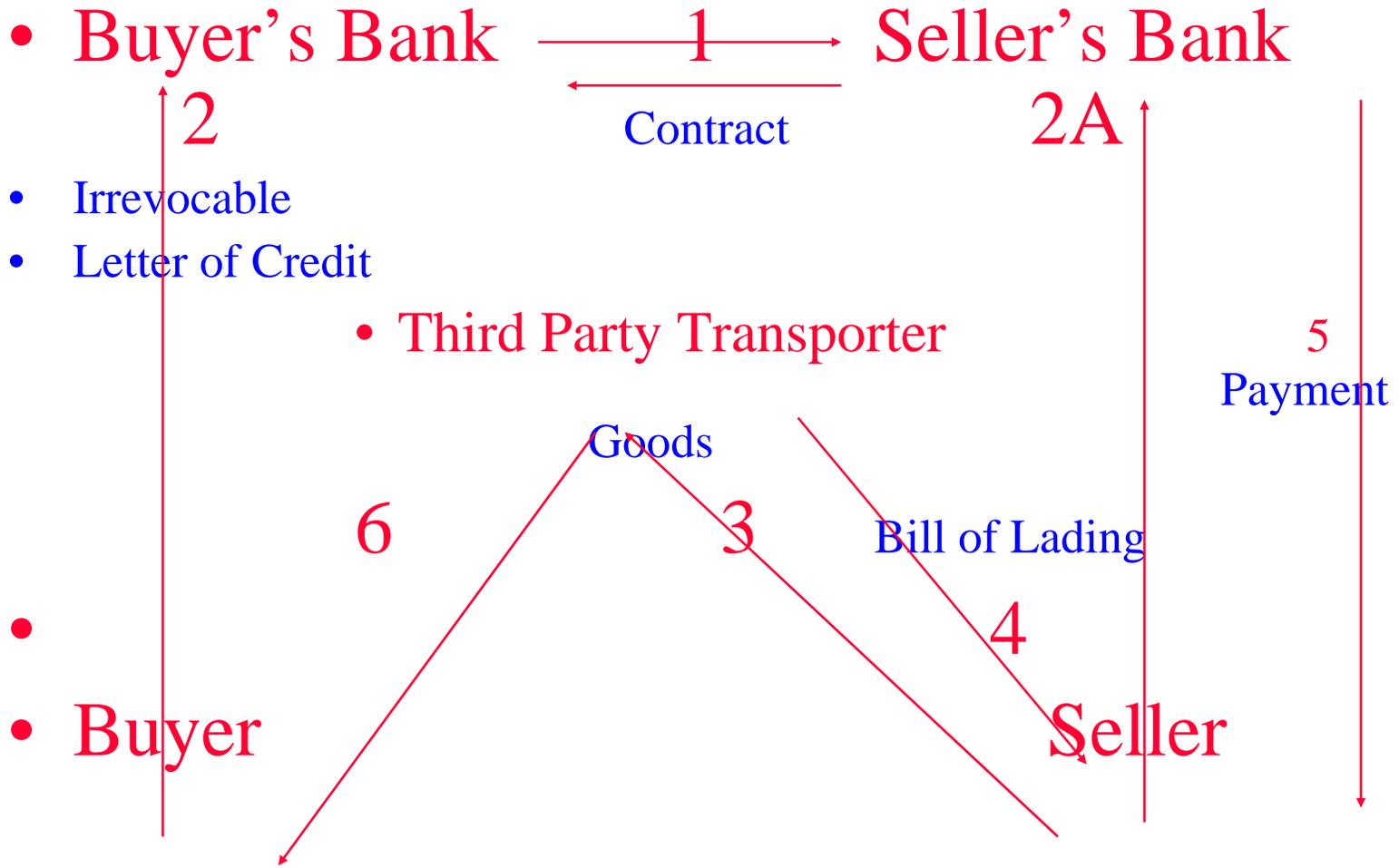
- Bar to compensation by foreign investors
- Immunity to foreign representative or country
- One country must respect the independence of other countries and their representatives



# International Dispute Resolution

- **International Court of Justice (ICJ)**
  - Only nations have standing--not individuals
  - Nations may make claims on behalf of persons
  - No mandatory compliance requirement
  - UN Security Council must enforce
- **Arbitration: 3rd neutral party decides outcome, which is binding**
- **Mediation: 3rd neutral party “suggests” outcome, which is not binding**
- **Litigation**
  - Differs within countries
  - Not enforceable outside of country
  - Treaties/Conventions may assist potential parties
  - Contract clauses assist courts in enforcement of claims
  - Usually need “minimum contacts” for jurisdiction

# Letters of Credit/Bill of Lading



- Irrevocable
- Letter of Credit

• Third Party Transporter

- Buyer

Seller

- Revocable only for Fraud.
- Not revocable for mere Breach of Contract

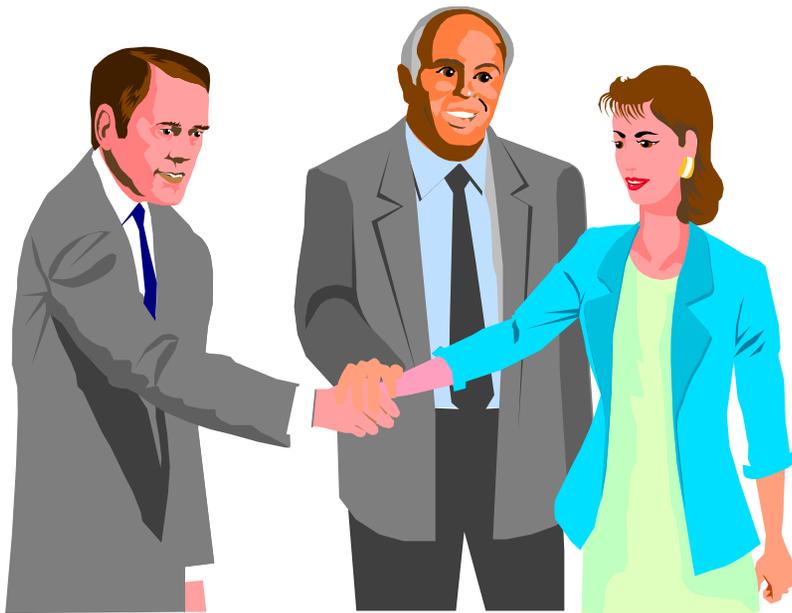
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# Sources of International Law

- Individual countries create their own laws
- Trade agreements between countries (NAFTA)
- Worldwide/regional organizations, i.e.
  - United Nations
  - European Union (EU)
- No universal international court system, although attempts made through
  - International Court of Justice
  - International arbitration attempts
  - Courts of individual countries
- Difficult to enforce decisions and contracts

# International Trade Agreements

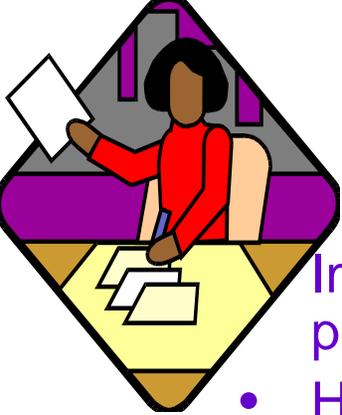


- Improve economic relations of countries
- Cover variety of commercial issues
- Tax agreements prevent double taxation
- Examples:
  - North American Free Trade Agreement (NAFTA, 1992) Canada/US/Mexico
  - General Agreement on Tariffs & Trade (GATT) replaced in 1995 by World Trade Organization (WTO)



# Taxes on Imports

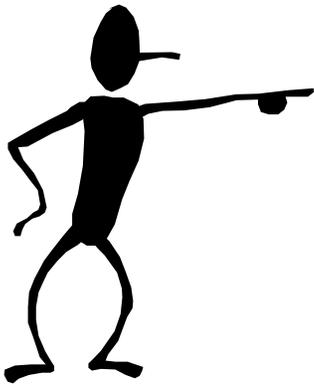
- ***Tariffs***--Taxes levied by government on imported goods
  - *specific tariffs*: fixed duties on products
  - *ad valorem tariffs*: % of price of product
  - See *Heartland By-Products, Inc. v. U.S.*
- ***Harmonized Tariff Schedules***--worldwide classification of goods for customs officials
- ***Bans on Certain Products***--i.e. weapons, illegal products, narcotics, national security concerns



## *Heartland By-Products v. U.S.*

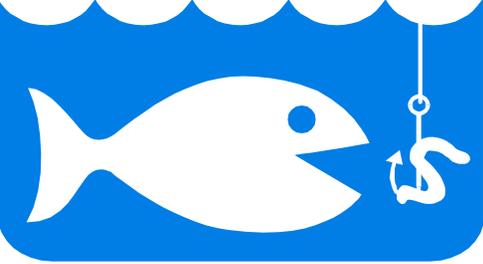
Imported sugar is controlled by Tariff Rate Quota (TRQ) as a product that produces more than 6% non-sugar solids.

- Heartland sought reclassification which Customs ruled on favorably under the U.S. Harmonized Tariff Schedule. Import is described as having a manufacturing process and composition of the syrup resulting in “less than 5%” of “soluble non-sugar solids.” Relying on the reclassification, Heartland began importing sugar syrup in 1997.
- Competitors complained that the classification was in violation of the TRQ for sugar. They filed a petition to have Heartland’s syrup reclassified. Customs reclassified; Heartland was then subject to the TRQ for sugar.
- Heartland sued in Court of International Trade. The court ruled for Heartland. Customs & U.S. Beet Sugar Assn. appealed.
- **HELD: Reversed. Custom’s revocation of its classification was “logical and well-reasoned”. Even though Customs was a little inconsistent, the tariff statute allows revocation of prior classification.**



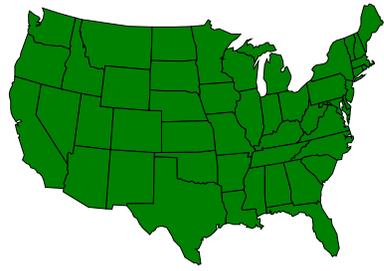
# Import Price Controls

- **In U.S.**--Dept. of Commerce through International Trade Administration (ITA) & International Trade Commission (ITC)
- ***Antidumping Orders***: When there is charging a lower price in an export market than in a home market. Duty is determined by comparing market price in home market vs. price charge in U.S. When item is imported, then duty is applied to product.
  - ***See Pesquera Mares Australes Ltda. v. United States***
- ***Countervailing Duties***: Tariff applied to offset subsidies provided by foreign governments to their industries that lower prices of products imported into the U.S. Duty applied is = to foreign governmental subsidy. (Purpose: To assist U.S. products to be competitive in the U.S. market)
- ***Foreign Trade Zones***: Goods processed. Duties assessed upon leaving zone.
- ***Duty Free Ports***: No duties or tariffs assessed on products, i.e. Hong Kong



## *Pesquera Mares Australes Ltda. v. U.S.*

- Coalition for Fair Atlantic Salmon Trade complained exporters of Atlantic fresh, farmed salmon in Chile were selling salmon in the U.S. at less than fair value.
- Commerce determined that prices were less in U.S. than in Japan & imposed a 2.23% antidumping duty.
- Exporters appealed, which was affirmed by Court of International Trade. Exporters appealed again.
- HELD: Affirmed. In looking at the “dumping margin” Commerce will look at the value, making a “fair comparison” between amounts charged for the product in the U.S. and other markets.
- Commerce looked at product characteristics and different classifications in countries & industry. Any differing classifications of items sold in U.S. & Japan were “minor”.



# Export Regulation and Promotion (To Reduce U.S. Trade Deficit)

- **Federal/State governments**
  - **Commerce Department helps promote exports through ITA activities**
  - **States help develop export promotion programs**
- **Export Restrictions, if goods, for instance:**
  - **Injure domestic industry**
  - **Jeopardize national security**
- **Export Licenses (types depend on goods exported)**
  - **Reexported Goods--Goods exported into country #1; then *reexported* into country #2 (May violate U.S. licensing regulations)**



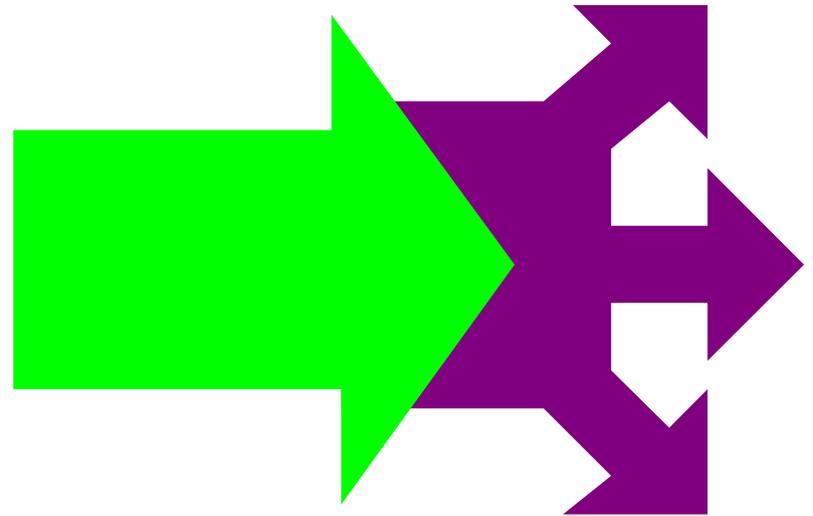
# Penalty Provisions for Violation of Commerce's Licensing Provisions



- Include criminal and civil penalties
- Can also have administrative sanctions
- If an exporter “knowingly” violates the Export Administration Act, there can be fines up to \$50,000 or 5 times the value of exports and receipt of up to 5 years in prison
- Person who “willfully” violates the Act, can be fined more and receive up to 10 years in prison, with a possible suspension or revocation of a business’s authority to export
- Example: McDonnell Douglas paid \$2.1 million fine for improper sale of equipment to China.

# Exporting Manufactured Products

- ***Indirect Exporting***
  - Using exporter who sells product in a foreign market for U.S. manufacturer
- ***Direct Exporting***
  - Developing an organization within the business that is responsible for exporting products





# Foreign Manufacturing

- **Wholly Owned Subsidiary**
  - Business owns the facilities--some countries limit % of ownership
- **Joint Venture**
  - Sharing ownership with foreign partners
- **Licensing Agreement**
  - *Licensor* grants *licensee* access to patents and technologies
- **Franchise Agreement**
  - *Franchisor* grants *franchisee* rights to sell products or services, i.e. McDonald's, Hertz
- **Contract Manufacturing**
  - Contract made for production of products
- **Issues to Consider**
  - Labor expenses
  - Shipping costs
  - Raw material costs
  - Avoid restrictions/tariffs



## *Keller v. Central Bank of Nigeria*

**Keller sells mobile hospitals. Was contacted by Prince Arthur Ossai, who said he was a member of the royal family of Nigeria and a government official.**

- **Ossai wanted to buy \$4.1 million worth of mobile hospital equipment. He said there was \$25.5 million in an account with Central Bank of Nigeria (CBN). Keller would be given funds to make payments: \$4.1 million for the equipment; \$2.52 million for profit for Ossai; \$7.65 million for “licensing fee” for himself; \$9.945 million to Ossai as commission; etc.**
- **Keller was to pay \$28,950 in bank fees & then get \$25.5 million to distribute. He pays, flies to London to meet the Nigerians. The joke is on him.**
- **Keller sues CBN employees & CBN for fraud and violating RICO.**
- **4 people didn't respond & default judgment was entered against them. Ct. dismissed claim vs. 3 others saying Keller had “unclean hands,” but allowed RICO claim. CBN appealed that suit should be dismissed under FSIA because the illegality of the deal precludes finding that this is a commercial activity.**
- **HELD: The “commercial activity” exception of the FSIA will allow the RICO claims to go forward and there will be no immunity.**
- **Illegality does not destroy the “commercial activity” exception under the FSIA which can apply to this case.**



# *“Disputes With Chinese Companies or Individuals”*

## Negotiation:

- Simple negotiation is the best method of dispute resolution in China.
- If a firm experiences difficulty in negotiation, it can seek assistance from Chinese officials to honor terms of contract.

## • Arbitration

- Arbitration is preferred next to negotiation.
- Two Chinese government-sponsored arbitration bodies used when transaction involves a foreign party: China International Economic and Trade Arbitration Commission (CIETAC); China Maritime Arbitration Commission (CMAC)

## • Litigation

- Foreign individuals and companies have same ability to sue as Chinese citizens and companies.
- The Chinese courts are not always up to international standards.
- Judges have minimal training. There are also corruption problems.
- (Arbitration has advantage of a panel of experts.)

- Enforcement of litigation and arbitral awards is difficult. China’s Supreme People’s Court is trying to address this issue.

# Origins of International Law

- Commercial codes date back to Egypt in 1400 B.C.
- Early trade centered around law of the sea
- 700 B.C.--Isle of Rhodes develops International Code
- Greek and Roman Empires had codes of trade
- Middle Ages: Lex Mercatoria (Merchant Law) Governed trading customs in Europe
- Today's codes partially derived from early efforts

