Going Global: A Legal Primer for Innovation- and Knowledge-Based Companies

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I. Introduction

As the world becomes increasingly interconnected, no company is immune to the impact of globalization. Technology has leveled the international playing field by increasing competition, access to less expensive resources, and exposure to new sales markets.

Innovation- and knowledge-based companies are the key beneficiaries of the global marketplace. Globalization has created a vast potential market for their goods and services. Globalization also allows such companies to obtain resources, deliver their goods and services at lower costs, and tap into the know-how of engineers and technicians around the world.

In addition to the typical hurdles and pitfalls faced by companies with international operations, innovation-based companies face special issues as they buy and sell products, obtain and deliver services, and share information and technology across national borders. Although globalization comes with both opportunities and risks, by planning ahead intellectual property owners can simultaneously take advantage of the opportunities that arise and preemptively protect their intellectual property.

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For some companies, expanding operations outside the United States (i.e., "going global") could be a simple as the occasional purchase of components and materials from overseas, or sale of products to a foreign customer who surfs into their website or views their products at a trade show. For others, going global may involve placing employees in another country, licensing brands or technology to a licensee outside the United States, building a foreign factory, or a number of other scenarios to establish a more direct and consistent involvement in one or more foreign markets. This article discusses several common means of going global, with a focus on the special issues and concerns of innovation-based enterprises.

II. Protecting Intellectual Property in International Transactions

Regardless of the chosen mechanism of "going global," before an innovation-based company initiates any international operations, it is imperative that the company ensures its intellectual property ("IP") is adequately protected. Due to the mercurial nature of IP assets and the differing rules and varying degrees of foreign IP protection, American IP owners are particularly vulnerable when they transact business internationally. However, many risks can be successfully mitigated through a well-planned and executed global IP strategy.

Contrary to popular belief, there is no comprehensive international IP enforcement system. IP rights that exist in the United States essentially end at American borders. To enforce IP rights in a foreign country's jurisdiction, intellectual property owners must avail themselves of the procedures and laws of each foreign nation. Since each nation has its own laws, protocols, and systems of enforcement, this can be a complicated and unfamiliar process.

There is no single "magic bullet" when it comes to protecting IP abroad. A prudent global IP strategy will involve a range of tactics and the application of cost-benefit principles. The following are some suggestions for how to implement a successful strategy.

1. IDENTIFY IP ASSETS AND SECURE DIRECT AND INDIRECT IP PROTECTION

The first step is to properly identify all IP assets. Many believe that only large "high tech" companies have IP, but *all* businesses have IP assets. IP assets can include: names, brands, and logos (trademarks and service marks); designs, websites, and software (copyright); and, inventions, ideas, and processes (patent and trade secrets).[1]

Once a company has identified and taken inventory of all of its IP assets, it needs to take action to protect them. There are two basic means of protecting IP: direct and indirect. Whenever possible, it is advisable to employ both direct and indirect means to protect IP, both in the United States and abroad.

Direct IP protection refers to using contracts and individual relationships to protect IP rights, such as using non-disclosure agreements with anyone exposed to the secrets (including employees). This allows IP owners to define the scope of their IP rights and identify when an infringement occurs. However, a key limitation is that IP owners can typically enforce their IP rights only against those with whom they have contractual relationships.

Indirect IP protection involves taking advantage of government registration protections to secure IP rights against a much broader group of would-be infringers.[2] Due to the broad scope of protection, a key limitation of indirect IP protection is that it is difficult to spot infringement, particularly when the infringing activity is isolated or remote. In addition, because IP owners must register in each country where they seek IP protection, this can become an expensive process and an administrative burden.[3]

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2. CONSIDER THE INTERNATIONAL IMPACT OF AMERICAN IP RIGHTS

For the most part, the rights granted to IP owners under United States American law stop at the United States border. However, a number of international treaties and conventions provide for some degree of protection as American IP owners and their IP move across borders. For example, the Trade Related Aspects of Intellectual Property Agreement ("TRIPS")[4] requires all member nations of the World Trade Organization ("WTO") to provide some basic levels of IP protection such as requiring minimum time periods of protection, and mandating that foreigners have the same rights provided to domestic companies to register and enforce their IP rights.[5]

In addition to TRIPS, several other treaties and conventions make international IP protection more practicable, such as those allowing American IP owners to claim the earlier priority filing dates based on their American registration applications and those providing for consolidated multi-national IP registration application filings.[6] Absent those special privileges afforded by treaty, if American IP owners want IP protection in other countries, they must avail themselves to the IP laws and registrations provided by each of those countries.[7]

3. KNOW THE BURDEN OF POLICY AND ENFORCEMENT

Consistent with American IP laws, the burden of policing and enforcing IP rights internationally rests with the owners of the IP.[8] IP owners must be vigilant in discovering IP infringement and take swift action to stop it.

As previously discussed, the laws of a specific country will define the American IP owner's rights in that country.[9] For example, if an American company wishes to stop infringement of its trademark in Japan, it must ensure that its IP is afforded IP protection under Japanese law, and then must consult Japanese law to discern what types of enforcement Japan provides. Moreover, any legal action against the infringer will likely take place in Japan.

However, if a manufacturer, distributor, vendor, or some other party with whom the American IP owner has a contract were the cause of the IP infringement, then the terms of the contract (including choice of law and forum) would impact the rights and remedies the American IP owner might

have.[10] Practically speaking, the ability of an American IP owner to enforce the contract will depend on the terms of the contract itself as well as the location of the infringer and its assets.

4. STOP FOREIGN-MADE "KNOCK-OFFS" FROM ENTERING THE UNITED STATES

A significant concern for American IP owners is the rampant IP counterfeiting and piracy that occurs outside the United States. According to the American government, American companies lose between $200 billion and $250 billion in sales annually due to international IP counterfeiting.[11] Although there is little that American law and legal authorities can do to directly disrupt international counterfeiting and piracy, Customs and Border Protection ("CBP") officers and import specialists are aggressively working together to intercept shipments containing counterfeit and pirated items once they arrive at the American border.[12]

To obtain the assistance of CBP in stopping goods from entering the United States that would infringe on their trademarks, trade names or copyrights, American IP owners can record their IP with CBP through a relatively simple and inexpensive online recordation process.[13] In the 2010 fiscal year alone, CBP seized counterfeit and pirated goods with a total domestic value of $188.1 million and a manufacturer's suggested retail price of $1.4 billion.[14] The total domestic value of seized counterfeit products that presented potential safety or security risks was $42 million.[15]

Stopping patent-infringing imports is more complex. Through a process involving the United States International Trade Commission ("ITC") known as "Section 337," holders of American patents can request that the ITC issues an order excluding patent-infringing products from importation to the United States.[16] The "Section 337" process can be lengthy and expensive, but it can be effective in stopping patent-infringing goods from entering the United States.

III. How to "Go Global"

After securing its IP, an innovation-based company that wants to implement international operations must next decide how it will operate outside the United States and must consider the legal implications, requirements and limitations related to those operations. Although "international business transactional law" does exist, it does not exist in a single source, but rather as codified national laws, treaties, contracts between parties, and industry standards and customs.[17] Companies can "go global" in four ways: (1) export; (2) hiring employees, sales agents, or distributors in the foreign market; (3) licensing; and, (4) foreign direct investment ("FDI"). Each method comes with its own unique advantages, disadvantages, technology-specific concerns, and pitfalls.

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Reliance on reputable third-party-service providers and international trade experts is highly recommended for companies seeking to do business internationally, particularly for a company making its first foray into the global marketplace. These third parties can include freight forwarders, customs brokers, insurance brokers, shippers, attorneys, banks, and a number of other experts and professionals who have experience with various aspects of international transactions. While these experts can provide crucial intelligence and experience to ensure smooth transactions, they must be identified and selected with care. A detailed analysis of how a company should select its international trade associates exceeds the scope of this article, but as a general rule, companies should rely heavily on referrals from their current network of advisors and service providers.

1. EXPORT

Goods can be exported in three ways: (a) directly, (b) through an independent contractor, or (c) through a distributor.[18] Export goods are marketed directly by selling them to customers in a foreign market without local assistance in the foreign country.

For most innovation-based companies, the international sale of goods will also involve the purchaser's use of the IP. For example, if a retailer in Spain buys 1,000 Dell computers for resale in its stores, the retailer will likely want to advertise the computers for resale. As one might expect, Dell will have an interest in how its products are marketed in Spain. As discussed above, it is imperative for an IP-based company to secure its IP rights in the export-destination countries prior to entering an international transaction. Otherwise, the purchaser or some other party could establish his or her own rights locally, which could prevent the true IP owner from further developing the market.

2. EMPLOYEES, INDEPENDENT CONTRACTORS, AND DISTRIBUTORS

American IP owners seeking to do business in foreign countries may create more direct and concrete ties to those countries by placing employees there, engaging local contractors or sales representatives, or finding a local distributor in the foreign country. These relationships can help American companies deliver goods and services more efficiently, tailor products and marketing material to local markets, and implement their sales and development initiatives effectively. However, this increased contact with the foreign market will also increase the potential impact of foreign laws on the company's operations, and can create additional risks to a company's IP assets.

I. Employees

To market its goods for export, American companies can send their own (i.e., American national) employees to the foreign country or they can hire foreign employees. Having employees "in country" provides companies more local contacts and the ability to assess local market conditions and address hiccups in the distribution process.

When a company chooses to hire an employee, it enters an employer–employee relationship, which will likely be impacted by the local employment and tax laws of the foreign country regardless of the wording of any written employment agreement. The company also becomes liable for any torts the employee commits during the scope of his or her employment.[19] Additionally, as an agent of the company, the employee has the power to contractually bind the company, which can be beneficial if the employee is skilled in negotiation, but can be detrimental if the employee has poor judgment.

If the foreign employee is involved in IP development, foreign laws may result in rather novel IP ownership arrangements. Under American law, employers enjoy the protections of "work for hire" laws and additional contractual provisions which automatically transfer inventions and developments to the employer. These laws are not the same in other countries, so IP owners must ascertain the potential impact of such foreign laws on IP developed in foreign countries by their foreign employees.

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II. Independent Contractors

International contractors generally handle one of two functions for American IP-based companies: (1) providing sales/marketing services, or (2) assisting in the development of products or delivery of services. The benefits and risks of each are fairly distinct, but the solution is generally the same: a clear and comprehensively written independent contractor agreement. However, local laws of the host country can sometimes supersede the language of any such agreement, so companies must ascertain any such impact on their independent contractor relationships.

American companies can also market exported goods through a sales representative, which is a middleman who does not accept delivery or take title to the goods.[20] Sales representatives are paid on commission, which is a benefit to the company if this compensation system acts as an incentive for higher performance.[21] But it could easily encourage representatives to fixate on sales to the detriment of customer service and brand image. Since agency principles do not apply to sales representatives, the corresponding benefits and risks are the opposite of those that accompany hiring an employee.[22] Moreover, unless agreed otherwise, the sales representative does not owe a duty of loyalty to the company, thus making the representative free to simultaneously promote competitors' goods and perhaps to share product and strategic information with those same competitors.[23]

Where the independent contractor is involved in the development or manufacture of products or the delivery of services, the primary concern is that the contractor will use the know-how and other IP for its own benefit. For example, suppose an American company contracts with a Chinese manufacturer and the Chinese manufacturer registers the American company's trademark in China. China has a "first to file" trademark system that does not require evidence of prior use or ownership which makes owners of foreign marks vulnerable to third-party registrants in China.[24] The Chinese manufacturer's intent may not be to sell the brands in China, but rather to serve as leverage to ensure the American company would not be able to replace it with another Chinese manufacturing company. Chinese port authorities will not allow trademark-bearing goods to be exported from China unless the exporter is the owner or licensee of all trademarks associated with the goods.[25] Thus,

if an American company uses a different Chinese manufacturer, the prior Chinese manufacturer who obtained the trademark could prevent the goods from leaving China.

When dealing with independent contractors, the best opportunity for a company to protect its IP assets is to ensure the contract clearly and comprehensively defines its rights and the contractor's obligations with respect to IP assets. Of course, agreements must be enforceable to be useful, and the laws of many countries would seem very strange to a company accustomed to the American system that gives significant credence to the principles of freedom of contract between two parties. The laws of the foreign contractor's jurisdiction often presume an unfair negotiating position between the company and the contractor, who is frequently an individual.[26] As such, the local laws may not enforce key provisions of the contract. Alternatively, if American law and venue are chosen in the contract, these are of little practical benefit if the other party is a foreign national with no assets in the U.S.

III. Distributors

Another method of marketing and distributing export goods is through a distributor who buys the goods, resells them, and keeps the margin as profit. Here, a distributor takes title to the product, so it bears the risk of loss and the risk of nonpayment by the foreign customers. Thus, using a distributor involves the least market risk for American companies.[27] An American company would only need one customer and one contract to cover the entire foreign market.

However, distributor relationships also involve other types of risks. The company must carefully select and investigate potential distributors because it must rely on the distributor's good faith and financial soundness in fulfilling responsibilities.[28] Those responsibilities, as well as all other aspects of the distribution relationship, should be clearly and comprehensively addressed in a written distribution agreement executed between the distributor and the company. This agreement must be carefully negotiated and drafted to ensure that the company's interests, including IP assets, are adequately protected.

If the agreement grants the distributor the exclusive right to distribute for 50 years and the distributor underperforms, the American company faces the consequences of breaching a contract or stunting the growth of the foreign market. Furthermore, the distributor may not be able to pay the American company for the goods, may go bankrupt, and may breach the contract and sell the goods in a third country, a market that the American company wanted to develop itself.[29]

[T]he best opportunity for a company to protect its IP assets is to ensure the distribution agreement clearly and comprehensively defines its rights and the contractor's obligations with respect to IP assets.

The IP-related aspects of the agreement are also very important. The distributor will likely be entrusted with the company's brand and given a great deal of control of marketing in the foreign country. In some instances, a distributor will obtain a trademark registration in its country for the products it buys from an American company and sells in its own country. This could present some significant problems if the American company wants to terminate its contract with the distributor. As the owner of the local trademark, the distributor could stop the American company from using the trademark in the foreign country.

As in the case of independent contractors, the best opportunity for a company to protect its IP assets is to ensure the distribution agreement clearly and comprehensively defines its rights and the contractor's obligations with respect to IP assets. Although foreign laws are often more protective of independent contractors than distributors (which are often companies rather than individuals), American IP is more likely to be usurped by a sophisticated and financially viable distributor than by an individual acting as an independent sales representative.

3. LICENSING

Another way to go international is to license production abroad by manufacturing through facilities in the foreign market. The primary benefit is access to the foreign market without substantial direct investment in the country.[30] This method of operating internationally is likely the one with the most obvious pitfalls and concerns for IP-based companies, but it is possible that IP-based companies are overlooking some opportunities. For example, if drafted carefully, a license agreement can be structured in such a way that it actually lowers customs duties.

A technology license is a relatively low-cost way for American companies to generate incremental revenue and have their products and brands enter foreign markets. However,

the risks include the possibility that the technology is not applied according to the licensor's specifications or that know-how and trade secrets are wrongfully disclosed.[31] In addition, the remoteness of the licensee can often make oversight more difficult, which creates the opportunity for the licensee to underreport sales (thus lowering royalty payments), or to continue using IP after the license is terminated.

As described above, in addition to careful license drafting, IP owners must avail themselves of local IP registration as much as possible. Adequate quality control, effective nondisclosure protection, and contractual enforcement are not guaranteed in foreign courts.

4. FOREIGN DIRECT INVESTMENT

The most direct and intimate way for an American company to expand its operations internationally is through foreign direct investment ("FDI"). FDI moves production overseas, typically under the direct or indirect ownership and control of the entity in the home country. In an FDI, companies establish a permanent business base of operations (liaison office, branch office, or subsidiary office)[32] in the foreign country to direct development, production, and sales in that region. An FDI faces more challenges and risks than exporting because the business entity is exposed to the foreign country's market environment as well as its legal, regulatory, and cultural environment. Under FDI, there are three investment options: (a) "Greenfield" investment, (b) mergers and acquisitions, and (c) joint ventures.[33]

I. Greenfield Investment

In a Greenfield investment, the parent company builds or acquires a manufacturing or office facility in the foreign country.[34] Greenfield requires the most upfront capital, has a steep learning curve, and takes the longest to retain capital, which makes this option very risky.[35] The parent company owns all production equipment, so it must liquidate everything to abandon the project.[36] Of course, the benefits are substantial: the company maintains control of the enterprise and does not have to share profits.

An FDI faces more challenges and risks than exporting because the business entity is exposed to the foreign country's market environment as well as its legal, regulatory, and cultural environment.

Some of the key legal risks associated with Greenfield investment for IP-based companies relate to: (1) the hiring and use of local labor to create IP assets, and (2) the way ownership and rights to those developments will be affected by the foreign country's laws. It is imperative that the company understand the IP and employment laws of the foreign country to ensure that all IP that is created and used in the foreign enterprise will be owned by the parent company.

II. Mergers & Acquisitions

Mergers and acquisitions are another FDI option. Mergers combine two entities, whereas acquisitions require one entity to buy the other.[37] Some of the risks associated with mergers and acquisitions include the difficulties of managing foreign employees, buying the company's existing culture, and paying a premium for intangibles. A key benefit is that the American company acquires a business unit that is already operating, which allows the American company to establish a foreign presence quickly.[38]

In addition, if part of the acquisition or merger involves IP assets to be obtained from the foreign company, the American company must conduct thorough IP due diligence prior to closing the transaction to ensure it will acquire all necessary IP rights as part of the transaction. Assuming the American company is the acquirer or controlling entity following a merger, the ongoing risks can be similar to those described above for Greenfield investment.

III. Joint Ventures

An international joint venture ("JV") involves an American company and one or more entities entering into a business venture to develop technology, manufacture and sell products, or deliver services in a foreign country. Benefits include sharing responsibilities, costs, and expertise among the venturers, and the comparative ease of ending the operation. The risks can include concerns over sharing IP, management and profit sharing, and potentially incurring liability of the other venturer.

A JV can be formed either contractually or equitably.[39] An equitable JV refers to a JV in which the participants form a new legal entity wherein each would own a share.[40] This provides a number of structural benefits

for the JV, and the focus is generally on: management, each party's contributions and responsibilities, and the distributions and divisions of assets upon termination of the venture. Contractual JVs do not involve the formation of a new entity, but are instead created via contract among the venturers.[41] Contractual ventures are less expensive and time consuming to form, since all that is needed is a contract. Since there is no legal entity to provide structure, the contract itself must be detailed and comprehensive.

Whether equitable or contractual in structure, innovation-based companies involved in a JV should take special care to ensure that all IP issues are addressed through written agreements among the joint venturers. JV participants commonly employ a "yours, mine, and ours" approach that ensures the IP a company brings to the venture remains its own and specifies how jointly-developed IP will be handled. With respect to jointly-developed IP or IP developed in connection with the JV operations, the participants should clearly specify who will own such IP, and if shared, the limits and rights of each participant regarding the use of the IP.

IV. International Business Transactions

A. International Contracts v. Domestic Contracts

An international sale of goods involves many of the same risks as its domestic counterpart, but the risks are multiplied because the transaction crosses borders. With a few exceptions, some of which are noted below, a well-drafted international contract is essentially the same as a well-drafted domestic contract. However, domestic contracts are usually not as detailed or as specific as they should be because the Uniform Commercial Code ("UCC") fills in the gaps for domestic contracts in the United States.[42] International sale of goods contracts do not share in this luxury and their gaps can result in ambiguities.[43] Thus, it is imperative that the parties of international contracts choose what law should be applied to fill in the gaps.

i. Choice of Law

Although choice of law is an important provision in a domestic contract, choice of law is often the single most important provision in an international contract. The law which would be applied to a contract is often case determinative because of variations in legal heritage, culture, and language. For example, it is likely that the application of Texas law to a contract would lead to a different result than the application of Brazilian law to the same contract. Therefore, by integrating the choice of law into the agreement, the parties can better anticipate how the contract provisions would be interpreted.

In addition to selecting the choice of law for the contract, the parties can select a jurisdiction to decide any disputes related to the contract.

ii. UCC v. CISG

As stated before, most domestic contracts are governed by the UCC, a harmonized system of commercial laws adopted by almost every state in the United States. However, in many international contracts for the sale of goods, the U.N. Convention on Contracts for the International Sale of Goods ("CISG")[44] will apply by default. Having the CISG as the governing law of a contract instead of the UCC can be of critical importance.

The CISG will apply by default in most contracts for the international sale of goods between an American company and a company that is a national of another CISG signatory.[45] Parties can opt out of or opt into the CISG as they wish, but the language in the agreement making the CISG election must be carefully crafted to avoid an accidental "opt in."[46]

iii. Choice of Forum

The choice of forum provision is another important provision in an international contract. Considerations that accompany the choice of forum provision include traveling to the forum country, the court's interpretation of the law, and the judge's ability to understand the language of the contract. In addition to selecting the choice of law for the contract, the parties can select a jurisdiction to decide any disputes related to the contract. Such provisions in international contracts are more important because of issues relating to jurisdiction over the parties and the transaction, enforcement of judgments, legal processes, and travel and litigation expenses.

In the alternative, if the parties do not want to deal with the court systems, they may choose to use arbitration to resolve disputes. If the parties do not agree to arbitration

in the contract, they cannot be forced into arbitration later on. A potential benefit to consider with arbitration is that a settlement can be confidential, whereas the jury verdict is always public.

iv. Translations

Languages and translation are also major considerations in international contracts.[47] Translations, by definition, involve a subjective element of interpretation, which can change the original meaning.[48] Because of subtle differences in translation, it is important for the parties to elect which version of the document will control if a dispute arises.

v. Currency & Payment

Currency and payment systems are also critical considerations in international contracts. Since currencies fluctuate, parties must find a pivot point, such as the exchange rate listed on the *Wall Street Journal* on a particular date. Cash and checks are not viable options of payment in international transactions. Instead, parties must consider wire transfers and letters of credit to manage the risk of non-payment. If a letter of credit is used, the parties must comply with strict documentary requirements if they expect to receive payment.

vi. Incoterms®

International business transactions are also subject to the International Chamber of Commerce's ("ICC") codified set of international commercial terms, called "Incoterms®," which are universally understood acronyms for certain duties and obligations placed on both buyers and sellers. Incoterms® standardize the meanings of these acronyms, which can vary widely from the UCC's definitions when taken out of the domestic context and used in international transactions.[49] The terms identify the exact acts that the buyer must do to receive delivery, what the seller must do to deliver, which party bears what cost, and at what point risk transfers from the seller to the buyer during delivery.[50] These terms are generally incorporated by the parties into a sales contract.

vii. Other Provisions

When dealing with international contracts, American companies must also be aware of the foreign country's laws about jurisdiction and notice. The American party must also recognize that American laws forbid bribery, whereas the foreign country may have alternative trade practices. Unlike domestic contracts, international contracts must make provisions, such as anti-diversion statements, that protect the American party from violating American export laws.

[P]arties must consider wire transfers and letters of credit to manage the risk of non-payment.

B. INTERNATIONAL CIVIL LITIGATION

Planning for international civil litigation is different from planning for litigation that arises from domestic contracts. A company can address many of the unique international concerns in the contract phase (see Section IV(1) "International Contracts v. Domestic Contracts"). However, there are still some issues that cannot be resolved by the terms of the contract such as service of process, enforcement of judgment, and collecting depositions.

Both the Hague Conference on Private International Law and United States Supreme Court opinions have tried to create uniformity and a clearer understanding of the rules involved. The Hague Conference is a global inter-governmental organization that has worked with over 60 non-member states that have become parties to the Hague Conventions.[51] The Conventions are unified rules adopted by the member states, which allow for greater efficiency in transnational litigation. The Hague Conventions have addressed issues regarding jurisdiction, service of process, and collecting evidence.[52]

The United States Supreme Court has sought to develop standards consistent with the Hague Conventions and with the United States Constitution through case law addressing jurisdiction.[53] With the growth of international trade, litigation resulting from international disputes has increased. Due to the general procedure-based nature of litigation, the majority of international civil litigation cases are based on domestic laws and procedures—those of the United States or of another country. However, due to differences in rules of law and procedure across countries, conflicts of law are inevitable.

Generally, the specific issues relating to international civil litigation relate to either an American company involved in a suit in a foreign country or a foreign country being sued in the United States. The key concerns

for American companies involved in a lawsuit in another country are the lack of familiarity with the laws, customs, and procedures, as well as the inability to predict how the court will interpret the agreement. Alternatively, the key issues for American companies seeking to sue a foreign company in American courts are getting jurisdiction over the foreign company and obtaining evidence from foreigners, which can often require the cooperation of foreign governments. Moreover, if the foreign company has no assets in the United States, the American company must face the difficult task of trying to enforce an American judgment against a foreign company in the foreign company's home country.

In addition, if an American company wishes to enforce its IP rights in a foreign country, it must utilize foreign courts that enforce foreign laws. In doing so, the company should anticipate that the remedies available from the courts will be very different from those they would expect from American courts.

V. International Trade Regulation

A. INTRODUCTION

International trade law refers to the regulation of the exchange of goods and services across international borders. If something is an import for one country, it is an export for another country.

Trade regulation involves the preparation and submission of documentation to governmental authorities, compliance with various regulations, and recordkeeping requirements. Compliance is important because non-compliance can result in substantial penalties such as civil and criminal penalties, seizures, forfeitures, and interruption to business. While the use of third parties such as customs brokers and forwarders are available to assist companies involved in international transactions, the parties themselves remain primarily liable for ensuring they are compliant with the international trade laws.

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B. IMPORTS

When goods enter a country from a foreign port, the import laws of the port of arrival will be implicated. In the United States, that means the Customs & Border Protection's ("Customs" or "CBP") regulations will apply.[54] The CBP is an agency within the American Department of Homeland Security that has primary responsibility for enforcing import laws.

American import statutes are found in Title 19 of the American Code and in the corresponding federal regulations.[55] Customs enforces these laws and also ensures that importers comply with the regulations of over forty other governmental agencies, such as the Environmental Protections Agency ("EPA") and the Food and Drug Administration ("FDA").[56] Customs also is responsible for collecting duties, taxes, and fees under the Tariff Act of 1930 as well as detecting and deterring terrorists and weapons from entering the country.[57] Customs assesses penalties and liquidated damages and may detain or seize goods that do not meet requirements.[58] Customs can enforce its legal mandates not only at ports of entry and at the border, but anywhere on American soil.

I. Customs Entry Process

When imports arrive at the American border, the importer of record must file entry documents with the port director at the port of entry. Customs takes possession of the shipment until the necessary paperwork is filed and duties or taxes are paid. To be legally entered all of the following must occur: (1) the shipment must arrive within a port of entry, (2) Customs must authorize the delivery of the imports, and (3) the estimated duties must be paid. Then the imports are released back to the importer of record.[59]

II. Key Elements of Import Declarations

The U.S. customs entry process requires the submission of entry documents containing key information about the shipment.[60] The four principal subjects of information provided to CBP are: classification, valuation, quantity, and country of origin.[61]

A. Classification

Classification is the process of selecting the correct category or subheading from the Harmonized Tariff Schedule of the United States ("HTSUS") which most specifically describes the commodity.[62]

B. Valuation

Both Customs and the Bureau of the Census require that importers accurately report the Customs Value (also called "Entered Value" and "Import Value") of all importations.[63] As such, importers could incur substantial penalties for misstating the value of imported goods on entry documents regardless of whether the value affects the payment of duty. "Transaction Value" is the method preferred by Customs, and it is also the easiest to determine.[64] However, Transaction Value is not always an option (e.g., circumstances in which there was no "sale").[65]

C. Quantity

Import quantity is simply the number or amount of items received by importers, and is usually taken directly from the commercial invoice.[66] The same quantity should be reported on invoices and entry documents.[67]

D. Country of Origin

The "country of origin" of goods is the country where the goods are manufactured, produced, mined, or grown. When production occurs in more than one country, the country of origin is the last country in which the goods underwent a "substantial transformation."[68] A substantial transformation results in goods having a new name, character, or use.[69] All foreign goods imported into the American market must be marked clearly, conspicuously, and indelibly so as to indicate to the ultimate purchaser the origin of the goods.[70]

III. Penalties

Importers are individuals, companies, and their agents—including brokers, carriers, forwarders, etc.—who cause goods to be imported through an American Customs port of entry. Importers must comply with all laws that relate to imports. If importers do not satisfy this burden, either because of negligence or intentional conduct, they can be penalized.

Violators of American import laws risk a host of penalties, even if no loss of duty occurred. Customs can penalize companies, but may also hold individual employees and officers personally liable. Penalties can result in fines and even criminal prosecution.[71] Maximum criminal penalties include forfeiture of goods, fines of up to $500,000, and up to five years imprisonment.[72] Civil enforcement measures include seizure, forfeiture, and penalties of up to 100% of the domestic value of the goods.[73] These are not the only potential penalties that concern importers since importers are also subject to the import-related rules of other agencies.[74] For example, importers of chemicals can also be penalized under laws of the Environmental Protection Agency.[75]

Violators of American import laws risk a host of penalties, even if no loss of duty occurred.

In addition, importing goods that infringe on the intellectual property rights of others can subject an importer to be fined in an amount equal to the domestic resale value of the genuine merchandise. Customs will detain alleged infringing products at the border and, unless the importer can prove it has the authority to use the IP incorporated into the goods, will seize and forfeit the goods.[76]

IV. Recordkeeping

Responsibility to Customs for importations does not end at entry. Importers are also required to maintain certain records related to each import transaction and are subject to hefty penalties for failure to do so.[77] Customs can penalize importers for recordkeeping violations, even if importers have not violated any substantive import law, such as classification or valuation.[78]

Customs often requests documents from importers. Upon receipt of such a request, importers generally have thirty days to produce the documents.[79] The age of the entry usually determines when importers must respond to these requests, and failure to meet that deadline may result in stiff penalties and fines against importers.[80] The maximum penalties include penalties of up to $100,000 per violation for willful violations, and $10,000 per transaction for negligence.[81]

C. EXPORTS

"Exports" are items, such as commodities, software, and technology, sent from the United States to a foreign country. "Re-exports" are items that are also subject to the Export Administration Regulation ("EAR") and are sent from one foreign country to another foreign country.[82] Numerous American agencies have the authority to regulate exports.

However, the export of nearly all commercial items is regulated by the Department of Commerce under the

Export Administration Regulations.[83] The EAR are sometimes referred to as "dual-use" regulations because they regulate items that can have both commercial and military applications.[84] Additionally, the Department of Commerce's Bureau of Industry and Security ("BIS") is the licensing agency responsible for the export or re-export of items subject to the EAR and regulates exports through its Commerce Control List.[85] The American Department of State's Directorate of Defense and Trade Controls implements International Traffic in Arms Regulation ("ITAR").[86]

Unlike imports, there are no duties charged on exported products. Instead, the primary regulatory focus of export laws is security—ensuring that the enemies of America and its allies are unable to obtain technologies and munitions that can be used to do harm. The export control process requires exporters to answer four questions regarding their proposed export:

1. What is it?

The classification of the exported goods will determine whether typical export controls or higher security ITAR controls will be applied to the shipment. Essentially, the more powerful and frightening a commodity is, the higher the level of control for the export.[87]

2. Where is it going?

After the goods have been classified, exporters can consult the regulations to determine if their goods may be shipped to their intended post of destination.

3. Who is receiving it?

A number of "bad guys" lists are maintained by various American government agencies, and American companies are prohibited from engaging in or assisting in any export transactions with a party appearing on any of those lists.[88]

4. How will they use it?

Some products have both a civilian and a military use ("dual use").[89] For these products, the actual intended use ("end-use") of the products will determine whether an export will be allowed.[90]

I. Classification (CCL vs. ITAR)

To determine which agency has jurisdiction over the product, submit a written commodity jurisdiction request to the Department of State.[91] In response, the Office of Defense Trade Control will provide a determination that states whether or not an item or service is covered by the American Munitions List and is therefore subject to the International Traffic in Arms Regulations. A commodity jurisdiction request may also be used for consideration of a re-designation of an article or service currently covered by the American Munitions List.[92] The determination entails consultation among the Departments of State, Defense, Commerce and other American governmental agencies and industry in appropriate cases.[93]

To determine which agency has jurisdiction over the product, submit a written commodity jurisdiction request to the Department of State.

II. Penalties

Violation of export regulations could result in serious fines, penalties, imprisonment, and denial of export privileges.[94]

III. Recordkeeping

The EAR also require records to be kept in certain circumstances. Records must be kept for transactions involving restrictive trade practices or boycotts; exports of commodities, software, or technology from the United States; known re-exports, transshipments, and diversions of items exported from the United States; and exports to Canada if the item involved is to be re-exported.[95] The EAR requires that specific types of records be kept for a period of five years. Documents must be retrievable and completely readable.[96]

IV. Special IP/Technology Issues—Pitfalls

The most common export pitfalls for innovation-based companies are unintended exports, or exports for which a license was required, but not obtained.

V. Non-Physical Exports

In addition to the physical shipment of goods across borders, an "export" includes the transfer of software, apps, or other technology and technical data by email, as well as downloads from a website or company intranet. Failure to recognize these transactions as exports could result in an inadvertent violation of American export laws.[97]

VI. "DEEMED EXPORTS"

An exporter may have to obtain an export license before it can share technological information with a foreign national, assuming that technology is controlled or restricted under the EAR.[98] Any release of technology to a foreign national, subject to the EAR, is deemed to be an export to the home country or countries of the foreign national.[99] An export license may be required even if the underlying technology itself is never actually exported.[100]

The potential penalties for "exporting" a deemed export without a license are identical to the penalties levied against those who actually export goods in violation of the EAR: fines, loss of export privileges, and even criminal prosecutions.[101]

VII. CO-DEVELOPMENT OF TECHNOLOGY

In addition, American companies working on technology developments with foreign partners must ensure their information and the sharing of their expertise do not violate American export laws. This involves ensuring that their cohorts are listed neither as "bad guys" nor nationals of prohibited countries. Additionally, it requires American companies to be certain that the technology is not improperly transferred by their co-developers in violation of American export laws.

D. OTHER TRADE REGULATIONS

In addition to the regulation of exports and imports, the American government enforces a number of other international trade laws to protect domestic markets, enforce U.S. trade policies, and minimize corruption. Some of these laws include: imposing antidumping/countervailing duties ("AD/CVD") passing the Foreign Corrupt Practices Act ("FCPA"), imposing sanctions, and imposing anti-boycott laws.

I. AD/CVD

AD/CVD laws are designed to protect domestic industries from injury due to unfair trade by assessing additional duties on subject products to effectively raise the domestic resale price of those goods.[102] There are two requirements for the imposition of AD/CVD: (1) there must be unfair trade practices (e.g., dumping or foreign subsidies), and (2) these practices must cause injury of adverse trade effects.[103] An affirmative final determination is issued from an original AD/CVD investigation whereby the AD/CVD rate is ordered.[104]

The United States can collect antidumping duties on imported goods sold for less than fair value (e.g., at a price below that of the home market and the exporter's domestic market) if the sale of the goods caused or is likely to cause material injury to an American industry.[105] If fair value cannot be determined by reference to the exporter's domestic market, the calculation of cost can be determined by production cost plus a reasonable amount for profit and administrative, selling, and general costs.[106] Similar to the collection of antidumping duties, the United States can collect countervailing duties to offset any unfair competitive advantage that a foreign producer might gain over an American producer because of foreign subsidies.[107]

The FCPA's accounting provisions are designed to prevent illegal conduct of publicly traded companies by requiring them to keep records that would reveal illegal payments.

II. FCPA

The FCPA[108] was enacted to make it illegal for certain classes of people and entities to make payments to foreign government officials to assist in obtaining or retaining business.[109] Issuers of securities, domestic concerns, and others all fall under the FCPA's anti-bribery provisions.[110] All American nationals and businesses, including their foreign subsidiaries, are prohibited from bribery anywhere in the world.[111] Foreign nationals and businesses also fall under the anti-bribery requirements when they are in the United States or its territory.[112]

However, the FCPA does not actually prohibit "bribery." Instead, it prohibits payments made to foreign officials to corruptly influence them to provide any improper advantage.[113] Yet, this prohibition is even broader than it seems. The FCPA's accounting provisions are designed to prevent illegal conduct of publicly traded companies by requiring them to keep records that would reveal illegal payments.[114]

The biggest pitfall facing American companies is the involvement of foreign companies. An American company that acquires a foreign subsidiary or enters a partnership with a foreign entity will often be exposed to the foreign entity's liability.[115] Even when these foreign companies agree

to comply with the FCPA they may not do so. Some will simply continue with business as usual while others may err because they are unfamiliar with FCPA requirements. American companies should take a firm position on FCPA compliance and take an active role in the oversight of foreign entities' practices.[116] Since American companies can be held vicariously liable for breaches of the FCPA of which they were unaware, the only way to prevent a surprise is to proactively seek out and remedy problems. Thus, American firms should seek to extend their normal compliance regime to their subsidiaries. Another important step is to integrate accounting practices where feasible, because consistency in compliance will increase transparency and help spot irregularities so they may be corrected.

A second pitfall is the increasing number of foreign anti-bribery laws. The FCPA imposes liability on American companies that violate local law, so a legal problem in some distant country can suddenly migrate home.[117] In most cases, this can be avoided by retaining reliable local counsel and following their advice.

Third, while this issue has not yet been raised in court, a parent company may expose itself to non-FCPA liability if the company's FCPA compliance efforts cause it to exert too much control over a subsidiary. When a parent company dominates a subsidiary, the corporate protections from liability may disappear. This can be avoided when the officers of a subsidiary have been vetted for awareness and understanding of FCPA compliance or by relying on external auditing by a third party.

III. Sanctions/OFAC

The Office of Foreign Assets Control ("OFAC")[118] is an agency of the American Department of the Treasury. OFAC enforces economic and trade sanctions which were put in place to carry out American foreign policy and national security goals.[119] For example, sanctions may be created to target terrorists, drug traffickers, and those who seek to proliferate weapons of mass destruction.[120] Sanctions can be comprehensive against substantially all commerce with a foreign country, such as the Cuban and North Korean sanctions, or more selectively, target-only dealings with the foreign government or certain industries.[121] In addition to limiting trade with certain foreign nationals, sanctions can block assets, making payments for past transactions difficult to obtain.[122]

Common anti-boycott pitfalls include providing information unwittingly, failure to report, and use of foreign agents or subsidiaries.

Although the OFAC is the agency with the primary responsibility for administering our nation's sanctions laws, the Bureau of Industry and Security and the State Department also have jurisdiction over the export of dual-use and munitions items.[123]

IV. Anti-Boycott Laws

Anti-boycott laws are designed to discourage American persons and businesses from cooperating with or participating in international boycotts, which are not sanctioned by the American government.[124] These laws were initially passed to impede the Arab League's boycott of Israel in the 1970s, but have been expanded to prohibit participating in or otherwise assisting any non-U.S. supported boycott.[125] Common anti-boycott pitfalls include providing information unwittingly, failure to report, and use of foreign agents or subsidiaries.[126]

E. TRADE AGREEMENTS & SPECIAL PROGRAMS

International trade agreements are pacts, potentially binding rules of both domestic and international law, which create preferential trade arrangements between the nations involved. They encompass a variety of commerce-related issues generally with the goal of liberalizing trade and fostering relationships with political allies. Free trade agreements provide reciprocal benefits while others offer unilateral benefits with more abstract aims in mind such as the spread of democracy or regional integration. The proliferation of free trade agreements is a move toward globalization.

I. WTO: TRIPS

For U.S. IP owners, one of the most significant international trade agreements for U.S. accession and involvement in and with the World Trade Organization, and its side agreement relating to IP rights, is Trade Related Aspect of Intellectual Property Rights ("TRIPS"). TRIPS is a mandatory side agreement that all WTO members must accept, which is critical since TRIPS requires each country to provide a number of key IP protections, such as "national treatment."[127] This protection ensures that

foreign IP owners have the same protections and rights under the foreign country laws as those afforded to the foreign country's own nationals.

What TRIPS does not do is require U.S.-style IP protection or enforcement. Instead, TRIPS merely establishes a baseline of IP protection that all WTO members must provide, and affords U.S. IP owners the opportunity to protect and defend its IP in member countries.[128]

II. Select Examples of Trade Agreements

In addition to the WTO, which covers the vast majority of all trade and all trading nations in the world, the U.S. is party to a number of regional and bi-lateral trade agreements to encourage the free movement of goods and services between the U.S. and various other trading partner nations. While these trade agreements do not generally or directly address IP rights, they do encourage the increase in trade in goods, which can allow U.S. IP owners to obtain international production and materials at lower costs, as well as to export their products into foreign markets more easily and cheaply. Of the numerous agreements to which the U.S. is a party, some key recent trade agreements include:

A. NAFTA

The North American Free Trade Agreement ("NAFTA")[129] is a free trade agreement among Canada, Mexico, and the United States which was implemented on January 1, 1994. NAFTA's objectives include eliminating barriers to trade between Canada, Mexico, and the United States; promoting fair competition; increasing investment opportunities; providing effective protection for intellectual property rights; and encouraging further multilateral cooperation.[130] NAFTA calls for the elimination of most import tariffs on goods originating in Mexico or Canada.[131]

B. CAFTA–DR

The Dominican Republic–Central America Free Trade Agreement ("CAFTA–DR") is a free trade agreement between the United States, Dominican Republic, and the Central American countries of Costa Rica, El Salvador, Guatemala, Honduras, and Nicaragua.[132]

III. Select Examples of Preference Programs (GSP, AGOA)

Congress enacted duty preference programs to assist less-developed economies. By allowing goods from these countries to be imported duty-free, these goods are more attractive to American importers. For example, the Generalized System of Preference ("GSP")[133] gives preferential treatment to developing countries, and the African Growth Opportunity Act ("AGOA")[134] expands duty-free benefits to thirty-seven African countries on certain product lines in addition to GSP.

IV. Foreign-Trade Zones

Foreign-trade zones ("FTZs") are areas within the territorial United States that are considered to be outside the American Customs Territory.[135] Because of this, these areas receive special treatment with regards to duties and certain taxes and fees.[136] Upon entering a zone, raw materials are assigned a status ("duty status") which could be either: Domestic, Privileged Foreign ("PF"), Non-privileged Foreign ("NP"), or zone restricted status.[137] Different rules regarding duties apply to each status.

Although there a number of benefits associated with FTZs, the principal benefit is the ability to manipulate tariff rates (e.g., by shipping raw materials into the FTZ, processing them into finished products, and then entering the goods into the American Customs territory at the lower of the two duty rates).[138] Other benefits include exemption from state and local inventory taxes as long as goods remain in the zone, and eligibility to participate in various money and timesaving programs, such as being able to file all shipments from the zone in a given week on a single "weekly entry," which is an enormous relief on administrative costs.[139]

VI. Conclusion

As discussed above, technology- and other innovation-based companies are key beneficiaries of globalization, but are also acutely vulnerable to a number of risks beyond those experienced by other types of companies. By working with experienced international counsel and other experts, IP-based companies can effectively manage their risks while taking advantage of the opportunities afforded by the international marketplace.

End Notes

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