

Chapter 7

The International Legal Environment:

PLAYING BY THE RULES



CHAPTER OUTLINE

Global Perspective: The Pajama Caper

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- Common vs. Code Law
- Islamic Law
- Marxist–Socialist Tenets

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International Dispute Resolution

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- Arbitration
- Litigation

Protection of Intellectual Property Rights: A Special Problem

- Counterfeiting and Piracy
- Inadequate Protection
- Prior Use versus Registration
- International Conventions
- Other Managerial Approaches to Protecting Intellectual Property

Cyberlaw: Unresolved Issues

- Domain Names and Cybersquatters
- Taxes
- Jurisdiction of Disputes and Validity of Contracts

Commercial Law within Countries

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U.S. Laws Apply in Host Countries

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- U.S. Antitrust Laws that Apply in Foreign Markets
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Export Restrictions

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- Determining Export Requirements
- ELAIN, STELA, ERIC, and SNAP

CHAPTER LEARNING OBJECTIVES

What you should learn from Chapter 7:

- LO1** The four heritages of today's legal systems
- LO2** The important factors in the jurisdiction of legal disputes
- LO3** The various methods of dispute resolution
- LO4** The unique problems of protecting intellectual property rights internationally
- LO5** How to protect against piracy and counterfeiting
- LO6** The many issues of evolving cyberlaw
- LO7** The legal differences between countries and how those differences can affect international marketing plans
- LO8** The different ways U.S. laws can be applied to U.S. companies operating outside the United States
- LO9** The steps necessary to move goods across country borders

Global Perspective

THE PAJAMA CAPER

Six headlines illustrate the entanglements possible when U.S. law, host-country law, and a multinational company collide:

- “Wal-Mart’s Cuban-Made Pajamas Defy Embargo”
- “Wal-Mart Ignites Row by Pulling Cuban Pajamas off Shelves in Canada”
- “Canada, U.S. Wager Diplomatic Capital in a High-Stakes Pajama Game”
- “Cuban Quandary: Wal-Mart in Hot Water for Yanking Pajamas”
- “Canada Probes Wal-Mart Move against Cuban Pajamas”
- “Wal-Mart Puts Cuban Goods Back on Sale”

The controversy arose over a U.S. embargo forbidding U.S. businesses to trade with Cuba and concern whether or not the embargo could be enforced in Canada. Walmart was selling Cuban-made pajamas in Canada. When Walmart officials in the United States became aware of the origin of manufacture, they issued an order to remove all the offending pajamas because it is against U.S. law (the Helms-Burton Act) for a U.S. company or any of its foreign subsidiaries to trade with Cuba. Canada was incensed at the intrusion of U.S. law on Canadian citizens. The Canadians felt they should have the choice of buying Cuban-made pajamas.

Walmart was thus caught in the middle of conflicting laws in Canada and the United States and a Canada–U.S. foreign policy feud over the extraterritoriality of U.S. law. Walmart Canada would be breaking U.S. law if it continued to sell the pajamas, and it would be subject to a million-dollar fine and possible imprisonment of its managers. However, if the company pulled the pajamas out of Canadian stores as the home office ordered, it would be subject to a \$1.2 million fine under Canadian law. After discussion with Canadian authorities, Walmart resumed selling the pajamas. Canada was upset with the United States for attempting to impose its laws on Canadian companies (Walmart Canada is a subsidiary of Walmart U.S.), while the United States says that Walmart was violating its laws in not abiding by the boycott against Cuba. The situation illustrates the reality of the legal environment and international marketing—companies are subject to both home-country laws and host-country laws when doing business in another country. The federal government finally settled with Walmart in 2003, and the pajama caper was finally closed. However, as indicated in the previous chapter, the governments of Cuba and the United States have yet to settle.

Sources: *Boston Globe*, March 3, 1997; *St. Louis Post-Dispatch*, March 9, 1997; *Washington Post*, March 14, 1997, p. A6; *The Wall Street Journal*, March 14, 1997, p. B4; John W. Boscardiol, “An Anatomy of a Cuban Pyjama Crisis,” *Law and Policy in International Business*, Spring 1999, p. 439; William Booth and Mary Beth Sheridan, “Cuba Detains U.S. Government Contractor,” *Washington Post*, December 13, 2009, p. A12.

How would you like to play a game in which the stakes were high, there was no standard set of rules to play by, the rules changed whenever a new player entered the game, and, when a dispute arose, the referee used the other players' rules to interpret who was right? This game fairly well describes the international legal environment. Because no single, uniform international commercial law governing foreign business transactions exists, the international marketer must pay particular attention to the laws of each country within which it operates.¹ An American company doing business with a French customer has to contend with two jurisdictions (United States and France), two tax systems, two legal systems, and other supranational sets of European Union laws and WTO regulations that may override commercial laws of the countries. The situation is similar when doing business in Japan, Germany, or any other country. Laws governing business activities within and between countries are an integral part of the legal environment of international business.

The legal systems of different countries are so disparate and complex that it is beyond the scope of this text to explore the laws of each country individually. There are, however, issues common to most international marketing transactions that need special attention when operating abroad. Jurisdiction, dispute resolution, intellectual property, the extraterritoriality of U.S. laws, cyberlaw, and associated problems are discussed in this chapter to provide a broad view of the international legal environment. Although space and focus limit an in-depth presentation, the material presented should be sufficient for the reader to conclude that securing expert legal advice is a wise decision when doing business in another country. The foundation of a legal system profoundly affects how the law is written, interpreted, and adjudicated. The place to begin is with a discussion of the different legal systems.

Bases for Legal Systems

LO1

The four heritages of today's legal systems

Four heritages form the bases for the majority of the legal systems of the world: (1) common law, derived from English law and found in England, the United States, Canada,² and other countries once under English influence; (2) civil or code law, derived from Roman law and found in Germany, Japan, France, and non-Islamic and non-Marxist countries; (3) Islamic law, derived from the interpretation of the Koran and found in Pakistan, Iran, Saudi Arabia, and other Islamic states; and (4) a commercial legal system in the Marxist–socialist economies of Russia and the republics of the former Soviet Union, Eastern Europe, China, and other Marxist–socialist states whose legal system centered on the economic, political, and social policies of the state. As each country moves toward its own version of a free market system and enters the global market, a commercial legal system is also evolving from Marxist–socialist tenets. China has announced that it will adopt a constitution-based socialist legal system with Chinese characteristics.

The differences among these four systems are of more than theoretical importance because due process of law may vary considerably among and within these legal systems. Even though a country's laws may be based on the doctrine of one of the four legal systems, its individual interpretation may vary significantly—from a fundamentalist interpretation of Islamic law as found in Pakistan to a combination of several legal systems found in the United States, where both common and code law are reflected in the legal system.

One measure of the importance of the legal system in each country is the number of attorneys per capita. Please see Exhibit 7.1. Judging by that metric, the legal system is called upon to settle commercial disputes much more frequently in the United States than in almost all countries, and particularly China. China's legal system is really only 30 years old; in the 1980s, the country had 3,000 attorneys, and now the number is closer to 150,000. The number of law schools has exploded from 8 in 1976 to almost 600 now.³ By comparison, the

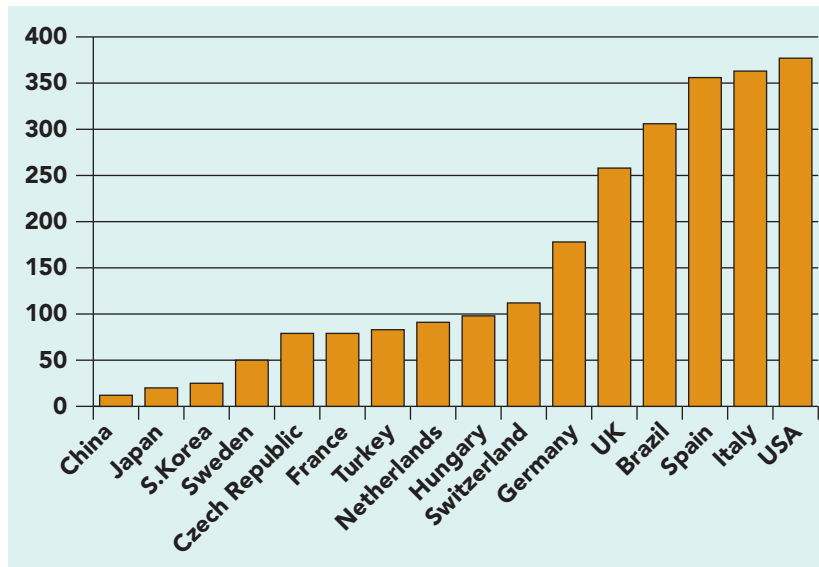
¹Ilan Greenberg, "American Snared in Kazakh Legal Dispute," *The New York Times*, April 23, 2007, p. A11; Lorraine Woellert, "Made in China. Sued Here." *BusinessWeek*, July 9 and 16, 2007, p. 9.

²All the provinces of Canada have a common-law system with the exception of Quebec, which is a code-law province. All the states in the United States are common law except Louisiana, which is code law.

³Randy Peerenboom, "Economic Development and the Development of the Legal Profession in China," presentation, Oxford University, 2006.

Exhibit 7.1**Lawyers per 100,000
People in Selected
Countries**

Sources: Kana Inagaki, "Major Legal Reforms Expected to Bring Wave of New Lawyers in Japan," *Associated Press*, August 22, 2007; Randy Peerenboom, "Economic Development and the Development of the Legal Profession in China," presentation at Oxford University, 2006; Council of Bars and Law Societies of Europe, <http://www.ccbe.edu>, 2010; <http://www.oab.org.br>, 2010; <http://www.abanet.org>, 2010.



legal system in Japan is much more developed. Even so, as the Japanese economy continues to become more integrated in the global market, the need for attorneys is burgeoning. There are approximately 23,000 attorneys there now, and the Japanese government intends to grow that number to 50,000 by 2018⁴.

**Common vs.
Code Law**

The basis for **common law**⁵ is tradition, past practices, and legal precedents set by the courts through interpretations of statutes, legal legislation, and past rulings. Common law seeks "interpretation through the past decisions of higher courts which interpret the same statutes or apply established and customary principles of law to a similar set of facts." **Code law**,⁶ in contrast, is based on an all-inclusive system of written rules (codes) of law. Under code law, the legal system is generally divided into three separate codes: commercial, civil, and criminal.

Common law is recognized as not being all-inclusive, whereas code law is considered complete as a result of catchall provisions found in most code-law systems. For example, under the commercial code in a code-law country, the law governing contracts is made inclusive with the statement that "a person performing a contract shall do so in conformity with good faith as determined by custom and good morals." Although code law is considered all-inclusive, it is apparent from the foregoing statement that some broad interpretations are possible in order to include everything under the existing code.

Steps are being taken in common-law countries to codify commercial law even though the primary basis of commercial law is common law, that is, precedents set by court decisions. An example of the new uniformity is the acceptance of the Uniform Commercial Code by most states in the United States. Even though U.S. commercial law has been codified to some extent under the Uniform Commercial Code, the philosophy of interpretation is anchored in common law.

As discussed later in the section on the protection of intellectual property, laws governing intellectual property offer the most striking differences between common-law and code-law systems. Under common law, ownership is established by use; under code law, ownership is determined by registration. In some code-law countries, certain agreements may not be enforceable unless properly notarized or registered; in a common-law country,

⁴Kana Inagaki, "Major Legal Reforms Expected to Bring Wave of New Lawyers in Japan," *Associated Press*, August 22, 2007.

⁵Also known as English law.

⁶Also known as the Napoleonic Code.

the same agreement may be binding so long as proof of the agreement can be established. Although every country has elements of both common and code law, the differences in interpretation between common- and code-law systems regarding contracts, sales agreements, and other legal issues are significant enough that an international marketer familiar with only one system must enlist the aid of legal counsel for the most basic legal questions.

Another illustration of how fundamental differences in the two systems can cause difficulty is in the performance of a contract. Under common law in the United States, the impossibility of performance does not necessarily excuse compliance with the provisions of a contract unless compliance is impossible because of an act of God, such as some extraordinary occurrence of nature not reasonably anticipated by either party of a contract. Hence floods, lightning, earthquakes, and similar events are generally considered acts of God. Under code law, acts of God are not limited solely to acts of nature but are extended to include “unavoidable interference with performance, whether resulting from forces of nature or unforeseeable human acts,” including such things as labor strikes and riots.

Consider the following situations: A contract was entered into to deliver a specific quantity of cloth. In one case, before the seller could make delivery, an earthquake caused the destruction of the cloth and compliance was then impossible. In the second case, pipes in the sprinkler system where the material was stored froze and broke, spilling water on the cloth and destroying it. In each case, loss of the merchandise was sustained and delivery could not be made. Were the parties in these cases absolved of their obligations under the contract because of the impossibility of delivery? The answer depends on the system of law invoked.

In the first situation, the earthquake would be considered an act of God under both common and code law, and impossibility of performance would excuse compliance under the contract. In the second situation, courts in common-law countries would probably rule that the bursting of the water pipes did not constitute an act of God if it happened in a climate where freezing could be expected. Therefore, impossibility of delivery would not necessarily excuse compliance with the provisions of the contract. In code-law countries, where the scope of impossibility of performance is extended considerably, the destruction might very well be ruled an act of God, and thus, release from compliance with the contract could be obtained.

Islamic Law

The basis for the *Shari’ah* (Islamic law) is interpretation of the Koran. It encompasses religious duties and obligations, as well as the secular aspect of law regulating human acts. Broadly speaking, Islamic law defines a complete system that prescribes specific patterns of social and economic behavior for all individuals. It includes issues such as property rights, economic decision making, and types of economic freedom. The overriding objective of the Islamic system is social justice.

Among the unique aspects of Islamic law is the prohibition against the payment of interest. The Islamic law of contracts states that any given transaction should be devoid of *riba*, which is defined as unlawful advantage by way of excess of deferment, that is, interest or usury. Prohibiting the receipt and payment of interest is the nucleus of the Islamic system. However, other principles of Islamic doctrine advocate risk sharing, individuals’ rights and duties, property rights, and the sanctity of contracts. The Islamic system places emphasis on the ethical, moral, social, and religious dimensions to enhance equality and fairness for the good of society. Another principle of the Islamic legal system is the prohibition against investment in those activities that violate the *Shari’ah*. For example, any investment in a business dealing with alcohol, gambling, and casinos would be prohibited.

Prohibition against the payment of interest affects banking and business practices severely.⁷ However, certain acceptable



Banking in Dubai, UAE, requires an understanding of Islamic law and customs. Prohibition against the payment of interest and prohibition against investments in businesses dealing with alcohol and gambling are two of the tenets of Islamic law that affect banking.

⁷Sugata Ghosh, “Government Asks RBI to Draw up Roadmap for Islamic Banking,” *Economic Times*, July 6, 2005.

practices adhere to Islamic law and permit the transaction of business. Mortgages for property are difficult because payment of interest is forbidden under Islamic law. Buyers of real property have to use a financier, who buys the property and then sells it to them in return for repayments of the capital. Instead of charging interest, a financier either sells the property at a higher price or sells it at the same price and takes additional payments to cover what would have been interest. Of the other ways to comply with Islamic law in financial transactions, trade with markup or cost-plus sale (*murabaha*) and leasing (*ijara*) are the most frequently used. In both *murabaha* and *ijara*, a mutually negotiated margin is included in the sale price or leasing payment. These practices meet the requirements of *Shari'ah* by enabling borrowers and lenders to share in the rewards as well as losses in an equitable fashion. They also ensure that the process of wealth accumulation and distribution in the economy is fair and representative of true productivity. Strict fundamentalists often frown on such an arrangement, but it is practiced and is an example of the way the strictness of Islamic law can be reconciled with the laws of non-Islamic legal systems.

Because the laws are based on interpretation of the Koran, the international marketer must have knowledge of the religion's tenets and understand the way the law may be interpreted in each region. Regional courts can interpret Islamic law from the viewpoint of fundamentalists (those that adhere to a literal interpretation of the Koran), or they may use a more liberal translation. A company can find local authorities in one region willing to allow payment of interest on deferred obligations as stipulated in a contract, while in another region, all interest charges may be deleted and replaced with comparable "consulting fees." In yet another, authorities may void a contract and declare any payment of interest illegal. Marketers conducting business in Islamic-law countries must be knowledgeable about this important legal system.

Marxist–Socialist Tenets

As socialist countries become more directly involved in trade with non-Marxist countries, it has been necessary to develop a commercial legal system that permits them to engage in active international commerce. The pattern for development varies among the countries because each has a different background, and each is at a different stage in its development of a market-driven economy. For example, central European countries such as the Czech Republic and Poland had comprehensive codified legal systems before communism took over, and their pre–World War II commercial legal codes have been revised and reinstated. Consequently, they have moved toward a legal model with greater ease than some others have. Russia and most of the republics of the former Soviet Union and China have had to build from scratch an entire commercial legal system. Under the premise that law, according to **Marxist–socialist tenets**, is strictly subordinate to prevailing economic conditions, such fundamental propositions as private ownership, contracts, due process, and other legal mechanisms have had to be developed. China and Russia differ, however, in that each has taken a different direction in its political economic growth. Russia is moving toward a democratic system. China is attempting to activate a private sector within a multi-component, or mixed, economy in a socialist legal framework; that is, it tries to "perform its functions according to law and contribute to the development of socialist democracy and political civilization in China."

Both countries have actively passed laws, though the process has been slow and often disjointed. China has implemented hundreds of new laws and regulations governing trade, yet the process is hampered by vaguely written laws, the lack of implementation mechanisms for the new laws, and an ineffective framework for dispute resolution and enforcement. A good example is China's attempt to control what goes on in Chinese cyberspace by applying the States Secrets Law to the Internet. The definition of a state secret is so broad that it can cover any information not cleared for publication with the relevant authorities.

Russia's experience has been similar to China's, in that vaguely worded laws have been passed without mechanisms for implementation. The situation in Russia is often described as chaotic because of the laws' lack of precision. For example, to illegally receive or disseminate commercial secrets has become a crime, but the law provides no exact definition of a commercial secret. Copyright law violations that cause "great damage" are listed but with no clear definition of how much damage constitutes "great." Both China and Russia

are hampered by not having the heritage of a legal commercial code to build on, as many of the Eastern-bloc European countries had.

The international marketer must be concerned with the differences among common law, code law, Islamic law, and socialist legal systems when operating between countries; the rights of the principals of a contract or some other legal document under one law may be significantly different from their rights under the other. It should be kept in mind that there could also be differences between the laws of two countries whose laws are based on the same legal system. Thus, the problem of the marketer is one of anticipating the different laws regulating business, regardless of the legal system of the country.

Jurisdiction in International Legal Disputes

LO2

The important factors in the jurisdiction of legal disputes

Determining whose legal system has jurisdiction when a commercial dispute arises is another problem of international marketing. A frequent error is to assume that disputes between citizens of different nations are adjudicated under some supranational system of laws. Unfortunately, no judicial body exists to deal with legal commercial problems arising among citizens of different countries. Confusion probably stems from the existence of international courts such as the World Court at The Hague and the International Court of Justice, the principal judicial organ of the United Nations. These courts are operative in international disputes between sovereign nations of the world rather than between private citizens and/or companies.

Legal disputes can arise in three situations: between governments, between a company and a government, and between two companies. The World Court can adjudicate disputes between governments, whereas the other two situations must be handled in the courts of the country of one of the parties involved or through arbitration. Unless a commercial dispute involves a national issue between nation states, the International Court of Justice or any similar world court does not handle it. Because there is no “international commercial law,” the foreign marketer must look to the legal system of each country involved—the laws of the home country, the laws of the countries within which business is conducted, or both.⁸

When international commercial disputes must be settled under the laws of one of the countries concerned, the paramount question in a dispute is: Which law governs? Jurisdiction is generally determined in one of three ways: (1) on the basis of jurisdictional clauses included in contracts, (2) on the basis of where a contract was entered into, or (3) on the basis of where the provisions of the contract were performed.

The most clear-cut decision can be made when the contracts or legal documents supporting a business transaction include a jurisdictional clause. A clause similar to the following establishes jurisdiction in the event of disagreements:

That the parties hereby agree that the agreement is made in Oregon, USA, and that any question regarding this agreement shall be governed by the law of the state of Oregon, USA.

This clause establishes that the laws of the state of Oregon would be invoked should a dispute arise. If the complaint were brought in the court of another country, it is probable that the same Oregon laws would govern the decision. Cooperation and a definite desire to be judicious in foreign legal problems have led to the practice of foreign courts judging disputes on the basis of the law of another country or state whenever applicable. Thus, if an injured party from Oregon brings suit in the courts of Mexico against a Mexican over a contract that included the preceding clause, it would not be unusual for the Mexican courts to decide on the basis of Oregon law. This tendency assumes, of course, it has been recognized that Oregon law prevailed in this dispute, either as a result of the prior agreement by the parties or on some other basis.

⁸For a legal and thorough discussion of the globalization of jurisdiction, see Paul Schiff Berman, “The Globalization of Jurisdiction,” *University of Pennsylvania Law Review*, December 2002, p. 311; Yadong Luo, “Transactional Characteristics, Institutional Environment, and Joint Venture Contracts,” *Journal of International Business Studies* 36, no. 2 (2005), pp. 209–30.

International Dispute Resolution When things go wrong in a commercial transaction—the buyer refuses to pay, the product is of inferior quality, the shipment arrives late, or any one of the myriad problems that can arise—what recourse does the international marketer have? The first step in any dispute is to try to resolve the issue informally, but if that fails, the foreign marketer must resort to more resolute action. Such action can take the form of conciliation, arbitration, or, as a last resort, litigation. Most international businesspeople prefer a settlement through arbitration rather than by suing a foreign company.

LO3

The various methods of dispute resolution

Conciliation Most disputes that arise in commercial transactions are settled informally. When resolution is not forthcoming however, conciliation can be an important first step in settling a dispute. **Conciliation** (also known as *mediation*) is a nonbinding agreement between parties to resolve disputes by asking a third party to mediate differences. The function of the mediator is to carefully listen to each party and to explore, clarify, and discuss the various practical options and possibilities for a solution with the intent that the parties will agree on a solution. Unlike arbitration and litigation, conciliation sessions are private, and all conferences between parties and the mediator are confidential; the statements made by the parties may not be disclosed or used as evidence in any subsequent litigation or arbitration. The track record for the conciliation process is excellent, with a majority of disputes reaching settlement and leading to the resumption of business between the disputants.

Conciliation is considered especially effective when resolving disputes with Chinese business partners, because they feel less threatened by conciliation than arbitration. The Chinese believe that when a dispute occurs, informal, friendly negotiation should be used first to solve the problem; if that fails, conciliation should be tried. In fact, some Chinese companies may avoid doing business with companies that resort first to arbitration. Conciliation can be either formal or informal. Both sides agreeing on a third party to mediate can establish informal conciliation. Formal conciliation is conducted under the auspices of some tribunal such as the Beijing Conciliation Center, which assigns one or two conciliators to mediate. If an agreement is reached, a conciliation statement based on the signed agreement is recorded. Although conciliation may be the friendly route to resolving disputes in China, it is not legally binding; thus, an arbitration clause should be included in all conciliation agreements. Experience has shown that having an arbitration clause in the conciliation agreement makes it easier to move to arbitration if necessary.

Arbitration If conciliation is not used or an agreement cannot be reached, the next step is *arbitration*. When all else fails, arbitration rather than litigation is the preferred method for resolving international commercial disputes. The usual **arbitration** procedure is for the parties involved to select a disinterested and informed party or parties as referees to determine the merits of the case and make a judgment that both parties agree to honor. Although informal arbitration is workable, most arbitration is conducted under the auspices of one of the more formal domestic and international arbitration groups organized specifically to facilitate the resolution of commercial disputes. These groups have formal rules for the process and experienced arbitrators to assist. In most countries, decisions reached in formal arbitration are enforceable under the law.

The popularity of arbitration has led to a proliferation of arbitral centers established by countries, organizations, and institutions. All have adopted standardized rules and procedures to administer cases, and each has its strengths and weaknesses. Some of the more active are the following:

- The Inter-American Commercial Arbitration Commission
- The Canadian-American Commercial Arbitration Commission (for disputes between Canadian and U.S. businesses)
- The London Court of Arbitration (decisions are enforceable under English law and English courts)
- The American Arbitration Association (www.adr.org/)
- The International Chamber of Commerce (www.iccwbo.org/; select Arbitration)

CROSSING BORDERS 7.1

České Budějovice, Privatization, Trademarks, and Taste Tests—What Do They Have in Common with Anheuser-Busch? Budweiser, That's What!

Anheuser-Busch (AB) launched a massive public relations program in the small Czech town of České Budějovice, where a local brewery produces “Budweiser Budvar.” Anheuser-Busch planted trees along main avenues, opened a new cultural center offering free English courses to citizens and management advice to budding entrepreneurs, and ran newspaper ads touting the possibilities of future cooperation.

Anheuser-Busch's goal was to win support for a minority stake in the Czech state-owned brewery, Budějovický Budvar N.P., when the government privatized it. So why was AB interested in a brewery whose annual production of 500,000 barrels is the equivalent of two days' output for AB?

Part ownership is critically important to Anheuser-Busch for two reasons. It is in search of new markets in Europe, and it wants to be able to market the Budweiser brand in Europe. So what's the connection? AB doesn't have the rights to use the Budweiser brand in Europe because Budějovický Budvar N.P. owns it. Its public relations plan didn't work because many Czechs see Budvar as the “family silver.” Although the Czech prime minister asked publicly for American investors to put money into the Czech Republic, Czech Budweiser was not on the government's privatization list. “I believe in the strength of American investors, but I do not believe in the quality of American beer.”

Anheuser-Busch established the name Budweiser in the United States when German immigrants founded the St. Louis family brewery and began selling under the Budweiser brand in 1876, 19 years before the Czech brewery opened. The Czechs claim they have been using the name since before Columbus discovered the New World and that Budweiser refers to Budwis, the original name of the city where Budvar is located. That is the name commonly referred to beer brewed in that area hundreds of years before AB started brewing Budweiser.

The Anheuser-Busch Company markets Budweiser brand beer in North America, but in Europe, it markets Busch brand beer, because the Czechs have the rights to the use of the name Budweiser. Diplomacy and public relations didn't work, so what next? The parties have each other tied up in legal wrangling over who has the rights to the Budweiser name and to derivations of it, such as Bud. More than 40 lawsuits and 40 administrative cases are pending across Europe. Because U.S. law protects Anheuser-Busch's rights to the Budweiser label in the United States, the Czechs sell their beer as “Czechvar.”

The Czech brewery exports to 37 countries, mainly in Europe, and AB has sales in more than 70 countries

around the world. Anheuser-Busch sought a court order to have the Czech company's products taken off the shelves in Hong Kong, won a ruling in Hungary, and has launched similar lawsuits in the United Kingdom and the United States. AB said the Czech brewery had imported and sold beer in the United States labeled “Budweiser Budvar” in the state of Maryland. It also says the Czech brewery is mimicking its name to confuse beer drinkers and cash in on the U.S. company's success.

The Czech government petitioned the WTO to grant beer regions the same kind of labeling protection that it gives to wine regions. Just as sparkling wines made in the Champagne region of France are the only ones legally entitled to call themselves champagne, it would mean that only beers brewed in České Budějovice could call themselves Budweiser and only those brewed in Pilsen, another Czech town, could claim to be Pilsner. It seems unlikely that this request will win approval, because Pilsner has become a generic designation for a style of beer, and unlike the grapes that come from Champagne, the malt and the hops that go into its beer do not come exclusively from České Budějovice.

The legal battle for the exclusive right to use the brand names Bud and Budweiser has spread worldwide. So far, this tactic hasn't worked too well either. Britain's high court allowed both companies to use the names Bud and Budweiser, whereas Switzerland's highest court banned Anheuser-Busch from selling beer under the Bud name.

We all know that the proof of who's best is in the tasting, right? Both lagers have legions of fans. The U.S. version lives up to its old slogan of “king of beers,” at least as far as sales go: It's the top-selling beer in the world. The Czech version—nicknamed the “beer of kings” because it comes from a town that once brewed for royalty—has large followings in Germany and other parts of Europe. So the *St. Louis Post-Dispatch* hosted a blind taste test to determine which beer is better—Budvar won. And, most recently the Europeans have won another battle: In 2009, Anheuser-Busch agreed to merge with InBev, with its global headquarters now in Leuven, Belgium.

Visit the Budvar Web site (www.budvar.cz) for the history of Budvar and a tour of the plant.

Sources: A1 Stamborski, “Battle of the Buds: Taste Testers Say That Budvar Is Better,” *St. Louis Post-Dispatch*, November 28, 1999, p. E1; “Prime Minister Says Budvar Will Stay Czech,” *Modern Brewery*, March 2000; Gregory Cancelada, “Czech Brewery Retains Right to Use ‘Budweiser’ and ‘Bud’ Trademarks,” *St. Louis Post-Dispatch*, February 17, 2003; <http://www.AB-Inbev.com>, 2010.

The procedures used by formal arbitration organizations are similar. Arbitration under the rules of the International Chamber of Commerce (ICC) affords an excellent example of how most organizations operate. When an initial request for arbitration is received, the chamber first attempts conciliation between the disputants. If this fails, the process of arbitration is started. The plaintiff and the defendant select one person each from among acceptable arbitrators to defend their case, and the ICC Court of Arbitration appoints a third member, generally chosen from a list of distinguished lawyers, jurists, and professors.

The history of ICC effectiveness in arbitration has been spectacular. An example of a case that involved arbitration by the ICC concerned a contract between an English business and a Japanese manufacturer. The English business agreed to buy 100,000 plastic dolls for 80 cents each. On the strength of the contract, the English business sold the entire lot at \$1.40 per doll. Before the dolls were delivered, the Japanese manufacturer had a strike; the settlement of the strike increased costs, and the English business was informed that the delivery price of the dolls had increased from 80 cents to \$1.50 each. The English business maintained that the Japanese firm had committed to make delivery at 80 cents and should deliver at that price. Each side was convinced that it was right.

The Japanese, accustomed to code law, felt that the strike was beyond their control (an act of God) and thus compliance with the original provisions of the contract was excused. The English, accustomed to common law, did not accept the Japanese reasons for not complying because they considered a strike part of the normal course of doing business and not an act of God. The dispute could not be settled except through arbitration or litigation; they chose arbitration. The ICC appointed an arbitrator who heard both sides and ruled that the two parties would share proportionately in the loss. Both parties were satisfied with the arbitration decision, and costly litigation was avoided. Most arbitration is successful, but success depends on the willingness of both parties to accept the arbitrator's rulings.

Contracts and other legal documents should include clauses specifying the use of arbitration to settle disputes. Unless a provision for arbitration of any dispute is incorporated as part of a contract, the likelihood of securing agreement for arbitration after a dispute arises is reduced. A typical arbitration clause is as follows:

Any controversy or claim arising out of or relating to this contract shall be determined by arbitration in accordance with the International Arbitration Rules of the American Arbitration Association.

Including the number of arbitrators, the place of arbitration (city and/or country), and the language of the arbitration in the clause is also useful.⁹

Although an arbitration clause in a contract can avert problems, sometimes enforcing arbitration agreements can be difficult. Arbitration clauses require agreement on two counts: (1) The parties agree to arbitrate in the case of a dispute according to the rules and procedures of some arbitration tribunal and (2) they agree to abide by the awards resulting from the arbitration. Difficulty arises when the parties to a contract fail to honor the agreements. Companies may refuse to name arbitrators, refuse to arbitrate, or, after arbitration awards are made, refuse to honor the award. In most countries, arbitration clauses are recognized by the courts and are enforceable by law within those countries. More than 120 countries have ratified the Convention on the Recognition and Enforcement of Foreign Arbitral Awards, also known as the New York Convention, which binds them to uphold foreign arbitration awards. Under the New York Convention, the courts of the signatory countries automatically uphold foreign arbitral awards issued in member countries. In addition to the New York Convention, the United States is a signatory of the Inter-American Convention on International Arbitration, to which many Latin American countries are party. The United States is also party to a number of bilateral agreements containing clauses providing for enforcement of arbitral awards. When all else fails, the final step to solve a dispute is litigation.

⁹The American Arbitration Association, www.iccwbo.org (select Arbitration).

Litigation Lawsuits in public courts are avoided for many reasons. Most observers of lawsuits between citizens of different countries believe that almost all victories are spurious because the cost, frustrating delays, and extended aggravation that these cases produce are more oppressive by far than any matter of comparable size. In India, for instance, there is a backlog of more than three million cases, and litigating a breach of contract between private parties can take a decade or more. The best advice is to seek a settlement, if possible, rather than sue. Other deterrents to **litigation** are the following:

- Fear of creating a poor image and damaging public relations.
- Fear of unfair treatment in a foreign court. (Fear that a lawsuit can result in unfair treatment, perhaps intentionally, is justifiable, because the decision could be made by either a jury or a judge not well versed in trade problems and the intricacies of international business transactions.)
- Difficulty in collecting a judgment that may otherwise have been collected in a mutually agreed settlement through arbitration.
- The relatively high cost and time required when bringing legal action. The Rheem Manufacturing Company, a billion-dollar manufacturer of heating and air conditioning systems, estimates that by using arbitration over litigation, it has reduced the time and cost of commercial-dispute resolution by half.
- Loss of confidentiality. Unlike arbitration and conciliation proceedings, which are confidential, litigation is public.

One authority suggests that the settlement of every dispute should follow four steps: First, try to placate the injured party; if this does not work, conciliate, arbitrate, and, finally, litigate. The final step is typically taken only when all other methods fail. Furthermore, in some cases, problem-solving approaches may be warranted within the context of even litigated disputes.¹⁰ This approach is probably wise whether one is involved in an international dispute or a domestic one.

Protection of Intellectual Property Rights: A Special Problem

LO4

The unique problems of protecting intellectual property rights internationally

Companies spend millions of dollars establishing brand names or trademarks to symbolize quality and design a host of other product features meant to entice customers to buy their brands to the exclusion of all others. Millions more are spent on research to develop products, processes, designs, and formulas that provide companies with advantages over their competitors. Such intellectual or industrial properties are among the more valuable assets a company may possess. Brand names such as Kodak, Coca-Cola, and Gucci; processes such as xerography; and computer software are invaluable. One financial group estimated that the Marlboro brand had a value of \$33 billion, Kellogg's \$9 billion, Microsoft \$9.8 billion, and Levi's \$5 billion; all have experienced infringement of their intellectual property rights. Normally, property rights can be legally protected to prevent other companies from infringing on such assets. Companies must, however, keep a constant vigil against piracy and counterfeiting. Moreover, with increasing frequency, companies are developing new technologies to prevent piracy, but counterfeiters are relentless in their criticism of and technological attacks on even the most sophisticated security measures.¹¹

Counterfeiting and Piracy

Counterfeit and pirated goods come from a wide range of industries—apparel, automotive parts, agricultural chemicals, pharmaceuticals, books (yes, even management books such as the one you are reading right now),¹² records, films, computer software, mobile

¹⁰Chang Zhang, David A. Griffith, and S. Tamer Cavusgil, "The Litigated Dissolution of International Distribution Relationships: A Process Framework and Propositions," *Journal of International Marketing* 14, no. 2 (2006), pp. 85–115.

¹¹Eric Schine, "Faking out the Fakers," *BusinessWeek*, June 4, 2007, pp. 75–79; Ethan Smith, "Napster Format Shift Would Enable More Players," *The Wall Street Journal*, January 7, 2008, p. B2.

¹²Don Lee, "Ripping Off Good Reads in China," *Los Angeles Times*, April 24, 2005, pp. C1, C10.

Exhibit 7.2**Piracy Rates for
Computer Software,
Top and Bottom 20**

Source: From 2010 BSA and IDC Global Software Piracy Study, Business Software Alliance. Reprinted with permission. *Seventh Annual BSA/IDC Global Software Piracy Study* (Washington, DC: Business Software Alliance, 2010), www.bsa.org/globalstudy. One hundred two countries and regions are ranked.

| Highest Piracy Rates | | Lowest Piracy Rates | |
|----------------------|-----|---------------------|-----|
| Georgia | 95% | United States | 20% |
| Zimbabwe | 92 | Japan | 21 |
| Bangladesh | 91 | Luxembourg | 21 |
| Moldova | 91 | New Zealand | 22 |
| Armenia | 90 | Australia | 25 |
| Yemen | 90 | Austria | 25 |
| Sri Lanka | 89 | Belgium | 25 |
| Azerbaijan | 88 | Finland | 25 |
| Libya | 88 | Sweden | 25 |
| Belarus | 87 | Switzerland | 25 |
| Venezuela | 87 | Denmark | 26 |
| Indonesia | 86 | United Kingdom | 27 |
| Vietnam | 85 | Germany | 28 |
| Ukraine | 85 | Netherlands | 28 |
| Iraq | 85 | Canada | 29 |
| Pakistan | 84 | Norway | 29 |
| Algeria | 84 | Israel | 33 |
| Cameroon | 83 | Ireland | 35 |
| Nigeria | 83 | Singapore | 35 |
| Paraguay | 82 | South Africa | 35 |

phones,¹³ baby formula, auto parts, and even cars themselves.¹⁴ Estimates are that more than 10 million fake Swiss timepieces carrying famous brand names such as Cartier and Rolex are sold every year, netting illegal profits of at least \$500 million. Although difficult to pinpoint, lost sales from the unauthorized use of U.S. patents, trademarks, and copyrights amount to more than \$300 billion annually. That translates into more than two million lost jobs. Software, music, and movies are especially attractive targets for pirates because they are costly to develop but cheap to reproduce and distribute over the Internet. Pirated CD music sales are estimated to exceed \$5 billion annually and are growing at 6 percent per year. And unauthorized U.S. software that sells for \$500 in this country can be purchased for less than \$10 in East Asia. The Business Software Alliance, a trade group, estimates that software companies lost over \$16.5 billion in the Asia-Pacific region, \$16.4 billion in Europe, and \$9.4 billion in North America in 2009. Judging from the press on the topic, one might conclude that China is the biggest piracy problem. However, China has moved fast off the list of 20 worst piracy rates, according to Exhibit 7.2. At this writing, it ranks #27 and piracy has fallen to 79 percent, down from 92 percent just a few years earlier. Moreover, the dollars lost in the United States because of software piracy are the most in the world at \$8.4 billion, with China coming in a close second at \$7.6 billion. China's progress is due primarily to education programs, enforcement, and Microsoft's historic agreement with Lenovo. We also note that other populous nations have made major progress in reducing software piracy (e.g., Russia down 11, Brazil down 10, Japan and Vietnam both down 7 percent, India down 11 percent) between 2004 and 2009.¹⁵

Recent research implies that for companies like Microsoft, some level of piracy actually can serve the company. It can be seen as a kind of product trial that ultimately builds commitment. As updated versions of products become available, purchases may actually follow. Particularly as countries such as China begin to enforce WTO statutes on piracy, customers conditioned on pirated goods may indeed be willing and able to pay for the new versions.

¹³"Talk Is Cheap," *The Economist*, November 21, 2009, p. 68.

¹⁴Mark Landler, "Germans See Imitation in Chinese Cars," *The New York Times*, September 12, 2007, p. B3.

¹⁵*Sixth Annual BSA and IDC Global Software Piracy Study* (Washington, DC: Business Software Alliance, 2009), <http://www.bsa.org/globalstudy>; Howard W. French, "China Media Battle Hints at Shift on Intellectual Property," *The New York Times*, January 6, 2007, p. A3; Bruce Einhorn and Steve Hamm, "A Big Windows Cleanup, China Is Discovering that It Pays to Sell PCs that Contain Legitimate Microsoft Software," *BusinessWeek*, June 4, 2007, p. 80.

Although counterfeit CDs, toys, and similar products cost companies billions of dollars in lost revenue and have the potential of damaging the product's brand image, the counterfeiting of pharmaceuticals can do serious physical harm. In Colombia, investigators found an illegal operation making more than 20,000 counterfeit tablets a day of the flu drug Dristan, a generic aspirin known as Dolex, and Ponstan 500, a popular painkiller made by Pfizer. The counterfeited pills contained boric acid, cement, floor wax, talcum powder, and yellow paint with high lead levels, all used to replicate the genuine medications' appearance.

Counterfeit drugs range from copies that have the same efficacy as the original to those with few or no active ingredients to those made of harmful substances. A pharmaceutical manufacturers' association estimates that 2 percent of the \$327 billion worth of drugs sold each year are counterfeit, or about \$6 billion worth. In some African and Latin American nations, as much as 60 percent are counterfeit. The World Health Organization thinks 8 percent of the bulk drugs imported into the United States are counterfeit, unapproved, or substandard.

Another problem is collusion between the contract manufacturer and illegitimate sellers. In China, exact copies of New Balance shoes were fabricated by contract manufacturers who were New Balance suppliers. They flooded the market with genuine shoes that were sold for as little as \$20. Unilever discovered that one of its suppliers in Shanghai made excess cases of soap, which were sold directly to retailers. One of Procter & Gamble's Chinese suppliers sold empty P&G shampoo bottles to another company, which filled them with counterfeit shampoo. Counterfeiting and piracy of intellectual property constitute outright theft, but the possibility of legally losing the rights to intellectual property because of inadequate protection of property rights and/or a country's legal structure is another matter.

Finally, it should be mentioned that some critics argue that MNCs have pushed the current intellectual property regime too far in favor of the firms, particularly with the most recent WTO TRIPS Agreement, to be discussed in more detail subsequently.¹⁶ The critics suggest that the so-called tight rein the firms hold on the production of intellectual property has actually served to limit creativity and the associated benefits to the people that the intellectual property (IP) laws are intended to serve. Such arguments pitch antitrust laws against IP laws. The argument goes on.

Inadequate Protection

The failure to protect intellectual property rights adequately in the world marketplace can lead to the legal loss of rights in potentially profitable markets. Because patents, processes, trademarks, and copyrights are valuable in all countries, some companies have found their assets appropriated and profitably exploited in foreign countries without license or reimbursement.¹⁷ Furthermore, they often learn that not only are other firms producing and selling their products or using their trademarks, but the foreign companies are the rightful owners in the countries where they operate.

There have been many cases in which companies have legally lost the rights to trademarks and have had to buy back these rights or pay royalties for their use. The problems of inadequate protective measures taken by the owners of valuable assets stem from a variety of causes. One of the more frequent errors is assuming that because the company has established rights in the United States, they will be protected around the world or that rightful ownership can be established should the need arise. This assumption was the case with McDonald's in Japan, where enterprising Japanese registered its golden arches trademark. Only after a lengthy and costly legal action with a trip to the Japanese Supreme Court was McDonald's able to regain the exclusive right to use the trademark in Japan. After having to "buy" its trademark for an undisclosed amount, McDonald's maintains a very active program to protect its trademarks.

¹⁶Susan Sell, *Power and Ideas, North-South Politics of Intellectual Property and Antitrust* (Albany: State University of New York Press, 1998); Susan Sell, *Intellectual Property Rights: A Critical History* (Boulder, CO: Lynne Rienner Publishers, 2006).

¹⁷John Hagedoorn, Danielle Cloudt, and Hans van Kranenburg, "Intellectual Property Rights and the Governance of International R&D Partnerships," *Journal of International Business Studies* 36, no. 2 (2005), pp. 156-74.

Similarly, a South Korean company legally used the Coach brand on handbags and leather goods. The company registered the Coach trademark first and has the legal right to use that mark in Korea. The result is that a Coach-branded briefcase that is virtually identical to the U.S. product can be purchased for \$135 in South Korea versus \$320 in the United States. A U.S. attorney who practices with a South Korean firm noted that he has seen several instances in which a foreign company will come to Korea and naively start negotiating with a Korean company for distribution or licensing agreements, only to have the Korean company register the trademark in its own name. Later, the Korean company will use that registration as leverage in negotiations or, if the negotiations fall apart, sell the trademark back to the company. Many businesses fail to take proper steps to legally protect their intellectual property. They fail to understand that some countries do not follow the common-law principle that ownership is established by prior use or to realize that registration and legal ownership in one country does not necessarily mean ownership in another.

Prior Use versus Registration

In the United States, a common-law country, ownership of IP rights is established by **prior use**—whoever can establish first use is typically considered the rightful owner. In many code-law countries, however, ownership is established by **registration** rather than by prior use—the first to register a trademark or other property right is considered the rightful owner. For example, a trademark in Jordan belongs to whoever registers it first in Jordan. Thus you can find “McDonald’s” restaurants, “Microsoft” software, and “Safeway” groceries all legally belonging to Jordanians. After a lengthy court battle that went to the Spanish Supreme Court, Nike lost its right to use the “Nike” brand name for sports apparel in Spain. Cidesport of Spain had been using Nike for sports apparel since 1932 and sued to block Nike (U.S.) sportswear sales. Because Cidesport does not sell shoes under the Nike label, Nike (U.S.) will be able to continue selling its brand of sports shoes in Spain. A company that believes it can always establish ownership in another country by proving it used the trademark or brand name first is wrong and risks the loss of these assets.

Besides the first-to-register issue, companies may encounter other problems with registering. China has improved intellectual property rights protection substantially and generally recognizes “first to invent.” However, a Chinese company can capture the patent for a product invented elsewhere; it needs only to reverse-engineer or reproduce the product from published specifications and register it in China before the original inventor. Latvia and Lithuania permit duplicate registration of trademarks and brand names. A cosmetics maker registered Nivea and Niveja cosmetics brands in the former Soviet Union in 1986 and again in Latvia in 1992, but a Latvian firm had registered and had been selling a skin cream called Niveja since 1964. Neither the Soviet nor the Latvian authorities notified either firm. Applicants are responsible for informing themselves about similar trademarks that are already registered. The case is being taken to the Supreme Court of Latvia. It is best to protect IP rights through registration. Several international conventions provide for simultaneous registration in member countries.

International Conventions

Many countries participate in international conventions designed for mutual recognition and protection of intellectual property rights. There are three major international conventions:

1. The Paris Convention for the Protection of Industrial Property, commonly referred to as the Paris Convention, includes the United States and 100 other countries.
2. The Inter-American Convention includes most of the Latin American nations and the United States.
3. The Madrid Arrangement, which established the Bureau for International Registration of Trademarks, includes 26 European countries.

In addition, the World Intellectual Property Organization (WIPO) of the United Nations is responsible for the promotion of the protection of intellectual property and for the administration of the various multilateral treaties through cooperation among its member states.¹⁸

¹⁸Visit <http://www.wipo.org>, the home page of the WIPO, for detailed information on the various conventions and the activities of WIPO.

Furthermore, two multicountry patent arrangements have streamlined patent procedures in Europe. The first, the Patent Cooperation Treaty (PCT), facilitates the process for application for patents among its member countries. It provides comprehensive coverage, in that a single application filed in the United States supplies the interested party with an international search report on other patents to help evaluate whether or not to seek protection in each of the countries cooperating under the PCT. The second, the European Patent Convention (EPC), established a regional patent system allowing any nationality to file a single international application for a European patent. Companies have a choice between relying on national systems when they want to protect a trademark or patent in just a few member countries and applying for protection in all 27 member states. Trademark protection is valid for 10 years and is renewable; however, if the mark is not used within 5 years, protection is forfeited. Once the patent or trademark is approved, it has the same effect as a national patent or trademark in each individual country designated on the application.

The Trade-Related Aspects of Intellectual Property Rights (TRIPs) agreement, a major provision of the World Trade Organization, is the most comprehensive multilateral agreement on intellectual property to date. TRIPs sets standards of protection for a full range of intellectual property rights that are embodied in current international agreements. The three main provisions of the TRIPs agreement required that participating members be in compliance with minimum standards of protection by 2006, set procedures and remedies for the enforcement of IP rights, and made disputes between WTO members with respect to TRIPs obligations subject to the WTO's dispute settlement procedures.¹⁹

Once a trademark, patent, or other intellectual property right is registered, most countries require that these rights be used and properly policed. The United States is one of the few countries in which an individual can hold a patent without the patented entity being manufactured and sold throughout the duration of the patent period. Other countries feel that in exchange for the monopoly provided by a patent, the holder must share the product with the citizens of the country. Hence, if patents are not produced within a specified period, usually from one to five years (the average is three years), the patent reverts to public domain.

This rule is also true for trademarks; products bearing the registered mark must be sold within the country, or the company may forfeit its right to a particular trademark. McDonald's faced that problem in Venezuela. Even though the McDonald's trademark was properly registered in that code-law country, the company did not use it for more than two years. Under Venezuelan law, a trademark must be used within two years or it is lost. Thus, a Venezuelan-owned "Mr. McDonalds," with accompanying golden arches, is operating in Venezuela. The U.S. McDonald's Corporation faces a potentially costly legal battle if it decides to challenge the Venezuelan company.

Individual countries expect companies to actively police their intellectual property by bringing violators to court. Policing can be a difficult task, with success depending in large measure on the cooperation of the country within which the infringement or piracy takes place. A lack of cooperation in some countries may stem from cultural differences regarding how intellectual property is viewed. In the United States, the goal of protection of IP is to encourage invention and to protect and reward innovative businesses. In Korea, the attitude is that the thoughts of one person should benefit all. In Japan, the intent is to share technology rather than protect it; an invention should serve a larger, national goal, with the rapid spread of technology among competitors in a manner that promotes cooperation. In light of such attitudes, the lack of enthusiasm toward protecting intellectual property can be better understood. The United States is a strong advocate of protection, and at U.S. insistence, many countries are becoming more cooperative about policing cases of infringement and piracy. After decades of debate, European Union ministers agreed on a common continentwide system for patented inventions. Instead of being forced to submit an application in all EU countries' languages, inventors can submit only one, in English, French, or German. Finally, as the legal system evolves in China, authorities there have now begun enforcing local companies' patents at the expense of foreign firms.²⁰

¹⁹For a discussion of TRIPs, visit <http://www.wto.org> and select Intellectual Property.

²⁰"Battle of Ideas," *The Economist*, April 25, 2009, p. 68.

The three faces of piracy and/or reform, depending how you look at them. (1) American youths, particularly on college campuses, are protesting the current intellectual property laws and the associated enforcement tools. The fellow with the eyepatch was attending a seminar on the topic led by former Attorney General Alberto Gonzales.²¹

(2) Aside from the United States, the biggest piracy problem is China. Here Jackie Chan helps the Chinese government crack down, forecasting the probable path of IP piracy in China. That is, pirates have turned into policemen historically in the United States, Japan, and Taiwan as the production of intellectual property took off in each country.²² The same will happen in China during the next decade as artists, researchers, and entrepreneurs there produce new ideas worth protecting.

(3) The HIV/AIDS epidemic is an economic and health catastrophe that many in sub-Saharan Africa and other developing countries²³ believe is exacerbated by drug companies' pricing policies and protection of intellectual property.²⁴ Here protestors march toward the U.S. embassy in Pretoria, South Africa.



Other Managerial Approaches to Protecting Intellectual Property

LO5

How to protect against piracy and counterfeiting

The traditional, but relatively feeble, remedies for American companies operating in countries such as China are several: (1) prevention, that is, engage local representation and diligently register IP with the appropriate agencies; (2) pursue negotiation and alternative dispute resolution; (3) complain to the Chinese authorities; and (4) complain to the U.S. government and World Trade Organization (WTO). Beyond these traditional strategies, research is now being conducted to better understand consumers' motivations with respect

²¹Lorenzo Munoz and Jon Healey, "Students Do Not Share Gonzales' View on Piracy," *Los Angeles Times*, April 29, 2005, pp. C1, C9.

²²N. Mark Lam and John L. Graham, *China Now, Doing Business in the World's Most Dynamic Market* (New York: McGraw-Hill, 2007).

²³Amelia Gentleman, "Battle Pits Patent Rights against Low-Cost Generic Drugs," *The New York Times*, January 30, 2007, p. C5; "Clinton, Drug Companies Strike Deal to Lower AIDS Drug Prices," *The Wall Street Journal*, May 8, 2007.

²⁴John E. Cook and Roger Bate, "Pharmaceuticals and the Worldwide HIV Epidemic: Can a Stakeholder Model Work?" *Journal of Public Policy & Marketing* 23, no. 2 (2004), pp. 140–52.

to counterfeit brands,²⁵ and creative thinkers of enterprise have come up with several new ideas that we briefly describe next.²⁶

Microsoft. Bill Gates's negotiation strategy with Chinese software pirates demonstrates his guile, prescience, and patience. He accidentally revealed his strategy in 1998 in an interview at the University of Washington:

Although about 3 million computers get sold every year in China, people don't pay for the software. Someday they will, though. And as long as they're going to steal it, we want them to steal ours. They'll get sort of addicted, and then we'll somehow figure out how to collect something in the next decade.

Well, it didn't take a decade for this marketing/product trial approach to work. On April 18, 2006, one day ahead of Chinese President Hu Jintao's arrival in Redmond, Washington, for dinner at Gates's home and on his way to a meeting with President George W. Bush, Gates inked a deal with Lenovo for \$1.2 billion of software to be included in the Chinese firm's computers.

Philips. One of the originators of "open innovation" is Philips Research in the Netherlands. Thirty years ago, it pioneered the concept of partnering²⁷ to develop and market new ideas. Open innovation for Philips also means that it buys ideas from R&D partners and sells ideas to marketing partners, rather than developing and marketing only its own ideas. One project exemplifies its innovative approach to developing and protecting intellectual property in China. The PHENIX Initiative was a commercial, industrial, and R&D project to develop mobile interactive digital services for the 2008 Olympics. Led by France Telecom, it involved financing and technology contributions from both European and Chinese corporations and governmental organizations.

Although many American firms have established design and R&D centers in China already, U.S. government restrictions on high-tech export and American executives' competitive angst prevent associations such as the PHENIX Initiative for U.S. firms in China. Thus, our arm's-length relationships in China limit both the amount of technology we develop and the degree of protection afforded it compared with European and Asian competitors. Moreover, our pleas for the Chinese government to "protect *our* intellectual property" sound exploitative to both the authorities and the public there.

Warner Bros. Finally, we suggest an excellent way for IP-rich firms to make money in China currently and in the near future, using the oldest pricing strategy of all: *Charge what the market will bear*. Even with the reluctant help of the Chinese authorities in enforcing the WTO/TRIPs agreement, Chinese consumers will continue the creative copying of foreign intellectual property until they are charged what they perceive as "reasonable" prices. Indeed, we applaud the recent heroic, albeit controversial, marketing strategies of Warner Bros. in China, which nearly halved the prices of its DVDs to \$1.88 and distributed the products within days of their release in theaters—earlier than anywhere else in the world.

This pricing approach is quite consistent with one we have long advocated, namely, adjusting prices on the basis of the comparative income levels in developing countries. That is, a fair price (from the Chinese point of view) would take into account the income and purchasing power differentials between consumers in the United States and China. For example, circa 2007, the ratio between U.S. and Chinese GDP per capita at purchase price parity was approximately \$40,000 to \$6,500. Adjusting the current U.S. price of about \$10 for a DVD on Amazon.com, a "reasonable" price to charge in China would be about \$1.50. And we particularly appreciate the tactical nuance of adding the \$.38 to achieve the very lucky price the Warner Bros. marketers are both charging and getting in China—\$1.88!

²⁵Keith Wilcox, Hyeong Min Kim, and Sankar Sen, "Why Do Consumers Buy Counterfeit Brands?" *Journal of Marketing Research* 46, no. 2 (2009), pp. 247–59.

²⁶See Lam and Graham, *China Now*, for more details.

²⁷"What's Mine Is Yours," *The Economist*, May 30, 2009, p. 80.

Warner Bros. is also trying to create a market for high-quality DVD rentals in a partnership with Union Voole Technology in China. Inexpensive video-on-demand systems price the multi-view rentals at less than \$1 and deliver via the Internet.²⁸

Cyberlaw: Unresolved Issues

LO6

The many issues of evolving cyberlaw

The Internet is by its nature a global enterprise for which no political or national boundaries exist. Although this global reach is its strength, it also creates problems when existing laws do not clearly address the uniqueness of the Internet and its related activities. Existing law is vague or does not completely cover such issues as gambling, the protection of domain names, taxes, jurisdiction in cross-border transactions, contractual issues, piracy²⁹ (as discussed in the last section), and censorship. The very public dispute between Google and the government of China during 2010 is an important example of the last issue.³⁰ The European Union, the United States, and many other countries are drafting legislation to address the myriad legal questions not clearly addressed by current law. But until these laws apply worldwide, companies will have to rely on individual-country laws, which may or may not provide protection.³¹ When you add together the unprecedented dynamism of the cyber industry to a fledgling legal system as in China, you end up with a rather wild regulatory environment. China is currently trying to monitor and censor text messaging.³² But perhaps the most interesting battle brewing in the Chinese bureaucracy is over which ministry will regulate the online version of *World of Warcraft*, the most popular such game in the country.³³ The General Administration of Press and Publication and the Ministry of Culture are the two combatants in this interesting game, and it's a certainty that Blizzard Entertainment hopes they do not reach an agreement to share the control over the Chinese operations of the company.

Domain Names and Cybersquatters

Unfortunately, the ease with which Web names can be registered and the low cost of registering has led to thousands being registered. **Cybersquatters (CSQs)** buy and register descriptive nouns, geographic names, names of ethnic groups and pharmaceutical substances, and other similar descriptors and hold them until they can be sold at an inflated price. For example, a cybersquatter sold "www.themortgage.com" for \$500,000; the record price paid so far is \$7.5 million for the domain name "www.business.com." If a cybersquatter has registered a generic domain name that a company wants, the only recourse is to buy it.

Another ploy of CSQs is to register familiar names and known trademarks that divert traffic from intended destinations or to sell competing products. eBay, the world's largest online auction house, was embroiled in a dispute with an entrepreneur in Nova Scotia who registered "www.ebay.ca," thus forcing the U.S. company to use "www.ca.ebay.com" for its newly launched Canadian Web site until it was successful in regaining the use of "www.ebay.ca"; both Web addresses now go to the same site.

Cybersquatters register a well-known brand or trademark that misdirects a person to the CSQ's site or to a competing company's site. For example, an adult entertainment Web site registered "www.candyland.com." Hasbro, the toy company, markets a game for children called "Candy Land." Disturbed by the thought that customers might end up at an adult entertainment site, Hasbro wanted to have the site vacated. It had the option of suing to have it removed or buying the domain name. Hasbro elected to sue, and though the adult Web site was not directly infringing on its trademark, the courts deemed it to be damaging to the reputation of Hasbro and its children's game. The Web address now takes you directly to a Hasbro site.

²⁸Dawn C. Chmielewski, "Warner Takes New Tack against Piracy," *Los Angeles Times*, November 4, 2008, pp. C1, C6.

²⁹"The Spider and the Web," *The Economist*, August 29, 2009, p. 49.

³⁰"Google and China, Flower for a Funeral," *The Economist*, January 16, 2010, pp. 41–42.

³¹Jefferson Graham, "File-Sharing Beat Goes On," *USA Today*, June 29, 2005, p. 3B.

³²Sharon LaFraniere, "China to Scan Text Messages to Spot 'Unhealthy Content,'" *The New York Times*, January 20, 2010, p. A5.

³³Michael Wines, "Online Warfare Prompts an Offline Clash in China," *The New York Times*, November 7, 2009, p. A4.



Potential customers visit a Microsoft booth in Beijing. When Chinese bloggers use Microsoft's service to post messages and type in such terms as "democracy," "capitalism," "liberty," or "human rights," they get a yellow light and a computer warning: "This message includes forbidden language. Please delete the prohibited expression." Microsoft has agreed to this sort of censorship, explaining that it is just following local laws and that the company still provides a most useful service to its Chinese clients. The critics disagree. The argument goes on.

Other cybersquatting abuses that can pose a serious threat to business include parody sites, protest sites, and hate sites. A good example is "www.walmartsucks.org," a site highly critical of Walmart. This type of Web site may be difficult to prevent because the right to free speech is protected. The only defense Walmart might have is to challenge the Web site's right to use a trade name to direct someone to the site.

It is easy to imagine many situations in which the actions of companies or information posted on a site can lead to a lawsuit when Internet content is unlawful in one country but not in the host country. For example, an American studio that makes a movie with nude scenes could be prosecuted in a country that bans nudity in movies. Not only would the movie studio be liable, but the Internet service provider could be liable for material posted on its Web site. Writers and publishers could face libel suits in countries with laws restrictive of free speech, where weak or nonexistent free speech protections are tools to intimidate and censor.³⁴ Internet publishers or individual Web site owners fear they can be sued for defamation from any or many jurisdictions, merely because their articles can be downloaded anywhere in the world. Lawsuits involving libel, defamation, and product liability cause companies to voluntarily restrict their Web sites to selected countries rather than leave themselves open to legal action. The Internet is not a libel-free zone.

Most country's courts are inclined to assert jurisdiction over online activity, wherever it originates, so long as harm is experienced locally and the sense is that the party responsible either knew or ought to have known that the harm was a likely consequence of its actions. Most agree, though, that laws that are expressly designed to apply not just in a single country but worldwide are necessary to untangle the legal hassles that are occurring.

Of 100 business leaders polled by the International Chamber of Commerce, more than one-third said legal uncertainty covering Internet operations affected "significant business decisions." The most immediate impact, according to the ICC, is clear: Many online merchants refuse to sell outside their home countries.

Taxes Another thorny issue in e-commerce concerns the collection of taxes. A typical tax system relies on knowing where a particular economic activity is located. But the Internet enables individual workers to operate in many different countries while sitting at the same desk. When taxes should be collected, where they should be collected, and by whom are all issues under consideration by countries around the world. In the past, a company was deemed to have a taxable presence in a country if it had a permanent establishment there. But whether the existence of a server or a Web site qualifies as such a presence is not clear. One proposal that has enthusiastic support from tax authorities is for servers to be designated as "virtual permanent establishments" and thus subject to local taxes.

To pinpoint when and where a sale takes place in cyberspace is difficult, and unless elusive taxpayers can be pinpointed, any tax may be difficult to collect. In "brick-and-mortar" sales, the retailer collects, but when the Internet site is in one country and the customer is in another, who collects? One proposal is to have shipping companies such as FedEx or credit card companies collect—obviously, neither party is receiving this suggestion enthusiastically.

The EU Commission has announced plans for a directive to force foreign companies to levy value-added tax (VAT) on services delivered via the Internet, television, or radio to customers in the European Union. Foreign companies with sales via the Internet of over €100,000 (~\$125,000) inside the European Union would have to register in at least one EU

³⁴Mark Magnier and Joseph Menn, "As China Censors the Internet, Money Talks," *Los Angeles Times*, June 17, 2005, pp. A1, A14.

country and levy VAT at that country's rate, somewhere between 15 percent and 25 percent. The tax is justified on the basis of leveling the playing field. That is, EU companies have to charge their EU customers VAT, whereas foreign companies supplying the same service to the same customers are duty free. However, U.S. companies are protesting, calling the proposal "e-protectionism." Although the EU plan is only a proposal now, as the value of Internet transactions increases, the taxman will sooner or later get his share.³⁵ Perhaps the most egregious example of strange Internet taxing comes from France. The Ministry of Culture there proposed a tax on online advertising revenues, aimed at American firms such as Google, Microsoft, AOL, Yahoo!, and Facebook, to pay for new subsidies for the French music, movie, and publishing industries.³⁶

Jurisdiction of Disputes and Validity of Contracts

As countries realize that existing laws relating to commerce do not always clearly address the uniqueness of the Internet and its related activities, a body of cyberlaw is gradually being created. Two of the most troubling areas are determining whose laws will prevail in legal disputes between parties located in different countries and establishing the contractual validity of electronic communications. The European Union is having the most difficulty in reconciling the vast differences in the laws among its member states to create a uniform law. For example, a draft regulation debated in Brussels and other European capitals would have required vendors to comply with 27 different, and sometimes bizarre, sets of national rules on consumer protection—ranging from dozens of restrictions on advertising to France's requirement that all contracts must be concluded in French, regardless of whether businesses intend to sell goods for export to France.

The EU Commission has adopted an e-commerce directive that will permit online retailers to trade by the rules of their home country unless the seller had enticed or approached the consumer by way of advertising. Then, any legal action is to take place in the consumer's country of residence. The rationale is that if a company actively seeks customers in a given country, it ought to be willing to abide by that country's consumer protection laws. Whether the directive will be accepted by all 27 member states is still problematic.

The European Commission has begun to review the entire regulatory framework for the technological infrastructure of the information society. The commission is working on various pieces of legislation intended to place electronic commerce on an equal footing with conventional commerce. One of the first steps was to introduce an EU-wide computer network dubbed EEJ net that provides an easy way to resolve small-scale disputes out of court. Problems over deliveries, defective products, or products that do not fit their description can be dealt with by a single one-stop national contact point, or clearinghouse, in each member state. The consumer will be able to find information and support in making a claim to the out-of-court dispute resolution system in the country where the product supplier is based.

Establishing the validity of contractual law for e-commerce is making substantial progress also. India, for example, recently passed a law that recognizes e-mail as a valid form of communication, electronic contracts as legal and enforceable, and digital signatures as binding. Several countries are preparing, or have passed, legislation similar to the United Kingdom's that allows digital signatures to be used in the creation of online contracts that are as legally binding as any paper-based original document.

Commercial Law within Countries

When doing business in more than one country, a marketer must remain alert to the different legal systems. This problem is especially troublesome for the marketer who formulates a common marketing plan to be implemented in several countries. Although differences in languages and customs may be accommodated, legal differences between countries may still present problems for a marketing program.

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The legal differences between countries and how those differences can affect international marketing plans

³⁵For a report on a resolution on cross-border tax issues proposed by the OECD, see "OECD Launches Project on Improving the Resolution of Cross-Border Tax Disputes," <http://www.oecd.org>, and select Taxation. The OECD proposes a variety of issues related to the Internet, all of which can be found at this site.

³⁶"France and the Internet, Helicopters at the Ready," *The Economist*, January 16, 2010, pp. 63–64.

Marketing Laws

All countries have laws regulating marketing activities in promotion, product development, labeling, pricing, and channels of distribution. Usually the discrepancies across markets cause problems for trade negotiators, particularly for managers and their firms. For example, the United States does not allow the buying or selling of human organs,³⁷ and it restricts the use of human stem cells in medical research to develop treatments for a variety of diseases.³⁸ Other nations have different laws.³⁹ The ethics of both issues are quite controversial, and adding an international dimension just complicates things even more. In the case of the current international trade in human organs, Europeans can legally travel to foreign countries for transplants. However, the European Union Parliament is considering making it a criminal offense to do so. Meanwhile, the U.S. government is considering relaxing laws regulating stem cell research as scientists in other nations, unfettered by similar restrictions, are making important advances in the field.

Some countries may have only a few marketing laws with lax enforcement; others may have detailed, complicated rules to follow that are stringently enforced. For example, Sweden banned all television advertising to children in 1991. Greece, Norway, Denmark, Austria, and the Netherlands all restrict advertising directed at children. Recently, the European Commission threatened to restrict all advertising of soft drinks and snack foods to children, and PepsiCo volunteered to curb its advertising to kids in response.⁴⁰ At the same time, the American food industry is arguing against such actions in the United States. It is interesting to note that the U.S. Federal Trade Commission and the sugared food and toy manufacturers went down a similar path toward restricting advertising to children in the late 1970s. The industry made a few minor concessions at the time but began ignoring previous commitments during the 1980s. All these developments will be interesting to follow as childhood obesity continues to be a major public health issue in all affluent countries.

There often are vast differences in enforcement and interpretation among countries with laws that cover the same activities. Laws governing sales promotions in the European Union offer good examples of such diversity. In Austria, premium offers, free gifts, or coupons are considered cash discounts and are prohibited. Premium offers in Finland are allowed with considerable scope as long as the word *free* is not used and consumers are not coerced into buying products. France also regulates premium offers, which are, for all practical purposes, illegal there because selling for less than cost or offering a customer a gift or premium conditional on the purchase of another product is illegal. French law does permit sales twice a year, in January and August, which can legally last four to six weeks. This event is so popular that it is advertised on radio and TV, and special police are even required to control the crowds. One poll indicated that over 40 percent of the French set aside money during the year for sale time, and 56 percent will spend less money on essentials to buy things on sale. The good news here is that many of these restrictions on marketing activities are being softened. Most recently, holiday sales⁴¹ and longer store hours⁴² are being allowed in several European countries. China has relaxed some of its restrictions on direct marketing that particularly affected companies such as Mary Kay.⁴³

The various product comparison laws, a natural and effective means of expression, are another major stumbling block. In Germany, comparisons in advertisements are always subject to the competitor's right to go to the courts and ask for proof of any implied or stated superiority. In Canada, the rulings are even more stringent: All claims and statements

³⁷Nancy Scheper-Hughes, "Organs without Borders," *Foreign Policy*, January/February 2005, pp. 26–27.

³⁸Robert L. Paarlberg, "The Great Stem Cell Race," *Foreign Policy*, May/June 2005, pp. 44–51.

³⁹Amelia Gentleman, "Transplant Scheme Preys on Poor Indians," *International Herald Tribune*, January 30, 2008, p. 2.

⁴⁰Andrew Ward and Jeremy Grant, "PepsiCo Says It Has Curbed Advertising to Children," *Financial Times*, February 28, 2005, <http://www.FT.com>.

⁴¹Cecilie Rohwedder, "Achtung Christmas Shoppers!" *The Wall Street Journal*, December 24, 2007, pp. B1, B2.

⁴²Marcus Walker, "Longer Store Hours in Germany," *The Wall Street Journal*, January 8, 2007, p. A5.

⁴³Katherine Yung, "Mary Kay Sales Plans Get Beijing Blessing," *Dallas Morning News*, December 5, 2006, pp. D1, D7.



Laws regarding healthcare marketing differ substantially around the world. In Mexico, prescriptions often are not required for powerful drugs. At this farmacia in the Cancun airport, tourists can buy the pictured antibiotic over the counter at bargain prices. Quality is an issue, but availability is not. In the Philippines and other developing countries, you can buy yourself a kidney on the black market—the global price is around \$2,000. However, U.S. laws prohibit the buying and selling of human organs. In South Korea, the government supports stem cell research that is restricted in the United States by federal laws.



must be examined to ensure that any representation to the public is not false or misleading. Such representation cannot be made verbally in selling or be contained in or on anything that comes to the attention of the public (such as product labels, inserts in products, or any other form of advertising, including what may be expressed in a sales letter). Courts have been directed by Canadian law to take into account, in determining whether a representation is false or misleading, the “general impression” conveyed by the representation as well as its literal meaning.⁴⁴ The courts are expected to apply the “credulous person standard,” which means that if any reasonable person could possibly misunderstand the representation, the representation is misleading. In essence, puffery, an acceptable practice in the United States, could be interpreted in Canada as false and misleading advertising. Thus, a statement such as “the strongest drive shaft in Canada” would be judged misleading unless the advertiser had absolute evidence that the drive shaft was stronger than any other drive shaft for sale in Canada.

China is experimenting with a variety of laws to control how foreign companies do business, and some of those experiments have gone well, but some badly. Some regulations are being relaxed, such as those controlling foreign advertising companies. Even so, censorship of advertising and program content⁴⁵ are constant concerns. Televised ads for “offensive” products such as feminine hygiene pads, hemorrhoid medications, and even athlete’s food ointment are not allowed during the three daily mealtimes.⁴⁶ The Chinese authorities banned a LeBron James Nike TV ad because it “violates regulations that mandate all advertisements in China should uphold national dignity and interest and respect the motherland’s culture.”⁴⁷ Apparently LeBron battling a kung fu master isn’t appropriate in the land of Confucius. Also, magazines have been ordered to use a direct translation of the often-obscure name that appears on their license or use no English name at all. Thus, *Cosmopolitan* would become “Trends Lady,” *Woman’s Day* would become “Friends of Health,” and *Esquire* would become “Trends Man.” The movie *Avatar* also competed for Chinese screens with a government-sponsored film about the life of Confucius; at least temporarily, *Avatar* was allowed to show only on 3D screens, thus allowing Confucius the “appropriate” screen time.⁴⁸ A Guns N’ Roses album was banned in the country for its objectionable title, Chinese Democracy.⁴⁹ Such diversity of laws among countries extends to advertising, pricing, sales agreements, and other commercial activities. Indeed, studies suggest that governmental policies affect marketing success in a variety of ways⁵⁰ including actually forestalling some firms from taking a marketing orientation in their operations.⁵¹

There is some hope that the European Union will soon have a common commercial code. One step in that direction is the proposal to harmonize the pan-European regulation of promotions based on the conservative laws that cover promotions in Germany, Austria, and Belgium. However, this proposal is meeting with strong resistance from several groups because of its complex restrictions.⁵² Meanwhile, others push for even broader-based

⁴⁴Richard W. Pollay, “Considering the Evidence, No Wonder the Court Endorses Canada’s Restrictions on Cigarette Advertising,” *Journal of Public Policy & Marketing* 23, no. 1 (2004), pp. 80–88.

⁴⁵“Bond in Beijing,” *The Wall Street Journal*, January 31, 2007, p. A12; Don Lee and Jim Puzanghera, “China Closing Curtains on U.S. Movies,” *Los Angeles Times*, December 12, 2007, pp. C1, C4; Geoffrey A. Fowler, “Online-Video Firms Brace as China Tightens Rules,” *The Wall Street Journal*, January 4, 2008.

⁴⁶Geoffrey A. Fowler, “China Cracks Down on Commercials,” *The Wall Street Journal*, February 19, 2004, p. B7.

⁴⁷“China Bans Nike’s LeBron Commercial,” *Associated Press*, December 6, 2004.

⁴⁸Ben Fritz and David Pierson, “Chinese Pull an ‘Avatar’ Switch,” *Los Angeles Times*, January 19, 2010, p. B6.

⁴⁹James T. Areddy, “Guns N’ Roses New Album Is Up Against a Chinese Wall,” *The Wall Street Journal*, November 22, 2008, online.

⁵⁰Stefan Stremersch and Aurelie Lemmens, “Sales Growth of New Pharmaceuticals across the Globe: The Role of Regulatory Regimes,” *Marketing Science* 28, no. 4 (2009), pp. 690–708.

⁵¹Rilian Qu and Christine T. Ennew, “Developing a Market Orientation in a Transitional Economy: The Role of Government Regulation and Ownership Structure,” *Journal of Public Policy & Marketing* 24, no. 1 (2005), pp. 82–89.

⁵²“EU Sets Cap on TV Ads and Product Placement,” *International Herald Tribune*, November 14, 2006, p. 16.



A Greenpeace protester peers out from inside a plastic rubbish bin in Hong Kong, where activists were calling on the government to develop a comprehensive recycling industry that they claim will create 2,000 new jobs. A study by Greenpeace found that only 148 out of 18,200 rubbish bins in Hong Kong have waste separation compartments. It called on the government to revamp its current waste management procedures to facilitate a comprehensive system to reduce, recover, and recycle.

Green Marketing Legislation

Multinational corporations also face a growing variety of legislation designed to address environmental issues. Global concern for the environment extends beyond industrial pollution, hazardous waste disposal, and rampant deforestation to include issues that focus directly on consumer products. Green marketing laws focus on environmentally friendly products and product packaging and its effect on solid waste management.

Germany has passed the most stringent green marketing laws that regulate the management and recycling of packaging waste. The new packaging laws were introduced in three phases. The first phase required all transport packaging, such as crates, drums, pallets, and Styrofoam containers, to be accepted back by the manufacturers and distributors for recycling. The second phase required manufacturers, distributors, and retailers to accept all returned secondary packaging, including corrugated boxes, blister packs, packaging designed to prevent theft, packaging for vending machine applications, and packaging for promotional purposes. The third phase requires all retailers, distributors, and manufacturers to accept returned sales packaging, including cans, plastic containers for dairy products, foil wrapping, Styrofoam packages, and folding cartons such as cereal boxes. The requirement for retailers to take back sales packaging has been suspended as long as the voluntary green dot program remains a viable substitute. A green dot on a package identifies manufacturers that have agreed to ensure a regular collection of used packaging materials directly from the consumer's home or from designated local collection points.

Reclaiming recyclables extends beyond packaging to automobiles. Since 2006, manufacturers based in European Union nations must take back any cars they produced that no

harmonization of marketing regulations involving the United States, United Nations, and the WTO.

Although the European Union may sometimes appear a beautiful picture of economic cooperation, there is still the reality of dealing with 27 different countries, cultures, and languages, as well as 27 different legal systems. Even though some of Germany's complicated trade laws were revoked in 2000, groups such as the Center for Combating Unfair Competition, an industry-financed organization, continue to work to maintain the status quo. Before the German law was revoked, the Center's lawyers filed 1,000 lawsuits a year, going after, for example, a grocery store that offered discount coupons or a deli that gave a free cup of coffee to a customer who had already bought 10; its efforts will surely continue.

Although the goal of full integration and a common commercial code has not been totally achieved in the European Union, decisions by the European Court continue to strike down individual-country laws that impede competition across borders. In a recent decision, the European Court ruled that a French cosmetics company could sell its wares by mail in Germany and advertise them at a markdown from their original prices, a direct contradiction of German law. As the Single European Market Act is implemented, many of the legal and trade differences that have existed for decades will vanish. Surprisingly enough, standards set by the European Union for food, software, cars, and other items affect U.S. product standards as well. In many cases, the reconciliation of so many different consumer protection standards that existed in European countries prior to the European Union resulted in rules more rigorous than those for many U.S. products. Consequently, many U.S. products have had to be redesigned to comply with European standards. For example, Carrier air conditioners have been redesigned to comply with European recycling rules; Microsoft has modified contracts with software makers; Internet service providers give consumers a wider choice of technologies; and McDonald's has ceased including soft plastic toys with its Happy Meals and has withdrawn all genetically engineered potatoes from its restaurants worldwide. All this change is because of the need to reconcile U.S. standards with those of the European Union.

longer have resale value and pay for proper disposal. Similarly, 85 percent of a scrapped car's material must be recovered for future use.

Many European countries also have devised schemes to identify products that comply with certain criteria that make them more environmentally friendly than similar products. Products that meet these criteria are awarded an "ecolabel" that the manufacturer can display on packaging to signal to customers that it is an environmentally friendly product. The European Union is becoming more aggressive in issuing new directives and in harmonizing ecolabeling and other environmental laws across all member states. Ecolabeling and EU packaging laws are discussed in more detail in the chapter on consumer products (Chapter 13).⁵³

Foreign Countries' Antitrust Laws

With the exception of the United States, antitrust laws were either nonexistent or not enforced in most of the world's countries for the better part of the twentieth century. However, the European Union,⁵⁴ Japan, and many other countries have begun to actively enforce their antitrust laws, patterned after those in the United States. Antimonopoly, price discrimination, supply restrictions, and full-line forcing are areas in which the European Court of Justice has dealt severe penalties. For example, before Procter & Gamble was allowed to buy VP-Schickedanz AG, a German hygiene products company, it had to agree to sell off one of the German company's divisions that produced Camelia, a brand of sanitary napkins. Because P&G already marketed a brand of sanitary napkins in Europe, the commission was concerned that allowing P&G to keep Camelia would give the company a controlling 60 percent of the German sanitary products market and 81 percent of Spain's. More recently, the European Union fined Intel \$1.45 billion for monopolistic abuses in its marketing in Europe. In addition, the firm must make mandated adjustments in its marketing practices and operations.⁵⁵

The United States also intervenes when non-U.S. companies attempt to acquire American companies. Nestlé's proposed \$2.8 billion acquisition of Dreyer's Grand Ice Cream hit a roadblock as U.S. antitrust officials opposed the deal on grounds that it would lead to less competition and higher prices for gourmet ice cream in the United States. At times, companies are subject to antitrust charges in more than one country. Microsoft had a partial victory against antitrust charges brought in the United States, only to face similar anticompetitive charges against Microsoft's Windows operating system in the European Union. The probe is based on possible competitive benefits to European software concerns if legal limits were placed on Microsoft. American companies have faced antitrust violations since the trust-busting days of President Theodore Roosevelt but much less so in other parts of the world. Enforcement of antitrust in Europe was almost nonexistent until the early stages of the European Union established antitrust legislation. And, now China is getting into the game. The Anti-Monopoly Bureau of the Ministry of Commerce considered its first such case and eventually approved the Anheuser-Busch/InBev merger.⁵⁶

U.S. Laws Apply in Host Countries

All governments are concerned with protecting their political and economic interests domestically and internationally; any activity or action, wherever it occurs, that adversely threatens national interests is subject to government control. Leaving

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The different ways U.S. laws can be applied to U.S. companies operating outside the United States

⁵³For information on the EU's environmental directives, as well as other information about the European Union, visit <http://www.europa.eu.int>. This address will take you to the home page, where you can search for topics and visit various information sources about the European Union.

⁵⁴Charles Forelle, "Microsoft Yields in EU Antitrust Battle," *The Wall Street Journal*, October 23, 2007; Charles Forelle, "EU Probes Pharmaceutical Industry on Dwindling New Patents, Drugs," *The Wall Street Journal*, January 16, 2008.

⁵⁵Charles Forrelle and Don Clark, "Intel Fine Jolts Tech Firm," *The Wall Street Journal*, May 14, 2009, pp. A1, A14.

⁵⁶"InBev-Anheuser-Busch: China's First Public Merger Decision Under the AML," *Venulex Legal Summaries* Q4 (2008), pp. 1–3.

the political boundaries of a home country does not exempt a business from home-country laws. Regardless of the nation where business is done, a U.S. citizen is subject to certain laws of the United States. What is illegal for an American business at home can also be illegal by U.S. law in foreign jurisdictions for the firm, its subsidiaries, and licensees of U.S. technology.

Laws that prohibit taking a bribe, trading with the enemy, participating in a commercial venture that negatively affects the U.S. economy, participating in an unauthorized boycott such as the Arab boycott, or any other activity deemed to be against the best interests of the United States apply to U.S. businesses and their subsidiaries and licensees regardless of where they operate. Thus, at any given time a U.S. citizen in a foreign country must look not only at the laws of the host country but at home law as well.

The question of jurisdiction of U.S. law over acts committed outside the territorial limits of the country has been settled by the courts through application of a long-established principle of international law, the “objective theory of jurisdiction.” This concept holds that even if an act is committed outside the territorial jurisdiction of U.S. courts, those courts can nevertheless have jurisdiction if the act produces effects within the home country. The only possible exception may be when the violation is the result of enforced compliance with local law.

Foreign Corrupt Practices Act

Recall from Chapter 5 that the Foreign Corrupt Practices Act (FCPA) makes it illegal for companies to pay bribes to foreign officials, candidates, or political parties. Stiff penalties can be assessed against company officials, directors, employees, or agents found guilty of paying a bribe or of knowingly participating in or authorizing the payment of a bribe. However, also recall that bribery, which can range from lubrication to extortion, is a common business custom in many countries, even though illegal.⁵⁷

The original FCPA lacked clarity, and early interpretations were extremely narrow and confusing. Subsequent amendments in the Omnibus Trade and Competitiveness Act clarified two of the most troubling issues. Corporate officers’ liability was changed from having *reason to know* that illegal payments were made to *knowing* of or authorizing illegal payments. In addition, if it is customary in the culture, small (grease or lubrication) payments made to encourage officials to complete routine government actions such as processing papers, stamping visas, and scheduling inspections are not illegal *per se*.

The debate continues as to whether the FCPA puts U.S. businesses at a disadvantage. Some argue that U.S. businesses are at a disadvantage in international business transactions in those cases in which bribery payments are customary, whereas others contend that it has little effect and, indeed, that it helps companies to “just say no.” The truth probably lies somewhere in between. The consensus is that most U.S. firms are operating within the law, and several studies indicate that the FCPA has not been as detrimental to MNCs’ interests as originally feared, because exports to developed and developing countries continue to be favorable.

Although U.S. firms seem able to compete and survive without resorting to corruption in the most corrupt societies, it does not mean that violations do not occur or that companies are not penalized for violations. For example, a U.S. environmental engineering firm was found to have made corrupt payments to an Egyptian government official to assist the company in gaining a contract. The company agreed not to violate the FCPA in the future, to pay a civil fine of \$400,000, and to reimburse the Department of Justice for the costs of the investigation. Furthermore, the company agreed to establish FCPA compliance procedures and to provide certifications of compliance annually for five years. Other firms have paid even larger fines in recent years, and the Justice Department has agreed not to prosecute firms with “excellent” training programs in place.

⁵⁷For discussions of the FCPA, updates, and other information, visit the FCPA home page at <http://www.usdoj.gov/criminal/fraud/fcpa.html>.

CROSSING BORDERS 7.2

The Kind of Correspondence an International Marketer Doesn't Want to See

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DPC (TIANJIN) LTD. CHARGED WITH VIOLATING THE FOREIGN CORRUPT PRACTICES ACT

WASHINGTON, D.C.—Acting Assistant Attorney General John C. Richter of the Criminal Division today announced the filing of a one-count criminal information charging DPC (Tianjin) Co. Ltd.—the Chinese subsidiary of Los Angeles-based Diagnostic Products Corporation (DPC)—with violating the Foreign Corrupt Practices Act of 1977 (FCPA) in connection with the payment of approximately \$1.6 million in bribes in the form of illegal “commissions” to physicians and laboratory personnel employed by government-owned hospitals in the People’s Republic of China.

The company, a producer and seller of diagnostic medical equipment, has agreed to plead guilty to the charge, adopt internal compliance measures, and cooperate with ongoing criminal and SEC civil investigations. An independent compliance expert will be chosen to audit the company’s compliance program and monitor its implementation of new internal policies and procedures. DPC Tianjin has also agreed to pay a criminal penalty of \$2 million.

The bribes were allegedly paid from late 1991 through December 2002 for the purpose and effect of obtaining and retaining business with these hospitals. According to the criminal information and a statement of facts filed in court, DPC Tianjin made cash payments to laboratory personnel and physicians employed in certain hospitals in the People’s Republic of

China in exchange for agreements that the hospitals would obtain DPC Tianjin’s products and services. This practice, authorized by DPC Tianjin’s general manager, involved personnel who were employed by hospitals owned by the legal authorities in the People’s Republic of China and, thus, “foreign officials” as defined by the FCPA.

In most cases, the bribes were paid in cash and hand-delivered by DPC Tianjin salespeople to the person who controlled purchasing decisions for the particular hospital department. DPC Tianjin recorded the payments on its books and records as “selling expenses.” DPC Tianjin’s general manager regularly prepared and submitted to Diagnostic Products Corporation its financial statements, which contained its sales expenses. The general manager also caused approval of the budgets for sales expenses of DPC Tianjin, including the amounts DPC Tianjin intended to pay to the officials of the hospitals in the following quarter or year.

The “commissions,” typically between 3 percent and 10 percent of sales, totaled approximately \$1,623,326 from late 1991 through December 2002, and allowed Depu to earn approximately \$2 million in profits from the sales.

DPC Tianjin’s parent company, Diagnostic Products Corporation, is the subject of an FCPA enforcement proceeding filed earlier today by the U.S. Securities and Exchange Commission. The SEC ordered the company to cease and desist from violating the FCPA and to disgorge approximately \$2.8 million in ill-gotten gains, representing its net profit in the People’s Republic of China for the period of its misconduct plus prejudgment interest ...

U.S. Antitrust Laws that Apply in Foreign Markets

Antitrust enforcement has two purposes in international commerce. The first is to protect American consumers by ensuring that they benefit from products and ideas produced by foreign competitors as well as by domestic competitors. Competition from foreign producers is important when imports are, or could be, a major source of a product or when a single firm dominates a domestic industry. This issue becomes relevant in many joint ventures, particularly if the joint venture creates a situation in which a U.S. firm entering a joint venture with a foreign competitor restricts competition for the U.S. parent in the U.S. market.

The second purpose of antitrust legislation is to protect American export and investment opportunities against any privately imposed restrictions. The concern is that all U.S.-based firms engaged in the export of goods, services, or capital should be allowed to compete on merit and not be shut out by restrictions imposed by bigger or less principled competitors.

The questions of jurisdiction and how U.S. antitrust laws apply are frequently asked but only vaguely answered. The basis for determination ultimately rests with the interpretation of Sections I and II of the Sherman Act. Section I states that “every contract, combination . . . or conspiracy in restraint of trade or commerce among the several states or with foreign nations is hereby declared to be illegal.” Section II makes it a violation to “monopolize, or attempt to monopolize, or combine or conspire with any other person or persons, to monopolize any part of the trade or commerce among the several states, or with foreign nations.”

The Justice Department recognizes that application of U.S. antitrust laws to overseas activities raises some difficult questions of jurisdiction. It also recognizes that U.S. antitrust-law enforcement should not interfere unnecessarily with the sovereign interest of a foreign nation. At the same time, however, the Antitrust Division is committed to controlling foreign transactions at home or abroad that have a substantial and foreseeable effect on U.S. commerce. When such business practices occur, there is no question in the Antitrust Division of the Department of Justice that U.S. laws apply.

Antiboycott Law

Under the antiboycott law,⁵⁸ U.S. companies are forbidden to participate in any unauthorized foreign boycott; furthermore, they are required to report any request to cooperate with a boycott. The antiboycott law was a response to the Arab League boycott of Israeli businesses. The Arab League boycott of Israel has three levels: A primary boycott bans direct trade between Arab states and Israel, a secondary boycott bars Arab governments from doing business with companies that do business with Israel, and a tertiary boycott bans Arab governments from doing business with companies that do business with companies doing business with Israel.⁵⁹

When companies do not comply with the Arab League’s boycott directives, their names are placed on a blacklist, and they are excluded from trade with members of the Arab League. Thus U.S. companies are caught in the middle: If they trade with Israel, the Arab League will not do business with them, and if they refuse to do business with Israel in order to trade with an Arab League member, they will be in violation of U.S. law.⁶⁰ One hospital supply company that had been trading with Israel was charged with closing a plant in Israel to get itself taken off the Arab League blacklist. After an investigation, the company pled guilty, was fined \$6.6 million, and was prohibited from doing business in Syria and Saudi Arabia for two years. A less costly fine of \$12,000 was paid by a freight forwarder who simply certified that the goods shipped for a third party were not of Israeli origin, were not shipped from Israel, and did not contain any material from Israel.

Extraterritoriality of U.S. Laws

The issue of the extraterritoriality of U.S. laws is especially important to U.S. multinational firms, because the long arm of U.S. legal jurisdiction causes anxiety for heads of state. Foreign governments fear the influence of American government policy on their economies through U.S. multinationals.⁶¹

⁵⁸The antiboycott law applies only to those boycotts not sanctioned by the U.S. government. Sanctioned boycotts, such as the boycotts against trade with Cuba and Iran, are initiated by the United States and must be honored by U.S. firms.

⁵⁹For those non-U.S. companies trading with the Arab League and complying with the boycott, each was required to include a statement on shipping invoices. On an invoice for 10 busses to be shipped from Brazil to Kuwait, the following statement appeared: “We certify that we are the producer and supplier of the shipped goods; we are neither blacklisted by the Arab Boycott of Israel nor are we the head office branch or subsidiary of a boycotted company. No Israeli capital is invested in this firm, no company capital or capital of its owners is invested in any Israeli company; our products are not of Israeli origin and do not contain Israeli raw material or labor.”

⁶⁰For a list of current cases against firms violating antiboycott law, visit <http://www.bxa.doc.gov> and select Antiboycott Compliance, then Antiboycott Case Histories.

⁶¹Anthony Ferner, Phil Almond, and Trevor Colling, “Institutional Theory and the Cross-National Transfer of Employment Policy: The Case of ‘Workforce Diversity’ in U.S. Multinationals,” *Journal of International Business Studies* 36, no. 3 (2005), pp. 304–21.

Especially troublesome are those instances when U.S. law is in conflict with host countries' economic or political goals. Conflict arises when the host government requires joint ventures to do business within the country and the U.S. Justice Department restricts or forbids such ventures because of their U.S. anticompetitive effects. Host countries see this influence as evidence of U.S. interference. When U.S. MNCs' subsidiaries are prohibited from making a sale in violation of the U.S. Trading with the Enemy Act, host governments react with hostility toward the extraterritorial application of U.S. foreign policy. This chapter's Global Perspective is a good illustration of the extraterritoriality of U.S. law and how it has an impact on a friendly neighbor as well as a major multinational company.

In an interesting development, MNCs are being held liable for the human-rights abuses of foreign governments. Lawsuits are being brought in U.S. courts against U.S. MNCs, charging them with doing business with oppressive regimes. Unocal Corporation was sued for doing business with Myanmar's (Burma's) military regime, which forced peasants at gunpoint to help build a pipeline for Unocal. Unocal denied the charges. This case was brought under the Alien Claims Act, originally intended to reassure Europe that the fledgling United States would not harbor pirates or assassins. It permits foreigners to sue in U.S. courts for violations of the "the law of nations." Businesses like IBM, Citibank, and Coca-Cola worry that they may be socked with huge jury damages for the misdeeds of oppressive governments. Employment lawyers warn that multinational companies are likely to face more lawsuits from the Third World.

When the intent of any kind of overseas activity is to restrain trade, there is no question about the appropriateness of applying U.S. laws. There is a question, however, when the intent is to conclude a reasonable business transaction. If the U.S. government encourages U.S. firms to become multinational, then the government needs to make provisions for the resolution of differences when conflict arises between U.S. law and host-government laws.

Export Restrictions

LO9

The steps necessary to move goods across country borders

Although the United States requires no formal or special license to engage in exporting as a business, permission or a license to export may be required for certain commodities and certain destinations. Export licensing controls apply to exports of commodities and technical data from the United States; re-exports of U.S.-origin commodities and technical data from a foreign destination to another foreign destination; U.S.-origin parts and components used in foreign countries to manufacture foreign products for exports; and, in some cases, foreign products made from U.S.-origin technical data. Most items requiring special permission or a license for exportation are under the control of the Bureau of Industry and Security (BIS)⁶² of the Department of Commerce.

The volume of exports and the number of companies exporting from the United States have grown spectacularly over the last decade. In an effort to alleviate many of the problems and confusions of exporting and to expedite the process, the Department of Commerce has published a revised set of export regulations known as the *Export Administration Regulations (EAR)*. They are intended to speed up the process of granting export licenses by removing a large number of items from specific export license control and concentrating licensing on a specific list of items, most of which pertain to national security, nuclear nonproliferation, terrorism, or chemical and biological weapons. Along with these changes comes a substantial increase in responsibility on the part of the exporter, because the exporter must now ensure that Export Administration Regulations are not violated.

The EAR is intended to serve the national security, foreign policy, and nonproliferation interests of the United States and, in some cases, to carry out its international obligations.⁶³ It also includes some export controls to protect the United States from the adverse impact

⁶²Formerly known as the Bureau of Export Administration (BXA).

⁶³For a primer on Commerce Department export controls, see "Introduction to Commerce Department Export Controls," <http://www.bis.doc.gov>, and select Export Control basics.

of the unrestricted export of commodities in short supply, such as Western cedar. Items that do not require a license for a specific destination can be shipped with the notation “NLR” (no license required) on the Shipper’s Export Declaration. Some export restrictions on high-technology products have been recently eased, which we hope marks the beginning of a new trend.⁶⁴

National Security Laws

American firms, their foreign subsidiaries, or foreign firms that are licensees of U.S. technology cannot sell products to a country in which the sale is considered by the U.S. government to affect national security. Furthermore, responsibility extends to the final destination of the product, regardless of the number of intermediaries that may be involved in the transfer of goods.

In the last century, an extensive export control system was created to slow the spread of sensitive technologies to the former Soviet Union, China, and other communist countries that were viewed as major threats to U.S. security. The control of the sale of goods considered to have a strategic and military value was extremely strict. But with the end of the Cold War, export controls were systematically dismantled until 1999, when a congressional committee reported Chinese espionage activities and American aerospace companies transferring sensitive technology irresponsibly. Following the report, legislation was passed again restricting the export of products or technologies that might be used by other countries for defense applications.

The events of September 11, 2001, added another set of restrictions related to weapons of mass destruction (WMD). Unfortunately, many of the products used in WMD are difficult to control because they have dual purposes; that is, they have legitimate uses as well as being important in manufacturing WMD. For example, Iraq, which was allowed to import medical equipment despite a U.N. embargo, purchased, under the pretext of medical benefits, six machines that destroy kidney stones. The manufacturer accepted the claim that Saddam Hussein was concerned about kidney stones in the Iraqi population and began shipping the machines. However, integral components of these machines are high-precision electronic switches that are also used to set off the chain reaction in thermonuclear weapons. When 120 additional switches as “spare parts” were ordered, a red flag went up, and the shipments were stopped.

Countless numbers of dual-purpose technologies are exported from the United States. A sticking point with dual-purpose exports is the intent of the buyer. Silicon Graphics Inc. (SGI) sold computer equipment to a Russian nuclear laboratory that contended it was for nonmilitary use, which would have been legal. However, the Department of Justice ruled that since the sale was made to a government-operated facility involved in both civil and noncivil activities, SGI should have applied for the correct export license. Thus, SGI paid a fine of \$1 million plus a \$500,000 fine for each of the export violations. National security laws prohibit a U.S. company, its subsidiaries, joint ventures, or licensees from selling controlled products without special permission from the U.S. government. The consequences of violation of the Trading with the Enemy Act can be severe: fines, prison sentences, and, in the case of foreign companies, economic sanctions.

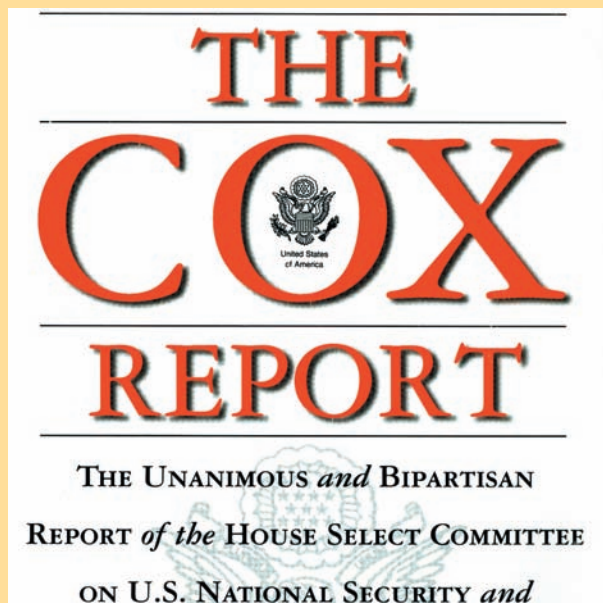
Exports are controlled for the protection and promotion of human rights, as a means of enforcing foreign policy, because of national shortages, to control technology,⁶⁵ and for a host of other reasons the U.S. government deems necessary to protect its best interests. In years past, the government restricted trade with South Africa (human rights) and restricted the sale of wheat to the Soviet Union in retaliation for its invasion of Afghanistan (foreign policy). Currently, the government restricts trade with Iran (foreign policy) and the sale of

⁶⁴James Auger, “United States to Ease Technology-Export Restrictions,” *Global Insight Daily Analysis*, January 23, 2008. We note that other countries also restrict exports for a variety of reasons. For example, see “Russian Government Mulls Additional Grain Export Restrictions,” *Russia and CIS General Newswire*, *Interfax*, November 15, 2007.

⁶⁵Deborah Zabarenko, “U.S. Policy Curbs Global Space Cooperation,” *Reuters*, June 23, 2005; “U.S. in Talks with Boeing over Sensor Sales to China,” *Reuters*, July 7, 2005; “Space Station, No Plan B for Outer Space,” *The Economist*, March 12, 2005, pp. 75–76.

CROSSING BORDERS 7.3

The Consequences of Mixing Politics and Security



In 1999 the Cox Report was published, making shocking claims about China's military aggressiveness toward the United States. The verbiage on the back cover delivered the gist of the argument:

China's Target: America

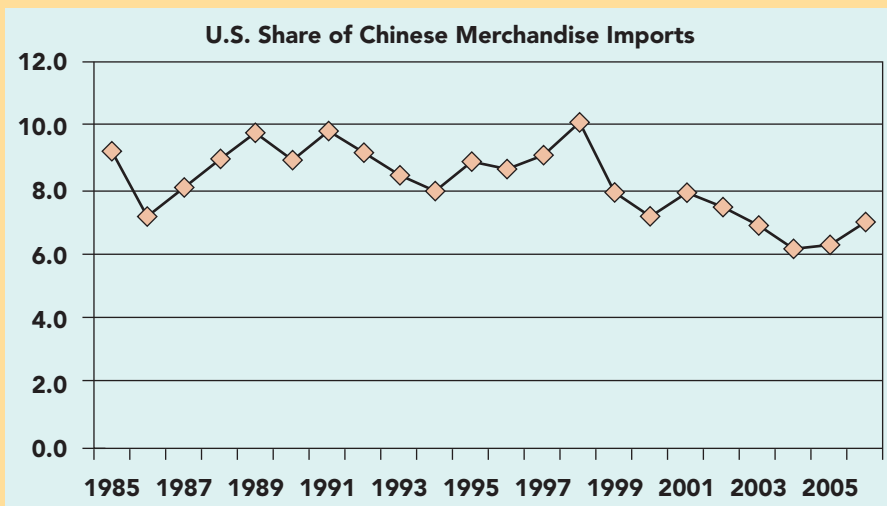
"The unanimous, bipartisan Cox Report is one of the most stunning documents ever to come from the U.S. Congress—a shocking account of how the People's Republic of China has targeted America for subversion, high-tech theft, and nuclear challenge.

How Communist China has replaced the former Soviet Union as America's chief military rival—and acquired the means to target nuclear missiles on American cities...."

At the time, the report was widely criticized as politically motivated and shallow in substance. Moreover, the events of September 11 rendered the argument, at best, obsolete. But the combination of the political attack on China and the associated renewed restrictions

on sales of high-technology goods and expertise has had a long-term chilling effect on U.S. sales in the world's fastest growing market. During 1999, the U.S. market share of merchandise exports to China fell from 10 percent to 8 percent, and the loss of competitiveness has remained permanent.

Sources: *The Cox Report* (Washington, DC: Regency, 1999); N. Mark Lam and John L. Graham, *China Now, Doing Business in the World's Most Dynamic Market* (New York: McGraw-Hill, 2007).



leading-edge electronics (control of technology), and it prohibits the export of pesticides that have not been approved for use in the United States (to avoid the return of residue of unauthorized pesticides in imported food and protect U.S. consumers from the so-called circle of poison). In each of these cases, U.S. law binds U.S. businesses, regardless of where they operate.

Determining Export Requirements

The first step when complying with export licensing regulations is to determine the appropriate license for the product. Products exported from the United States require a general or a validated export license, depending on the product, where it is going, the end use, and the final user. The *general license* permits exportation of certain products that are not subject to EAR control with nothing more than a declaration of the type of product, its value, and its destination. The *validated license*, issued only on formal

applications, is a specific document authorizing exportation within specific limitations designated under the EAR.

The responsibility of determining if a license is required rests with the exporter. This is a key point! The steps necessary to determine the type of license required and/or if an item can be shipped are as follows:

- The exporter is responsible for selecting the proper classification number, known as the *Export Control Classification Number (ECCN)*, for the item to be exported. The ECCN leads to a description in the *Commerce Control List (CCL)*, which indicates the exportability status of the item.
- The exporter must decide from the CCL if the items have end-use restrictions, for example, use in nuclear, chemical, and biological weapons. The exporter must also determine if the product has a dual use, that is, if it can be used in both commercial and restricted applications.
- The exporter is responsible for determining the ultimate end customer and end uses of the product, regardless of the initial buyer. This step includes carefully screening end users and uses of the product to determine if the final destination of the product is to an unapproved user or for an unapproved use. U.S. law requires firms to avoid shipments if the firm has knowledge that customers will use its products for illegal purposes or resell the product to unauthorized end users.

As is true of all the export mechanics that an exporter encounters, the details of exporting must be followed to the letter. Good record keeping, as well as verifying the steps undertaken in establishing the proper ECCN and evaluating the intentions of end users and end uses, is important should a disagreement arise between the exporter and the Bureau of Industry and Security. Penalties can entail denial of export privileges, fines, or both. For example, a five-year denial of export privileges was imposed on a resident of Pittsfield, Massachusetts, based on his conviction of illegally exporting 150 riot shields to Romania without the required export license. At the time of the shipment, the riot shields were controlled for export worldwide for foreign policy reasons.

Chinese air force officers undergo a training session on the latest command center instruments at a training school in Beijing. China successfully test-fired a new type of long-range ground-to-ground missile within its territory as tensions between China and Taiwan intensified after Taiwan's president declared that relations between Taipei and Beijing should be regarded as "special state-to-state relations." Most recently China and the United States have both shot down their own "errant" satellites with missiles.⁶⁶ Much of the electronic technology used in long-range missiles is dual-use; that is, the technology can be used for both nonmilitary and military applications. It is the exporter's responsibility to ensure that the final user of restricted dual-use products complies with export restrictions.



⁶⁶ "China Confirms Anti-Satellite Test to US, Says Not a Threat," *AFX UK Focus*, January 22, 2007; Yochi J. Dreazen, "U.S. Missile Hits Satellite—Military Strike Raised Hackles in China; Test Charges Denied," *The Wall Street Journal*, February 22, 2008, p. A9.

ELAIN, STELA, ERIC, and SNAP

Although the procedure for acquiring an export license may seem tedious on first reading, four electronic services facilitate the paperwork and reduce the time necessary to acquire export licenses.

- **ELAIN** (Export License Application and Information Network) enables exporters that have authorization to submit license applications via the Internet for all commodities except supercomputers to all free-world destinations. When approved, licensing decisions are conveyed back to the exporters via the Internet.
- **STELA** (System for Tracking Export License Applications), an automated voice-response system for tracking applications, can be accessed using a touch-tone phone. It provides applicants with the status of their license and classification applications and is available 24 hours a day, seven days a week. STELA can give exporters authority to ship their goods for those licenses approved without conditions.
- **ERIC** (Electronic Request for Item Classification), a supplementary service to ELAIN, allows an exporter to submit commodity classification requests via the Internet to the Bureau of Export administration.
- **SNAP** (Simplified Network Application Process), an alternative to paper license submissions, enables an exporter to submit export and re-export applications, high-performance computer notices, and commodity classification requests via the Internet. Acknowledgments of submissions will be received the same day, and electronic facsimiles of export licenses and other validations can be obtained online. SNAP is one of the changes made by the Department of Commerce to move it from being a paper-based bureaucracy to an all-digital department.

Summary

Businesses face a multitude of problems in their efforts to develop successful marketing programs. Not the least of these problems is the varying legal systems of the world and their effect on business transactions. Just as political climate, cultural differences, local geography, different business customs, and the stage of economic development must be taken into account, so must such legal questions as jurisdictional and legal recourse in disputes, protection of intellectual property rights, extended U.S. law enforcement, and enforcement of antitrust legislation by U.S. and foreign governments. A primary marketing task is to develop a plan that will be

enhanced, or at least not adversely affected, by these and other environmental elements. New to the international legal scene is the Internet, which, by its nature, creates a new set of legal entanglements, many of which have yet to be properly addressed. One thing is certain: The freedom that now exists on the World Wide Web will be only a faint memory before long. The myriad questions created by different laws and different legal systems indicate that the prudent path to follow at all stages of foreign marketing operations is one leading to competent counsel, well versed in the intricacies of the international legal environment.

Key Terms

Common law
Code law
Islamic law

Marxist–socialist tenets
Conciliation
Arbitration

Litigation
Prior use

Registration
Cybersquatters (CSQs)

Questions

1. Define the key terms listed above.
2. How does the international marketer determine which legal system will have jurisdiction when legal disputes arise?
3. Discuss the state of international commercial law.
4. Discuss the limitations of jurisdictional clauses in contracts.
5. What is the “objective theory of jurisdiction”? How does it apply to a firm doing business within a foreign country?

6. Discuss some of the reasons seeking an out-of-court settlement in international commercial legal disputes is probably better than suing.
7. Illustrate the procedure generally followed in international commercial disputes when settled under the auspices of a formal arbitration tribunal.
8. What are intellectual property rights? Why should a company in international marketing take special steps to protect them?
9. In many code-law countries, registration rather than prior use establishes ownership of intellectual property rights. Comment.
10. Discuss the advantages to the international marketer arising from the existence of the various international conventions on trademarks, patents, and copyrights.
11. “The legal environment of the foreign marketer takes on an added dimension of importance since there is no single uniform international commercial law which governs foreign business transactions.” Comment.
12. Why is conciliation a better way to resolve a commercial dispute than arbitration?
13. Differentiate between conciliation and arbitration.
14. Assume you are a vice president in charge of a new business-to-business e-commerce division of a well-known major international auto parts manufacturer. A cybersquatter has registered the company name as a domain Web name. What are your options to secure the domain name for your company? Discuss the steps you should take to ensure worldwide protection of your domain name.
15. Discuss the issues of a Web site owner being liable for information posted on the site.
16. Discuss the motives of a cybersquatter. What recourse does a company have to defend itself against a cybersquatter?