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WHO COULD BE AT RISK FOR PERSONAL LIABILITY IN CUSTOMS VIOLATIONS?

Dan Swartz
Director of Customs and Compliance

An interview with Thomas J. O'Donnell, attorney at Clark-Hill, PLC.

Trek Leather, Inc., and its owner were found guilty by the Court of International Trade (CIT) in 2011 for violating 19 U.S.C. §1592 for the undervaluation of imported merchandise. *United States v. Trek Leather, Inc., and Harish Shadadpuri, 781 F.Supp.2d 1306, (CT.Int'l Trade, 2011)*. This was a landmark decision, as the owner—an officer of the corporation—was found personally liable for violations by Trek Leather, Inc., a corporation.

Clark Hill attorney **Thomas J. O'Donnell**

The case was appealed to the Court of Appeals for the Federal Circuit (CAFC), which reversed the CIT in July 2013. This would have seemed to settle the question about personal liability for customs violations. However, in March 2014, the Government requested an en banc rehearing by the CAFC on the matter of personal liability. On September 16, 2014, the CAFC reversed its original decision and ruled that Trek Leather's owner was, in fact, personally liable. *U.S. v. Trek Leather, Inc., No. 11-1527 (Fed.Cir. Sept. 16, 2014)*.

Dan: Tom, why the change in decision by the CAFC?

The language in the Customs penalty statute, commonly referred to as "Section 592," provides that no person shall by fraud, gross negligence, or negligence "enter, introduce, or attempt to enter or introduce" merchandise into the United States or "aid or abet" any person in doing so. In the arguments advanced by the Government in the CIT, it concentrated on the terms "enter" and "aid or abet," dropping its argument as to aiding or abetting when the case reached the CAFC. In its initial decision, the CAFC focused on the word "enter" and concluded that Mr. Shadadpuri, the owner of Trek, did not "enter" the goods because Trek was the importer of record. Thus, the CIT decision turned on the fact that Mr. Shadadpuri was not the "person" who "entered" the goods (the importer of record).

In its *en banc* decision, the CAFC did not focus on the word "enter" but instead focused on Section 592's use of the word "introduce," an issue that had not been touched on at the CIT level. It then cited a line of cases that held that the term "introduce" is broader than the term "enter" and applies to actions that occur prior to formal entry or attempted formal entry of goods. Specifically, the CAFC cited a 1913 Supreme Court decision *(U.S. v. 25 Packages of Panama Hats)* that broadly interpreted the term "introduce" in a prior Customs penalty statute. In that case, the Supreme Court held that presenting false invoices to an American consulate abroad amounted to an attempt to "introduce" the goods, even though the importer never attempted to enter them. The CAFC explained:

Panama Hats establishes that "introduce" is a flexible and broad term added to ensure that the statute was not restricted to the "technical" process of "entering" goods. It is broad enough to cover, among other things, actions completed before any formal entry filings made to effectuate release of imported goods. We need not attempt to define the reach of the term. Under the rationale of Panama Hats, the term covers actions that bring goods to the threshold of the process of entry by moving goods into CBP custody in the United States and providing critical documents (such as invoices indicating value) for use in the filing of papers for a contemplated release into United States commerce even if no release ever occurs.

Thus, the CAFC has overturned the generally accepted concept that the importer of record is the only person who normally is liable for Customs law violations.

Dan: How did the Court conclude that the owner of Trek Leather was personally liable?

The Customs penalty statute states that "no person" shall enter or introduce or attempt to enter or introduce goods by fraud, negligence, or gross negligence. In reaching its decision, the Court cited a 1909 Supreme Court case that interpreted the term "person," which appeared in the Customs penalty provisions enacted in the Tariff Act of 1890. The Supreme Court rejected the argument that the term "person" was limited to owners, importers, consignees, or agents. The CAFC then examined the legislative history of Section 592 and noted that Congress stated that they had no intention of narrowing its reach. The CAFC said, "There is, in short, no basis for giving 'person' in section 592(a)(1) less than its ordinary broad meaning." The owner of Trek Leather is, of course, a "person" in the ordinary broad meaning of that term.

Dan: How does this ruling relate to the "piercing of the corporate veil"?

This really is the reason this case is so controversial and has received the attention it has. The CAFC stated:

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"Applying the statute to Mr. Shadadpuri does not require any piercing of the corporate veil. Rather, we hold that Mr. Shadadpuri's own acts come within the language of subparagraph (A). It is longstanding agency law that an agent who actually commits a tort [a civil wrong] is generally liable for the tort along with the principal, even though the agent was acting for the principal . . . We do not hold Mr. Shadadpuri liable because of his prominent officer or owner status in a corporation that committed a subparagraph (A) violation. *We hold him liable because he personally committed a violation of subparagraph (A).* [Emphasis added.]"

This decision seems to open the door to personal liability for anyone who provides entry documents or electronic data to Customs because it permits Customs to impose liability on individuals who are acting as agents of a corporation. The Court was clear that individual liability arises from the law of agency, which means that not only is a principal (corporation, LLC, LLP) liable for the act of its agents; agents are personally liable as well.

Dan: Who could be at risk for personal liability in customs violation matters in the future? Many of our clients have personnel who are responsible for customs compliance in their companies. Are they at risk?

Again, according to the Court, any agent of the importer can be liable. Compliance people, as agents of the their companies, are on the front line as are small businesses owners. Import managers and compliance personnel certainly are at risk because this is what they do day in and day out. Small businesses and closely held businesses also have higher risks because often the owners are intimately involved in all aspects of their business, including the information that is provided to Customs. I also suspect that Customs will aggressively use this new authority to extract higher penalties from limited liability entities. Frankly, it's a scary proposition for importers. Who wants to risk their own personal assets on what Customs may decide amounts to a violation of Section 592?

Dan: How can company officers, employees, and business owners mitigate risk for personal liability?

The key element to Section 592, which also has a provision for recovery of duties that are owing, is that it only comes into play if the importer (or his employee/agent) is at fault. If the importer is exercising "reasonable care," Section 592 does not apply.

I think the first line of defense is to have in place a good compliance program and to make sure that it is being followed. A good compliance program is one that covers all the significant risk areas and is tailored to a specific importer's processes. This means having written procedures and policies that are embedded into job descriptions and the actual paperwork flow of the company. A generic compliance program that is not specific to the way a company actually does business is not going to work. Also, following up to ensure that procedures are being followed is a must. Customs is not impressed when you pick up your compliance manual from the top shelf and blow off the dust before you hand it to them. Specific compliance subjects include tariff classification databases, obtaining rulings in doubtful situations, dealing with valuation issues such as assists, buying commissions, royalties, related party pricing, etc. Most companies have specific areas that present the highest risks, and these areas have to be addressed.

Hiring knowledgeable, diligent import personnel, of course, is another must, as is choosing a knowledgeable, compliance-oriented Customs broker. For smaller importers or for companies that do not import significant quantities of goods, a good Customs broker is an absolute necessity, because these companies may not be in a position to hire dedicated compliance specialists. Therefore, they will need to rely more heavily on the expertise of their Customs broker. Regardless of a company's size, good communication with its brokers is essential.

I expect that some of the front line people mentioned earlier will be looking for indemnification agreements from their employers.

Finally, penalty liability for Customs brokers generally is governed by Section 641 and not Section 592. However, Section 592 is applicable to Customs brokers if they are guilty of fraud or are guilty of negligence or gross negligence and share in the proceeds of the violation with the importer (e.g., a broker gets a $10,000 entry fee while using a questionable tariff classification).

Thomas J. O'Donnell is a Member in Clark Hill's Customs and International Trade Law practice group. He focuses on all aspects of the import and export process, including tariff classification and valuation of imported merchandise, country of origin determinations, country of origin marking, comprehensive import, export and NAFTA compliance programs, antidumping and countervailing duty proceedings, defense of sureties, broker/forwarder matters, intellectual property issues, quota/visa issues, and drawback.

Tom received a Bachelor of Science degree, cum laude, from Florida Atlantic University in 1967, a Juris Doctor degree from Loyola University in 1973, and was admitted in that same year to the Illinois State Bar and the Bar of the U.S. District Court for the Northern District of Illinois. In 1974, he was admitted to the U.S. Court of Appeals for the Federal Circuit and the U.S. Court of International Trade; the New York Bar in 1978; the District of Columbia Bar in 1988; and the U.S. Supreme Court in 1995. He is also a licensed Customs broker. Tom is member of the Illinois State, Chicago and American Bar Associations, the District of Columbia Bar, and the Customs & International Trade Bar Association.