Fed. Circ. Brings Stability To Import Penalty Cases

By **Alex Lawson**

Law360, New York (December 2, 2015, 6:58 PM ET) -- The Federal Circuit handed a decisive victory to Nitek Electronics Inc. on Tuesday when it ruled the U.S. Department of Justice couldn't hold the company to a different level of culpability for duty evasion penalties than U.S. Customs and Border Protection, bringing consistency to administrative and civil proceedings.

In its **Nitek decision**, the three-judge panel made clear that the government could not bring its case against the importer for penalties stemming from unpaid duties on Chinese gas meter parts based on a standard of negligence because CBP had handed down its penalty based on the higher standard of gross negligence.

On its face, the decision appears to significantly clip DOJ's wings with regard to how it may handle its litigation against importers for penalties, according to Barnes Richardson & Colburn LLP partner Lawrence M. Friedman.

"The decision fundamentally changes the Justice Department's role in penalty actions," Friedman told Law360. "Formerly, there was a belief that as long as Customs completed the administrative process and made a penalty claim, the Department of Justice was free to pursue the matter without regard to Customs' findings on the level of culpability."

Distinguishing between the three levels of culpability under Section 1592 of the customs code — negligence, gross negligence and fraud — is no minor step, as each carries different burdens of proof for the government and the targeted importer.

At the heart of the panel's decision is the notion that three different levels exist independently from one another, and that alleging a higher level does not necessarily imply an allegation of all levels existing below it.

With this discrepancy addressed by the court, Sandler Travis & Rosenberg PA attorney Beth C. Ring said that CBP officials will have to take steps to ensure their allegations are precisely tailored to the facts at hand.

"This means that the government can't just do anything it wants, it is constrained by the

law," she said. "They have to be more careful in terms of how they pursue penalty cases, they better dot the i's and cross the t's."

When deciding in favor of Nitek, the Federal Circuit looked to its own precedent in case known as U.S. v. Optrex. The distinction between the two cases was that Optrex featured the DOJ pursuing a higher level of culpability than CBP while the Nitrek case featured a shift to a lower standard.

The government attempted to exploit this difference to keep its case alive, but to no avail, as the panel saw that the Optrex decision's holding on the obligations within the different culpability levels stood regardless of the direction of the shift.

"This decision fully converts penalty cases from being de novo in the traditional sense to collections cases in which the court decides whether the evidence brought to court supports Customs' right to collect on the specific claim it perfected during the administrative phase," Friedman said. "It is still a de novo process, but the scope is limited to the administrative claim."

Clif Burns, the Bryan Cave LLP partner who represented Nitek, told Law360 that he expected the decision would lead CBP to allege all three levels of culpability in alternating forms in the administrative penalty stages, which could conceivably free up the DOJ to pursue whatever route it believes is strongest in court.

"This will require importers to be more detailed in their responses to penalty notices, but will eliminate the uncertainty and confusion caused by the government shifting theories in the middle of the process," Burns said.

CBP actually began taking this path around the time Nitek first prevailed at the CIT in 2012, but some on the importers' side of the bar viewed the Federal Circuit's decision as pushing back against such a strategy.

While CBP can initiate a penalty proceeding alleging multiple levels of culpability in the alternative, the penalty it ultimately assesses is based on one level alone. It is that final level, not any other standard articulated earlier in the process that must now take precedent in a subsequent CIT complaint, according to Neville Peterson LLP attorney John M. Peterson.

“Customs has tried to hedge its bet by alleging different levels of culpability in penalty notices,” he told Law360. “This suggests that the government can only allege one level at a time, must notify the importer if they change it, and whatever they decide at the end of the process — they're stuck with it in court.”

U.S. Circuit Judges Pauline Newman, Raymond Clevenger III and Kathleen O'Malley sat on the panel for the Federal Circuit.

Nitek is represented by Robert Clifton Burns and Michael Benjamin Zara of Bryan Cave LLP.

The government is represented by U.S. Department of Justice attorneys Stephen C. Tosini, Jeanne E. Davidson, Patricia M. McCarthy and Benjamin C. Mizer and U.S. Customs and Border Protection attorney Eric Paul Delmar.

The case is U.S. v. Nitek Electronics Inc., case number 15-1166, in the U.S. Court of Appeals for the Federal Circuit.

--Editing by John Quinn and Emily Kokoll.