



September 2004

Exporting Refresher: Knowing the Basics and Getting Answers

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A local software company makes software designed to screen prospective employees for employment. When they first began looking into China as a market, they were initially surprised to hear that in China, there were no screening or qualifying tests used to qualify potential employees. At this point the company went from “How do we find a partner to sell into that market?” to “Can we create demand and change the business culture to need our product?”

Sometimes, the fundamental differences between countries and cultures will acutely alter your country marketing strategy and market opportunity.

Mr. Dana Shannon, International Trade Advisor for the Small Business International Trade Center, is one of the most experienced educators on developing global markets with a distribution channel. When asked about the most important factors for small businesses to consider before exporting, he stated, “Finding the right distributor and conducting thorough market research are essential.”

He went on to say, “One of the things that is a major issue is knowing who your distributor is going to be and building that relationship. If you don’t have the right distributor your product is not going to get distributed properly and you can lose control.”

As we head back to school and begin to focus on new projects in our respective companies, I want to provide you with a refresher course for developing and maintaining your high-technology export markets.

Global software market still hot

Software continues to be a very dynamic and fast-changing global industry. Competition is fierce and small businesses need to build in efficiencies and advantages to stay on top. Software is the fastest-growing segment of the IT market worldwide.

The demand for software in foreign markets is huge. But despite its significance in the global market and the potential even for small US software companies abroad, software’s diversity and accessibility present a challenge to companies looking to export.

The many types of software, and the many distribution methods, inevitably confuse the export process. Some countries welcome US software, while others attempt to create a domestic software market to meet local demand, eliminating or discouraging its import. These attitudes and inconsistencies can create trade barriers between the US and other countries, making the export process for software and other IT technologies particularly daunting.

I talked to a small, Eugene-based software company, CBT Nuggets (www.cbtnuggets.com), about the global software market outlook for their company. CBT Nuggets makes IT training and certification videos. I asked Mr. Jeff Short, director of marketing, to comment on regions of growth for his firm: “We still do about 30% internationally – a good portion is UK, Canada and Australia because they’re English-speaking. We’ve had a lot more interest from India and the Middle East, but not a lot of actual sales coming through.”

What are the major issues?

While identifying many trade barriers requires country-specific market research, having a general understanding of some major **trade barriers and regulations** and where to research them is helpful.

Some of the major issues are:

- Logistics: tariffs and taxes
- Intellectual property protection
- Software/IT product classification
- Intellectual property rights protection
- Export licensing

Logistics: tariffs

For companies of all sizes, exporting logistics can be cumbersome. Tariffs, taxes, licensing, fraud and IPR are just some of the complications SMEs must overcome when selling globally. Fortunately, there are companies out there that can help you with the shipping and order fulfillment process. Delivery via the Internet can diminish this burden, but for firms that still send hard disks and equipment there is labor and experience needed to navigate the often-complex requirements. There are three major firms that specialize in this:

Federal Express Global Trade Manager

<http://www.fedex.com/us/international/?link=1&lid=//International&hbxrootmenuid=//International&hbxrootmenuorientation=down>

DHL International Services

<http://www.dhl-usa.com/IntlSvcs/IntlSvcsHome.asp?nav=InternationalService>

UPS Shipping International

http://www.ups.com/content/us/en/resources/advisor/intl_shipping/index.html

I asked Mr. Short how he handles the logistics of being a small company: “FedEx has been a great partner because they take care of all the taxes and details for us. If we had to do this ourselves it would put a significant strain on our resources.”

NAFTA

The signing of the North American Free Trade Agreement (NAFTA) in 1994 established tariff-free trade on a multi-sectoral basis between the U.S., Canada, and Mexico. Software tariffs were thus eliminated. Further information on NAFTA is given at <http://www.mac.doc.gov/nafta/naftatext.html>. For help with **NAFTA Certificates of Origin**, go to <http://web.ita.doc.gov/ticwebsite/ticit.nsf/>.

EU/VAT

In the EU, tariffs are consistent throughout the region with software at 0%. However, each country has their own VAT and some markets have Withholding Taxes on Software Royalties. These taxes can be confusing. A VAT is similar to a sales tax and each EU country has a different VAT percentage. Markets such as Italy, Poland and Spain have the withholding tax too. These back-end taxes will affect your price point. To find EU VATs for Software and Withholding Taxes on Software Royalties (HS # 8524), go to this US Department of Commerce link at: <http://web.ita.doc.gov/ITI/itiHome.nsf/9b2cb14bda00318585256cc40068ca69/02a8ed8c1550b42a85256d8100739caa!OpenDocument>.

To find out **import tariffs and taxes** on software by country, visit <http://web.ita.doc.gov/ITI/itiHome.nsf/9b2cb14bda00318585256cc40068ca69/85e97beb145b069585256d82005db175!OpenDocument>.

B2B/B2C in the EU

The Internet has changed the way business is conducted throughout the world. It has shrunk the business universe and bridged countries half a world away. One important development is the Internet as a sales delivery tool. Many countries are not sure how to deal with it. Here in the US, we have had similar growing pains with assessing state sales taxes.

The EU's solution to this problem, as of 2002, was to tax B2C sales into the EU regardless of the origin of the selling firm. For example, Amazon.com would be subject to VAT collection on sales to the EU. However, firms selling B2B into the EU are exempt from this law. Please see the June 2002 article in the SAO Cursor on the subject at [http://www.sao.org/newsletter/documents/Brad Anderson_0602.pdf](http://www.sao.org/newsletter/documents/Brad_Anderson_0602.pdf).

Software classification

Software classification is a major issue worldwide, especially with increased use of online delivery systems (is software a good or a service?). Even in countries with free-trade agreements with the US, it must be determined which imported products should receive tax and tariff breaks, meaning that rules-of-origin must be met and product qualification confirmed.

The Information Technology Agreement (ITA), which has 60 signatories worldwide, has eliminated import tariffs on software in most major countries. For more **information about the ITA**, and a **list of signatories**, go to <http://web.ita.doc.gov/ITI/itiHome.nsf/8a463e0c5fef335685256ccb006184ab/56c5c43580267d2285256cf70069b2a0!OpenDocument>.

Intellectual property protection

While standards for the protection and enforcement of intellectual property exist under some treaties and international agreements, there is no worldwide protection of intellectual property, and software piracy remains a problem globally. If you are looking to export your software, you should **apply for intellectual property protection** in the country of import in order to protect your code.

The **Madrid System for the International Registration of Marks** simplifies this issue by giving a trademark owner the possibility of having his or her mark protected in several countries. The trademark owner simply needs to file one application in one office, in one language, with one set of fees in one currency (Swiss francs). For more information about this system and the participating countries (those party to the Madrid Agreement), visit <http://www.wipo.int/madrid/en/index.html>

For additional information about intellectual property protection, check out my SAO Curser article next month on software piracy.

Customs classification

Standard Harmonized System (HS) codes play a key role in the export process. Exports and imports are classified by their HS codes, and taxes and tariffs are applied accordingly. The four-digit HS heading for software is 8524, but this code is expanded to six digits for further specification. Some countries may implement a 10-digit HS code system, although only the first six digits are standardized worldwide.

To **search for an HS code**, go to <http://www.census.gov/foreign-trade/schedules/b/index.html>.

Export licensing regulations

The Bureau of Industry and Security (BIS) is responsible for most export licensing in the US. Contrary to popular belief, only a small number of US companies require export licenses. According to the **BIS website** (www.bis.doc.gov), "License requirements are dependent upon an item's technical characteristics, the destination, the end user and the end use."

Regulations most relevant to software companies are the **Deemed Export Rule** and **encryption controls** of export and re-export of commercial encryption products. What is a "deemed" export? In short, "an export of technology or source code (except encryption source code) is 'deemed' to take place when it is released to a foreign national within the United States."

Regarding encryption controls, the June 6, 2002 changes to the encryption policy are of particular interest: “Mass market’ encryption commodities and software with symmetric key lengths exceeding 64 bits may now be exported and re-exported under ECCN [Export Control Classification Number] 5A992 or 5D992, following a 30-day review.”

These regulations are explained in further detail on the website. Remember that it is also important to **look into import licensing requirements and restrictions** in the country of import.

Additional resources

- **The Basic Guide to Exporting**
This online handbook, developed by Unz & Co., is a useful tool for the beginning/learning stages of the export process. It gives you an idea of what to consider when looking to export, and provides useful background information on key issues related to exporting.
<http://www.unzco.com/basicguide/index.html>
- **Trade barriers by country**
There are several useful resources on trade barriers and regulations by country. The office of the United States trade representative provides **National Trade Estimate Reports** on Foreign Trade Barriers by country:
<http://www.ustr.gov/reports/ntr/2004/index.htm>.
- The **Country Commercial Guides** (CCGs) – published by the US Commercial Service – provide useful information about all aspects of doing business in foreign countries. Access the CCGs and other market research at http://www.buyusainfo.net/adsearch.cfm?search_type=int&loadnav=no (this is a free service, but it will require Export.gov registration). Information about trade barriers will be in the “Trade Regulations and Standards” chapter.
- **International web resources portal**
See this new feature of the SAO website for additional export-related links.

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