Chapter 7: The Environment of Electronic Commerce: Legal, Ethical, and Tax Issues

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Objectives

In this chapter, you will learn about:
- Laws that govern electronic commerce activities
- Laws that govern the use of intellectual property by online businesses
- Online crime, terrorism, and warfare
- Ethics issues that arise for companies conducting electronic commerce

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Objectives (continued)

- Conflicts between companies’ desire to collect and use data about their customers and the privacy rights of those customers
- Taxes that are levied on electronic commerce activities

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The Legal Environment of Electronic Commerce

- Online businesses:
  - Must comply with the same laws and regulations that govern the operations of all businesses
  - Face complicating factors
    - The Web extends a company’s reach beyond traditional boundaries
    - The Web increases the speed and efficiency of business communications
    - The Web creates a network of customers

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Borders and Jurisdiction

- Territorial borders in the physical world mark the range of culture and reach of applicable laws very clearly
- European Union (EU)
  - Allows free movement within the EU for citizens of member countries
  - Adopted a common currency

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Borders and Jurisdiction (continued)

- Power
  - A form of control over physical space and the people and objects that reside in that space
  - A defining characteristic of statehood
- Jurisdiction
  - Ability of a government to exert control over a person or corporation
- Effects
  - Impact of a person’s behavior

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Borders and Jurisdiction (continued)

- Legitimacy
  - Idea that those subject to laws should have some role in formulating them
- Notice
  - The expression of a change in rules
- Constructive notice
  - Individuals become subject to new laws and cultural norms when they cross an international border

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**Jurisdiction on the Internet**

- Power, effects, legitimacy, and notice do not translate well to the virtual world of electronic commerce
- Governments that want to enforce laws must establish jurisdiction over business conduct
- Contract
  - Promise or set of promises between two or more legal entities

**Subject-Matter Jurisdiction**

- Subject-matter jurisdiction is a court’s authority to decide a type of dispute
- Personal jurisdiction
  - Determined by the residence of the parties
- Forum selection clause
  - States that a contract will be enforced according to the laws of a particular state
- Long-arm statutes
  - Create personal jurisdiction over nonresidents who transact business in the state

**Contracting and Contract Enforcement in Electronic Commerce**

- Contract
  - Includes three essential elements
    - An offer, an acceptance, and consideration
    - Formed when one party accepts the offer of another party
- Offer
  - Commitment with certain terms made to another party
- Acceptance
  - Expression of willingness to take an offer

**Contracting and Contract Enforcement in Electronic Commerce (continued)**

- Statute of Frauds
  - The following must be created by a signed writing
    - Contracts for the sale of goods worth over $500
    - Contracts requiring actions that cannot be completed within one year

**Contracting and Contract Enforcement in Electronic Commerce (continued)**

- A writing
  - Exists when the terms of a contract have been reduced to some tangible form
- Signature
  - Any symbol executed or adopted for the purpose of authenticating a writing
- Warranties on the Web
  - Any contract for the sale of goods includes implied warranties

**Tort**

- Intentional or negligent action taken by a legal entity that causes harm to another legal entity

A court has sufficient jurisdiction in a matter if it has both subject matter jurisdiction and personal jurisdiction

**Figure 7-2** Forum selection clause on the Opasq Web site
Contracting and Contract Enforcement in Electronic Commerce (continued)

- Warranty disclaimer
  - Statement declaring that the seller will not honor some or all implied warranties
- Authority to bind
  - Determining whether an individual has the authority to commit a company to an online contract
- Terms of service (ToS)
  - Intended to limit a Web site owner’s liability

Use and Protection of Intellectual Property in Online Business

- Intellectual property
  - Includes all products of the human mind
  - Products can be tangible or intangible
- Intellectual property rights
  - Include protections by governments through:
    - Granting of copyrights and patents
    - Registration of trademarks and service marks

Web Site Content Issues

- Copyright
  - Right granted by a government to an author or creator of a literary or artistic work
- Creations that can be copyrighted include all forms of artistic or intellectual expression
- Works copyrighted by corporations or not-for-profit organizations are protected for 95 years

Web Site Content Issues (continued)

- Fair use of a copyrighted work
  - Includes copying it for use in criticism, comment, news reporting, teaching, or research
- Vicarious copyright infringement
  - Entity becomes liable if:
    - It is capable of supervising infringing activity
    - It obtains financial benefit from infringing activity

Patent Infringement

- Patent
  - Exclusive right granted by a government to an individual to make, use, and sell an invention
- To be patentable the invention must be genuine, novel, useful, and not obvious, given the current state of technology
- Business process patent
  - Protects a specific set of procedures for conducting a particular business activity

Trademark Infringement

- Trademark
  - Distinctive mark, device, motto, or implement that a company affixes to goods it produces
- Service mark
  - Used to identify services provided
- Trade name
  - Name that a business uses to identify itself
- Common law
  - Part of British and U.S. law established by the history of court decisions

Domain Names, Cybersquatting, and Name Stealing

- Cybersquatting
  - Registering a domain name that is the trademark of a person or company and hoping to sell it to that person or company for money
- Name changing
  - Registering misspelled variations of well-known domain names
- Name stealing
  - Ownership of a site’s assigned domain name is changed to another site and owner

Domain Names, Cybersquatting, and Name Stealing (continued)

- U.S. Anticybersquatting Consumer Protection Act
  - Protects trademarked names from being registered as domain names by other parties
  - Parties found guilty of cybersquatting can be held liable for damages of up to $100,000 per trademark
Protecting Intellectual Property Online

- Proposed solutions to problems in digital copyright protection include:
  - Host name blocking
  - Packet filtering
  - Proxy servers

Defamation

- Defamatory statement
  - Statement that is false and injures the reputation of another person or company
- Product disparagement
  - If a defamatory statement injures the reputation of a product or service instead of a person
- Per se defamation
  - Court deems some types of statements to be so negative that injury is assumed

Advertising Regulation

- Federal Trade Commission
  - Regulates advertising in the United States
  - Publishes regulations and investigates claims of false advertising
  - Provides policy statements
  - Policies cover specific areas such as:
    - Bait advertising
    - Consumer lending and leasing
    - Endorsements and testimonials

Online Crime, Terrorism, and Warfare

- Online crime
  - Obstacles faced by law enforcement:
    - Jurisdiction
    - Difficulty applying laws written before the Internet became prone to criminal actions
- Online warfare and terrorism
  - Sustained effort by a well-financed terrorist group could slow down operation of major transaction-processing centers

Ethical Issues

- Web businesses find ethical issues are important to consider when making policy decisions
- Electronic Communications Privacy Act of 1986
  - Main law governing privacy on the Internet today
- Differences in cultures throughout the world have resulted in different expectations about privacy in electronic commerce

Ethical Issues (continued)

- Principles for handling customer data:
  - Use data collected to provide improved customer service
  - Do not share customer data with others outside your company without the customer’s permission
  - Tell customers what data you are collecting and what you are doing with it
  - Give customers the right to have you delete any of the data you have collected about them

Communications with Children

- Children’s Online Privacy Protection Act of 1998 (COPPA)
  - Provides restrictions on data collection that must be followed by electronic commerce sites aimed at children
- Children’s Internet Protection Act (CIPA)
  - Requires schools that receive federal funds to install filtering software on computers
Taxation and Electronic Commerce

- Income taxes
  - Levied by national, state, and local governments on net income generated by business activities
- Transaction taxes
  - Levied on products or services that a company sells
- Property taxes
  - Levied by states and local governments on personal property and real estate used in business

U.S. Income Taxes

- Internal Revenue Service (IRS)
  - U.S. government agency charged with administering the country’s tax laws
- Basic principle of the U.S. tax system
  - Any verifiable increase in a company’s wealth is subject to federal taxation
- Any company whose U.S.-based Web site generates income is subject to U.S. federal income tax

U.S. State Sales Taxes

- Use tax
  - Levied by a state on property used in that state that was not purchased in that state
- In most states use tax rates are identical to sales tax rates
- Purchasers exempt from sales tax include certain charitable organizations and businesses buying items for resale

European Union (EU) Value Added Taxes

- Value Added Tax
  - Most common transfer tax used in the EU
  - Assessed on the amount of value added at each stage of production
- EU enacted legislation
  - Companies based in EU countries must collect VAT on digital goods

Summary

- Legal concept of jurisdiction on the Internet is still unclear and ill defined
- Relationship between geographic boundaries and legal boundaries are based on power, effects, legitimacy, and notice
- Innocent inclusion of photographs and other elements on a Web page can lead to infringement of trademarks, copyrights, or patents

Summary (continued)

- The Internet can be used to perpetrate crimes, advocate terrorism, and wage war
- Web business practices have led to questions of ethics regarding online privacy
- Companies that conduct electronic commerce are subject to the same laws and taxes as other companies
- The international nature of business complicates tax obligations