

# Legal Obligations and Potential Risks for Chinese Electric Guitar Enterprises from a Perspective of International Commercial Law

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**Abstract:** With the rapid trend of globalization, enterprises are exposed to the challenges of cross-border transactions and international business. It is thus very crucial for business entities to understand international commercial law. This article applies the knowledge of international commercial law to analyze the obligation that Chinese electric guitar enterprises need to fulfil. The article finds that electric guitar enterprises need to pay close attention to product quality, product liability, and intellectual property laws and regulations. In addition, this article discusses the risks arising from the qualification of the counterparty, the selection of contract terms, the payment method of letter of credit and the transportation of goods. In the end, concrete measures are proposed to cope with the risks discussed above.

**Keywords:** International commercial law; international trade; electric guitar; corporate compliance.

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## 1. Introduction

Nowadays, China has played an active role in international trade. Enterprises are inevitably exposed to international commercial laws and regulations when engaging in international trade and business.

Corporate compliance has been implemented in Europe and the United States for over half a century and introduced in China for over a decade [1]. Corporate compliance means that corporate behaviour should align with laws and regulations, industry rules, external regulatory requirements and business ethics. International commercial law is a general term for legal norms that adjust international commercial relations, and its primary sources are international treaties, international commercial practices and domestic commercial law [2]. Understanding international commercial law is a precondition for enterprises to conduct compliance operations. It also plays a vital role in promoting the international development of enterprises.

This paper discussed the obligations and potential risks in international trade from the perspective of the Chinese electric guitar industry. Regarding obligation fulfilment, I discussed the obligations of product quality and product liability that enterprises must fulfil. Besides, I applied knowledge of international treaties and international commercial practices to provide the electric guitar enterprises with some suggestions. Regarding risk avoidance, I have analysed the potential risks in the selection of the trading partner, the terms used in the contract of sale and the mode of payment. In addition, I discussed the risks involved in transporting goods and provided appropriate measures to avoid these risks.

## 2. Legal Obligations of Electric Guitar Enterprise

### 2.1. Compliance with Product Quality

Product quality is the key to business practices. The Law of the People's Republic of China on Product Quality (Product Quality Law) stipulates product quality responsibility and supervision. Moreover, Product Quality Law has a vital role in regulating the operation of electric guitar enterprises.

The product quality supervision and management system contain a product inspection management system, standardization management system and enterprise quality system certification system. In the standardization management system, the Standardization Law of the People's Republic of China formulates and implements product standards. As a musical instrument, electric guitar has an industry standard and its industry standards need to be enforced in production practice.

Recently, Epiphone, an internationally renowned electric guitar company, has been strongly condemned by consumers because the wood used in one of its electric guitars does not comply with the product description. The electric guitar featured a mahogany body and maple top as the product description, but the actual body and top materials were birch and olive wood, respectively. The internet has fermented the incident, and Chinese electric guitar consumers questioned and boycotted Epiphone. Therefore, the electric guitar enterprise must strictly abide by the responsibility of product quality and firmly hold the bottom line of product quality.

### 2.2. Compliance with Product Liability

Product liability is an essential area of tort law. The laws of most countries in both legal systems have regulated the product liability of producers. According to Restatement of the Law, Third, Torts by The American Law Institute, "One engaged in the business of selling or otherwise distributing products who sells or distributes a defective product is subject to liability for harm to persons or property caused by the defect." According to the Consumer Protection Act 198, if any damage is caused wholly or partly by a defect in a product, the producer shall be liable for the damage. In China, the Civil Code of the People's Republic of China, the Law of the People's Republic of China on Product Quality and the Law of the People's Republic of China on the Protection of Consumers' Rights and Interests help build the frame of the legal system of product liability.

China and many other countries choose strict liability as the principle of attribution in product liability legislation. This means that the manufacturer or seller should bear the responsibility as long as the product is defective. In the process of globalization, electric guitar enterprises need to understand

the regulations on product quality in different countries or regions. The enterprise should set strict production standards in their production practices and ensure that their products are fully controlled during the production process.

### **2.3. Respect of Intellectual Property Rights**

At the end of 1993, the Uruguay Round of General Agreement on Tariffs and Trade negotiations was concluded, and it gave birth to the agreement on Trade-Related Aspects of Intellectual Property Rights, or TRIPs. The agreement has a significant impact on international trade and plays an irreplaceable role in developing world intellectual property rights protection [3]. As one of the contracting parties to the agreement, China needs to comply with the obligations of TRIPs in its practice of international trade. Chinese electric guitar enterprises should pay attention to the specific scope of the general obligations of TRIPs while respecting and protecting intellectual property rights.

According to Trips, Article 1, Section 2, "For the purpose of this Agreement, the term 'intellectual property' refers to all categories of intellectual property that are the subject of Sections 1 through 7 of Part II". Among all the intellectual property mentioned in TRIPs, what electric guitar enterprises need to focus are trademarks and patents.

Trademarks are the key to distinguishing the goods and services of an enterprise from those of other enterprises, and they are an indispensable part of enterprise brand building. In recent years, many of China's well-known trademarks have been seized by foreign businessmen, and Chinese export enterprises have suffered a lot from this [4]. Electric guitar enterprises also need to pay attention to registering trademarks in international organizations to prevent trademarks from being maliciously seized.

A patent is the exclusive right of a right holder to the fruits of his intellectual labour. Concerning electric guitars, the one of the main categories of patents is electric guitar appearance patent. The body of electric guitar is the most intuitive feature of the electric guitar, and standard classic bodies such as Les Paul, Telecaster, flying V can be used for reference in the production of electric guitars because the patents have already expired or have not been applied for at all. However, there are often quite a few design patents for the electric guitar headstock. For example, the open-book headstock of the Gibson guitar [5] is not authorized for use by its subsidiary, Epiphone. For electric guitar enterprises, it is necessary to apply for some patents if they have advantageous product design and invention. This would significantly improve the competitiveness of the brand. Meanwhile, enterprises should also pay close attention to the patents of other brands in order to avoid the risk of infringement.

## **3. Risks in International Trade for Electric Guitar Enterprise**

### **3.1. Risks Arising from the Counterparty of Poor Credit**

In international trade, some subjects may maliciously escape from contractual obligations and engage in intentional fraud as a limited liability company [6]. They register the limited liability company with merger capital, obtain the parties' qualifications, sign a large contract, and defraud the other party, causing great economic losses to them. They will file for company bankruptcy if a large liability or damage is caused.

In order to avoid the risk caused by the severe asymmetry of information in cross-border transactions, enterprises should choose honest and reliable enterprises to cooperate. Before

cooperation, it is necessary to review the other party's situation and investigate the contract subject's performance ability.

There are three different scenarios where enterprises should conduct corresponding reviews. 1. If the other party is a natural person, the review should focus on whether the party has total capacity for civil behavior. 2. If the other party is a legal person, it is necessary to review its business registration. 3. If intermediaries and agents are involved, the exporter should first verify the agency rights of the intermediaries and pay attention to the creditworthiness assessment of the intermediaries.

When investigating the performance ability of the subject of the contract, the enterprise should understand the business situation of the other party from the total economic activities, such as the nature of the enterprise, the industry, the enterprise's location in the region, and whether there are traditions or special provisions on transactions [7].

### **3.2. Risks Arising from the Terms of Shipment**

When concluding a contract, the parties will choose the appropriate trade term by Incoterms. For the contract using FOB, the buyer generally designates the carrier. However, many buyers have recently committed fraud at the designated carrier's convenience. In that case, the carrier may deliver the goods to the designated consignee with no bill of lading, thus inveigling the seller to export goods. In that case, the seller will lose money and goods [8]. However, the FOB transaction stipulates that the buyer should designate the shipping company and pay the sea freight. However, in reality, the sellers would often help designate the shipping company upon the buyer's request. Therefore, the seller may need more shipping space and other reasons to complete the chartering and booking task.

Electric guitar enterprises should maintain sufficient vigilance when signing foreign trade contracts. Using the CFR or CIF terms is advisable so the enterprises can take control of the goods in the whole process. If foreign buyers propose FOB terms, enterprises should consider the risk of releasing goods without a bill of lading. Provided that the enterprises have to accept the FOB term, they should only accept the designated shipping company rather than the non-vessel operation carrier (NVOCC) as far as possible because the creditworthiness of the shipping company is better than that of the NVOCC [9]. For the FOB term, when the buyer entrusts the seller to charter and book on behalf of the seller, the buyer should be required to pay the subsequent freight charges if the buyer refuses to take delivery of the goods. At the same time, the seller should sign a proxy contract to avoid the risk of the buyer shirking its responsibility.

### **3.3. Risks Arising from Letter of Credit Payment**

As the one of the standard terms of payment in international trade, letters of credit (L/C) are widely used by importers and exporters. However, using L/C payment may contain potential risks for buyers and sellers.

According to Uniform Customs and Practice for Documentary Credits (UCP600), Article 34, "A bank assumes no liability or responsibility for the form, sufficiency, accuracy, genuineness, falsification or legal effect of any document, or for the general or particular conditions stipulated in a document or superimposed thereon". Fraudsters, however, are likely to commit fraud using the disclaimer on the effectiveness of documents [11]. The seller may have yet to complete the contract according to the buyer's requirements or even failed to fulfil the contract at all. However, as long as the seller can provide the bank with the documents required under

the L/C, the seller can obtain payment from the bank, which is exempted from liability on this principle. In this way, the buyer is likely to be left without the goods and the money. On the other hand, a buyer could commit fraud by forging a letter of credit, stealing a blank form letter of credit printed by another bank, or altering a letter of credit.

When purchasing commodities, electric guitar enterprises should make strict requirements and examination of the documents submitted by the seller so that the beneficiary is unlikely to forge documents and letters of credit. When selling products, enterprises should review the letter of credit and contract terms promptly and carefully.

### 3.4. Risks Arising from Carriage of Goods by Sea

Risks in the carriage of goods by sea are divided into maritime and external risks. Maritime risks include natural disasters and accidents. Natural disasters refer only to bad weather, lightning, floods, drift ice, earthquakes, tsunamis, and other irresistible human disasters; accidents mainly include major accidents with prominent marine characteristics. External risk refers to all kinds of risks other than the marine risk, which is divided into general external risk and particular external risk: general external risk refers to theft, breakage, leakage, defilement, moisture and heat, a cascade of flavor, rust, hook loss, short volume, freshwater rain, etc. Particular external risk mainly refers to the risk caused by military, political and administrative decrees and other reasons.

When importing overseas commodities, electric guitar enterprises should consider various maritime transport risks. At the same time, they should be clear about the various types of marine transport insurance and their liability to choose the appropriate cargo insurance and maintain their economic rights and interests in cross-border transactions.

## 4. Conclusion

Electric guitar enterprises should always have corporate compliance at heart. In production, they should pay attention to the quality and liability of the product. They should safeguard the legitimate rights and interests of consumers. In brand building, they must raise awareness of protecting intellectual property rights, especially trademarks and patents.

There are various risks in international trade. This paper summarizes the risks involved in four scenarios in international trade with the knowledge of international commercial law. In selecting a counterparty, the risk of fraud may be caused by the poor credit of the trading object. When

signing a sales contract, potential risks are due to improper shipping terms. When selecting a L/C as a term of payment, there may be a risk of L/C fraud. In transporting goods, there may be maritime and external risks.

Electric guitar enterprises should strictly abide by international practices in the era of rapid globalization and prosperous international trade. They should pay close attention to the quality and infringement of products in production and conduct business with corporate compliance. In the face of multiple challenges in international trade, they should avoid possible risks and use the means of insurance to transfer risks.

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