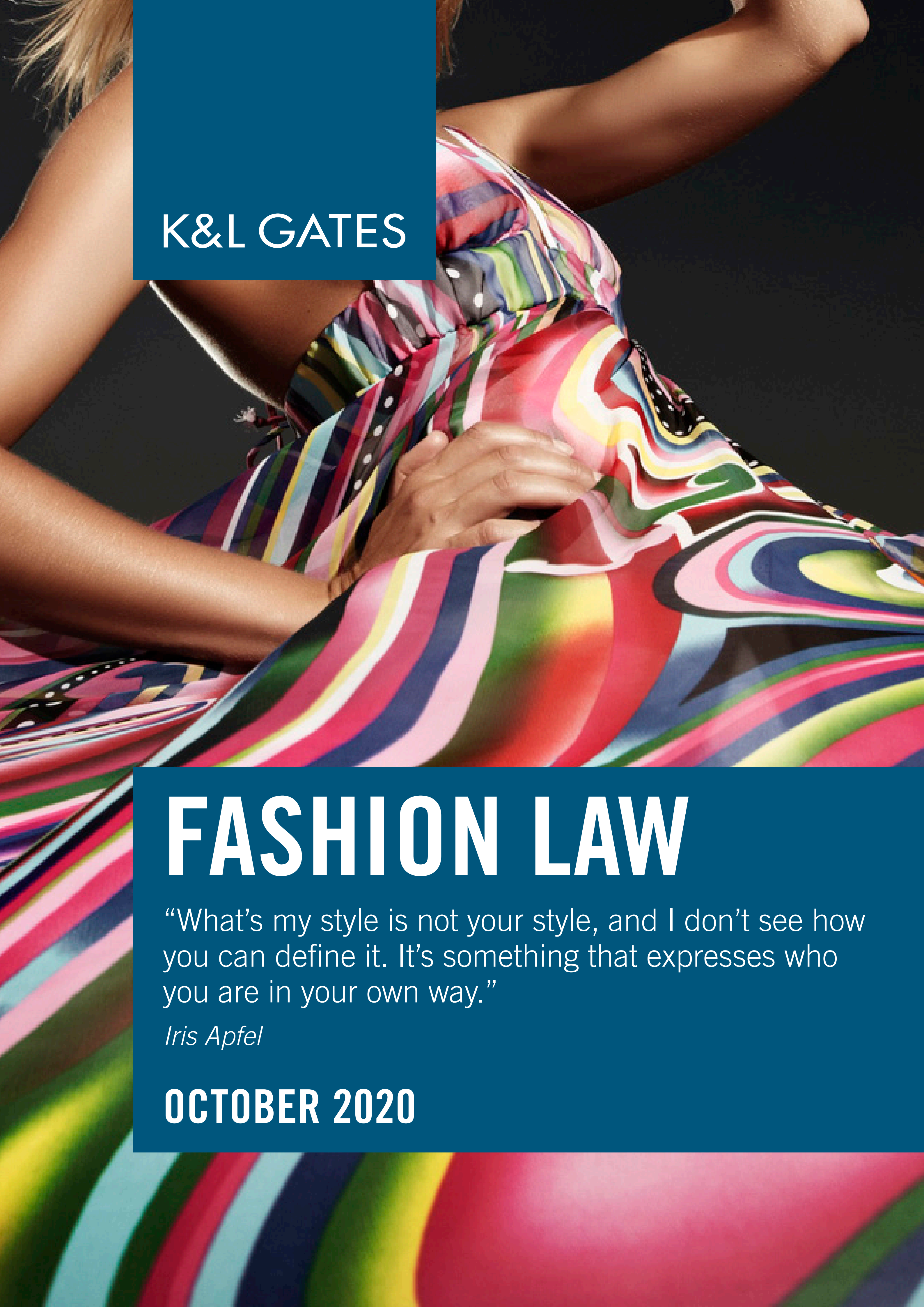

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FASHION LAW

"What's my style is not your style, and I don't see how you can define it. It's something that expresses who you are in your own way."

Iris Apfel

OCTOBER 2020

WELCOME

WELCOME TO A NEW EDITION OF FASHION LAW.

Even though the year is not yet finished, 2020 will be long remembered as a unique year that has presented many challenges for the retail, luxury goods, and fashion sectors. It is a time to reinvent, a time to connect and engage with consumers in new and genuine ways. Now more than ever, brands can start movements, earn trust, and survive and thrive.

A Business of Fashion and McKinsey annual executive survey found that 55 percent of respondents expected conditions in the fashion industry to worsen. Now the industry is on “red alert.”

According to a July 2020 survey of 800 people in the United States of America and the United Kingdom by personalisation platform Qubit, more than 40 percent of consumers plan to do more of their holiday shopping online this year. The significant shift to e-commerce is a real opportunity for fashion retailers. However, with this comes increased costs along the supply chain, and delivery and logistical challenges.

McKinsey’s *The State of Fashion 2020* report, updated in April 2020 with a special Coronavirus update, identified key themes crucial to reimagining the industry and how changes to the global economy and consumers’ behaviour will affect fashion in our post-Coronavirus world. These fit into three categories: the global economy, consumer shifts, and the fashion system, shown on page 4.

The pandemic has accelerated trends, including consumers’ heightened expectation for purpose-driven, sustainable action. The increasing importance on sustainability is a conversation that has framed fashion discussions for some time, and was the topic at the K&L Gates Fashion Law seminar during the 2019 Melbourne Fashion Festival. As consumers become aware of how and where manufacturing occurs, brands need to become more transparent with their customers.

This focus on corporate social responsibility continues to be a major trend in the *European apparel industry*. Consumers want to know how, where, and by whom their clothes are made. In fact, 37 percent of consumers in Germany, France, Italy, Spain, and the UK say that environmental impacts influence their choice when making purchases.

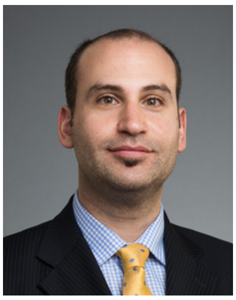
In addition, there is a focus on alternative materials and sustainable substitutes which are also key for ethical brands. This "material revolution" has led to companies filing nearly eight times as many fibre-innovation patent applications in 2019, compared to 2013.

Following in the footsteps of the United Kingdom, many Australian businesses will submit their Modern Slavery Statement in the coming year as part of the *Modern Slavery Act 2018* (Cth). In this edition, we provide an update about what this means for Australian companies.

In 2019, we saw iconic brands like Barneys New York, Forever 21 and Debenhams go into *voluntary administration*. The pandemic has accelerated this trend in 2020–with additional "main-stay" brands filing for bankruptcy such as Neiman Marcus, Brooks Brothers, Lord & Taylor, J. Crew, and Lucky Brand, among others. While some of these brands can be saved through restructuring, licensing deals, and investments, others have closed their doors leading to unemployment, empty storefronts, and an overflow of stock. We are seeing more brands saved from closing through venture capital and investment deals, securing employees positions.

Our Fashion Law publication is global with articles contributed by many of our offices covering many of the issues highlighted above, such as restructuring, supply chain, and protecting your brand.

We hope you find this edition insightful. If we can be of any assistance, no matter where you are in the world, please contact us.



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THE STATE OF FASHION 2020, CORONAVIRUS UPDATE

Global Economy

Survival Instincts

Recovery from the pandemic will coincide with a recessionary market, compelling fashion players to ramp up resilience planning and adapt their operating models. Companies surviving the immediate crisis will have made bold and rapid interventions to stabilise their core business before seeking out new markets, strategic opportunities, and future pockets of growth in a global fashion industry undergoing dramatic transformation.

Consumer Shifts

Discount Mindset

As deep discounting plagues retailers for the remainder of 2020, a decade-long build-up of bargain shopping culture will be exacerbated by a rise in anti-consumerism, a glut in inventory, and cash-strapped consumers looking to trade down or turn to off-price channels. To reach increasingly frugal and disillusioned consumers, brands must find inventive ways to regain value and rethink their broader business mission.

Digital Escalation

Social distancing has highlighted the importance of digital channels more than ever and lockdowns have elevated digital as an urgent priority across the entire value chain but, unless companies scale up and strengthen their digital capabilities in the recovery phase of the crisis, they will suffer in the longer term. Consumers will continue to demand more in this space and brands must act fast to deliver.

Sustainability First

The time for talk has ended. Brands need to take real and actual steps towards building a sustainable industry.

Fashion

Darwinian Shakeout

The crisis will shake out the weak, embolden the strong, and accelerate the decline of companies that were already struggling before the pandemic, leading to massive waves of consolidation, M&A activity, and insolvencies. To secure their future, companies must adapt to the new market environment by evaluating divestment and acquisition opportunities to strengthen their core and capture whitespaces that emerge from the reshuffle.

Innovation Imperative

To cope with new restrictions, mitigate the damaging impact of the pandemic, and adapt to economic and consumer shifts, companies must introduce new tools and strategies across the value chain to future-proof their business models. Fashion players must harness these innovations and scale up those that work in order to make radical and enduring changes to their organisations—and to the wider industry—after the dust settles.

The State of Fashion 2020, Coronavirus Update, April 2020, McKinsey & Company

IN THIS ISSUE

Subscribe to our global intellectual property (IP) blog 'IP Law Watch' at www.iplawwatch.com to learn about all IP related matters.

TOP TIPS FOR ACHIEVING A SUCCESSFUL RESTRUCTURING

By Alex Smith and Gayle Dickerson (KPMG)

The COVID-19 pandemic has driven a new reality for both fashion brands and the consumers they serve, with the changes being sharp and vast, and many of which will be permanent, such as the shift to online. Fashion brands have acutely felt the disruption to supply chains, retail stores, and delivery networks.

We have witnessed numerous well-known brands filing for insolvency or seeking to restructure their businesses, such as Brooks Brothers, Aldo, G-Star, and Lucky Brands. Many of these businesses were the most exposed when COVID-19 hit, due to pre-existing challenges, such as a high debt burden, under-performing store network, and lacklustre brands.

Whilst some retailers have accelerated growth in this new environment, particularly those with a strong online offering, fashion has been hardest hit due to COVID-19. The harsh reality is that the majority of fashion businesses will need to consider restructuring, in some form, to harness the opportunities of the new retail environment. The “post-pandemic” consumer has permanently shifted behaviour to being less brand conscious, less brand loyal, more value savvy, and buying more online.

In this article, restructuring partner Alex Smith teams up with retail restructuring expert Gayle Dickerson of KPMG, to consider the key factors in ensuring that a financial and operational restructuring succeed and that businesses put themselves in the best possible position to withstand the deep economic impacts of the global health crisis. Below are their top tips.

1. Early engagement with key stakeholders and funders

The stakeholders in any restructuring are likely to include shareholders, lenders, lessors, suppliers of goods, licensees of brands, logistics providers, manufacturers, key management, designers, employees, government agencies (taxation office) and, of course, customers.

A restructuring will stand a better prospect of success if the management team engage early with key stakeholders to sound out critical pillars of the restructuring, such as the willingness of lenders to continue to support the business (through standstill or forbearance arrangements, as necessary) and the terms on which suppliers are willing to continue to support the business.

2. Strategic planning with appropriately skilled advisers

Engaging advisers who have the right sector expertise and the ability to pull together a realistically achievable restructuring plan is vital and can be particularly effective in ensuring the credibility of the restructuring plan and in facilitating effective communications with key stakeholders. Whilst this comes at a cost when cash flow is no doubt tight, there should be an immediate return on investment if you work with the right adviser.

3. Operational streamlining and effective cost cutting

A restructuring will invariably require an element of identifying operational improvements and targeting how to use available capital most effectively. External, independent advice with these elements can be critical to ensure that management is appropriately challenged and tested as to which business processes could benefit from refinement. Cost cutting for its own sake without a holistic look at the business can lead to a downward spiral, for example, reckless cuts to marketing could slash sales.

Typically in a fashion business operational restructure, it is the one percent marginal gains that when combined lead to incremental improvements. Identification of assets (such as brands, inventory) that might be capable of being sold or monetised to generate additional funding may be critical in demonstrating to creditor groups how their exposure is to be reduced to an acceptable level.

4. Enabling agile reactions to market forces

In this new retail reality, fashion businesses will need to be agile to respond to an environment where there may be ongoing lock-downs for some time. This can be a particular challenge for brands and retailers with a lengthy delay from the planning, design, and manufacturing phase to product delivery. Brands already behind the curve risk being left high and dry during the transition from bricks and mortar to online.

Fashion brands need a laser-like focus on inventory management and merchandise planning, as well as working capital. The disruption and lack of trading in bricks and mortar stores will leave fashion retailers having to clear stock in a tough market or not having the right stock mix for the upcoming peak trading period in November and December.

A restructure or turnaround requires decisive and assertive leadership, sometimes based on imperfect information and a lack of time. At the leadership table, a strong, capable, and assertive financial controller or chief financial officer can make the difference between success and failure.

5. Identification of key financial and legal risks in process

Risks such as the loss of key contracts with counterparties will need to be assessed and acted on appropriately. Many global jurisdictions have made automatic contract termination rights unlawful, but this may need legal analysis on a case by case basis for the most critical of arrangements. A further important example may be the flexibility to stand down employees and make use of government sponsored reliefs, such as the JobKeeper allowances available in Australia.

In summary, a pragmatic, planned, and proactive response is required to rise to this business challenge. Many fashion business owners, especially the brand itself, can find it difficult to make the tough decisions needed early to successfully restructure their business. Any restructuring can be a bumpy ride, but early action, with the support of the right advisers to help work through the issues, can provide optionality, challenge old ways of thinking, and share the emotional burden of the journey.

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AS SUPPLY CHAINS REOPEN AFTER COVID-19, WHAT ARE THE RISKS?

By Tony Kerr and Chian Voen Wong

The Chinese government's decision to close factories in January 2020 was completely unexpected and took most companies by surprise. China, after all, was considered "the factory of the world," and the widespread business closures created a lot of confusion and anxiety for companies without alternative supply chains. With the rapid spread (and fear) of COVID-19 globally, business and public life have been totally disrupted.

The COVID-19 pandemic has changed the way that we live, work, communicate, and socialise. Borders have closed, along with factories and nonessential businesses; people are working from home while many others are on forced leave or have lost their jobs.

In this article, we focus on the customs and international trade implications and dangers facing global business in respect to fraud, direct and indirect tax evasion, corruption, and money laundering, which should be of particular concern during the COVID-19 pandemic. The rapidly evolving situation and increased pressures on certain supplies have given rise to opportunities, particularly arbitrage opportunities, as well as opportunistic actions. As the world slowly reopens for business (China has already started doing so, and many other jurisdictions are considering going back to work), we provide below cautionary reminders about core compliance responsibilities.

What we are seeing and hearing on the ground?

By all accounts, the global commercial environment will have changed substantially due to the COVID-19 pandemic. The business networks and relationships (partners and contacts) built up over years in various markets may no longer exist or may not exist in the pre-pandemic form. Workers who are fully trained in certain industries and operations may not return to work. Third-party service providers may no longer be in business, or, due to the implementation of regulatory measures taken during the pandemic, relationships between business partners and obligations between buyers and sellers may be stressed.

For example, as part of its effort to relieve the financial and supply burdens of its companies, the Chinese government has issued a record number of so-called "force majeure certificates" to allow companies to break contracts with local as well as foreign suppliers and buyers. Given the tight and urgent demands for medical supplies, companies are worried that some of these certificates may be granted to medical suppliers to allow them to only cater to local needs.

Unexpected events like the COVID-19 pandemic present an ideal climate for enterprising, if not necessarily unscrupulous, opportunists.

In late March 2020, as a result of complaints from the Netherlands, Turkey, Spain, and the United Kingdom and the return of faulty medical equipment and personal protective equipment products to suppliers in China, the Chinese government tightened rules governing the export of medical equipment in an attempt to address the concerns of those countries. It announced that only manufacturers who were accredited to sell their products within China could export test kits, surgical masks, protective gowns, ventilators, and infrared thermometers.

Since the rule change, China Customs has confiscated 11.2 million medical supplies from unaccredited manufacturers, according to customs data released on 5 April 2020. This included 9.9 million masks, 155,000 protective suits, and 1.08 million testing kits. Unfortunately, there are also recent reports of new "traders" and "suppliers" sprouting up in other countries offering such medical supplies to customers around the world.

During these trying times, companies are facing additional pressures and risks to supply chain and distribution networks. In a rush to procure materials or goods, or obtain needed services, internal procedures in assessing new third-party suppliers or service providers may be loosened. Companies may also face a variety of new regulations, including closer scrutiny of exports and imports, which could affect their operations and/or products. Authorities in various countries are also on the lookout for price gouging, commercial scams, low-quality goods, and corruption. Companies involved in cross-border trade must be on alert as brands and business reputations can be at risk.

What actions should businesses consider?

Evaluate regulatory change

To gain a better understanding of what is going on in your operations and identify risk areas, companies should actively review and evaluate regulatory changes in the various markets where they do business or trade.

- As government departments put out updates, law firms, consultancies, anti-corruption specialists, and export control specialists are producing and disseminating good overviews and in-depth analyses on various developments, much of which can be accessed free of charge. We suggest that companies designate at least one person to gather and disseminate such information.
- Where companies have a presence in different locations, local personnel are good sources of on-the-ground information. Companies should have effective internal communication channels so information can be shared from people on the ground to relevant business units, such as legal, logistics, supply chain, trade/customs, and purchasing/procurement departments.

Assess and realign trading priorities

Companies should take a step back, assess, and where necessary, realign their priorities to ensure continued success operating in the new international trading environment.

- It is important that companies draft and implement short term plans that take into account their current priorities and determine how to realign those priorities in order to fully support the reopening and continuation of their businesses.
- Businesses considering diversification of their global footprint or even divesting from a specific market should obtain proper advice before making any moves. In the current political and economic climate, countries have resorted to retaliatory "sabre rattling," urging companies to relocate back to home countries or pressing them to exit host countries. Exiting any market totally or partially must be well planned, and all potential risks (both short term and long term) must be fully evaluated. Otherwise, companies may find their assets and inventories confiscated or, even worse, be totally locked out from the market.

Maintain compliance programs

In a crisis such as the current pandemic, a company's critical compliance functions that would normally serve to mitigate risks can be severely tested and overwhelmed. Business should maintain their focus on all areas of compliance. Customs and trade due diligence, anti-corruption, and third-party due diligence are just a few essential areas.

- Despite lockdowns in many countries, the authorities responsible for investigating corruption and bribery have not stopped working. Many have, in fact, set goals of increasing their investigations and enforcement of anti-corruption and anti-bribery laws. Those in the supply chain, procurement, and customs/international trade community should be sensitive to and be vigilant against the potential surge in incidents of kickbacks, rebate arrangements, and suspect commissions; under-the-table payments to government officials and family members; and payments to third parties and individuals unrelated to the manufacturer or supplier. Revenue authorities will review invoicing and import/export documents to identify what may appear to be questionable payments to offshore third-party entities and unconventional invoicing techniques.
- For operations in key locations severely affected by the pandemic, companies may need to employ new staff or new service providers. It is important that a sound and robust hiring process and a third-party due diligence process be or continue to be in place.
- Worker safety, labour conditions, product quality, and consumer protection are all becoming major components of a sustainable business. For sourcing and purchasing, companies should consider having a trusted agent or employee on the ground in the sourcing country to review the manufacturing conditions and the quality and standard of products.
- The pandemic has created an ideal environment for the sale and supply of defective, contaminated, and second-hand or reused goods. Companies should be vigilant about unauthorised production of branded products, knock-offs, or products that are not appropriately audited or inspected for quality, safety, and labelling.

Evaluate new and existing suppliers

As part of supplier and third-party risk mitigation, we encourage companies to thoroughly scrutinise new and existing suppliers and analyse proposed business transactions. We suggest the following best practices:

- Collect as much information and documentation about the supplier(s) and verify that the supplier is duly qualified, in good standing, and that the individuals representing the supplier are properly authorised representatives.
- Request a copy of its business license, proper identification, and other relevant registrations and certifications.
- Where the third party is a supplier of services, such as customs brokers and logistics services providers, request copies of the qualifications of their employees that will be handling the work on behalf of your company.
- If you have a standard supplier or third-party questionnaire, make sure it is updated, relevant, and covers key matters such as:

  - background information
  - qualifications and required licenses
  - legal and regulatory compliance, including appropriate customs licenses and approvals
  - exporter/importer approval status, and
  - contractual obligations and considerations.

- Verify the information provided through online research on the supplier(s) and third parties as well as related individuals and entities. This should also include research on ownership, the significant owners, shareholders, and management, as well as any affiliated entities, agents, and consultants. Other information, such as credit history, financial health, adverse inspection findings, import alerts placed by any regulatory authority, and noncompliance incidents, is also important.
- It is important to conduct thorough due diligence to identify the level of risk of a proposed transaction. It will also identify potential red flags that could prevent the transaction from going through and provide an opportunity to consider possible legal or regulatory solutions.

Conclusion

Given the volatility of the current supply chain and customs environment, if you are considering undertaking a risk assessment of your current operational risks, please contact us. We will be happy to assist you with your local, regional, or global needs.

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"I WANNA REALLY REALLY REALLY WANNA…TAKE YOU TO COURT." VB TRADEMARK DISPUTE HEADS TO THE FEDERAL CIRCUIT COURT IN AUSTRALIA

By Keisha Phippen and Simon Casinader

Fashion mogul and former Spice Girl, Victoria Beckham lost the first round of a trademark battle with Australian skincare brand, VB Skinlab, in relation to two of VB Skinlab's pending Australian trademark applications for the "VB" brand filed in March 2018. A full copy of the decision can be found here.

The oppositions

VB Skinlab had applied to register the marks "VB SALON" and "VB SKINLAB" in order to market beauty salon services, skincare products, and cosmetics. The applications were opposed by Victoria Beckham, who claimed that the marks were likely to cause confusion with Victoria Beckham's own "VB" cosmetics collection amongst consumers. Although the VB mark was not registered in Australia, it was claimed that Victoria Beckham "extensively used and promoted the VB word mark in Australia and overseas in relation to various beauty and fashion related goods, including cosmetics."

Whilst the Hearing Officer acknowledged that Victoria Beckham has a distinguished reputation in her VB brand for fashion and accessories, the Hearing Officer concluded that this could not be extended to the cosmetics and skincare sector, particularly given the limited sales figures provided by Victoria Beckham's counsel in this regard.

Similarly, although there was evidence that Victoria Beckham had been using her "VB" mark in Australia since September 2016, it was held by the Hearing Officer that Victoria Beckham's use of the VB brand for cosmetics in Australia was relatively short and, as such, it had "acquired, at best, a very limited reputation."

Victoria Beckham also claimed that VB Skinlab's trademark applications had been made in bad faith. She contended that VB Skinlab's website featured a picture of "a slim brunette with long hair" similar to her own image and that its marketing (using the letters "VB") was purposely attempting to "deceive" consumers.

The Hearing Officer was "particularly unpersuaded" by the argument relating to the brunette woman and could not conclude that the decision of VB Skinlab to adopt and seek to register two marks containing the letters "VB" was a decision made to take advantage of the reputation of the VB mark.

Conclusion

Although Victoria Beckham lodged an appeal against the Australian Federal Circuit Court, which was due to be heard on 5 June, the case has now been settled after the parties reached an undisclosed agreement.

The VB Skinlab marks have since proceeded to registration and Victoria Beckham is pursuing registration of her VB Mark in Australia.

The case serves as a useful reminder that without registering a trademark, it cannot be assumed that a reputation (even the reputation of a particularly well-known individual, such as Victoria Beckham) can and will provide protection of a related trademark across any number of territories and sectors.

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AUSTRALIA: ADAPTING TO COVID-19 IN A TIMELY FASHION – ESSENTIAL COMPETITION AND CONSUMER LAW RULES

By Ayman Guirguis and Mei Gong

The retail industry has undoubtedly been one of the hardest hit by the COVID-19 pandemic. The fashion industry has been particularly vulnerable to the pandemic due to a number of factors, including weakened consumer spending, forced store closures, and drying government stimuli. A number of companies have also threatened store closures with the potential to impact hundreds of stores, workers, and shopping centre landlords.

While the ideal scenario would be for a quick and complete economic recovery, the reality of an extended economic slump suggests a more gloom reality. What does this all mean for your business?

This article seeks to provide an easy and accessible summary in Q&A format for fashion business owners, with key snapshots of competition and consumer law they should be aware of during COVID-19.

Why should you care about the rules?

Put simply, the law is not "on hold" even when there are extraordinary circumstances like the global health pandemic we are all facing. Maximum corporate penalties can be up to 10 percent of the business' annual turnover for the preceding 12 months of the contravening conduct. For cartel conduct, individuals could also face up to 10 years in jail.

"Business as Usual" activities during COVID-19

Although the Australian Competition and Consumer Commission (ACCC) is likely going to take a pragmatic enforcement approach during COVID-19 to not result in undue burden to businesses, their priority enforcement areas are likely to be the following:

- **Consumer guarantees** – It is important to note that consumer guarantees cannot be abrogated or excluded by contract. In particular, businesses should be aware of their obligation to comply with consumer guarantees relating to the supply of products/services within a reasonable time in the context of delay of supply orders due to COVID-19.
- **Misleading or deceptive conduct** – Businesses should be cognisant, particularly in the context of determining whether to allow for a refund, incorrectly representing consumer guarantees rights, and any other consumer contractual rights.
- **Unconscionable conduct and unfair contract terms** – The ACCC will prioritise enforcement efforts on any price-gouging behaviour. In particular, businesses should not artificially inflate the prices of essential products or enforce unfair contract terms against other suppliers.

a) Supply chain disruptions (read more HERE)

Q: I am worried about being able to fulfil consumer orders on time. What should I do?

COVID-19 has precipitated significant business disruptions, including uncertainty regarding product delivery timeframes due to unprecedented demand for certain products and logistics services.

Suppliers are expected to continue to uphold all consumer guarantees during COVID-19, including relevantly, providing goods “within a reasonable time” where a supply time period has not been set.

In light of the above, suppliers should carefully consider whether to accept consumer orders in circumstances where they are unsure that the relevant products will arrive on time.

Suppliers should clearly set out the potential for delay before the consumer finalises their order and where possible, stating the maximum delay period so that consumers can make an informed purchasing decision.

b) Opportunities for competitor collaborations (read more HERE)

Q: Can I collaborate with my competitors? If so, how?

Given the currently challenging and uncertain trading environment, some forms of industry collaboration may be desirable and necessary to help businesses adjust to the impacts of COVID-19. However, collaboration with competitors may breach Australian competition laws, either automatically (if they amount to cartel conduct) or if they result in a substantial lessening of competition.

Good intentions are no defence. Key risk areas for the fashion industry include where competitors:

- share resources, information, and/or knowledge about inventories, procurement, and logistics, or

- fix, control, or maintain prices, even where competitors agree to limit increasing their prices on goods or services.

There are a number of statutory exemptions/ defences which can make competitor collaboration legal, which include:

- **the joint venture defence to cartel conduct** (self-assessed, no application to the ACCC is needed) – key test is whether the joint venture is "reasonably necessary" for achieving the competitors' objectives.
- **applying for an application for Authorisation from the ACCC** – the ACCC has granted approximately 26 applications for Authorisation during COVID-19, approving competitor collaborations across the grocery, pharmaceutical, hospital, energy, telecommunication, and finance sectors.

  Of particular interest to fashion retailers are the Australian Retailers Association and the National Retailers Association (NRA)'s applications for Authorisation which relates to enabling their tenant members to share information and collectively negotiate with landlords regarding any COVID-19 related support to provide to their tenants (and in NRA's case, also vice versa for their landlord members).
- **class exemption** – the ACCC is currently considering two class exemptions, one for international ocean liners, and one to allow small businesses to collectively bargain with other larger businesses. Although any business that falls under a class exemption will be covered, there have been no class exemptions yet made and the formality associated with this process also makes it undesirable for supporting businesses who want to respond to COVID-19 impacts in a timely fashion.

Shifting business models

Q: My business model has been directly affected by government restrictions. What should I be aware of when shifting my business model to pursue other commercial opportunities in light of COVID-19? (Read more here)

While businesses are free to adapt and shift their business model to adjust to emerging commercial opportunities, they should always ensure that they are engaging in fair commercial practices.

Recently, some businesses have started to supply essential high demand products, such as face masks and hand sanitisers, even if they do not supply such products in the ordinary course of business.

While businesses can generally charge what they want based on supply and demand dynamics, businesses should be wary about setting excessive prices for essential products, particularly when the product is considered to be critical to the health or safety of vulnerable consumers.

Price gouging is not illegal in Australia. However, please note there was a national biosecurity determination by the Minister for Health in late March this year that prohibits price gouging on essential goods during the COVID-19 pandemic. Further, charging excessively high prices for essential products may be considered as misleading or deceptive conduct (if there are misrepresentations as to the reasons for any price increases) or unconscionable conduct (particularly if vulnerable/disadvantaged consumers are involved). The ACCC has a particular regulatory focus in this area during COVID-19.

For businesses who may want to shift their operations, either entirely or significantly to online platforms, they should be aware of complying with all of their existing ACL obligations in addition to any data/privacy considerations.

Options for struggling businesses

Q: Do I need the ACCC's approval if I am looking to sell my business?

There is no mandatory merger notification regime in Australia. Although the statutory test is whether the acquisition would substantially lessen competition in relevant markets in Australia, if the parties approach the ACCC for approval, the ACCC can take into account public benefits considerations, that is, whether the public benefits of the transaction outweighs public detriment. The ACCC has a set of merger guidelines to provide guidance to businesses for when they should approach the ACCC to assess a merger or acquisition and the considerations the ACCC will take into account (access the ACCC's merger guidelines here).

If you are looking to sell your business to a foreign purchaser, it may also need to be reviewed by the Foreign Investment Review Board (FIRB), who will as a matter of course, consult with the ACCC as a part of its consideration of whether the transaction is in Australia's national interest, with FIRB approval timelines extended to up to six months due to COVID-19 impacts.

One notional threshold the ACCC has included in its guidelines is that if post-merger, the merged entity's business share will be more than 20 percent in the relevant market, the parties are encouraged to approach the ACCC for merger assessment. It is important to note that even for businesses who proactively approach the ACCC for review, the majority of such transactions are assessed confidentially under the ACCC's pre-assessment regime rather than through the ACCC's public review process.

If businesses are considering making "failing firm" arguments to the ACCC, such as if they cannot sell to the purchaser, they will exit the market in any event, it is important to note that the ACCC will not accept such arguments easily, even in a depressed economic market. Rather, it will take into account longer term considerations of the impact of the merger on any change in the structure of the markets.

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ARE VALENTINO'S ROCKSTUD® SHOES AS DISTINCTIVE AS THE RED SOLES?

By Susan Kayser and Terrance Roberts

Has Valentino stepped up enough to show that their Rockstud® design has acquired distinctiveness similar to Christian Louboutin's red soles? In a recent response to a United States Patent and Trademark Office (USPTO) office action, Valentino asserted similar notoriety in its Rockstud® design as Louboutin's red soles.

Valentino applied for three different trademarks featuring the design of their Rockstud® shoes (U.S. App. Serial Nos. 88/672,186; 88/672/019; and 88/672,225). This design consists of a shoe with a single ankle strap, and T-strap and collar, which are adorned with pyramid shaped studs. The USPTO refused all three applications as non-distinctive product design and merely ornamental features.

Non-distinctive product design or features are not registrable as trademarks because they do not function as a trademark to indicate source. However, if a brand owner can show its product design acquired distinctiveness and the public associates the mark with a particular brand, then the mark can function as a trademark and be registered.

The three basic types of evidence to show acquired distinctiveness are 1) prior registrations of the mark on similar goods, 2) five years prior use of the mark, and 3) "other evidence," such as long term use of the mark, advertising expenses, declarations that assert recognition of the mark as a source indicator, survey evidence, market research, and consumer reaction studies.

In Valentino's initial application, they provided the second type of evidence – a declaration noting exclusive and continuous use of the mark for five consecutive years prior to the application. In response to a February 2020 refusal based on non-distinctive product design, and merely ornamental feature of the product, Valentino responded with arguments of acquired distinctiveness, and over 200 pages of "other evidence."

This other evidence included Valentino's long term use of the mark, including that these shoes have been a mainstay in stores for over a decade; millions invested in marketing and advertising the shoe; and its extreme profitability for the brand as its revenues doubled within five years since introducing the Rockstud shoes. Valentino also highlights that the Rockstud shoes have been featured on numerous celebrities, and have been the subject of extensive press and media coverage, making them well known to the purchasing public.

In addition to this evidence, Valentino also argues that if Christian Louboutin's red soles have acquired distinctiveness, so have their Rockstud® shoes. Valentino references the Second Circuit decision, *Christian Louboutin S.A. v. Yves Saint Laurent Am. Holdings, Inc.*, 696 F.3d 206, 226 (2d Cir. 2012), where the court held Christian Louboutin had demonstrated evidence that the purchasing public associated the red soles with Louboutin. The evidence provided by Louboutin consisted of "extensive evidence of Louboutin's advertising expenditures, media coverage, and sales success." Valentino then argues that due to the similar success of the Rockstud pump as compared to Louboutin, Valentino's mark has acquired distinctiveness and is similarly a signal to the consumer that the source is Valentino.

Valentino's play of stepping into another brand's shoes to help prove acquired distinctiveness in its iconic Rockstud® shoe paid off. This additional evidence appears to have been persuasive. All three applications have since been approved for publication, illustrating the importance of the types of evidence required to prove acquired distinctiveness for design marks.

Brand owners: keep your records of advertising expenditures, media coverage, sales success, and length of time the mark has been used as this is necessary evidence to prove up acquired distinctiveness in what may become not just an iconic design, but your exclusive brand identifier.

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ROLLING TOWARD BROADER COPYRIGHT PROTECTION IN THE EU – THE BROMPTON BICYCLE DECISION AND WHAT IT MEANS FOR FASHION

By Arthur Artinian and Simon Casinader

On 11 June 2020, the Court of Justice of the European Union (CJEU) handed down its decision in the referral from the Belgium Companies Court (Tribunal de l'entreprise de Liège) arising from copyright infringement proceedings by Brompton Bicycle Ltd (Brompton) against a Korean company Get2Get Chedech (Get2Get) relating to its folding bike (C-833/18).

The decision is good news for designers and creative businesses (including those in the fashion and luxury goods industry) as it lays a foundation for new opportunities for copyright protection and enforcement in Europe. The decision confirms that copyright can subsist in functional products. This evolving area of law now across Europe only requires a low threshold for protection, with a suggestion from the CJEU that minor creative choices in products will be sufficient for a finding of copyright protection. Merely because a garment, bag, or item of jewelry is protected by design or patent protection, does not inherently mean that it is not also protected by copyright.

While the decision is not novel in some European Union (EU) countries, it represents an important step in the harmonisation of copyright across the EU as a whole and will require some countries, like the UK, to closely review their copyright systems which have historically restricted protection for functional products.

Background

The UK company Brompton markets a folding bicycle, sold in its current form since 1987 (the Brompton Bicycle) and has been a staple of UK and EU consumers for many years (shown below):

Following the expiry of Brompton's patent for the Brompton Bicycle, Get2Get started selling similar folding bikes in Belgium. In response, Brompton sued Get2Get for copyright infringement. In its defence, Get2Get argued that the appearance of its bicycle is dictated by the technical solution sought, being so that the bicycle can fold into three different positions.

The Belgium Companies Court was not certain as to whether copyright subsists in shapes "necessary to obtain a technical result" so it referred the following questions to the CJEU for a preliminary ruling:

1. Must EU law, in particular Directive [2001/29] (the Information Society Directive), which determines, inter alia, the various exclusive rights conferred on copyright holders, in Articles 2 to 5 thereof, be interpreted as excluding from copyright protection works whose shape is necessary to achieve a technical result?
2. In order to assess whether a shape is necessary to achieve a technical result, must account be taken of the following criteria:
    a. The existence of other possible shapes which allow the same technical result to be achieved?

b. The effectiveness of the shape in achieving that result?

c. The intention of the alleged infringer to achieve that result?

d. The existence of an earlier, now expired, patent on the process for achieving the technical result sought?

Answers to the questions referred

Ultimately, the CJEU held that copyright protection may arise for products whose shape is, at least in part, necessary to obtain a technical result, provided that the:

> "product is an original work resulting from intellectual creation, in that, through that shape, its author expresses his creative ability in an original manner by making free and creative choices in such a way that that shape reflects his personality."

In reaching its decision, the CJEU considered earlier case law, including the influential decision from late 2019 in *Cofemel* (C-683/17), whereby for an item to be original subject matter:

> *"it is both necessary and sufficient that the subject matter reflects the personality of its author, as an expression of his free and creative choices."*

The *Cofemel* decision dealt with the copyright G-Star's t-shirt and jeans designs. Additionally, the CJEU reiterated that copyright protection arises for the expressions of ideas and not the ideas themselves.

With respect to the proposed criteria put forward in the referral, the CJEU found that the existence of other possible shapes which allow the same technical result to be achieved is not decisive and may be considered, but the intention of the alleged infringer is entirely irrelevant. The other two criterion meanwhile could also be considered in so far as they make it possible to reveal what was considered in choosing the shape of the product concerned, however the existence of patent or other IP rights in the same product does not automatically preclude copyright protection. Designs may be protected both under design and copyright law and this is consistent with the different purposes of protection of these rights.

Accordingly, with respect to the Brompton Bicycle, it is now for the Belgium Companies Court to determine, taking account of all the relevant aspects of the case as they existed at the time the design was created:

1. Whether it is a "work," and
2. Whether its shape is exclusively dictated by technical considerations, rules, or other constraints, which have left no room for creative freedom.

Implications

Ultimately, the CJEU's decision builds on the line of EU case law in recent years and extends copyright protection to functional products across all EU member states. This protection was limited historically in countries such as the UK. Building on decisions such as *Cofemel*, it is apparent EU intellectual property rights are more likely to be considered independently and the mere fact that multiplicity of rights may arise is irrelevant provided that the specific eligibility requirements are met.

Accordingly, copyright protection does not lead to monopolisation of design products with technical features nor exclude protection under design law. Copyright is not awarded for the technical function but for the aesthetic elements resulting from the author's intellectual creation. Competitors may use the technical function (if this is not otherwise protected) as long as the impression of their work is sufficiently different from the original work.

Additionally, it is noteworthy that the CJEU declined the opportunity to follow the approached suggested by Advocate General Campos Sánchez-Bordon in the preliminary ruling that the original designer's intention could be a relevant consideration as they would have been seeking either to achieve an intellectual creation or to protect and commercialise a product. If the Advocate General's approach had been followed this could have bad news for Brompton and other EU designers, although the constraints of copyright protection for functional items remain clear.

Following this decision, it is important that design-led businesses consider the potential opportunities afforded by the prospects of dual protection both with respect to protection of rights and enforcement.

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PROTECTION OF STORE LAYOUT UNDER COPYRIGHT LAW: THE KIKO CASE

By Serena Totino and Georgina Rigg

The Italian Supreme Court decision on the KIKO case (*Cass. 780/2020*) is one of the most recent judgements made in the wake of the *Cofemel* decision (*case C-683/17*) and follows the UK Intellectual Property Enterprise Court decision in *Response Clothing* (see our previous blog post).

In this latest development, KIKO S.p.a, a well-known make-up store was able to secure copyright protection for its signature store layout, made of its open space entrance with digital screens, the white/black/pink/purple colour combination, the disco lighting effects, the size, proportions, materials, and position of furniture.

The *Cofemel* case

The *Cofemel* decision outlined that for copyright to subsist in a design the proprietor needs to demonstrate two key points:

1. that it is a "work" of "authorship," meaning that it is the intellectual creation of its author, and
2. that it is sufficiently original (and **not necessarily** a work with artistic or aesthetic merit).

This is a departure from previous Italian case law, as although Italian copyright law does not provide a set list of subject matter protected by copyright (unlike English law), the courts used to require a work to have some artistic value for copyright to subsist.

The KIKO case

KIKO claimed that Wycon S.p.a, also an Italian make-up chain, had infringed the copyright in KIKO's store layout. KIKO was successful in both the first instance and appeal, as the courts held that copyright subsisted in the KIKO store layout and that Wycon had infringed their copyright and acted against honest commercial practice.

Wycon filed an appeal to the Italian Supreme Court on the basis that the KIKO store layout could not be classified as a work of architecture, given that it was not incorporated into a building or a permanent info structure, and that each element of the layout should be considered as a design and, therefore, satisfy the additional requirement of artistic value under Italian law.

Wycon also claimed that given that the European Union Intellectual Property Office had previously denied trademark protection to the KIKO store layout due to lack of distinctive character, the same would translate into lack of originality from a copyright perspective.

However, the court partially upheld the decisions of the lower courts and found that the KIKO store layout should be classified as a work of architecture which results in interior designs being an original combination of elements able to adapt spaces to increase their usability. Hence, the court has confirmed that the requirement of a stable incorporation to buildings no longer applies to works of architecture.

In addition, the court stressed that multiple intellectual property rights can subsist on the same work, and failing to meet all requirements for protection under one of these rights does not imply that another right cannot be claimed. As such, KIKO's failure in registering its store layout as a European trademark did not preclude it from obtaining copyright protection.

Lastly, the KIKO decision provides an interesting point of view on unfair competition under European law (which can differ quite significantly under English law). The Court of Appeal of Milan will now have to consider the issue related to the behaviour of competitors, including choosing similar sale assistants' uniforms, comparable look and feel of single products, packaging, and bags as well as analogous marketing campaigns.

Comment

This decision will be welcomed by companies investing in their store layouts as part of their brand identity and it will give other companies greater comfort to do so by developing a creative and consistent look of their stores to apply worldwide and possibly protect as a trademark, design, and copyrighted work.

We believe that items that could have previously failed to have copyright protection may now qualify and, as a result, companies may have a greater ability to enforce their rights against infringers. This is of great importance, given that with increasing online sales, brands wish to provide customers with unique experiences in store.

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SHOW ME THE MONEY: U.S. SUPREME COURT RULES THAT TRADEMARK INFRINGERS MAY DISGORGE PROFITS EVEN IF THE LAW WAS NOT WILLFULLY VIOLATED

By Alexis Crawford Douglas, Anisha Mehta and Brittany Kaplan

The U.S. Supreme Court confirmed that brand owners are not required to prove willful intent before obtaining a defendant's lost profits. On 23 April 2020, the Supreme Court resolved a longstanding circuit split and unanimously held that trademark infringers may have to hand over their profits even if they did not willfully infringe.

In *Romag Fasteners, Inc. v. Fossil Group, Inc.*, the Supreme Court was tasked with determining whether the rule that a plaintiff can win a profit remedy only after showing a defendant willfully infringed its trademark can be reconciled with the statute's plain language. Ultimately, the Supreme Court sided with the plaintiffs, Romag Fasteners (Romag), holding that:

> "[a] plaintiff in a trademark infringement suit is not required to show that a defendant willfully infringed the plaintiff's trademark as a precondition to a profits award."

Romag and defendant Fossil Group (Fossil) signed an agreement to use Romag's handbag fasteners in Fossil's leather goods. Later Romag discovered that factories in China, which Fossil hired to make its products, were using counterfeit Romag fasteners and Fossil was not working to curb the infringement. Romag sued Fossil, along with certain Fossil retailers, for trademark infringement pursuant to 15 U. S. C. § 1125(a). This provision establishes a cause of action for the false or misleading use of trademarks.

Although the jury found that Fossil acted "in callous disregard," the jury did not find Fossil acted willfully, as it was defined in the case. In deciding whether to award profits, the district court noted that controlling Second Circuit precedent requires a plaintiff seeking a profits award to prove that the defendant's violation was willful so it did not award Fossil's profits to Romag.

Fossil argued that courts have historically required a showing of willfulness before authorising a profits remedy in trademark disputes. The First, Second, Eighth, Ninth, Tenth, and D.C. Circuit all required willfulness. Meanwhile, the Third, Fourth, Fifth, Sixth, Seventh, and Eleventh Circuit allow for disgorgement of profits without willfulness. However, the Court pointed out that only the dilution section of the Lanham Act (§ 1117(a)) requires a showing of willfulness as a precondition to a profits award.

In this case, Romag alleged and a jury found Fossil violated § 1125(a) and engaged in trademark infringement and false representation, not dilution.

Although the Supreme Court noted that a trademark defendant's mental state is highly important in determining whether an award of profits is appropriate, it found that the text of § 1125(a) has never required a showing of willfulness as a precondition to win a defendant's profits award. The fact that other sections of the Lanham Act speak expressly about mental states, and the absence of any such language in § 1125(a), further supported the Supreme Court's finding in favor of Romag. The Supreme Court's decision was unanimous.

Moving forward, this decision will give intellectual property rights owners more support in enforcing against counterfeiters and infringers who disregard those owners' rights. While there may be a rise in frivolous trademark actions being brought with the potential for windfall judgments, it is more likely that this decision will incentivise companies and manufacturers to think twice and be more cognizant of potential counterfeit products being used in their businesses and global supply chains. Looks like it is indeed time to show brand owners the money.

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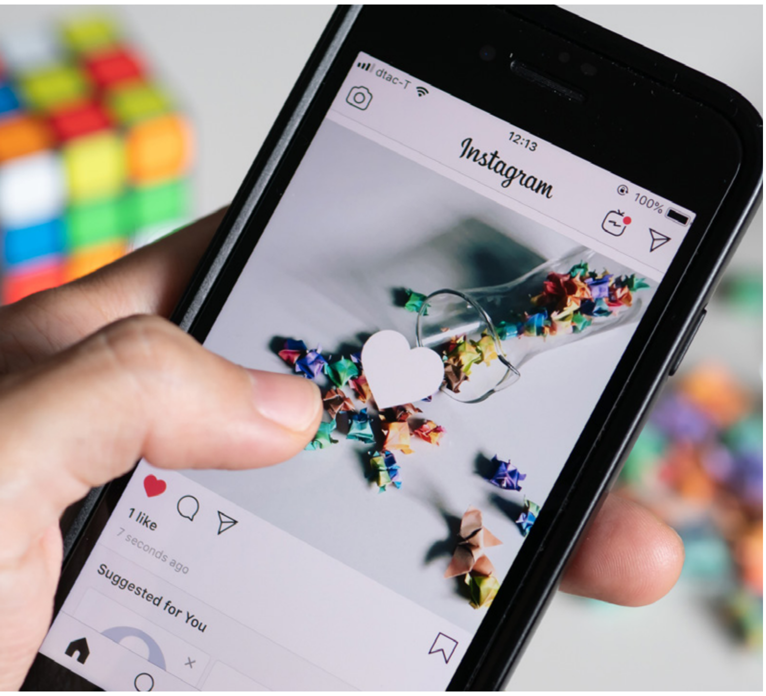
PHOTOGRAPHER'S CLAIM OF COPYRIGHT INFRINGEMENT OVER USE OF EMBEDDED INSTAGRAM PHOTO STILL ALIVE

By Susan Kayser and Terrance Roberts

User beware – you may be held to a social media platform's terms of use – or not. Most people are aware that by using a social media platform, they give up some rights to the content that they share. What rights and to what extent depends on the platform and the specific terms of use.

A district court in the *Sinclair* case in April 2020 found no copyright infringement by the website Mashable, where it used one of photographer Sinclair's Instagram photos in an article, even after an unsuccessful attempt to license the photo directly from Sinclair. *Sinclair v. Ziff Davis, LLC, and Mashable, Inc.*, No. 1:18-CV-00790 (S.D.N.Y. April 13, 2020). The April 2020 decision concluded that Instagram's terms granted Mashable a sublicense to use the application programming interface (API) to embed the photograph in its website.

That decision, however, was in conflict with other similar cases and upon Plaintiff's Motion for Reconsideration, the Court in *Sinclair* held in June 2020 that the pleadings were insufficient to show that Instagram granted Mashable a sublicense to embed Sinclair's photograph on its website. In order for a license to be valid, it must convey the licensor's "explicit consent" to use a copyrighted work. Given that Instagram's terms are not clear, the Court held dismissal of Plaintiff's case at this phase was not warranted.



Plaintiff Sinclair had a "public" Instagram account and posted a copy of the subject photograph. Defendant Mashable, a digital media and entertainment platform, published on its website an article about female photographers that embedded the publicly posted photo from Sinclair's Instagram account. Notably, prior to using the Instagram photo, an employee from Mashable contacted Sinclair about licensing the same photo to be used in the article. Sinclair declined Mashable's US$50 offer to license the use of the photo. Sinclair later demanded that Mashable remove the embedded photograph from their website and demanded compensation. Mashable refused. Sinclair then sued for copyright infringement.

Sinclair argued that Mashable infringed her copyright in the photo since it did not have permission to use the photo. Mashable contended that it had a valid sublicense from Instagram to use the photo and therefore did not infringe Sinclair's copyright. The court sided with Mashable.

By creating an Instagram account, Sinclair was bound to Instagram's Terms of Use, which grant Instagram the right to sublicense content that is posted and made public by the user. Instagram then exercised that right by granting Mashable a sublicense to display the photo through sharing the embedded photo. Instagram utilises API which allows users to share public content posted by other users.

The court held that Sinclair's right to license the photo directly and Instagram's right as a licensee to sublicense the photo to Mashable were independent from one another.

Sinclair also contended that the authorisation of Instagram to sublicense the photo was invalid because of the complex and interconnected documents which established the rights. While the court agreed that Instagram could make their terms of service and policies more concise and accessible, they were under no obligation to do so.

Lastly, Sinclair argued that it was unfair of Instagram to force a professional photographer to choose between keeping her work "private" on one of the most popular photo sharing apps or to post publicly which would allow Instagram a sublicense to her photographs to users like Mashable. While the court noted this dilemma was very real, the court held that Sinclair had already made her choice by opting to post the photo publicly.

The court also noted that because it held that Instagram had granted Mashable a valid license to display Sinclair's photo, it did not have to reach the question of unsettled law in the circuit of whether embedding an image is considered a 'display' capable of infringing a copyright in an image. That issue was addressed on a motion for summary judgment in *Goldman v. Breitbart News Network LLC et al.*, 1:17-CV-03144 (S.D.N.Y. February 15, 2018), where the court came to the exact opposite conclusion.

In the *Goldman* case, a different Judge in the same jurisdiction held that the use of embedded Tweets on news media websites featuring a picture of Tom Brady **did** infringe the copyright of the photographer. The decision for partial summary judgment in favor of the photographer in the *Goldman* case was highly criticised, and the case ultimately settled outside of court.

In a June 2020 decision in *McGucken v. Newsweek LLC*, the Court denied a Motion to Dismiss, where the defendant Newsweek was also relying on Instagram's sublicense to use the API to embed the Plaintiff's Photograph on their website. *McGucken v. Newsweek LLC* 19-CV-9617, 2020 WL 2836427, at *4–5 (S.D.N.Y. June 1, 2020). The Court in *McGucken* held that while Instagram's Terms could be interpreted to grant a valid sublicense, they **do not expressly grant** a sublicense. Given the limited review at the Motion to Dismiss phase, the Court could not find Newsweek acted pursuant to a sublicense from Instagram.

Jury is still out on whether use of a public Instagram photo as embedded in an article on a third-party website is covered by Instagram's Terms of Use. Nor should anyone assume that Instagram's terms grant a blank check regarding the use of publicly posted content.

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WHAT IS THE ITALIAN HISTORICAL TRADEMARK?

By Serena Totino

We increasingly hear about "brand value" along with figures and suggested strategies to assist brands in difficult times.

In Italy, new provisions have been approved to recognise the value of the so called historical trademarks (ie. *marchio storico*). To be clear, these provisions are not related to COVID-19 economic measures aiming to boost the Italian economy. They have been in the agenda for quite some time with the aim of promoting the Made in Italy and increase the value of Italian brands abroad. However, they can be considered as additional measures available to companies in such challenging times.

How does it work?

The Italian "Growth Bill" published on 7 April 2020 defines the application rules of the historical trademark. Specifically, it states that a new trademark register will be established in Italy. Applications were opened on 16 April 2020 and access to the register is reserved to historical trademark owners and exclusive licensees who own a registered (and timely renewed) trademark with the Italy IP Office (ie. Ufficio Italiano Brevetti e Marchi (UIBM)) for at least 50 years or an unregistered mark if evidence of uninterrupted use of the mark for 50 years can be provided.

Applications must be submitted online through the UIBM website and are subject to a small fee. The UIBM will have 60 days to examine the application of registered marks and 180 days for unregistered marks. The duration of the historical mark is not subject to a time limit or renewals. A searchable database has also been created to allow the public to access information about historical marks.

Specific procedures are provided in case applications are made by licensees instead of owners. Moreover, informative obligations to the Italian Ministry of Economic Development are due by owners of historical trademarks in case of business crisis, involving, for instance, shutting down the original or a main production site, in order to safeguard employment levels and the continuation of production activities in Italy.

Although the historical trademark does not establish a new IP right, the owners of such mark will be able to use the below logo in their transactions and marketing material.

Background

The introduction of the historical trademark has been originally identified as a tool to prevent Italian brands from moving their main production site outside of Italy. A controversial issue that was lately brought to the public attention when the well-known chocolate brand PERNIGOTTI planned to move their production outside Italy after the acquisition of the brand by Sanset Food, part of the Toksöz Group, a Turkish company.

A new law was therefore needed to safeguard the Made in Italy and avoid that the owners of brands immediately associated with the "Bel Paese" would cut jobs in Italy to save on production and human costs, while still taking advantage of the Italian heritage of their products. A measure to discourage the so-called "Italian Sounding" products for the benefit of consumers around the world.

Conclusions

The historical trademark appears to be an innovative measure to assist Italian brands in their marketing strategy and, on the other hand, it gives consumers one more tool to address their trust towards a genuine Made in Italy.

From an international perspective, we wonder if such trademarks will be considered as valuable evidence of reputation outside of Italy and if other measures may follow to what may be a first step towards an enhanced protection of the Italian creative industry in the world.

For more information, click here:

Italian Ministry of Economic Development, Official Gazette, Decree 10 January 2020

Italian Ministry of Economic Development, Official Gazette, Decree 27 February 2020

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TRANSFER PRICING ROUSING CUSTOMS AUTHORITIES TO ACTION

By Tony Kerr, Chian Voen Wong and Cecil Leong

As the world slowly emerges from the COVID-19 pandemic, companies are busy grappling with the huge disruption to global manufacturing and supply chains, the permanent closure of some businesses, the downsizing, consolidation, or divestment of other operations, and the retrenchments or displacement of workers. While most focus on measures governments are taking to support businesses and workers, very little attention is paid to how governments will be paying for such financial assistance programs.

Below we focus on several countries' customs authority, specifically considering concerns in regard to transfer pricing and related party transactions, and the actions businesses can take to mitigate exposures.

The primary revenue source for governments are through direct (individual income tax and corporate tax) and indirect taxes (import/export duties, VAT/GST/sales tax, and excise duties) which are collected by the customs authority (indirect taxes) and the tax authority (direct tax). In the current economic environment, even though there is a drastic drop in revenue collection due to the huge disruption to trade and business activities, these two revenue authorities would still need to meet their annual revenue collection targets. In other words, the authorities would need to ensure that the revenue collected is correct and where possible, seek to collect additional revenue through other means provided under the law, such as fines and penalties for offences. We note that penalties can be as high as 10 times the revenue short-paid, and managers responsible for the customs compliance function or their managers may face jail time.

Given the revenue shortfalls, it is no surprise that these two revenue authorities are increasing their post-import audits, investigations, and requests for more documentation. These audits and investigations are normal "tools" the customs and tax authorities use to verify the accuracy, completeness, and authenticity of revenue declarations made to them by businesses. These actions are usually taken post-clearance (in the case of customs) or post-reporting/filing (in the case of tax). In Asia, the customs authorities in China, Korea, Thailand, and India are most active in conducting audits and investigations into cross-border trade in goods. Korea has been conducting free trade agreement country of origin verifications, while China is focusing on customs valuation and transfer pricing, particularly in relation to royalties and management fees.

During a customs audit or investigation, the customs authority will likely speak directly with a company's finance/accounting personnel, particularly in regard to transfer pricing. Based on past customs audit/investigation experience, we found that most finance/accounting personnel usually understand transfer pricing from a direct tax perspective but do not appreciate its relevance from a customs valuation perspective. In other words, most companies' transfer pricing policies do not take customs valuation rules into account. In case of customs audit or investigation, the company's customs and supply chain personnel will be placed in a vulnerable position as they would not be able to explain the company's transfer pricing policy to the customs authority; the finance/accounting personnel will also not be able to respond satisfactorily to Customs. This is a situation in which the company may not have any choice as it will be customs who are the primary drivers, and they will expect that the accounting and finance personnel will not have a great deal of knowledge on customs valuation. Thus, we recommend that key transfer pricing personnel should ensure that they understand customs valuation rules, or better yet, the transfer pricing team should involve customs and supply chain personnel at the time of setting transfer prices and adjusting those prices.

Accounting for related-party transactions

The following are some examples of how some countries in Asia have amended their operations, laws, and processes to ensure that the revenue being collected is in fact accurate and complete.

Thailand

A key area of focus for the Royal Thai Customs Department when carrying out post-clearance audits has been related party transactions.

In November 2019, the Revenue Department of Thailand released the Notification of the Director General of the Revenue Department on the Official Transfer Pricing Form (Disclosure Form). Companies trading with related parties must complete and submit the form. The Disclosure Form applies to taxpayers who have related party transactions, with total annual operating revenues of THB฿200 million or higher, and have an accounting period starting from 1 January 2019 onwards.

The disclosure to the Revenue Department of Thailand of intra-company payments such as royalties, license fees, technical service fees, commissions, and management fees will be made available to the Royal Thai Customs Department. The Customs Department can then use information provided in the disclosure to determine whether such inter-company payments meet the conditions prescribed under the customs regulation for inclusion into the customs value of imports.

Besides the information obtained from the new Disclosure Form, the Customs Department also receives from the Revenue Department, the withholding tax returns (Form P.N.D. 54) and the self-assessment VAT returns (Form P.P.36). This information, when combined with the information already provided to customs by importers and their third-parties, provides substantive insight into a company's operations.

We note that the Thai Customs Act rewards customs officers for uncovering certain offences. Currently, the total award is 40 per cent of duty shortfall plus fines (comprising 20 per cent incentive payment and 20 per cent reward). The reward and incentive payments are separately capped at THB฿5 million (approximately US$158,000). Thus, Thai customs officers have a huge incentive to audit or investigate companies for customs offences. Based on our successful work assisting clients in dealing with Thai Customs' audits/investigations, we fully appreciate Thai customs' capacity and tenacity in this regard. We suggest that importers in Thailand conduct regular due diligence on their import activities and bonded operations. Otherwise, a duty evasion offence under Section 243 of the Customs Act B.E. 2560 (2017) would attract a maximum imprisonment not exceeding 10 years and/or a penalty ranging between 50 to 400 per cent of customs duty shortfall.

Taiwan

In November 2019, Taiwan introduced new rules on the management of Transfer Pricing Adjustments (Tax Ruling No. 10804629000). The new rules apply to the handling of retroactive one-time transfer pricing adjustments.

Coinciding with the new Tax Ruling, the Taiwan Customs Administration released "Guidelines on assessing one-time transfer pricing adjustment to determine the dutiable value" ("Guidelines"). The Guidelines are designed to assist companies which have imported or are importing goods from related parties and would like to adopt the Tax Ruling.

According to the Guidelines, at the time of goods importation, the importer should declare a provisional customs value using a pro-forma invoice, provide a customs value declaration form, and apply for release of their goods upon the payment of a deposit. On the import declaration form, the importer must indicate Code 136 (special relationship field) and Code 65 (payment method as duty estimate); in the "Other declared items" field, indicate that the declared item(s) is/are subject to a one-time transfer pricing adjustment in the fiscal year.

Within one month after the end of the fiscal year, the importer must apply to the Customs Department for a final customs value assessment for all goods imported under provisional values.

Information sharing

With the implementation of many of the action items recommended in the Organisation for Economic Co-operation and Development (OECD) report on Base Erosion and Profit Shifting (BEPS), the Tax authorities can now access a substantially increased amount of information which companies operating in jurisdictions that have agreed to comply with OECD BEPS standards must provide. This includes information on a company's supply and value chains which may be detailed in country-by-country (CbC) reports. Although such information is specifically required by the Tax authority, it may be shared with its sister agency (customs) through a collaborative arrangement. Furthermore, there are increasing efforts by revenue authorities to cooperate on a cross-border basis. Jealously guarding information appears to be a thing of the past; now, the holistic or "single-window" approach has permeated revenue collection and enforcement efforts as well. With access to such detailed information, the customs authorities can more accurately profile companies for audit or investigation.

An example of this is the 4 March 2020 announcement by the Inland Revenue Department of Hong Kong that China and Hong Kong have entered into an arrangement for the automatic exchange of CbC reports. This exchange would be applied retrospectively to accounting periods beginning on or after 1 January 2018. While the sharing of CbC reports will benefit companies in regard to tax filings, it also means that such information will also be available to the tax authorities in China and Hong Kong. For many companies using Hong Kong as a transit, transhipment and/or re-invoicing hub for goods exported from China or destined for China, this would mean greater exposure to customs review, audit and/or investigation, including transfer pricing and customs valuation audits and investigations. This could be undertaken by either Hong Kong or China Customs or a combined audit/investigation. This trend can also be seen in other Asian jurisdictions, including India, Thailand, and Korea.

Additional considerations

Although we are highlighting customs valuation and transfer pricing concerns in this alert, businesses should also be aware of other changes that have already occurred or are being proposed by countries in Asia. These include new classifications of products, increases in import duty rates, drops in the value threshold for import duty exemption for goods imported via courier, closer monitoring, and possible non-acceptance of self-certified preferential origin claims.

Businesses need to examine their operations, agreements, arrangements, etc., especially intra-company transactions, to ensure that all their activities are fully compliant with the relevant laws and regulations. In particular, businesses need to ensure that the information provided to the revenue authorities is accurate, complete, and consistent, especially in respect to transfer pricing reports.

How we can help?

K&L Gates' customs and international trade team provides advice and assistance to companies in reviewing their current and past operations for customs and trade compliance. During this restricted travel phase, our team can remotely review all contracts, agreements, and arrangements, as well as conduct video interviews with key personnel.

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K&L GATES CROWNED LUXURY LAW FIRM OF THE YEAR 2020, LUXURY LAW AWARDS 2020

On 3 September 2020 in London, K&L Gates was recognised as "Luxury Law Firm of the Year" during a virtual edition of the Luxury Law Awards ceremony.

LUXURY LAW AWARDS
3 SEPTEMBER 2020
VIRTUAL EVENT

Organised in conjunction with the Luxury Law Summit, the Luxury Law Awards each year recognise the law firms, in-house legal teams, deals, individuals, and lifetime achievements required to guide a luxury business or brand to profitable success.

In selecting K&L Gates for the award, the judging panel commented:

> "K&L Gates has clocked up a number of successes in the luxury sector in a relatively short period of time and now represents some of the top names across the luxury industry – from fashion, design, beauty, accessories and architecture to travel, home and leisure. The judges were impressed with the firm's efforts to support the industry through initiatives with industry bodies, its stellar list of clients and its wide range of transactions for high profile clients."

K&L Gates' recognition acknowledges recent notable work by the firm's lawyers, including advising longstanding client Coty on a highly publicised US$600 million global licensing and collaboration deal with Kylie Jenner and a global collaboration with actress Lili Reinhart to be the new face of COVERGIRL.

The firm also advises iconic luxury fashion, retail, and e-commerce companies on their global IP, commercial, distribution, logistics, and regulatory issues, including leading brands from the U.S., UK, Italy, France, Germany, and Australia.

"We are delighted to receive this award, which is a testament to our firm's commitment to the luxury, fashion, and retail industries and the truly global work we undertake for our clients," said London partner Arthur Artinian. "K&L Gates is proud to partner with many of the leaders in these industries on cutting-edge legal and business issues globally."

To read more, go to:
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national and international designers, luxury fashion brands, clothing and footwear retailers, specialty retailers, boutiques, start-ups, and fashion outlets

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We have over 80 lawyers active in fashion and retail globally – meaning we can assist wherever you need it

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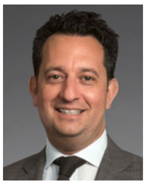

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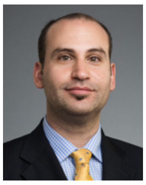

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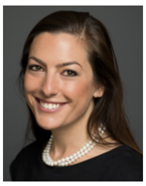

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