K&L GATES

FASHION LAW

"In order to be irreplaceable, one must always be different." — Coco Chanel

NOVEMBER 2017

WELCOME

Welcome to our latest edition of Fashion Law.

Fashion is a truly international business – from following the trends on international catwalks to the ability of consumers to shop the world's labels from the comfort of their couch, there is no doubting the global nature of this business.

From a fashion brand's perspective, there is also the international nature of the design and manufacturing process. Designs may be created in one country with the fabric sourced in another, before the garment is put together in yet another country and then shipped around the world for sale.

Customers' shopping data can provide critical insights to a business as to how consumers behave – from how much they spend and what styles they like, to how often they visit a website.

All of this creates a myriad of issues for businesses, many of which are considered in this edition. From paying duty at the border, the perils of not having your brand protected in the various jurisdictions in which you trade, the need to ensure compliance with the way you manage customer data, and ensuring correct labelling of garments, we have got you covered with tips in the articles that follow.

Also topical in Australia this year is the change to the penalty rates system. The fashion industry trades so heavily outside the (no longer) typical 9-5 Monday to Friday week so this has will have a huge impact. In this issue we set out the key dates and changes you should be aware of.

Even more critical to new businesses is the need to have sufficient capital to get up and running or to grow your business. There are now more options than ever before and our article on crowd-sourced funding provides another option you may not have previously considered and one which will soon be available in Australia.

We hope you enjoy reading this edition's articles and welcome your feedback.

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Subscribe to our global Intellectual Property (IP) blog '*IP Law Watch*' at iplawwatch.com to learn about all IP related matters.

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Savannah Hardingham

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In 2016 in New Zealand, fashion label Federation was found to have deliberately undervalued clothing it imported from China into New Zealand between December 2010 and February 2014. New Zealand Customs identified over 100 erroneous import entries submitted by Federation and found that Federation had undervalued its total imports by over NZD2.8 million and evaded Customs fees of NZD680,000. The directors of the defendant companies were held personally liable and one former director was fined NZD40,000 for her role in this conduct.

Similarly, in Australia it is an offence to provide false or misleading information to Customs that results in a loss of the amount of duty payable, and penalties will be imposed for such conduct. This includes providing inaccurate information as to the value of goods being imported, as the declared value is used to assess whether customs duty (and other costs) apply and, if so, calculate the amount payable. Customs duty is payable on imports of goods with a value of over AUD1,000. The declared value of the goods also impacts the quantum of further costs that are payable for the import, such as clearance fees, GST and other taxes.

It is also important for fashion businesses importing goods to be aware that, as the importer, they are liable to the Australian Government for any unpaid customs duties. This is the case even if the supplier (the exporter) has agreed to be liable for or attend to the payment of any duties. Unpaid import duties are treated as debt and Customs may demand payment of such amounts or sue for the recovery of the debt in Court.

In 2015 the CEO of Customs issued a demand to Australian fashion retailer Studio Fashion for the payment of duty and GST it had underpaid for the import of goods from a supplier in China. Under the arrangement between the parties, the Chinese supplier had undertaken to deliver the goods 'DDP', meaning 'delivery duty paid'. Studio Fashion argued that it should not have been required to pay the duty when the Chinese supplier had undertaken to deliver the goods with the applicable duties paid. However, the Administrative Appeals Tribunal held that while under the contract the Chinese supplier was liable to pay the duty, as the supplier had not in fact paid the duty, the goods continued to have duty imposed upon them when they entered the country and when the goods were delivered to Studio Fashion. As the importer, Studio Fashion was therefore liable to pay the duty.

These two cases highlight the importance of examining your business' obligations when it comes to importing fashion goods from overseas suppliers. While your fashion label may be experiencing rapid growth and it is desirable to focus on the creative aspects of your business, it is essential that you turn your eye to your legal obligations to avoid penalties and other consequences down the track.

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PENALTY GOAL

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As part of the Fair Work Commission's four yearly review of modern awards, various employers made applications to review the penalty rates payable under a number of awards in the retail and hospitality industries.

Relevantly for fashion brands and boutiques, this included changes to the penalty rates payable under the *General Retail Industry Award 2010* (**Retail Award**).

The Full Bench handed down its decision on 23 February 2017.

In considering whether changes were justified, the Full Bench noted that the traditional function of penalty rates was two-fold:

- firstly, they were intended to compensate employees for working outside of normal hours, and
- secondly, they were intended to deter employers from scheduling work outside of normal hours.

In the context of the Fair Work Act and the terms of the modern awards objectives, the Full Bench decided that the deterrence justification for the implementation of penalty rates was no longer relevant. Rather, the only consideration in setting penalty rates was to compensate employees for the inconvenience of working on weekends and public holidays.

In light of this conceptual shift, the Full Bench considered that Saturday penalty rates sufficiently met the modern awards objective, but that the Sunday and Public Holiday penalty rates did not.

The Full Bench decided to reduce the Sunday penalty rates, although not to the same level as Saturday penalty rates. It acknowledged that there was an additional inconvenience associated with working on a Sunday as opposed to a Saturday, but that this added inconvenience was not as high as it had been in the past.

The Full Bench also noted that the disutility of working on public holidays was greater than working on weekends, but considered that a proportionate reduction was necessary. It also noted that the inconvenience of working on public holidays had been somewhat reduced following the introduction of the statutory right to refuse to work public holidays on reasonable grounds.

The changes to penalty rates in Australia under the Retail Award vary between employees. For full-time and part time employees, Sunday penalty rates will drop from 200% to 150%. For casual employees, this will be from 200% to 175%. Meanwhile, public holiday rates will drop down from 250% to 225% for full-time and part-time employees, while casual employees will see their rates drop from 275% to 250%.

THE TRANSITION

The changes to public holiday rates have applied in full in Australia from since the start of the first full pay period following 1 July 2017.

The changes to Sunday penalty rates in the Retail Award also commenced on 1 July 2017, however they will be phased in over the next three years, with incremental decreases being applicable each year. Presently, full-time, part-time and casual employees are entitled to loading of 195% for hours worked on a Sunday. On 1 July 2018, this will decrease to 180% for full-time and part-time employees and to 185% for casual workers. These transitional arrangements will continue until rates reach 150% for full-time workers and 175% for casual workers from 1 July 2020.

Businesses whose employees are covered by the Retail Award will need to make adjustments to their employees' rates in accordance with these arrangements.

The Fair Work Commission's decision has been incredibly controversial, with all sides of politics weighing in heavily with their opinions.

Bill Shorten has promised that the Labor Party will fully restore Sunday penalty rates if it wins the next election. Labor had previously introduced a private members bill seeking to nullify the effect of the Fair Work Commission's decision, and prevent any future decisions from reducing penalty rates. The Bill was voted on and narrowly defeated 73-72 on 20 June 2017.

The political division regarding the penalty rates decision means that its future remains uncertain. Businesses affected by the decision should ensure that they stay abreast of any new developments.

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SUPPLY CHAIN GAME

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TRADE MARK PROTECTION

The first step is to consider which markets will be a part of your business' supply chain. You may want to source fabric from a supplier in the United States, buy leather from an agent in Italy and engage a manufacturer in China. Wherever you plan to conduct business, you should consider whether trade mark protection should be obtained prior to entering such markets.

Even if you do not intend to supply goods in those countries, it is essential to consider whether trade mark protection is required to operate in these countries. For example, if someone else registers your brand's trade mark in China (which has a first to file trade mark system) before you do, this can create issues in terms of being able to have goods manufactured within China.

New fashion businesses need to consider the markets that will be a part of your supply chain and the suppliers you will use.

While developing businesses may have limited budgets to allocate to intellectual property protection, Australian lawyers can register trade marks in numerous countries at once using the cost effective international "Madrid Protocol" system. Further, taking these steps early can avoid costly legal issues later, such as having to rebrand because you were unable to secure the necessary trade mark protection in all countries where your products are sold.

DUE DILIGENCE ON SUPPLIERS

Before agreeing to engage a supplier, it is essential that you conduct due diligence on that party. It is also prudent to ask for a certificate of incorporation.

If the supplier is a manufacturer, consider sending a staff member or agent to conduct an on-site visit to the factory. Visiting a potential manufacturer in person will help you to determine the integrity of the factory and its staff. A useful indicator will be the manufacturer's response when you ask to see examples of the factory's work in order to get an idea of the quality of the garments the factory produces and its capabilities. If the manufacturer only shows you examples of collections from prior years, then this is a good indication of the factory's integrity. However, if the manufacturer is willing to show you examples of new items

in development for upcoming collections and is open to you ordering copies of those garments, reconsider whether you want to engage that factory.

WRITTEN AGREEMENTS

Once you have decided on a supplier, it is important to ensure that your rights and their obligations are clearly documented in a written contract. A cost effective way to do this can be to engage a lawyer to create template agreements that you can use with other service or product suppliers in the future. It is important to always have an agreement in place, even if a long term business relationship exists, as you never know when a dispute or disagreement will arise.

Using the example of a manufacturer again, some key considerations for appropriate contracts include:

- Ensure that your business has the right to carry out inspections and audits while garments are under production.
- Set out key performance criteria to ensure that garments are consistently made to a quality standard.
- Clarify that your business, and not the manufacturer, owns the intellectual property comprised in the goods and whether the same products can be made for third parties.
- If moulds, patterns or software are provided to the manufacturer as part of the production process, ensure that the factory is required to return these articles at the end of the manufacturing process and clarify that your business owns the intellectual property in these items.
- Specify what the factory is to do with any overruns and excess product that is made including in the case of defects. Ensure that the factory cannot sell overruns to outside markets.

Putting the above considerations into action will help minimise the risks involved when engaging overseas suppliers.

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IS YOUR CUSTOMERS' INFORMATION IN SAFE HANDS?

Rob Pulham and Allison Wallace

With the popularity of online shopping growing daily and new laws coming into effect in Australia in early 2018, now is the time for those operating in retail to ask themselves – am I keeping my customers' information safe?

WHAT IS PERSONAL INFORMATION?

Under Australian privacy laws, personal information includes information or an opinion about an "identified" or "reasonably identifiable" person – for example, a customer's name, their address (both physical and email), phone number, gender, date of birth, employment details, and their credit card information.

This is the kind of information that is very useful to retailers, and the kind of information that is often collected when signing customers up for mailing lists, or when they place an order instore or online.

WHY SHOULD I KEEP IT SAFE?

A recent case involving a former employee of Showpo provides a timely example of why it's commercially important to keep customers' information safe.

One of Showpo's former graphic designers was accused of taking and passing on Showpo's customer database to her new employer, the rival online retailer Black Swallow, which then began sending promotional emails to the 306,000 customers on the list.

A New South Wales court ordered Black Swallow to pay Showpo AUD60,000. Arguably no amount of money could win back a customer disgruntled by the fact the information they trusted you with was leaked to another company.

If losing customers' trust isn't reason enough to keep their information safe, it's also worth considering whether your legal obligations require you to do so. These can arise under legislation, contract or the law of negligence. Under Australian privacy laws, organisations doing business in Australia with an annual turnover of more than AUD3 million are required to comply with the Australian Privacy Principles (**APPs**). The APPs require (with limited exceptions) that personal information is:

- only used for the purpose for which it was collected for (for example, to ship an order), and
- kept securely (and not stolen by departing employees!).

If your business breaches the APPs it could face significant fines, and it could even be required by the Office of the Australian Information Commissioner (**OAIC**) to take specific steps to correct its privacy practices.

From February 2018, it will become compulsory for businesses bound by the APPs to notify the OAIC and affected customers if they become aware of an "eligible data breach". This means that the OAIC and your customers must be notified if

there has been any unauthorised disclosure of their personal information that would be likely to result in serious harm to the affected individual. This won't be a pleasant experience for any affected business.

HOW CAN I KEEP IT SAFE?

Analysts, including Deloitte, have found that employees are one of the leading causes of data security issues in workplaces. While it's impossible to completely safeguard your business from rogue employees, there are measures you can take to ensure you are in the best position to protect customer information, prevent leaks, and respond adequately if they do occur. These include:

- educating yourself and staff about what information your business collects and holds about your customers, why it needs to be protected, and the risks associated with it being leaked
- putting in place privacy and confidentiality policies for staff to follow as part of their employment contracts
- ensuring your agreements with third parties who handle customer information on your behalf place appropriate obligations on those third parties to protect it, and to notify you of any issues
- ensuring customer information is stored on secure servers that can only be accessed by authorised individuals on a 'need to know' basis, and
- preparing and implementing a response plan to guide your actions in the event of a breach.

At the end of the day, your business may not have a legal obligation to keep customers' personal information safe – but if your customers expect you to do so, you could find your business in more trouble commercially than legally, if you break their trust.

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Crowdfunding has now been around for many years and platforms like Kickstarter and Pozible have been used to raise money for all kinds of kooky things. It is estimated that the global crowdfunding industry raised US$45 billion in 2015. So, what about companies using crowdfunding to raise capital for their businesses?

Australian law doesn't currently allow for 'crowd-sourced funding' (**CSF**), which is a type of crowdfunding by which companies raise equity. But that's all about to change, thanks to new federal laws set to take effect by early 2018. These changes will open the door for Australia's numerous fashion start-ups and small-to-medium sized labels to use CSF to fund growth, potentially taking these businesses into their next phase.

WHAT IS CSF?

With usual crowdfunding, you might 'pledge' to a campaign online for a musician to record an album and then, if the project gets off the ground, receive an album in return. CSF is similar, but instead it allows companies to raise funds and, in exchange for financial contributions, investors receive shares in the company (rather than a product or service).

Currently, proprietary companies can only issue shares to 50 non-employees before having to 'float' and become a public company. Also, to issue shares to the public, a formal disclosure document called a prospectus may be needed and the costs of preparing this document can make going public to raise equity unattractive to smaller businesses.

That is where CSF comes in. When the new CSF regime takes effect, companies will be able to use a licensed online crowdfunding platform to issue shares without having to go through the formalities of disclosure and financial reporting obligations that have ordinarily gone along with becoming a public company. Companies can create their own CSF campaign, get direct access to people who want to support their brand, and get as many investors as they can to invest smaller amounts in the company.

WHO CAN USE CSF?

The new laws will only allow for CSF fundraising by public unlisted companies with annual revenue and gross assets of less than AUD25 million. Here are just a few features of the new CSF regime:

- Proprietary companies will be able to convert to public unlisted companies in order to access CSF and its associated exemptions from ordinary disclosure and financial reporting requirements.
- Companies can raise a maximum of AUD5 million through CSF.
- Companies are not required to appoint an auditor or have audited financial reports until more than AUD1 million has been raised from CSF offers.
- A 'CSF offer document' must be prepared for a CSF offer, however, this will be much lighter than a formal prospectus.
- CSF investors can only invest AUD10,000 per company per year.

Crowd-sourced funding (CSF), is a type of crowdfunding for companies to raise equity.

WHAT'S NEXT FOR CSF?

As outlined above, under the new laws, CSF will only be available to unlisted public companies. However, the Australian Government announced a proposal to also allow *proprietary* companies to use CSF, which would further reduce cost and compliance burdens.

If these touted changes come to pass, there would be further requirements upon proprietary companies in order to be able to access CSF. Here are some to keep in mind, which would apply in addition to the requirements above:

- CSF will be available to proprietary companies that have at least two directors.
- Proprietary companies that have CSF shareholders will have to prepare annual financial and directors' reports in accordance with accounting standards.
- Proprietary companies that make a CSF offer will have to include details about the offer and CSF shareholders as part of their company registers.

CSF could become even more accessible in the future under the Government's new proposal for proprietary companies. It could be time to start thinking about whether CSF could be a component of your business' growth strategy. Why not chat to a lawyer about what is involved in order for your business to meet the requirements of the new scheme and benefit from CSF.

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ORIGIN-AL SIN

Jaimie Wolbers

It may be the case that you have never given much thought to the label on the inside of your shirt, beyond whether or not it provided the right size information or whether or not it was irritating the back of your neck. However, a label with the incorrect information can cause more than an irritated neck to clothing manufacturers and retailers.

As a general rule, businesses must remember that under the Australian Consumer Law (**ACL**), they cannot:

- make a false or misleading representation about a good, or
- engage in misleading or deceptive conduct.

Additionally the *Commerce Trade Descriptions Act 1905* (Cth) and the *Commerce (Trade Descriptions) Regulations 2016* (Cth), prescribe that imported textile products and clothing must contain a trade description which includes the name of the country in which the goods were made or produced and a true description of the goods in prominent and legible characters. This must be in the form of a label that is attached in a permanent and prominent position on the goods.

However, it can sometimes be tricky to convey accurate messages regarding an item's country of origin in a world of global supply chains, particularly when a label only offers a limited space to include brand, size and care information.

The consequences of including incorrect or misleading information on a label or in your product advertising can include significant fines, the inconvenience and expense of recalling and relabelling products, not to mention damage to your reputation for being found to have engaged in misleading or deceptive conduct.

GLOBALISED GARMENTS

Fortunately, section 255 of the ACL provides a number of rules that assist in ensuring country of origin representations are correct.

GROWN IN...

You may wish to identify where natural fibres like cotton, wool, or bamboo were grown if they comprise a significant component of your garments.

A representation that goods were "grown in" a particular country should only be made where:

a. each significant ingredient or significant component of the goods was grown in that country, and
b. all, or virtually all, processes involved in the production or manufacture of the goods happened in that country.

If the fibres are from mixed origins, or the supply chain changes through the course of production (perhaps due to changes in crop quality over a particular season) it might be best to steer clear of "grown in" country of origin claims unless you are prepared to update your labels to represent the true state of affairs relating to your products.

PRODUCT OF...

A representation that goods are a "product of" a particular country should only be made where:

a. the country was the country of origin of each significant ingredient or significant component of the goods, and

b. all, or virtually all, processes involved in the production or manufacture of the goods happened in that country.

In many respects "product of" representations are similar to "grown in" representations, although they can obviously extend to synthetic fibres and components.

MADE IN...

A representation that goods are "made in" a particular country should only be made where the goods were last substantially transformed in that country.

Goods can be considered to be "made in" a particular country if they meet the criteria to be considered "grown in" or a "product of" that country, or if, as a result of one or more processes, they are fundamentally different in identity, nature or essential character from all of the ingredients or components that were imported in order from them to be created.

The concept of "substantial transformation" requires more than merely finishing off or adding a decorative element to a product. For example, printing a design on a T-shirt in the United States would not be sufficient for it to be "substantially transformed" in the U.S. (presuming the shirt was imported from another country). However, importing leather from Italy and then cutting, sewing, constructing and finishing off a pair of shoes in Australia, could lead to a "made in Australia" representation as the final product, the shoes, are fundamentally different and have been "substantially transformed" from the imported component, the leather.

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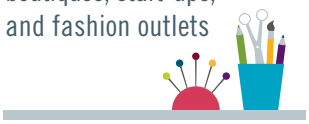

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We can help you **across all stages** of your company's lifecycle including establishing your business and e-commerce structures, protecting your brand and designs, and any employment and real estate needs

We have over 40 lawyers active in fashion and retail globally – meaning we can assist wherever you need it

We are passionate about fashion and have been recognised for our work in this space by being shortlisted as a **Luxury Law Firm of the Year (Luxury Law Summit 2017)**

For any questions relating to your company's needs, please contact **Lisa Egan** on +61 3 9205 2099 or lisa.egan@klgates.com


I love you more than Kanye
loved Kanye...

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