RETAIL INDUSTRY

YEAR IN REVIEW

2020

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HUNTON ANDREWS KURTH

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[HUNTON LAWYERS] ARE VERY PRACTICAL IN THEIR ADVICE AND HAVE A GOOD SENSE OF WHAT REGULATORS AND CONSUMERS REALLY CARE ABOUT.

"

– *Chambers USA*, 2020

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DEAR CLIENTS AND FRIENDS,

Needless to say, 2020 was a challenging and unprecedented year for businesses worldwide, particularly in the retail industry. As always, Hunton Andrews Kurth is committed to supporting our clients as we navigate these extraordinary times that have been marked with dramatic change and great uncertainty.

Our established retail and consumer products working group meets regularly to discuss developments and changes in the industry. This enables us to stay ahead of challenges and proactively advise our retail and consumer products clients across a broad spectrum of complex transactional, litigation and regulatory matters. In the past year, we welcomed 80 new retail and consumer products clients and we continue to grow and expand our services to meet changing client demands. We are proud to have been recognized by *Chambers USA* as one of the top retail groups in the country, which reflects our outstanding client service and our deep understanding of issues facing the retail industry.

Our *2020 Retail Industry Year in Review* summarizes many of the developments and obstacles that retailers faced in 2020, as well as forecasts and considerations for 2021. We closely examine innovations in technology around contactless payment systems, as well as workplace safety issues related to COVID-19 and vaccines. We also provide updates related to merger and acquisition activity, insurance coverage, The California Privacy Rights Act, Chapter 11 bankruptcy, PFAS-containing consumer products and much more.

I hope that our *2020 Retail Industry Year in Review* will be a valuable resource to help guide you through these uncertain times. Our retail team is always standing by to assist with any issues that arise or to answer any questions you have.

Wally

Wally Martinez

Managing Partner

THE CASHIER-LESS TECHNOLOGY REVOLUTION – ARE YOU PREPARED?

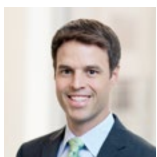
INTRODUCTION

Over the last few years, cashier-less checkout systems have flourished and found implementation in an array of environments, including stadiums, parks, grocery stores, convenience stores and other brick-and-mortar retail stores. The concept of eliminating a checkout process has gained traction not only due to a desire to improve customer experience by promoting swift movement, but also as a consequence of COVID-19. Indeed, cashier-less checkouts promise to shorten the time that customers spend in stores, thus reducing the probability of contact among shoppers.

The technology powering cashier-less checkout systems generally consists of two instruments. The first, which generally takes the form of either a dedicated smartphone application—like a mobile wallet or merchant app—or a credit, debit or prepaid card, functions as a ticket for entry and charges the customer upon their exit from the store. Second, cameras and sensors throughout the store track customers and the items with which they interact. Camera systems, sometimes powered by machine-learning software, anonymously identify customers, record which items a customer is picking up and add said items to the customer's virtual shopping cart. Simultaneously, weight sensors, placed either on shelves or in shopping carts, help ensure that the correct quantity of an item is recorded by the camera system.

While Amazon pioneered this industry with the opening of its first Amazon Go store in January 2018, other players have since joined the race. Sam's Club and Albertsons are piloting their own cashier-less technology across multiple grocery stores. Further, technology companies such as Zippin, Grabango, Standard Cognition and Trigo Vision seek to retrofit existing retailers with cashier-less checkout systems.

A revolution pertaining to the manner in which customers buy goods at brick-and-mortar stores is underway, as retailers seek to improve the shopping experience they provide to their customers. However, with this revolution comes new risks. There are a wide range of potential issues that retailers should consider before launching cashier-less checkout systems, several of which are discussed in more detail below.



Andrew Geyer and Florian Uffer

Andrew is a partner and Florian is an associate in the global technology, outsourcing and privacy practice in the firm's Richmond office.

CONTACTLESS RETAIL BEFORE AND AFTER COVID

During COVID-19 contactless payment methods have seen growth; these include tap-and-pay cards and devices, mobile wallets, QR code-based options and the use of applications to execute payments automatically, such as cashier-less checkout systems, like kiosk and geo-fencing checkout options.[1] The appeal of these technologies in a global pandemic is obvious. Public and shared surfaces, like touch screens, can be avoided and social distancing more easily accomplished using contactless payment options and cashier-less transactions.

Meanwhile, radio-frequency identification (RFID) technology and next-generation near-field communication (NFC) chip-enabled devices from tap-and-pay cards to wearables are poised for continued growth.[2] To date, these solutions have been deployed with much success in closed-loop systems such as amusement parks, entertainment venues and transit systems. However, as contactless payment options grow, enabled by the nearly-universal, worldwide adoption of mobile devices, NFC devices in particular are poised for adoption by customers who are increasingly growing accustomed to transacting in retail settings without cash, checks or physical cards (including in-store and cashier-less settings).

While the pandemic has propelled a number of contactless and digital payment technologies in the rush to meet the immediate challenges of COVID-19, we may only be seeing the tip of the iceberg in terms of what may prove to be a larger, unstoppable shift toward contactless and digital payment options that may finally transform the point of sale, both in-store and digitally. In the short term, retailers will want to facilitate contactless and digital payments to meet customer demand and have the most up-to-date information on emerging customer preferences and customer loyalty to trusted brand names in the contactless and digital payment space. Over the long term, we expect retailers to continue to look for innovative partners with the infrastructure to support the contactless and digital payment experiences of the future, perhaps eventually relying on customers' connected devices to act as the point of sale, breaking down one of the remaining dividing lines between brick-and-mortar retail and e-commerce.

How is something as mundane as the payment system at the core of fundamental shifts in customer attitudes and behavior and the dividing line between brick-and-mortar retail and e-commerce? Understanding the shifts occurring all around us may lie in appreciating the nature of

[1] Rooney, K. Contactless payments jump 40% as shoppers fear germs on cash and credit cards, MasterCard says. April 29, 2020. https://www.cnbc.com/2020/04/29/mastercard-sees-40percent-jump-in-contactless-payments-due-to-coronavirus.html Accessed December 2020. Walden, S. Banking After COVID-19: The Rise of Contactless Payments in the US June 12, 2020. https://www.forbes.com/advisor/banking/banking-after-covid-19-the-rise-of-contactless-payments-in-the-u-s/ Accessed December 2020.

[2] *Id*.

contactless and digital cards, the end point to which we believe this trend is barreling full steam. While credit, debit and prepaid cards continue to undergird payments, reliance on such physical cards is declining as they are increasingly being replaced by the deployment of a wide range of technologies, including mobile wallet and digital (such as retailer app) card options. A physical card is often used in e-commerce as a "card-not-present" transaction where the buyer has to provide the retailer the primary card account number (PAN) and the security code associated with the card in order to process a "card-not-present" transaction. The less often a physical card is used to carry out a payment (through a third-party mobile wallet or through a retailer's mobile app), and the more often a customer experiences a secure transaction without using a physical card, the more the deployment of contactless and digital payments seems logical, even inevitable, opening up a whole new range of possibilities related to contactless and digital payments and customer loyalty programs tied to checkout and payments.

Today, the types of digital cards commonly used are reloadable prepaid cards, credit cards and debit cards that are "loaded" into mobile wallets such as Apple Pay, Google Pay and Samsung Pay. The loading of physical cards into mobile wallets and retailer mobile apps has the advantage that such cards can be made available for use on a cardholder's mobile device almost instantaneously. In addition, they can provide more secure transactions because the retailer is never provided a full PAN during the transaction—rather, the full card PAN and security codes are "tokenized" in a way that uses low-value tokens to authorize and settle the transaction, with only the card networks (American Express, Discover, MasterCard or Visa) and the card-issuing bank ever seeing the full PAN and card security information.

For retailers looking to add contactless or digital payment options for their customer base, whether this be through the deployment of cashier-less technology that includes payment functionality or otherwise, the first step is for the retailer to have a discussion with its current payment card processor. Depending on the processor, the retailer may have optional contactless or digital payment options they can choose to activate. The retailer may have to complete an optional services addendum to its existing payment processing agreement for either contactless or digital payments, or may otherwise have to execute an additional addendum for merchant acceptance of third party mobile wallet payments. While there are a host of issues to be addressed in such new or expanded contract terms, four important items to address in such agreements are: (1) what the per-transaction fees will be for contactless and/or digital payments, which may depend on whether the card network considers the transaction a "card present" or a "card not present" transaction; (2) whether the retailer will still be able to get the necessary transaction activity and authorization information in order to successfully investigate customer chargeback claims process and proof of authorized transactions; (3) making sure the retailer is not asked to take on any additional transaction liability in addition to what the retailer already has for physical card or existing e-commerce transactions; and (4) ensuring the retailer still has full access to sales and transaction information equal to what it has in the physical card processing environment, such as transaction SKU information and other details for inventory management, customer loyalty and rewards programs, and all other uses the retailer currently has for such transaction information. These payment-specific contract concerns are part of the overall contracting considerations for cashier-less technology, but such cashier-less technologies should be interoperable with the retailer's existing payment processing framework to the extent possible.

Erin Fonte and Sharon Harrington

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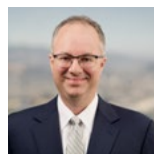
DISABLED CUSTOMERS – ACCESSIBILITY AND LITIGATION RISK CONSIDERATIONS

As retailers continue to develop and implement new types of customer-facing cashier-less technology, it is important for them to consider as early as possible whether and how disabled customers can access and use the technology. Some considerations seemingly are obvious regardless of the particular technology—if the technology conveys visual information (e.g., through a screen or smartphone), then in most situations audio should be available for disabled customers who cannot see it; if the technology conveys audio content (e.g., video clips or auditory prompts), then in most situations captions should be available for disabled customers who cannot hear it; if customer information is conveyed through keypads (particularly private information such as PIN numbers), then in most situations tactile features should be available for disabled customers who cannot view the keypad to enter the information without assistance or concern of disclosure; and controls should be within reach ranges so that disabled customers who use wheelchairs while accessing the technology can use them. Other considerations may depend on the particular cashier-less technology at issue. For example, cashier-less technology that is dependent upon using smartphones and mobile applications should ensure that any website or mobile app comply with WCAG 2.1 guidelines (or other current accessibility guidelines or legal standards). Cashier-less technology that is dependent on "smart shopping carts" should take into account the ability of a disabled customer with mobility impairments to carry, navigate and use the carts. And cashier-less technology such as self-checkout machines and kiosks that are used by disabled customers should ensure height, reach and other considerations detailed in ADA standards and US Department of Justice guidance, as applicable. Finally, the possibility that some accessibility considerations may not be apparent, or that accessibility guidelines or legal standards may change, makes negotiating strong warranty and indemnity provisions in contracts with third-party cashier-less technology providers essential.



M. Brett Burns

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CASHIER-LESS TECHNOLOGY AND PRODUCT WITHDRAWAL / RECALL

Cashier-less technology introduces an opportunity to provide more targeted and, therefore, more effective warnings to customers about recalled products in the near term. Ultimately, cashier-less technology also can be expected to shrink the amount of time between when the need for the recall is identified and the delivery of a warning that could help stop the sale of the recalled product until such time as it can be removed from the retail shelves and the supply chain.

Product recalls and withdrawals are conducted to minimize (if not prevent) a suspected hazardous product from reaching the customer and to warn customers of the hazard in a manner that prevents use or consumption. Getting a recalled product off the retail shelves and out of the supply chain before purchase is the most effective way to mitigate against risks associated with it. The next best option is to deliver effective notice to stop the sale and, if not, stop the use or consumption of the product or otherwise mitigate the risk of harm.

Recall campaigns generally rely on generalized messaging—e.g., through the Consumer Product Safety Commission (CPSC) websites, press releases, advertisements, posters, store signs—that asks customers to determine if they have purchased a recalled product. Because cashier-less checkout technology can track a customer's specific purchases, it has the potential to connect a specific recalled product to an actual purchaser and deliver targeted warnings to known purchasers.

In theory, cashier-less checkout technology also has the potential to instantly recognize when a customer removes a recalled product from the shelf or the store. Still in a budding phase, however, cashier-less checkout technology in beta stages may not yet deliver such instantaneous notifications. Accordingly, time delays may continue in connecting products removed from the shelf or the store to recall notices or customer invoices.

Any gap in time between a recall announcement and pulling product from the shelf presents some risk that recalled products could be sold in violation of federal laws such as the Food, Drug, and Cosmetic Act or the Consumer Product Safety Act. Time gaps may also increase products' liability risk for selling defective products, as harmed customers might cite the failure to timely stop sale or effectively warn of the danger in support of a liability claim. Until this delay can be eliminated, retailers should continue to focus "stop sale" efforts on removing product from the shelf as quickly as possible.

To the extent that cashier-less technology disrupts current stop sale measures, that risk may not be material if retailers can quickly remove affected product from the shelf or find another alternative to prevent product removal. Although it is a violation to sell recalled product, both the Food and Drug Administration and the CPSC work to achieve voluntary reporting and recall compliance. Accordingly, it is likely that either agency would assess a recall plan on the merits of its overall timeliness and effectiveness and credit the potential benefits of more targeted and effective warnings when sale cannot be stopped.

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Active with major organizations supporting the retail industry, including the Retail Industry Leaders Association, the National Retail Federation and the Women in Retail Leadership Circle

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"Cashier-less" often means "cashless" as well. Retailers should beware that a growing number of states and cities have adopted laws requiring retailers to accept cash payment on certain transactions. These rules are primarily directed at protecting the "unbanked" portion of our population. According to Federal Reserve data, approximately 22 percent of US households, representing about 55 million adults, were considered unbanked or underbanked in 2018. These terms mean that the affected households do not have ready access to payment means other than cash.

Under US Treasury Department guidance, federal law does not require that private businesses accept US currency or coin as payment. Retailers can adopt policies limiting payment methods to debit, credit or other electronic means, like Square, Venmo, PayPal or Apple Pay, unless limited by state or local law. However, galvanized by concerns that cashless businesses disadvantage communities with poor access to traditional banking systems, a national movement protecting customers' ability to pay in cash may be emerging.

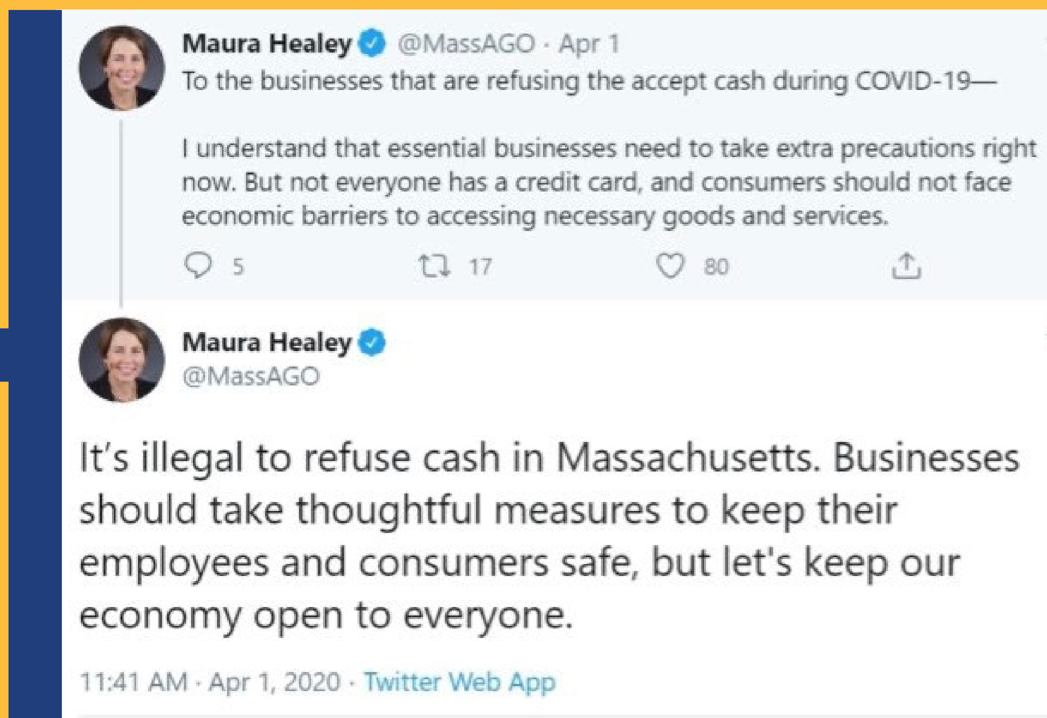
Before 2019, no city and only one state—Massachusetts—prohibited retailers from refusing cash. Now, however, at least 21 cities and states have adopted or are considering cashless retail bans. Massachusetts, Rhode Island, New Jersey and New York City have already enacted bans, and at least 10 states may be poised to follow. Berkeley, Philadelphia and San Francisco also prohibit retailers from refusing cash, and at least four other major cities are considering bans of their own. There are also cashless transaction bans in place in various municipalities across the country. How vigorously cities, states and municipalities enforce these laws, particularly during COVID-19, remains to be seen. On April 1, 2020, Massachusetts State Attorney General Maura Healey tweeted a warning to Bay State businesses—pandemic or no pandemic, it is still illegal for retailers to refuse to accept cash.

Although there is little evidence that these laws are routinely enforced, many carry substantial penalties for violation. New York City's law bans food and retail establishments from refusing cash or charging cash customers a higher price, but exempts online, mail and phone transactions. Businesses that violate the law face fines of up to $1,000 for the first violation and not more than $1,500 for each subsequent violation.

Before converting to a cashless model, retailers should confirm that local and state laws do not ban discrimination against cash payments. Because many cashless retail bans carve out internet, mail and phone transactions, businesses may be able to continue delivery and curbside pickup without violating the ban, so long as their in-store customers can pay with cash. Once a cashless policy is implemented, retailers should regularly monitor state and local legislatures for cash payment protection proposals, especially if they do business in a large number of jurisdictions.

Torsten Kracht

Torsten is a partner in the commercial litigation practice in the firm's Washington office.



> A FURTHER CLIENT SAYS: 'THEIR WORK PRODUCT IS OUTSTANDING.'
>
> – *Chambers USA*, 2020

PRIVACY

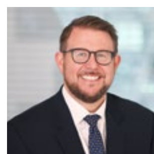
Along with the convenience and speed of cashier-less technology come important privacy and data security concerns. From the moment a customer enters into a retail location using the technology, their movements are tracked by cameras and sensors and their shopping habits are recorded and analyzed. While this information provides valuable insights, retailers must make sure to consider any guardrails that might need to be imposed on account of applicable privacy and data security laws.

In the cashier-less checkout context, of particular importance is providing transparency to customers regarding the retailer's use of the technology, both in the retailer's privacy policy and through in-store signage. This is especially important if the cameras and sensors are placed in areas of the store that are not conspicuous or obvious to the average customer. While notice is generally important in this context, it takes on added importance in California due to the newly enacted California Consumer Privacy Act (CCPA). Under the CCPA, businesses must provide notice to California customers "at or before the time of collection" of their personal information, which under the CCPA includes "products or services purchased, obtained, or considered." Retailers also will need to ensure that the data collected by the cashier-less technology is accounted for in response to requests from customers to exercise their rights under applicable privacy law. Under the CCPA, for example, California customers have the right to request access to, deletion of and opting out of the sale of their personal information (and they will have additional rights under the California Privacy Rights Act come January 2023).

In addition to providing notice and choice to customers, retailers should carefully consider their compliance obligations with respect to their use of any cashier-less technology that uses facial recognition technology. Three US state laws—in Illinois, Texas and Washington—impose stringent requirements on the collection, use, disclosure and protection of biometric information, which includes facial templates that are generated by facial recognition technology. Illinois's law in particular provides a private right of action, which has resulted in a flurry of class action litigation in the biometric privacy context. Facial recognition technology has increasingly come under regulatory scrutiny at both the federal and state levels, particularly with respect to the potential for discriminatory application of the technology. This is an area that will likely continue to attract media and regulatory attention in the future. Additionally, if the cashier-less technology cameras record audio, retailers will need to ensure compliance with applicable US federal and state eavesdropping laws, the violation of which can result in civil fines and even criminal penalties.

Data security also is an important consideration. Because cashier-less technology can lead to a significant expansion of the data that retailers already collect from customers, both through monitoring the customer's in-store actions and from the customer's phone (where an app is used), the greater the target such data will become in the eyes of bad actors. Retailers therefore should ensure that reasonable and appropriate data security measures are employed to protect the information that they collect through the cashier-less technology, some of which is particularly sensitive (e.g., biometric and payment card data).

Lastly, most retailers will use third-party vendors to facilitate the cashier-less technology in stores. As with all vendor contracts, retailers should consider appropriate data use restrictions, data security requirements and data protection law compliance obligations with respect to its cashier-less technology vendors. Because the customer insight data generated by such technology is so valuable, a retailer should limit its vendor's use and disclosure of such data to only perform services for the retailer. Retailers also should ensure that strong indemnification language is included in such agreements, particularly if the vendor will use facial recognition technology or artificial intelligence.



Aaron Simpson and Jenna Rode

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INSURANCE

While cashier-less checkout environments provide valuable insights (in addition to efficiencies), primarily due to the mountains of valuable data available to improve customers' shopping experiences, penetrate new markets, influence product choice and potentially attract new customers, they also raise a host of insurance coverage issues under a variety of coverage lines. As retailers increase the amount of personal and payment data that will be transmitted through phones and mobile devices and likely stored in cloud-based software platforms—as the scope of data held by retailers increases—new entry points for hackers emerge, thus increasing the risk of cyber breach events, misappropriation of data and a myriad of privacy vulnerabilities. This in turn increases the need for a robust cybersecurity, data breach and cyber liability insurance program. Specifically, users of cashier-less technology should ensure, at a minimum, (1) that comprehensive insurance coverage specifically tailored for risks associated with a cashier-less environment is in place; (2) that "legacy" insurance coverages preceding the implementation of a cashier-less environment are modified to address the new scope of risk and magnitude of exposure; and (3) that all insurance coverages specifically comport with heightened cybersecurity and data protection protocols that may be specific to a cashier-less environment.

Although retailers cannot fully eliminate the potential of cyber liability or error and omissions for cashier-less environments, comprehensive insurance coverage can provide robust protection when needed. Comprehensive insurance coverage should include coverage for cyber liability, such as data breaches, business interruption and extra expense, data restoration, social engineering and extortion, property damage, regulatory fines and penalties, and bodily injury for an alleged security vulnerability or privacy breach. Coverage for errors and omissions, such as negligence in professional service or technology, misrepresentation or errors in services provided, is also important. Careful review and scrutiny of policy language to confirm that definitions and coverage are broad enough to ensure that coverage extends to cashier-less technology are key.

But as with any coverage, it is not enough to protect against first-party risks; businesses utilizing a cashier-less environment also must ensure that appropriate coverage is in place for exposure related to third-party vendors on which the business relies for connectivity, software maintenance or upgrades, service patches and other critical services. In addition, while a comprehensive insurance program should address this exposure directly, retailers must understand how risk transfers under its third-party vendor and service agreements, including indemnification provisions and insurance requirements.

The trend toward a cashier-less retail environment is a welcome one, but it comes with some exposure to certain risks. A comprehensive insurance program can help mitigate these risks. Importantly, because cashier-less checkout is a new, unique area to the insurance market, retailers that venture into the cashier-less checkout environment should consult knowledgeable counsel to provide assistance in evaluating their business risk and to ensure they have or are getting the insurance protection they need.

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CONTRACTING CONSIDERATIONS

Retailers that decide to use cashier-less technology are likely going to be reliant on third-party vendors for at least a portion of their cashier-less checkout systems, whether they are developing all or a portion of their own technology or licensing it from a third party. The contracting considerations that arise in agreements for the procurement of cashier-less technology in many respects reflect the typical considerations associated with procuring and deploying any technology, such as technology use rights, implementation plans and costs, service levels and warranties, termination rights, indemnities and limitations of liability. The nature of the cashier-less technology and the relative newness of this technology, however, enhance the importance of some of these typical considerations and how they are handled contractually. Unlike certain technology that may enhance a retailer's ability to sell its products, cashier-less technology literally runs the cash registers of the retailer. Accordingly, in addition to some of the contractual considerations referenced in the other sections above, close attention needs to be paid to the liability provisions in the agreement. For example, is the cashier-less technology provider responsible for a retailer's damages due to technology outages or defects? And, even if the cashier-less technology provider is responsible, are there any limitations on this liability? Are lost revenue or lost profits expressly excluded from recovery? These important contractual considerations cannot be overlooked when the cash registers of a retailer are on the line.

Beyond damages arising from outages or defects in the technology, which party is responsible for loss prevention, including theft and fraud? Which party is responsible for the risk of bad debt (i.e., the lack of payment arising from use of the instrument used by a customer to enter the store)? Which party is responsible for security breaches of customer data that is processed or stored via the cashier-less technology? Which party is responsible for operating the technology in accordance with federal, state and local laws and regulations and for ensuring that the technology complies with the American Disabilities Act (ADA), including for ensuring that those portions of the technology that are the scope of the WCAG 2.1 guidelines (or other current accessibility guidelines or legal standards) are complied with? And, which party is responsible for any costs associated with changes in these laws or regulations?

While the agreements proposed by cashier-less technology providers may address several of the typical contractual considerations (albeit likely not in a way that a retailer finds acceptable), retailers that are considering procuring cashier-less technology need to also consider what considerations are not addressed, or addressed very scantily, in these agreements. For example, what are the cashier-less technology provider's obligations for business continuity and disaster recovery of the technology? What are the cashier-less technology provider's obligations with respect to support and maintenance of the technology? Does the retailer need any on-site audit rights or audit reporting in connection with the technology? Does the agreement allow the retailer to continue using the technology for a certain period of time after termination in order to be able to transition to another cashier-less technology or to switch back to non-cashier-less technology? How will the implementation of the technology take place and are there monetary credits or termination rights available to the retailer in the event the implementation goes sideways?

As you can see, venturing into the cashier-less technology space requires the consideration of several contractual considerations, only a few of which have been mentioned herein. However, those retailers that do not start thinking about these considerations now may find themselves left behind as the revolution to this technology continues to gain momentum.

Andrew Geyer

THE RETAILER'S LAW DEPARTMENT AS A PROFIT CENTER?

Most retailers' in-house law departments deal with problems that cost the company money, not with opportunities to make the company money. From the perspective of company leadership, the law department often not only costs money in terms of salary, benefits, overhead, etc., but, because they are generally in an advisory role or defensive posture in litigation, the value of successful outcomes (i.e., good counseling for the business or defense victories) is difficult to quantify and frequently underappreciated. How can this situation be changed so that company leadership looks to the law department as more than a cost center and recognizes it as a potential profit center? Many companies have achieved this seemingly difficult task by establishing a "Global Recoveries Initiative" or "GRI." How can you get there? Three words: opportunity, discipline and partnership.

OPPORTUNITY

To turn a retailer's law department into a profit center, you first need to look at viable sources of potential income relevant to your business. For many retailers, these include monetizing intellectual property, prosecuting insurance claims, asserting indemnification rights against vendors and making claims in antitrust and other class actions for goods or services that that you purchase at scale. Every retailer we have counseled in this area has the possibility of meaningful recoveries in at least one—and normally several—of these areas of opportunity. But opportunity requires more than just a pipeline of potential claims to file; it also requires a framework within the law department that makes one or more individuals the "champions" of the recovery process. Those individuals must have ownership responsibility for their area of recovery and the opportunity to be recognized for their successes. Of course, you also need a champion in company leadership that encourages you to pursue your opportunities. This will most likely be the CFO's office.

DISCIPLINE

Expectations, of course, must be tempered. Recovery efforts are not "quick and easy found money." While there can be some easy or particularly lucrative one-offs, the real, consistent money comes from a disciplined and careful strategy that is implemented and constantly tweaked over years. The goal being that, at some point in the near future, your fully functioning and systematic GRI program runs smoothly and turns into a form of annuity, with relatively predictable average annual returns. Patience and consistency are critical to ultimate success.

A comprehensive GRI system, thus, must include a system for identifying, evaluating and pursuing all viable recoveries. Because it is sometimes difficult to assess accurately the profitability of any particular opportunity, it is the aggregation of potentially lower-paying recoveries in a cost-effective and efficient manner, coupled with the occasional "score" of higher-return recoveries, that keeps the annuity engine turning. Companies that successfully turn their GRI programs into profit-making ventures have a comprehensive system of monitoring, assessing, engaging and maximizing these recovery opportunities across all business lines. The areas of recovery are almost limitless. The most common originate from the company's supply chain, where antitrust or other pricing issues have led to large claims against manufacturers, distributors and others. For example, over the last few years, major supply-chain products have included food commodities like chickens, tuna, salmon and eggs. They have also included prescription and over-the-counter medications that are frequently paid for by retailers' self-funded prescription insurance programs. And, they have included industrial goods, including ball bearings, polyurethane foam, capacitors and industrial chemicals. Operational products and services—such as company iPhones or fleet vehicles—have also been sources of recovery. In any area where a company pays for and receives goods or services on a large scale, the possibility of eventual recovery opportunities may exist. For highly diversified retailers, the potential areas of recovery can be exponentially greater.

PARTNERSHIP

While some very large retailers may be willing and able to invest in creating their own GRI programs, most are not. The barriers to entry include potentially large capital infrastructure to monitor, track and prosecute claims. As such, many companies quickly realize that they need a trusted law firm partner with expertise and bandwidth to tackle the bulk of the GRI program—with one or more specific in-house "recovery champion(s)" steering the ship.

Perhaps most critical to a law department's decision making is the ability to implement a GRI at no internal cost. Many programs, for example, are offered on a pure contingency—including expenses. Of course, payment structures can vary depending on the client or the particular case. For example, routine monitoring of class actions and the filing of claims that will amount to smaller recoveries may be simply "set it and forget it" on a contingency basis, with your outside law firm carrying all expenses. Larger matters in which direct litigation is required and material recoveries are possible may be structured differently or funded by a third party. Any way matters are structured, the key is that the partnership—client and law firm—are in it together to maximize the recovery and turn the law department from cost center to profit center.

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COVID-19 PUSHES DEMAND FOR SURFACE DISINFECTANTS TO FEVER PITCH, RAISING REGULATORY AND LITIGATION RISK

INTRODUCTION

Since the COVID-19 pandemic began, retailers have struggled to meet consumer demand for surface disinfectants—products claiming to kill viruses and bacteria. To ensure surface disinfectants used in homes and businesses are safe and effective, the United States Environmental Protection Agency (EPA) took two important steps early in 2020:

- In January, EPA activated its Emerging Viral Pathogen Guidance for Antimicrobial Pesticides (Emerging Pathogen Guidance) for the first time, allowing an expedited application and approval process for companies seeking to make claims about a product's expected efficacy against SARS-CoV-2.
- In March, EPA released "List N," a list of products expected to kill SARS-CoV-2 when used as directed.

While intended to assist in the fight against COVID-19, both the Emerging Pathogen Guidance and List N contain traps for the unwary. Those traps, coupled with consumer demand and public scrutiny, mean that retailers could face increased regulatory and litigation risk in 2021.

LIST N

List N has grown from 85 initial products to over 500 products. It is one of EPA's most visited web pages, reportedly receiving over 2 million weekly hits.

When EPA published List N, many outlets erroneously reported that it contained products known to kill SARS-CoV-2. Most products on the list, however, have never been tested against the virus. Instead, List N comprises products EPA believes will be effective given their past performance against similar or harder-to-kill viruses.

Further, inclusion on List N does not grant companies carte blanche to claim that their products can kill SARS-CoV-2. Companies cannot make that claim unless the product has specifically been tested against the virus and EPA has approved the claim. To date, EPA has only approved a handful of products which claim that they kill SARS-CoV-2. Nevertheless, many companies continue to make incorrect efficacy claims about SARS-CoV-2, unaware that those claims create potential liability.

EMERGING PATHOGEN GUIDANCE

Even if EPA includes a product on List N, companies cannot market the product as likely effective against the virus without separate approval as outlined in the Emerging Pathogen Guidance. For companies to make that claim legally, they must apply to EPA with data demonstrating the product's efficacy against a "supporting virus"—one that is harder-to-kill than SARS-CoV-2. Once approved, a company may only make the following two statements:

- **[Product name]** has demonstrated effectiveness against viruses similar to SARS-CoV-2 on **[hard, porous and/or non-porous surfaces]**. Therefore, **[product name]** can be used against SARS-CoV-2 when used in accordance with the directions for use against **[name of supporting virus(es)]** on **[hard, porous/non-porous surfaces]**. Refer to the CDC website at https://www.cdc.gov/coronavirus/2019-ncov/index.html for additional information.
- COVID-19 is caused by SARS-CoV-2. **[Product name]** kills similar viruses and therefore can be used against SARS-CoV-2 when used in accordance with the directions for use against **[name of supporting virus(es)]** on **[hard, porous/non-porous surfaces]**. Refer to the CDC website at https://www.cdc.gov/coronavirus/2019-ncov/index.html for additional information.

Approved companies may only make these statements in four places: technical literature distributed exclusively to health care professionals; "1-800" consumer information services; social media sites; and company websites. Companies may not make any statements about a product's efficacy against SARS-CoV-2 anywhere else, including on product labels or promotional literature.

REGULATORY AND LITIGATION RISK FOR RETAIL INDUSTRY

In 2020, EPA Administrator Wheeler called on the retail industry to help protect Americans from products making false or misleading SARS-CoV-2 claims. While EPA has focused its past enforcement efforts on manufacturers, anyone in the supply chain—including retailers—can be liable for unregistered or misbranded surface disinfectants. EPA has already issued several "stop-sale" orders for unregistered products making noncompliant efficacy statements. Moving forward, retailers should keep a close watch on EPA's enforcement strategy, particularly as EPA leadership changes under the Biden administration.

On the litigation front, the pandemic has expanded the pool of potential litigants. Increased consumer use means more potential plaintiffs, especially those unfamiliar with personal protective equipment requirements, Safety Data Sheets and the importance of following label instructions. The increased emphasis on disinfecting public spaces means that plaintiffs could also seek to hold employers and public-facing businesses liable, in addition to the manufacturers and retailers typically targeted in litigation.

Although courts have held that the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA) may preempt product liability claims based on a "failure to warn" theory, other liability theories remain viable. Motivated plaintiffs' counsel may leverage the virus's novelty to both challenge

the preemption status quo and seek recovery on theories not typically preempted. Even if surface disinfectants do not form the basis of a claim, failure to use products from List N could potentially be evidence of negligence by a company facing COVID-19 personal injury or wrongful death claims.

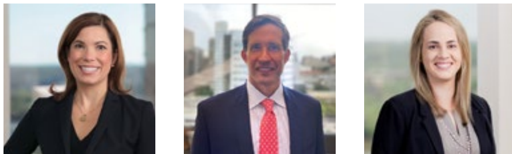
Claims related to surface disinfectants could take several forms:

- Consumer class actions arising out of alleged misrepresentations about virus efficacy, price gouging, price premiums, breach of warranty and similar theories. Similar suits have already been filed involving hand sanitizers and respirators.[1] Every state has a statutory scheme to protect consumers from deceptive trade practices, and most permit consumers to recover attorney's fees, as well as double, treble or punitive damages.
- Personal injury claims alleging that a particular product was not effective against the virus, leading plaintiffs to contract COVID-19. For decades, plaintiffs in asbestos and silica litigation have pursued similar claims asserting that certain respirators failed to protect against inhalation hazards. However, given the limited evidence of virus spread from surfaces and the difficulty of proving causation in any COVID-19 case, we do not expect such cases would ultimately be successful.
- More conventional product liability claims, including that exposure to unvetted or misused chemicals caused plaintiffs to develop some other condition, like a respiratory ailment, skin irritation or more serious injury. At least one suit alleging injury from an EPA-registered chemical used to coat COVID-19 personal protective equipment has already been filed.[2]

CONCLUSION

Lessons learned in 2020 provide a valuable roadmap for risk mitigation in 2021. We recommend that companies in the retail industry:

- Vet surface disinfectant products to ensure all claims are EPA-approved and comply with EPA's Emerging Pathogen Guidance;
- Use only products on List N when disinfecting workplaces and businesses, and follow label instructions carefully; and
- Avoid making independent statements about product efficacy (including through advertising, in-store displays and salespeople or customer service representatives).



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> "ONE CLIENT CALLS [THE RETAIL DEPARTMENT] A 'HIGH-PERFORMING TEAM THAT IS VERY STRONG TOGETHER,' NOTING THAT 'EVERYONE KNOWS WHAT ROLE TO PLAY AND THEY LEVERAGE EACH OTHER'S STRENGTHS'"
>
> – *Chambers USA*, 2020

[1] *See*, e.g., *Anthony Moreno et al. v. Vi-Jon, Inc.* (S.D. Cal.); *Joseph Mier v. CVS Health*, No. 20-cv-1979 (C.D. Cal.); *SourceAmerica v. World Tech Toys, Inc.*, No. 20-cv-00914 (E.D. Va.).

[2] *See Ulysses Lazenby v. Renfro Corp.*, No. 1:20-cv-00178 (E.D. Tenn.).

INSURANCE COVERAGE DEVELOPMENTS IN 2020

BUSINESS INTERRUPTION COVERAGE FOR COVID-19 LOSSES

2020 is now synonymous with COVID-19. While the pandemic has certainly taken a massive toll on our health and well-being and radically altered everyday life, the pandemic also has had a devastating impact on our economy, with retail ranking among the top of industries to be adversely affected. The prospect that these losses are covered by insurance has fueled thousands of lawsuits, with more being filed each day. Central to virtually all of these lawsuits is whether COVID-19 causes "physical loss or damage to property," as that phrase is used in "all-risk" insurance policies. Courts have addressed the issue under initial motions challenging policyholders' complaints and as a matter of law on more developed factual records. As one federal judge recently concluded from his analysis of the phrase as interpreted in pre-COVID-19 decisions, the outcomes present a "spectrum" of different reasonable interpretations. The interpretations in the context of COVID-19 are no different. Below are a sampling of decisions addressing the central "loss or damage" debate in the context of lawsuits seeking recovery of COVID-19 business interruption losses.

- *Elegant Massage, LLC v. State Farm Mut. Auto. Ins. Co.*, No. 2:20-cv-265 (E.D. Va. Dec. 9, 2020). The Eastern District of Virginia recently denied most of State Farm's motion to dismiss a suit seeking to recover COVID-19-related losses. The policyholder, doing business as Light Stream Spa, alleged that it experienced losses due to the various executive orders that required it to shut down its business due to COVID-19. In denying State Farm's motion, the court analyzed decisions spanning decades of litigation over the meaning of the phrase "direct physical loss." The court concluded that the outcomes present a "spectrum" of meanings that fall into three general categories: including (1) decisions that require "structural damage"; (2) decisions that require a "distinct and demonstrable physical alteration"; and (3) decisions that found coverage where the property was rendered "uninhabitable, inaccessible, and dangerous to use." Because the phrase has been interpreted to have multiple reasonable meanings, the court was constrained to apply the meaning most favorable to the policyholder, concluding that "while the [policyholder] was not structurally damaged, it is plausible that [the policyholder] experienced a direct physical loss when the property was deemed uninhabitable, inaccessible, and dangerous to use by the Executive Orders because of its high risk for spreading COVID-19, an invisible but highly lethal virus."

  The court also rejected the insurer's attempt to apply the policy's virus exclusion, acts and decision exclusion, and ordinance and law exclusion. After refusing to apply the exclusion's broad anti-concurrent causation provision as being inconsistent with controlling Virginia law, the court ruled the virus exclusion did not apply because it "particularly deals with the '[g]rowth, proliferation, spread or presence' of 'virus, bacteria or other microorganism' " and the policyholder did not allege the presence of a virus at the covered property or that a virus was the direct cause of the property's physical loss. Likewise, the policyholder did not allege that the executive orders issued were as a result of "growth, proliferation, spread or presence" of virus contamination at the insured property. Instead, the policyholder alleged that the executive orders were the "sole cause" of the policyholders' "loss of business income and extra expense." The court likewise found the "acts or decisions" exclusion inapplicable, finding that the exclusion, if applied literally, would render the policy "practically worthless." Finally, the court refused to apply the "ordinance or law" exclusion, finding that the governmental closure orders were neither "ordinances" nor "laws."

- *JGB Vegas Retail Lessee, LLC v. Starr Surplus Lines Insurance Co.*, No. A-20-816628 (Nev. Dist. Ct. Nov. 30, 2020). A Nevada state court denied an insurer's bid to toss a COVID-19 business interruption suit brought by a commercial real estate operator and owner. The court ruled that JGB Vegas Retail sufficiently alleged losses stemming from the direct physical loss and/or damage to property caused by COVID-19, triggering coverage for general business interruption and civil authority losses. The court held that based on JGB Vegas Retail's allegations, it was "highly likely" that COVID-19 "has been present" at its insured property and that the allegations, therefore were sufficient to allege the "physical presence" of COVID-19. The court further found that the insured has sufficiently alleged that manner by which COVID-19 damages property, such as how the virus is transmissible through droplets that "are physical objects that attach to and cause harm to other objects," and that COVID-19 can survive on property surfaces and infect individuals, thereby transforming otherwise safe property into dangerous transmission instrumentalities.

  Further, in denying the insurer's motion to dismiss, the court made two other significant rulings. First, the court held that Starr failed to prove that the policyholder's interpretation of the policy's Pollution and Contamination exclusion as applying only to instances of traditional environmental and industrial pollution and contamination was an unreasonable interpretation. The court made this ruling even though the exclusion contains the word "virus." Second, the court ruled that JGB Vegas Retail adequately alleged that Starr "misrepresented facts" in stating that the government closure did not prohibit access to its property, thereby finding that the policyholder pled a proper claim for violation of Nevada's consumer protection laws.

- *Studio 417 v. The Cincinnati Insurance*, No. 20-cv-03127-SRB (W.D. Mo. Aug. 12, 2020). The Western District of Missouri denied an insurer's motion to dismiss a complaint seeking to recover COVID-19-related losses. The court held that the insured, an operator of hair salons and restaurants in Kansas City, Missouri, adequately pled a case for recovery under all of the relevant time element coverages.

Contrary to the position taken by insurers, the court concluded that COVID-19 can constitute a "direct physical loss" to property sufficient to trigger coverage. The court first reasoned that a "loss," based on its plain and ordinary meaning, necessarily encompasses "the act of losing possession" and "deprivation" of property. Because COVID-19 is a physical substance that attaches to surfaces and renders property "unsafe and unusable," and because this has led to governmental orders prohibiting businesses from remaining open in order to prevent the spread of that physical substance, COVID-19 losses meet the threshold for a "physical loss." Moreover, the court focused on the fact that the policy language extends coverage for direct physical loss or damage. While Cincinnati argued that both "loss" and "damage" require some form of tangible or physical alteration, the court disagreed. Following the rules of policy construction, the opinion aptly concluded that these two terms must have different meanings because of the use of the disjunctive word "or." "Even absent a physical alteration, a physical loss may occur when the property is uninhabitable or unusable for its intended purpose."

After deciding this cornerstone issue in the policyholders' favor, the court went on to reject another argument advanced by insurers to deny civil authority coverage. Despite the obvious and apparent impact of nationwide governmental orders restricting and prohibiting access to all types of businesses, carriers have argued that civil authority coverage is unavailable unless the order completely forbids access to the property. This has become a common refrain particularly regarding restaurants, which were frequently forced to close their dining rooms but permitted to remain open for take-out and delivery services. Rejecting the insurer's argument, the court observed that the policy does not require a prohibition of "all access" or "any access." The fact that there was some prohibition of access with an appreciable decrease in business was sufficient to state a claim for civil authority coverage.

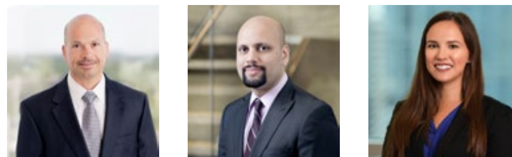
COVERAGE FOR RIOT-RELATED DAMAGE AND INCOME LOSSES

Following the deaths of George Floyd, and so many others, protests against systematic racism in general, and police brutality in particular, have swept the globe. These protests have largely been peaceful, but a small, fractious group of individuals has used the protests as cover to incite violence, damage property and loot businesses. While it might be cold comfort to the affected business owners to hear that property damage is not the norm, most have insurance that protects their pecuniary interest.

First-party property insurance policies generally include riot and civil commotion as covered causes of loss, unless there is a specific exclusion in the policy. Although courts have acknowledged that defining a "riot" can be difficult because they can vary in size, courts have identified at least four elements: (1) unlawful assembly of three or more people (or lawful assembly that due to its violence and tumult becomes unlawful); (2) acts of violence; (3) intent to mutually assist against lawful authority where "lawful authority" is not limited to official law enforcement, but extends to those whose rights are or may be injured and who seek to protect those rights; and (4) some degree of public terror (i.e., any minor public disturbance does not rise to the level of "riot"). *Blackledge v. Omega Ins. Co.*, 740 So. 2d 295, 299 (Miss. 1999).

Civil commotion likewise is undefined in most property policies. As a starting point, the term necessarily means something other than "riot," since each term in an insurance policy is presumed to have its own meaning. *See,* e.g., *Portland Sch. Dist. No. 1J v. Great Am. Ins. Co.*, 241 Or. App. 161, 171 (2011). Thus, while "civil commotion" may be similar to a riot, courts have construed the term more broadly, finding that civil commotion entails "either a more serious disturbance or one that is a part of a broader series of disturbances." *Pan Am. World Airways, Inc. v. Aetna Cas. & Sur. Co.*, 368 F. Supp. 1098, 1138 (S.D.N.Y. 1973), aff'd, 505 F.2d 989 (2d Cir. 1974). In fact, most property policies contain no limitation on the breadth of commotion or the type of harm that it might pose to person or property.

If a policy covers riot or civil commotion, covered losses may include property damage to the building and its contents, and lost income while the building is under repair or subject to government orders affecting the business's operations (e.g., curfews limiting hours of operation) where the order is the result of property damage elsewhere. Business insurance policies may also cover costs incurred in protecting insured property from future, imminent harm or continued damage. These costs might include hiring (or increasing) security personnel, boarding up windows and doors, securing inventory in place or moving inventory and operations off-site.



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2020 RETAIL M&A YEAR IN REVIEW

OVERVIEW OF 2020

2020 was clearly a challenge for almost every sector, especially traditional retail. Global M&A activity totaled US $2.3 trillion during the first three quarters of 2020, which amounted to a decrease of 18 percent compared to 2019 levels.[1] Global deal volume for the same period declined 10 percent, which was a six-year low.

The COVID-19 pandemic caused M&A activity to slow in the first quarter of 2020, and transaction volume continued to decline throughout Q2, as most everyone and everything slowed to a crawl. However, M&A activity quickly swelled to a brisk pace in the third quarter of 2020; there was a total of $896.3 billion in M&A transactions, representing a 94 percent increase compared to the second quarter. Q3 2020 was the strongest quarter for deal-making since the second quarter of 2018. Total deal value was bolstered, of course, by a series of so-called "mega deals," which accounted for $496 billion (or more than 55 percent).[2]

According to a report by PwC, in the first half of 2020, deal activity in the consumer markets sector (which consists of the hospitality and leisure, consumer and retail subsectors) declined in both volume and value (34 percent and 10 percent, respectively).[3] This was the fourth year in a row that the consumer and retail industry experienced a decline in M&A activity.[4] During the first nine months of 2020, M&A activity in the retail subsector increased in value but decreased in volume. A total of $66.1 billion in deal activity in the retail subsector was recorded between Q1-Q3 2020, representing an increase of 15 percent over 2019 numbers.[5] Q3 total M&A value in the retail subsector reached $40.7 billion, the highest quarterly total in over three years, bolstered by Seven & i Holdings' (7-Eleven's parent company) $21 billion acquisition of Speedway LLC, the retail network of Marathon Petroleum. By contrast, volume fell, and Q3 accounted for the second-lowest quarterly M&A volume in the retail subsector since Q1 2009.[6]

LOOKING AHEAD TO 2021

With all of the well-documented causes for concern for retail, particularly brick-and-mortar, there are a number of positive data points, both anecdotal and quantitative, for retail M&A in 2021. Despite economic uncertainty created by the COVID-19 pandemic, a recent survey conducted by Kearney of 100 executives in the consumer and retail sector reported an optimistic outlook for 2021 M&A activity.[7]

One of the main drivers of acquisitions that will likely persist will be storied brand names available for attractive valuations. As of November 25, 2020, 29 well-known retailers had filed for bankruptcy protection, such as Neiman Marcus, J. Crew and Brooks Brothers, to name a few.[8] Strategic competitors and private equity investors have been active participants in auction and prepackaged processes to consolidate or restore these brands.

Second, and relatedly, the relative strength of established digital and e-commerce channels, already an important evolution within retail, was brought to the forefront during the pandemic. Many acquirers will look to strengthen and improve upon distressed retail companies' digital footprint in order to bring immediate growth and increased value to investments in the sector. Despite reservations about investing in existing portfolio brands during the pandemic, private equity, in particular, continues to maintain a mountain of "dry powder" (almost $1.5 trillion, by some estimates) with which to engage in new transactions at better multiples and on more attractive terms.[9]

Thus, we expect the torrid pace of deal-making in the retail sector to continue in 2021 as buyers and sellers better align with "new market" terms and valuations. New investments in technology and those skilled in the digital marketplace should continue to create eye-catching opportunities in many corners.

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[1] https://thesource.refinitiv.com/thesource/getfile/index/bca0e431-5726-438c-a6e6-0e3fc574a639
[2] https://www.refinitiv.com/perspectives/market-insights/records-broken-in-global-capital-markets-to-q3/
[3] https://www.pwc.com/us/en/industries/consumer-markets/library/insights-q3-2020.html
[4] https://www.es.kearney.com/consumer-retail/article/?/a/2020-consumer-and-retail-m-a-report
[5] https://mergers.whitecase.com/highlights/retail-ma-focuses-on-the-essentials-in-2020#!
[6] https://mergers.whitecase.com/highlights/retail-ma-focuses-on-the-essentials-in-2020#!
[7] https://www.es.kearney.com/consumer-retail/article/?/a/2020-consumer-and-retail-m-a-report
[8] https://www.retaildive.com/news/the-running-list-of-2020-retail-bankruptcies/571159/
[9] https://www.wsj.com/articles/private-equitys-trillion-dollar-piggy-bank-holds-little-for-struggling-companies-11593212136

THE CALIFORNIA PRIVACY RIGHTS ACT OF 2020: CCPA REDUX

On November 3, 2020, California voters approved Proposition 24, the California Privacy Rights Act of 2020 (the CPRA).[1] The CPRA ballot initiative was championed by Californians for Consumer Privacy, the group behind the proposed 2018 ballot initiative that coerced the California legislature into passing the groundbreaking California Consumer Privacy Act of 2018 (the CCPA).[2] The CPRA significantly amends and expands upon the CCPA, creating new compliance obligations for businesses, including retailers and consumer products companies, subject to the law.

Most of the CPRA's substantive provisions will become operative on January 1, 2023, and will apply to personal information collected after January 1, 2022.[3] A few of the CPRA's provisions become operative upon the law's effective date,[4] including:

- **An extension of the HR and B2B exemptions:** The CPRA extends, until January 1, 2023, existing exemptions for certain personal information obtained in the HR[5] and business-to-business contexts.[6]
- **Establishment of the California Privacy Protection Agency:** The CPRA establishes the California Privacy Protection Agency (CPPA), which will be responsible for enforcing and implementing the CCPA/CPRA and imposing administrative fines.[7]
- **Authority for expanded regulations:** The CPRA requires new regulations to be issued on a variety of topics, including with respect to cybersecurity audits and risk assessments and automated decision-making and profiling.[8]

KEY CHANGES UNDER THE CPRA

Key provisions and changes under the CPRA include:

1. **Applicability:** Most of the law's obligations apply to a "business," which is defined to mean any for-profit organization that (1) does business in the state of California; (2) collects consumers' (i.e., California residents') personal information, or on whose behalf the information is collected, and that alone, or jointly with others, "determines the purposes and means" of the processing of consumers' personal information; and (3) satisfies one or more of the following thresholds: (a) as of January 1 of each calendar year, had annual gross revenues in excess of $25 million in the preceding calendar year; (b) alone or in combination, annually buys, sells or shares (as the term "shared" is defined below), the personal information of 100,000[9] or more consumers or devices; or (c) derives 50 percent or more of its annual revenues from selling or sharing California consumers' personal information.[10]

   The law also applies to (1) any entity that controls or is controlled by and shares common branding with a business that meets the thresholds described above; (2) a joint venture or partnership in which each business has at least a 40 percent interest; and (3) any person that does business in California and that voluntarily certifies to the CPPA that it is in compliance with and agrees to be bound by the CPRA.[11]

2. **Sensitive Personal Information:** The CPRA establishes a new category of "sensitive personal information," which means (1) a Social Security number, driver's license, state identification card or passport number; (2) a consumer's account log-in or financial account, debit card or credit card number in combination with any required security or access code, password or credentials allowing access to an account; (3) precise geolocation; (4) racial or ethnic origin, religious or philosophical beliefs or union membership; (5) the contents of a consumer's mail, email or text messages, unless the business is the intended recipient of the communication; (6) genetic data; (7) the processing of biometric information for the purpose of uniquely identifying a consumer; and (8) personal information collected and analyzed concerning a consumer's health, sex life or sexual orientation.[12]

   Notably, the CPRA grants consumers the right to limit a business's use and disclosure of sensitive personal information to the extent the information is used to infer characteristics about the consumer.[13]

3. **Right to Correction:** The CPRA grants California consumers the right to request the correction of their personal information if the information is inaccurate.[14] Upon a verifiable consumer request, a business must use "commercially reasonable efforts to correct the inaccurate personal information."[15]

[1] Prop. 24: 19-0021A1, The California Privacy Rights Act of 2020, Version 3 (2020), https://oag.ca.gov/system/files/initiatives/pdfs/19-0021A1%20%28Consumer%20Privacy%20-%20Version%203%29_1.pdf (last visited Dec. 3, 2020).
[2] Alastair Mactaggart, A Letter from Alastair Mactaggart, Board Chair and Founder of Californians for Consumer Privacy, Californians for Consumer Privacy, https://www.caprivacy.org/a-letter-from-alastair-mactaggart-board-chair-and-founder-of-californians-for-consumer-privacy/ (last visited Dec. 3, 2020).
[3] Prop. 24: The California Privacy Rights Act of 2020, Sec. 31(a).
[4] Prop. 24: The California Privacy Rights Act of 2020, Sec. 31(b). In accordance with subdivision (a) of section 10 of article II of the California Constitution, the CPRA will take effect on the fifth day after the Secretary of State files the statement of the vote for the November 3, 2020, election.
[5] Prop. 24: The California Privacy Rights Act of 2020, Sec. 15, 1798.145(m)(4).
[6] Prop. 24: The California Privacy Rights Act of 2020, Sec. 15, 1798.145(n)(3).
[7] Prop. 24: The California Privacy Rights Act of 2020, Sec. 24, 1798.199.
[8] Prop. 24: The California Privacy Rights Act of 2020, Sec. 21, 1798.185.
[9] This threshold increased from 50,000 under the CCPA. Prop. 24: The California Privacy Rights Act of 2020, Sec. 14, 1798.140(d)(1)(B).
[10] Prop. 24: The California Privacy Rights Act of 2020, Sec. 14, 1798.140(d)(1).
[11] Prop. 24: The California Privacy Rights Act of 2020, Sec. 14, 1798.140(d)(2)-(4).
[12] Prop. 24: The California Privacy Rights Act of 2020, Sec. 14, 1798.140(ae).
[13] Prop. 24: The California Privacy Rights Act of 2020, Sec. 10, 1798.121.
[14] Prop. 24: The California Privacy Rights Act of 2020, Sec. 6, 1798.106(a).
[15] Prop. 24: The California Privacy Rights Act of 2020, Sec. 6, 1798.106(c).

4. **Opt Out of Sharing:** The CPRA adds "sharing" as a defined term, which specifically addresses sharing personal information with a third party "for cross-context behavioral advertising."[16] Consumers will have the right to opt out of sharing. In essence, the "right to opt out of selling" under the CCPA becomes the "right to opt out of selling and sharing."[17]

   The CPRA also expands the CCPA's requirement that a business obtain opt-in consent to sell a consumer's personal information if the business has actual knowledge that the consumer is under the age of 16.[18] Under the CPRA, the opt-in requirement also will apply to instances where a business has actual knowledge that it "shares" personal information of a minor under 16.[19]

5. **Privacy Notices:** The CPRA will require businesses to provide certain disclosures in addition to the highly prescriptive language currently required by the CCPA. For example, a business will need to provide notice, at or before the point of collection, of the length of time it intends to retain each category of personal information, including sensitive personal information, or if that is not possible, the criteria used to determine the retention period.[20] A business also will need to provide certain information regarding its processing of sensitive personal information.[21]

   In addition, a business's privacy policy must include a description of all consumer rights under the law, including the new rights granted by the CPRA (i.e., the right of correction, the right to opt-out of sharing and the right to limit use of sensitive personal information).[22]

6. **Necessity/Proportionality Concept:** Under the CPRA, a business's collection, use, retention and sharing of a consumer's personal information must be reasonably necessary and proportionate to achieve the purposes for which the information was collected or processed, or for another disclosed purpose that is compatible with the context in which the information was collected.[23]

7. **Service Provider, Contractor and Third-Party Contracts:** The CPRA clarifies that a service provider or contractor is not a third party, a point which, due to muddled language, caused confusion under the CCPA.[24] Notably, the CPRA requires that businesses enter into written contracts with service providers, contractors and third parties (collectively, Recipients), and those contracts must contain required provisions.[25]

8. **Data Breach Liability:** The CPRA extends the CCPA's limited private right of action to certain data breaches involving a consumer's email address in combination with a password or security question and answer that would permit access to the consumer's account.[26]

9. **Enforcement:** As previously discussed, the CPRA establishes the CPPA, which will be responsible for enforcing and implementing the CCPA/CPRA and imposing administrative fines.[27] Importantly, the CPRA removes the mandatory 30-day cure period that currently exists under the CCPA with respect to enforcement actions.[28]

CONCLUSION

The CPRA significantly changes and expands the obligations imposed on businesses subject to the law. Moreover, forthcoming regulations undoubtedly will bring new developments and clarifications. Businesses would be well advised to closely examine their CCPA compliance programs to identify the actions needed to comply with the CPRA prior to January 1, 2023.

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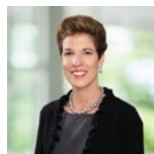
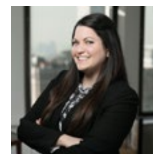

Lisa Sotto and Danielle Dobrusin

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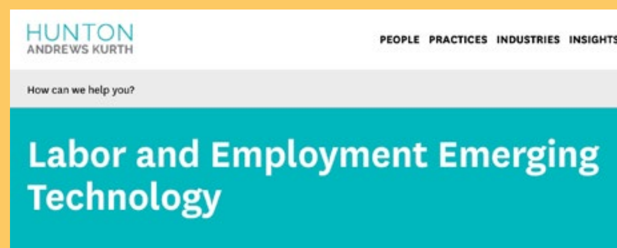
CLIENT RESOURCE

LABOR AND EMPLOYMENT EMERGING TECHNOLOGY PRACTICE



Hunton's Labor and Employment Emerging Technology attorneys are thought leaders in the application of new workplace technologies, particularly in the retail environment. Our team brings an understanding of the full spectrum of emerging opportunities and risks for the in-house legal or HR team, and marries that with a practical approach to helping companies implement these technologies in a way that meets the company's business goals. Our Emerging Technology practice has guided some of the nation's largest coast-to-coast employers, as well as small start-up enterprises, to identify new technology options, assess suitability for their operations and minimize the risks. Special areas of focus include artificial intelligence in HR support tools, robotics, online analytics, biometrics, and connectivity tools, among others. Contact us for a briefing on the latest L&E emerging technology developments.

[16] Prop. 24: The California Privacy Rights Act of 2020, Sec. 14, 1798.140(ah)(1). "Cross-context behavioral advertising" is defined as "the targeting of advertising to a consumer based on the consumer's personal information obtained from the consumer's activity across businesses, distinctly-branded websites, applications, or services, other than the business, distinctly-branded website, application, or service with which the consumer intentionally interacts." Prop. 24: The California Privacy Rights Act of 2020, Sec. 14, 1798.140(k).
[17] Prop. 24: The California Privacy Rights Act of 2020, Sec. 9, 1798.120.
[18] Cal. Civ. Code §1798.120(c).
[19] Prop. 24: The California Privacy Rights Act of 2020, Sec. 9, 1798.120(c).
[20] Prop. 24: The California Privacy Rights Act of 2020, Sec. 4, 1798.100(a)(3).
[21] Prop. 24: The California Privacy Rights Act of 2020, Sec. 4, 1798.100(a)(2).
[22] Prop. 24: The California Privacy Rights Act of 2020, Sec. 12, 1798.130(a)(5)(A).
[23] Prop. 24: The California Privacy Rights Act of 2020, Sec. 4, 1798.100(c).
[24] Prop. 24: The California Privacy Rights Act of 2020, Sec. 14, 1798.140(ai).
[25] Prop. 24: The California Privacy Rights Act of 2020, Sec. 4, 1798.100(d); Sec. 14, 1798.140(j) and (ag).
[26] Prop. 24: The California Privacy Rights Act of 2020, Sec. 16, 1798.150(a)(1).
[27] Prop. 24: The California Privacy Rights Act of 2020, Sec. 24, 1798.199.
[28] Cal. Civ. Code §1798.15(b).

LITIGATION FORECAST FOR PFAS-CONTAINING CONSUMER PRODUCTS

In recent years, we have seen a substantial uptick in regulation and litigation involving per- and polyfluoroalkyl substances (PFASs), a group of over 500 man-made compounds commonly referred to as "forever chemicals" due to their biological and environmental persistence. The frenzy of activity has only heightened during the COVID-19 pandemic, spurred in part by the United States Centers for Disease Control and Prevention and the Agency for Toxic Substances and Disease Registry's June 2020 call for research into whether the posited immunosuppressive effect of elevated PFAS exposure may impact COVID-19 outcomes. *See* CDC/ATSDR, *Per- and Polyfluoroalkyl Substances (PFAS) and Your Health*, https://www.atsdr.cdc.gov/pfas/health-effects/index.html (last visited January 19, 2021). To be clear, scientific literature has not established a definitive causal link between PFAS exposure and any immune system impact, let alone an increased risk of contracting COVID-19 or experiencing worsened outcomes. Regardless, PFASs continue to garner significant national and international attention, which will undoubtedly drive litigation risk for retailers in the year ahead and beyond.

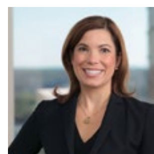
Importantly, PFAS litigation to date has largely not centered on consumer products. Instead, it has arisen primarily in the context of drinking water source contamination allegedly caused by PFAS use in various industrial settings. Lawsuits have been filed by individuals, public and private water authorities, and states and municipalities against PFAS and PFAS-containing product manufacturers, site owners and others to recover for property damage and environmental clean-up damages—and in some instances, to institute medical monitoring regimes for exposed individuals. Although the industrial uses at issue have been diverse, a significant driver of the litigation has been historical use of aqueous film-forming foam (AFFF) as a fire-fighting agent at military establishments, airports and other locations where flammable liquid hazards are present. A multi-district litigation docket has been established in the United States District Court for the District of South Carolina to handle the large volume of AFFF-related filings.

Likewise, PFAS regulation to date has primarily targeted permissible PFAS levels in drinking water. Although the United States Environmental Protection Agency has set only "health advisory" levels (i.e., non-enforceable and non-regulatory levels) for two specific PFASs in drinking water (PFOA and PFOS), a number of states have more aggressively regulated broader categories of PFAS in this context. States have also reached beyond drinking water into other arenas, including consumer products. For example, California passed legislation banning certain PFASs from use in cosmetics and personal care products, effective January 2025. Washington, Maine and New York have passed bans on PFAS in food packaging. Maine and Oregon have legislated strict reporting requirements for certain PFAS-containing children's items (e.g., clothing, toys, craft supplies and others) sold within each state.

The current litigation and regulatory environment, and the associated and widespread media attention, may be setting the stage for a wave of consumer products litigation in the foreseeable future—one that, in fact, may have already begun. In January 2019, a putative class action was filed against Procter & Gamble on the allegation that the company failed to inform consumers that its Oral-B dental floss contained a level of PFAS that allegedly could be detrimental to human health, and thus, violated the California False Advertising Act and Unfair Competition Law. *See Andrews v. The Procter & Gamble Company*, No. 5:19-cv-00075-AG-SHK (C.D. Cal. 2019). Although the case was voluntarily dismissed after a motion to dismiss briefing, it provides an example of a relatively ubiquitous consumer product that enterprising plaintiffs' attorneys could target, regardless of whether they have a basis to do so, as a means of capitalizing on current PFAS hysteria. Two consumer product cases filed in June 2020 provide additional examples. *See Ambrose v. Kroger, Inc.*, No. 3:20-cv-04009-EM, and *Nguyen v. Amazon.com, Inc.*, No. 4:20-cv-04042-YGR (N.D. Cal. 2020). Plaintiffs in both assert violations of the California False Advertising Act and Unfair Competition Law, breach of express warranty and unjust enrichment based on allegations that the defendant retailers at issue advertised, marketed and sold disposable plates and bowls as "compostable," although in reality, the PFASs contained in the products purportedly do not break down over time.

Although we have not seen any litigation in which plaintiffs seek recovery for purported health effects allegedly resulting from PFAS-containing consumer products, we expect those claims may be next up. Even absent an established dose-response (causative) relationship between any PFAS and any particular health endpoint, entrepreneurial plaintiffs' law firms may nonetheless attempt to leverage current regulatory activity and the still-developing science into novel legal claims. Medical monitoring claims, for example, have the potential to be lucrative in the PFAS context because, unlike personal injury, such claims typically have a lower causation hurdle and may be brought either as class actions or as individual claims that could potentially be consolidated for trial in certain jurisdictions.

Given this landscape, retailers should stay apprised of applicable PFAS legislation and regulation and implement measures to ensure compliance. Retailers should also recognize the increased risk of litigation in this arena, even in the absence of regulatory noncompliance. To the extent further consumer product claims are filed, aggressive defense grounded in sound science will be necessary to prevent similar claims from becoming the next tort litigation wave.



Alexandra Cunningham and Merideth Daly

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CONSIDERATIONS FOR RETAIL EMPLOYERS BEFORE MANDATING THE COVID-19 VACCINE

As 2020 came to a close, efforts to develop an effective COVID-19 vaccine produced two candidates with FDA approval. An effective vaccine brings with it questions about whether retail employers can mandate that employees must take a COVID-19 vaccine. In short, yes—retail employers can legally require employees to take a COVID-19 vaccine as a condition of employment, subject to exceptions for disabilities, religious beliefs and any other local or state laws.[1]

The Equal Employment Opportunity Commission (EEOC) has stated in guidance that while a vaccine is not a medical exam under the Americans with Disabilities Act (ADA), any pre-vaccination medical screening is a medical exam under the ADA. Since no vaccines are likely to be administered without medical screening, the EEOC's distinction between the vaccine and the pre-vaccine questions makes no difference. Thus, as a practical matter, vaccination must meet the EEOC's criteria for medical exams, which is that they only can be mandated if they are job-related and consistent with business necessity.[2] Such criteria can be met if an individual poses a direct threat to the health or safety of others in the workplace. The EEOC previously took the blanket position that "an individual with [COVID-19] will pose a direct threat to the health of others," but in the vaccine-specific guidance, the EEOC backs off this position and requires an individualized assessment to determine whether an employee poses a direct threat that cannot be eliminated or reduced by reasonable accommodation.[3] The EEOC does provide a carve out, though, in that the employer does not need to conduct this analysis if it mandates the vaccine, but has the vaccine administered by a third party with whom it does not have a contract. In sum, an employer can mandate the vaccine for its employees, but the EEOC's guidance muddies the analysis, and any decision to do so should be based on a careful risk and reward analysis.

ADVERSE REACTIONS

Vaccines can cause adverse reactions of varying degrees of severity. Such adverse reactions may be covered by workers' compensation insurance where retail employers encourage or require employees to take the vaccine to improve workplace safety.[4] However, this outcome is not a certainty and employers should be aware that the risk of negligence claims is real if workers' compensation offers no remedy.[5] Also, employees may raise negligence claims in a number of ways that would not be covered by workers' compensation. For example, an employee could claim that the employer over-encouraged vaccination that was not effective, picked the wrong vaccine or discouraged vaccination and the employers' actions caused harm.

DISCRIMINATION

Retail employers must ensure that a COVID-19 vaccine mandate does not lead to unlawful discrimination. For example, a vaccine mandate must include an opportunity for an employee with a disability that interferes with vaccination to be reasonably accommodated. Similarly, any employee with a sincerely held religious belief, practice or observance that prevents the employee from taking the COVID-19 vaccine must be given an opportunity to seek accommodation.[6]

As stated above, the ADA does not permit mandatory vaccination of an individual who has raised a disability-based objection to vaccination, absent an individualized assessment and determination that the individual poses a direct threat to the health of others and further, the individual cannot be excluded from the workplace (and the employer cannot take other adverse action against the individual) "unless there is no way to provide a reasonable accommodation (absent undue hardship) that would eliminate or reduce the risk so the unvaccinated employee does not pose a direct threat."[7] Likewise, with respect to religion, employers must accommodate employees who refuse the COVID-19 vaccine because of sincerely held religious practices or beliefs.[8]

[1] Certain employers, such as those in high-risk industries like health care, routinely require certain vaccines as a condition of employment. See, e.g., CDC, Influenza Vaccination Information for Health Care Workers, https://www.cdc.gov/flu/professionals/healthcareworkers.htm (last reviewed Nov. 23, 2020) (noting that some employers, including hospitals, have required staff to get flu or hepatitis B vaccines to enhance patient and staff safety). Also, some vaccines are required as a matter of state law for teachers, childcare providers and others and are required as a matter of federal immigration law for certain immigrants.

[2] EEOC, What You Should Know About COVID-19 and the ADA, the Rehabilitation Act, and Other EEO Laws, *https://www.eeoc.gov/wysk/what-you-should-know-about-covid-19-and-ada-rehabilitation-act-and-other-eeo-laws* (last updated Dec. 16, 2020) (hereinafter EEOC COVID Guidance) (likewise, employers are permitted to test/screen employees for COVID-19 as such is job-related and consistent with business necessity).

[3] *Id.* at Section H, K.

[4] *See*, e.g., *E.I. Dupont De Nemours & Co. v. Faupel*, 859 A.2d 1042, 1053-54 (Del. Super. Ct.), *aff'd sub nom. E. I. Dupont Denemours & Co. v. Faupel, 860 A.2d 810* (Del. 2004) (adverse reaction from the flu vaccine was compensable under the Delaware Workers' Compensation Act where it was administered by the employer); *Maher v. Workers' Comp. Appeals Bd.*, 33 Cal. 3d 729, 735 (1983) (it is well settled in California that "where an employee submits to … a vaccination *at the direction of the employer* … any injury resulting from an adverse reaction is compensable" under the California Workers' Compensation Act) (emphasis in the original); *see also Payne v. Galen Hosp. Corp.*, 28 S.W.3d 15, 20-21 (Tex. 2000) (adverse reaction caused by employer-provided medication was compensable under the Texas Workers' Compensation Act).

[5] Typically, retail employers would not face negligence claims if an adverse reaction was covered by workers' compensation insurance, because, in most cases, workers' compensation insurance would be the exclusive remedy for the employee who suffered the adverse vaccine reaction. *See*, e.g., Tex. Labor Code Ann. § 408.001(a) (Texas); N.Y. Workers' Comp. Law § 11 (New York); Ariz. Rev. Stat. Ann. § 23-1022(A) (Arizona); Colo. Rev. Stat. Ann. § 8-41-104 (Colorado).

[6] A belief in the inefficacy of the COVID-19 vaccine, or that the vaccine does more harm than good, will likely not be afforded protection under Title VII. *See Fallon v. Mercy Catholic Med. Ctr. of Se. Penn.*, 877 F.3d 487, 492 (3d Cir. 2017) (deeming such beliefs to be medical beliefs, not religious beliefs). However, the basis of a practice or belief that precludes one from taking the COVID-19 vaccine need not actually be religious to be afforded protection under Title VII, but can be moral or ethical so long as one's belief is "sincerely held with the strength of traditional religious views." *See* 29 C.F.R. § 1605.1.

[7] EEOC COVID Guidance, at Section K.5.

[8] *Id.* at Section K.6.

Accordingly, retail employers who institute a COVID-19 vaccine mandate will be required to reasonably accommodate employees with objections based upon qualifying disabilities and religious practices or beliefs, unless such accommodation poses an undue hardship.

Further, while not entirely clear, employees who object to taking the COVID-19 vaccine on political grounds may have a plausible basis for raising discrimination or retaliation claims under the laws of some states.[9]

PUBLIC AND HUMAN RELATIONS

Viewpoints on COVID-19 vaccination run the gamut. Retail employers who mandate vaccines as a condition of employment could face backlash from groups that oppose vaccines generally, and those that oppose vaccine mandates specifically. Those that do not mandate could face backlash from other constituencies, including customers who may believe that the company is not doing enough for its employees or for public health. These decisions can also have human resources complications. Employees who refuse vaccination may face ostracism or criticism from fellow employees. If the refusal to vaccinate was based on an exercise of legally protected rights, negative or retaliatory treatment by coworkers could have legal consequences. Retailers should carefully consider these issues in advance and make sure they have a response plan in place if conflict arises.

THE NATIONAL LABOR RELATIONS ACT

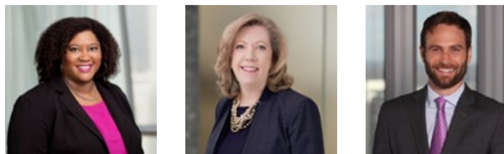
Retail employers who are unionized will have to involve their employees' representative in vaccination mandate decisions. Retail employers who are not unionized should also be mindful that employees' refusal to take the COVID-19 vaccine may be protected by the National Labor Relations Act (NLRA). Section 7 of the NLRA provides employees the right to engage in concerted activities for the purposes of mutual aid or protection. If employees collectively oppose a retail employer's mandatory vaccination program, such opposition may be protected by the NLRA as a "concerted activity" and the retail employer may be exposed to an NLRA violation if it clamps down on employee opposition.

ALTERNATIVES

The government may mandate vaccination, particularly if voluntary vaccination does not achieve the levels necessary for herd immunity, though such a mandate will most certainly face constitutional challenges, especially if it does not provide an exception for disability or religious beliefs.[10] A government COVID-19 vaccine mandate that does not provide an exception for religious beliefs has been considered by some jurisdictions.[11] A government mandate would give retail employers certainty regarding the best course of action and substantially limit legal risk.

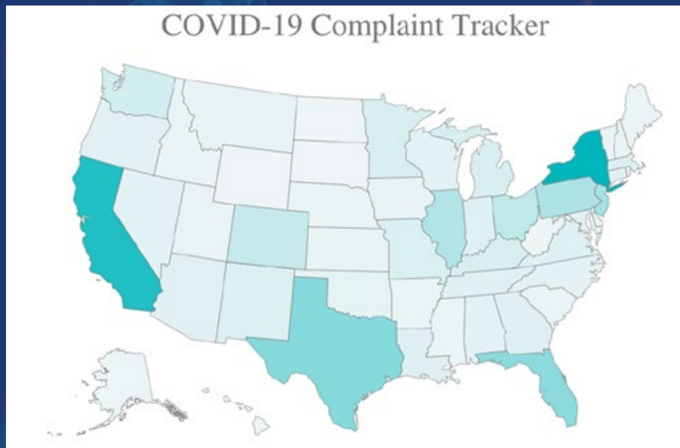
Even if the government does not mandate vaccination, employers may be able to obtain high levels of workforce vaccination without imposing their own mandate. Steps to consider include on-site vaccination clinics, incentives and paid time off to get the COVID-19 vaccine.[12]

Retail employers face difficult decisions regarding how to approach employee vaccination. Workplace safety must be weighed against legal risks, while also considering possible customer reaction. Planning is made more difficult by how quickly the landscape is changing with new vaccine approval, new known side effects and a workforce and public weary of COVID. Careful planning with regular review and revision of those plans is required.



Amber Rogers, Susan Wiltsie and Lukas Moffett

Amber and Susan are partners on the labor and employment team in the firm's Dallas and Washington offices, respectively. Lukas is an associate on the labor and employment team in the Dallas office.



The Hunton litigation team developed the interactive COVID-19 Complaint Tracker, an infographic-based tool that tracks coronavirus litigation at the federal and state levels. The tracker is an authoritative resource on the number and types of litigation related to COVID-19 and has received extensive media attention nationally over the past year.

[9] States, cities and territories that may afford employees such protections on the basis of political beliefs or affiliation include California, Colorado, Connecticut, the District of Columbia and Puerto Rico.

[10] Additionally, government-mandated vaccinations may be challenged on Fourth Amendment grounds (the right against unreasonable searches and seizures) and Fourteenth Amendment grounds (the right against deprivation of life, liberty or property without due processes). *But see Jacobson v. Commonwealth of Massachusetts*, 197 US 11 (1905) (the Fourteenth Amendment did not invalidate a state law that provided for a $5.00 fine for individuals who refused to get a mandatory smallpox vaccine).

[11] *See* New York State Bar Association, Report of the New York State Bar Association's Health Law Section Task Force on COVID-19, p. 65 (May 13, 2020).

[12] To protect against discrimination claims, retail employers should be prepared to offer employees with qualifying disabilities or religious beliefs (and, in some states, possibly political beliefs) equivalent benefits.

NOT ALL AUDITS ARE BAD: INTELLECTUAL PROPERTY AUDITS CAN PROTECT AND CREATE VALUE IN YOUR RETAIL BUSINESS

The COVID pandemic forced retailers into new realities. Most notably, it accelerated the transition to e-commerce, and created a myriad of practical (and legal) retail challenges, including health and safety issues, counterfeit products, remote workers and, in some cases, staff reductions, reduced demand and decreased profitability.

While these issues dominated most companies' focus for the last ten months, many are now beginning to shift focus, to ways to improve the bottom line. One—sometimes overlooked—means to do so is by maximizing the value and protection of existing intellectual property assets and identifying areas of intellectual property growth and development (and potential concern).

This article focuses on the basics of systematically auditing intellectual property holdings and strategies. Such audits can identify gaps in protection, avoid potential liabilities and result in new (and/or previously untapped) revenue sources.

CONFIDENTIALITY/TRADE SECRET PROTECTIONS

While it happens all the time, particularly in 2020 due to COVID, more companies than usual have taken steps that test the limits of existing confidentiality and trade secret protections. Actions such as (i) letting go of staff who possess confidential and trade secret information, (ii) hiring new staff who bring confidential information from a prior employer, (iii) sharing confidential information with third-party service providers or (iv) accelerating the use, development or licensing of technology, each implicate confidentiality and trade secrets.

Now is a good time to make sure you are well protected. There has been a 27 percent increase in confidentiality and trade secret-related litigations in the past three years (compared to the prior three years), with very high-dollar judgments awarded for misappropriation, sometimes more than $500M.

To protect confidential/trade secret information, a company needs to show that it has (i) designated certain information as confidential/trade secret, (ii) taken reasonable steps to maintain the confidentiality of that information and (iii) insured that employees (or third parties with whom you share information) know that they have an obligation to protect that confidential/trade secret information.

In conducting a confidentiality/trade secrets audit, some questions to ask your team include:

Preventative measures: Have you created a culture of respect for confidential information in which employees feel that the careful safeguarding of confidential information is as important as any other business consideration for the company, including your HR, sales, marketing, engineers, legal and cybersecurity teams? Do you send annual reminders of the importance of safeguarding confidential information? Do you monitor for unusual patterns or volumes of copying data?

Exiting/Incoming employees: Does your exit interview of departing employees who possess sensitive confidential information include a supervisor who has knowledge of the types of confidential information possessed by the employee? For new hires coming from a competitor, what steps have you taken to ensure that the new employee will not be using confidential information of the former employer?

Agreements: Are your nondisclosure agreements, employment contracts, technical service agreements, licenses and joint venture documents generic or are they tailored to particular situations? Do all of your team members (not just your legal team) fully understand the terms? Do you revise the documents and update the affected individuals as circumstances change?

While many specific elements can go into a confidentiality/trade secret audit, the overarching reminder is that a company must be constantly vigilant in its protection of that information, or risk losing it (and recovery of damages for someone else's misappropriation).

TRADEMARKS AND TRADE DRESS

Trademarks and trade dress—your own and your rights to use others'—are essential to all retailers. The value of marks and branding has been borne out by the unfortunate shuttering of many retailers during the COVID pandemic. At liquidation, it has been the brand names, not inventory or other assets, that command the highest price. *See* https://news.bloomberglaw.com/ip-law/bankrupt-retailers-ip-assets-draw-more-demand-in-online-shift.

To maximize the strength and value of your trademark portfolio and avoid unnecessary, costly litigation, a thoughtful trademark audit can ensure that you are carrying out an effective trademark strategy.

The following issues, among others, should be considered in any such audit:

Existing registrations: Have you reevaluated in what classes and countries you register your marks to take into account changes in business? Do

they cover the appropriate goods and services (and the ones you expect to sell/provide in the future)? Do you continue to pay for marks you no longer use or countries in which you do not have foreseeable business? Do your registrations reflect the current version/usage of the mark (e.g., has a logo been updated, or a brand name shortened)? Have Section 15 Declarations of Incontestability been filed for all eligible marks? What other marks exist in similar spaces with similar commercial impressions, and how much room for expansion of the brand is there?

Possible new registrations: Is there anything consumers associate with your company that you have not registered (including nontraditional associations, such as color, packaging shape, fonts, shelving displays or even a smell (*see* TMEP § 1202.13))? Have you considered the use of design patents, which are inexpensive and relatively easy to obtain, to protect look and feel aspects of your brand until secondary meaning is established and a trademark registration can be secured? Do you have new products, brands or packaging for which you have not obtained protection?

Clearance and enforcement: Do you have a systematic, regular procedure in place to police potential infringements of your trademarks? Before investing in new marks, do you conduct a rigorous, thorough clearance search and address any arguable blocking marks before you invest in developing your new trademark?

Licensing: For inbound licensing, are your business teams in full compliance with the terms of your contracts? For outbound licensing, do you have a systematic way to ensure that your licensees are not abusing your trademarks and going beyond the scope of their license? Are your licensees (or others) attempting to register your marks or similar marks in other countries (including those where you do not have registrations)? Are you including and enforcing quality control terms in your licenses? If you agree to celebrity and/or brand collaborations, do they include a license beyond the scope of the collaboration? Who owns what rights?

PATENTS

Retailers are often the target of patent infringement suits. A thoughtful intellectual property audit and subsequent patent strategy can help retailers protect themselves from patent litigation—and explore developing (or monetizing) their own portfolio.

At least these basic concepts should be included:

Existing and prospective patents: What technology does your company use that you believe is novel? (Keep in mind that technology can include novel business methods.) Is any of it already patented? If so, is it being properly maintained? If you have existing patents, have you reassessed ways to broaden their scope, especially to uses outside of your business or that cover your competitors' products? Are you marking your products either physically or "virtually" with the relevant patent numbers (but not expired patents)?

Employment agreements: Does your standard employment agreement include a strong intellectual property assignment provision (e.g., does it include the language "do hereby assign," as opposed to "will" assign), and what is the scope of assigned inventions (e.g., those made in the course of employment, those made utilizing company resources or something else)? Are all employees required to sign the agreement?

Patent litigation defense: Do you have strong indemnification provisions against infringement claims in all your supplier contracts (e.g., will it protect you if only the main elements of the infringement claim are provided by the supplier)? Do you investigate the financial strength of the supplier to determine if it can stand behind its indemnification or require insurance coverage? Have you looked into whether any infringement threats have been made against the product the supplier is providing you?

Patent litigation offense: Do you have a systematic way of monitoring the industry for use of your technology (e.g., are your engineers and salespeople aware of your patents and do they know to report any possible infringements)? If you have inbound or outbound patent licenses, who has the right, obligation and/or standing to enforce the patents? Who is responsible for monitoring for infringement? For those same licenses, how are you monitoring compliance with the terms internally and externally?

SOFTWARE AUDITS

With an increased move to online services and the accelerated trend to web-based products, third-party software licenses are on the rise. An effective audit of your software licenses and use of licensed software can save hundreds of thousands of dollars. We covered this issue in our 2019 Annual Review, at https://www.huntonak.com/en/insights/2019-retail-industry-year-in-review.html.

CONCLUSION

Intellectual property can be an underappreciated value proposition. But the drive towards shopping online has emphasized the critical importance and tremendous value of brand identity and other intellectual property to a business. And studies show that intellectual property and intangible assets represent roughly 80 percent of the value of an S&P 500 company. Aon PLC, 2019 Intangible Assets Financial Statement Impact Comparison Report (2019).

At the start of any new year, (and especially this year with the upheaval caused by the pandemic, including changes to numbers and types of employees, new areas of business and expanded use of software and technology), companies will benefit from a careful review of their intellectual property assets and protections.

What assets are strong already? What protections can be strengthened? Where are the areas of concern and potential liabilities? Asking these questions, taking a proactive approach, can avoid (or at least mitigate) legal and business problems and unnecessary losses, while improving profitability and securing your company's competitive advantages.

Whether you undertake an audit in-house or with assistance from outside counsel, the key is to take an unbiased, fresh look at your intellectual property assets, procedures and related legal documents to increase value, discourage violations, protect against challenges and prevail in litigation if necessary.

John Flock, Josh Kalb and Aimee Soucie

John is a partner, Josh is counsel, and Aimee is special counsel in the intellectual property practice in the firm's New York, Atlanta and Washington offices, respectively.

CHAPTER 11 PROVIDES FLEXIBILITY FOR DISTRESSED RETAILERS TO PRESERVE VALUE DURING GLOBAL PANDEMIC

The COVID-19 pandemic has wreaked havoc on brick-and-mortar retailers in an already battered industry. Commencing in mid-March, governors from a majority of states issued executive orders shuttering nonessential retail business locations to combat the spread of COVID-19. Retailers who rely on foot traffic to support their businesses felt a swift and severe impact. Supply chain disruptions compounded retailer difficulties. Retailers who recently had filed bankruptcy under chapter 11 had their reorganization efforts disrupted in unprecedented fashion. After more than nine months of enduring the global pandemic, nary a retail business has escaped unscathed.

The impact was particularly severe for businesses in the midst of restructuring. With expenses still accruing and revenue drastically cut, retailers already in chapter 11 faced the risk that their bankruptcy proceedings would devolve into a chaotic (and expensive) motions practice in which creditors raced to obtain court relief against the debtors and their assets. Such an onslaught could eliminate any hope for a successful chapter 11 case. To address this risk, some retail debtors sought to put their cases "on ice" by requesting orders suspending their cases for a limited period until they could resume operations. At least one retailer relied upon section 305(a) of the Bankruptcy Code, an infrequently cited provision that allows a bankruptcy court to suspend all proceedings if it serves the interests of creditors and the debtor.

This rare, if not unprecedented, tactic aimed at preserving value for stakeholders through a time period in which retail businesses were producing little to no revenue played out in several bankruptcy courts at the inception of the pandemic. In the US Bankruptcy Courts for the District of Delaware and the Eastern District of Virginia—both prominent destinations for retail companies seeking chapter 11 relief—CraftWorks Parent, LLC, a restaurant chain operator, and Pier 1 Imports, Inc., a home goods retailer, each obtained orders from the respective courts granting relief that allowed them to mothball their cases for a short, fixed duration until state governors allowed businesses to re-open.

The standstill orders generally authorized the debtors to defer payment of noncritical expenses, including rent, for a period of time and restricted the ability of creditors to seek disruptive relief against the debtors and their assets. In approving the temporary standstill in the Pier 1 case, Bankruptcy Judge Kevin R. Huennekens commented that "we're not going to go on forever and ever" in response to vociferous objections from Pier 1's landlords who were not receiving post-petition rent during the period. In the interim, the court permitted the furniture retailer to operate under a limited budget that included only critical expenses, such as employee wages, insurance and trust fund taxes, until such time as the company could arrange for a wind-down budget with its lenders.

After obtaining an initial standstill order from Delaware Bankruptcy Judge Brendan L. Shannon, CraftWorks sought an extension while simultaneously announcing a deal with its senior secured lender to effectuate a semi-private sale. Judge Shannon described the deal as a "welcome prospect" in the midst of the COVID-19 crisis.

In another chapter 11 case, In *re Modell's Sporting Goods, Inc.*,[1] in which the company was already committed to liquidating when the pandemic struck, the debtor filed a motion to suspend all payments except for wages and insurance pursuant to section 305(a). The US Bankruptcy Court for the District of New Jersey approved the motion for an initial 30-day period. In granting the relief, the court acknowledged arguments of frustration of purpose and intervening impossibility triggered by the COVID-19 pandemic. That order was subsequently extended for several months until Modell's could resume its store closing sales. The company, its landlords and the creditors' committee appointed in the bankruptcy case ultimately negotiated a stipulation providing for the partial payment of rent during the standstill period in exchange for the agreement of the consenting landlords not to object to plan confirmation based on the failure to pay postpetition rent in full, which is typically required in order to confirm a chapter 11 plan.

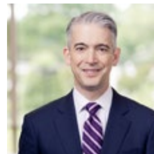
[1] *In re Modell's Sporting Goods, Inc.*, Case No. 20-14179 [Docket No. 115] (Bankr. D.N.J. March 23, 2020).

The mothballing of retail chapter 11 bankruptcy cases during the COVID-19 pandemic demonstrates the flexibility of the Bankruptcy Code to accommodate even the most dire of business interruptions. Through entry of the standstill orders, the courts allowed the debtors to preserve substantial value for the benefit of their creditors and other constituencies. Although not a panacea, the orderly business wind-downs or going-concern sales that followed were far superior to a chaotic free-for-all that could have ensued without bankruptcy court intervention. Underscoring the uniqueness of these decisions and the flexibility of bankruptcy courts, these proceedings occurred remotely through video. Bankruptcy courts were among the first in the nation to fully adopt this technology to accommodate the exigent needs of struggling businesses.

Even the extended duration of the pandemic has not proven impossible for some larger retailers to overcome through use of chapter 11. Notably, Chinos Holdings, Inc., owner of the J.Crew and Madewell retail clothing brands, filed chapter 11 to effectuate a pre-arranged financial restructuring in May 2020 in the midst of the pandemic.[2] The company obtained plan confirmation in less than four months despite the temporary closure of 500 of its retail stores. In November 2020, Guitar Center, the largest music retail chain in the US, sought chapter 11 protection in the US Bankruptcy Court for the Eastern District of Virginia.[3] On the first day of the case, the company filed a pre-packaged chapter 11 plan seeking to consummate a balance sheet restructuring and pay unsecured trade creditors in full. The company was successful in obtaining first-day relief to seamlessly transition into chapter 11 with the goal of exiting in less than two months despite the substantial disruption the COVID-19 pandemic had caused to its business.

The depth of the unprecedented economic crisis caused by the COVID-19 pandemic has forced many retail establishments to close simply because foot traffic has fallen off the cliff. Nevertheless, as the above examples illustrate, chapter 11 bankruptcy provides flexibility for retailers to maximize value for their stakeholders, whether through a reorganization or a liquidation. The pandemic has revealed that bankruptcy judges in jurisdictions where retailer companies commonly seek chapter 11 protection will exercise their equitable powers appropriately to balance the requirements of the Bankruptcy Code with the stark reality of the impact of the current economic crisis on both retail tenants and their landlords and other creditors. Although the chapter 11 process is expensive, it remains the most prudent and predictable option for many retailers to address severe financial challenges, even an unforeseen global pandemic.

Hunton Andrews Kurth LLP and its corporate restructuring attorneys have experience advising distressed retailers and their creditors across the country in effectuating restructurings or liquidations. Attorneys with Hunton Andrews Kurth LLP represented interested parties in the chapter 11 bankruptcy cases of *In re Craftworks Parent, LLC* and *In re Pier 1 Imports, Inc.*, and serve as co-counsel to the debtors in *In re Guitar Center, Inc.* and *In re Chinos Holdings, Inc.*



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THE [RETAIL] TEAM'S 'STRENGTH LIES IN ITS BUSINESS-FRIENDLY APPROACH.'

– *Chambers USA*, 2020

[2] *In re Chinos Holdings, Inc.*, Case No. 20-32181 (Bankr. E.D. Va.).

[3] *In re Guitar Center, Inc.*, Case No. 20-34656 (Bankr. E.D. Va.).

THE SEC'S NEW HUMAN CAPITAL REPORTING RULES

New Securities and Exchange Commission (SEC) rules requiring reporting on human capital resources took effect November 9, 2020. Publicly traded retailers should begin the analysis to assess whether disclosure will be required in the upcoming Form 10-K, and if so, what will be disclosed in 2020 annual reports to shareholders. Retailers determining that disclosure is immaterial under the federal securities laws may still elect to provide a human capital narrative in corporate sustainability reports, which are not filed with the SEC, in an effort to address increasing stakeholder demand for such information.

"Human capital resources" is a flexible concept used broadly to connote a wide range of enterprise-wide employment-related issues, depending on the context, and may include items such as employee demographics, talent development, diversity and inclusion efforts, worker health and safety, compensation design and assessment, employee review and retention, labor-management relations, employment law compliance programs and overall corporate culture concerning the foregoing matters. Some speakers use the phrase as an umbrella term that includes the full range of these employment issues, and others use it only to encompass a subset of matters. Usage of the "human capital resources" term varies across industries, including within the retail space, and even at individual retailers. As a subset of the larger ESG movement, management of human capital has become an increased focus in recent years of not only a growing number of investors, but also a range of other stakeholders including current and prospective employees, customers and consumers, labor unions, NGOs and political activists, to name just a few.

The SEC's new human capital disclosure requirements are largely principles-based. Under new Item 101(c)(2)(ii) of Regulation S-K, public companies (including publicly traded retailers) will be required to provide a description of their human capital resources, including the number of persons employed by the company, and any human capital measures or objectives that the company focuses on in managing the business (such as, depending on the nature of the company's business and workforce, measures or objectives that address the development, attraction and retention of personnel). Disclosure is only required to the extent material to an understanding of the company's business taken as a whole, except that, if the information is material to a particular segment, a company should additionally identify that segment.

The SEC specifically declined to adopt a definition of "human capital" as part of the rulemaking because it believes this term may change over time and may be tailored to the circumstances and objectives of individual companies and industries. Thus, retailers may be situated differently than businesses of similar size in other industries. Even reporting within the retail space may differ by company.

The new SEC disclosure requirement does not, of course, relieve retailers from compliance with federal, state and local labor and employment laws. In crafting human capital policies and disclosures for their SEC reports, retailers must continue to take into account employment discrimination laws and other labor regulations. Companies can lawfully take many actions to promote the laudable goal of advancing diversity in their workforce, for example, but they must continue to be mindful of potential claims that could seek to challenge these efforts as discriminatory in one way or another. These concerns are not merely hypothetical; recently the Department of Labor has reportedly questioned several prominent public companies about their diversity initiatives and whether those initiatives comply with employment law.

Numerous private-sector standard-setters have developed a wide range of their own suggested human capital disclosures, which vary based on country, industry and numerous other subjective factors. An entire cottage industry has emerged to provide human capital and other ESG metrics, rankings and consulting services for both investors and public companies. Retailers that determine to make human capital disclosures in SEC filings should carefully consider which of these metrics are most appropriate for their businesses, giving attention to preferences of their own investors, who may favor some sets of metrics over others based on various idiosyncratic factors.

Human resources executives and counsel can play a key role in implementing effective human capital programs and reviewing public disclosures, especially diversity, equity and other social disclosures in the proxy statement, annual report and other SEC filings. Indeed, human resources counsel and executives who have historically had a nominal role in the SEC disclosure review process and often have not been part of the disclosure review committee may now need to feature more prominently in these procedures.

Furthermore, a number of well-known public companies have recently been the subject of shareholder litigation regarding human capital issues. These suits typically allege violations of board fiduciary duties for not maintaining a sufficiently diverse workforce in one way or another. They also claim that the companies violated the antifraud provisions of the federal securities laws by touting diversity efforts and achievements in proxy statements and other SEC filings even though such statements were allegedly untrue. The litigation is at too early a stage to draw any affirmative conclusions, but it is clear that some shareholders (and plaintiffs' counsel) are now focused on these issues and have begun to look for potential misstatements and omissions on such matters in companies' public statements.

In light of the foregoing, boards, disclosure committees and compensation committees may also need to expand their oversight of human capital matters, in particular those affecting rank-and-file employees. These efforts will vary by company, but may include enhanced discussion and review of compensation design, material employment litigation, internal investigations and shareholder communications regarding employee welfare and diversity. Board and committee governance principles and charters, as well as annual self-evaluations, may need to expand as appropriate to cover diversity, inclusion and other human capital issues. Meeting agendas may need to expand to give due attention to these issues, which in turn could affect the frequency and duration of board and committee meetings. Board recruitment efforts may need to expand to ensure that sufficient expertise in these topics resides on the full board and the compensation committee. Of course, any expansion of the board's oversight must be balanced against heightened litigation risks associated with involving the board in enterprise-wide employment decisions.

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CLIENT RESOURCE

HUNTON RETAIL LAW RESOURCE

Written by members of our firm's experienced team of lawyers who serve retailers from factory floor, to retail outlet, to online store, the Hunton Retail Law Resource Blog helps you stay abreast of the legal and regulatory issues facing your company and helps you minimize risk in this highly competitive and ever-changing industry. With a regular digest of breaking legal news and information delivered to your desktop, our blog reports cover topics including corporate law, FTC and SEC consumer protection and antitrust matters, labor law, litigation, retail class actions, and privacy and cybersecurity.

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WORKPLACE SAFETY IN THE TIME OF COVID-19

COVID-19 changed everything about retail workplace health and safety by adding infectious disease management to the already substantial list of compliance issues. This article will focus on the current state of federal, state and local COVID-19 regulations as we begin 2021.

WHAT RULES RULE? COMPLIANCE LANDSCAPE COMPLICATED BY OSHA, CDC, STATE REGULATION

America's response to COVID-19 has been marked by inconsistent and constantly evolving federal, state and local requirements. To ensure compliant workplace safety programs, it is vital for retail employers to recognize which legal obligations govern their businesses.

Throughout the pandemic, the first point of reference has been the Center for Disease Control (CDC) guidance. This focal point is appropriate as the CDC guidance informs the requirements imposed by state and local authorities. However, unless incorporated through federal, state or local regulation, CDC guidance is just that—guidance. It does not have the force of law, although it will likely set the standard of care for negligence tort claims related to COVID-19. With respect to day-to-day compliance, retail employers must monitor whether state or local regulators have adopted CDC guidance through legally enforceable executive orders or rulemaking. Almost all states have issued executive orders on COVID-19; and in some states, localities can issue orders that can be more restrictive than the state requirements. These state and local requirements have the force of law and are enforced through the state and local police authority.

The federal Occupational Safety and Health Administration (OSHA) has issued a number of industry-specific guidance documents, including retail-specific guidance for workers and employers. This guidance largely follows CDC recommendations, including physical barriers to separate workers from members of the general public, promotion of self-checkout kiosks to minimize worker interaction with customers and effective disinfection protocols. OSHA has not been hesitant to use its enforcement authority to cite employers for alleged violations related to COVID-19. As of December 24, 2020, OSHA had issued citations arising from 294 inspections for violations relating to coronavirus exposure, resulting in proposed penalties totaling over $3.4M. The agency has largely used the general duty clause for enforcement under the theory that an employer's failure to follow OSHA guidance created recognized hazards likely to cause death or serious bodily harm. In some cases, OSHA has issued general duty clause citations related to alleged COVID-19 hazards prior to the time period when OSHA had issued any industry-specific guidance at all. So far, the retail industry has largely escaped OSHA's COVID-related enforcement activity, with most citations being issued to nursing homes and other medical and health care facilities and the foodservice and meatpacking industries.

Some state-plan states—those states that administer safety and health regulations at the state level—have adopted infectious disease Emergency Temporary Standards (ETSs) to address COVID-19. Virginia led the way, adopting its program in July, with Michigan, California and other states following thereafter. These standards have the force of law, and the departments of labor in these states have been aggressively conducting investigations and issuing penalties for noncompliance. Some of these ETSs provide a safe-harbor for employers who comply with CDC guidance, allowing employers to follow CDC standards that are equally protective rather than the specifics of the state ETS. However, not all states have such safe harbors, so retail employers must review and comply with the specific details of the relevant standards in the states where they operate to avoid potential penalties.

CLIENT RESOURCE

GC HOT TOPICS MEMO

Hunton Andrews Kurth is pleased to provide an informative communication focused on the issues facing retail General Counsel. This quarterly publication features items on advertising, antitrust, consumer health and safety, corporate governance and securities disclosure, immigration, insurance, intellectual property, labor and employment, privacy and cybersecurity, and retail finance.

Easy-to-read and focused on the latest hot topics, if you are interested, please email our editor Phyllis Marcus at pmarcus@HuntonAK.com to receive the next publication.

HUNTON
ANDREWS KURTH
DECEMBER 2020

Hot Topics for Retail General Counsel

OSHA RECORDKEEPING AND REPORTING

One of the most challenging COVID-19 legal issues has been compliance with OSHA's recordkeeping and reporting requirements. Many retail employers are exempt or partially exempt from the obligation to log work-related injuries and illnesses, but all employers are required to report any work-related fatality within 8 hours or in-patient hospitalization within 24 hours (with slight differences in some state-plan OSHA states). Determining whether a worker's COVID-19 infection is "work-related" is immensely difficult, as no layperson can determine with certainty how any employee was infected, particularly given the reality of asymptomatic transmission.

At the start of the pandemic, OSHA took the position that only certain high-risk employers had to record or report COVID-19 illnesses. In May, the agency updated its guidance and required all employers subject to its recordkeeping requirements to investigate COVID-19 infections among employees and record them if it appeared "more likely than not" that workplace exposure caused the infection. Relevant factors include evidence of clusters of infection at the workplace, the employee's working conditions and whether the employee engaged in any out-of-work activities that could have caused infection. This necessarily requires that employers contact trace positive cases in the workplace and obtain information from employees regarding their off-work possible sources of infection. This latter analysis can be fraught as many employees are reluctant to share personal life information with their employers. However, a failure to pursue these lines of questioning can leave employers with no defenses to an alleged failure to record or report COVID-19 cases.

The decision to record a COVID-19 case is consequential beyond OSHA compliance, as reporting or recording a case could be deemed an admission by the employer that the employee contracted COVID-19 at work. That admission can impair an employer's defense to workers' compensation or tort claims, making it more difficult to defend on causation, which would ordinarily be the employer's most effective defense in an alleged occupational disease case.

LOOKING AHEAD

Workplace safety regulations related to COVID-19 will continue to expand and evolve in 2021. President Joe Biden has signaled that his Department of Labor will promulgate a permanent OSHA standard for infectious disease prevention, likely preceded by a federal ETS. The vaccine rollout is also likely to breed new requirements. Retail employers will not get any relief soon from the burden of compliance with constantly evolving federal, state and local requirements related to COVID-19.

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> "'THEY ARE SMART, EXPERIENCED ATTORNEYS FROM A VARIETY OF BACKGROUNDS THAT ENABLE THEM TO PROVIDE HIGH-QUALITY LEGAL SERVICES,' SAYS ANOTHER SOURCE."
>
> – *Chambers USA*, 2020

THE METEORIC RISE OF BUY NOW, PAY LATER PLANS

"Buy now, pay later plans are booming in the Covid economy" is the headline of one CNBC article issued December 14, 2020,[1] and reality appears to be living up to the hype from what we have heard from our clients.

Investors have been convinced. In May 2020, Chinese tech giant Tencent acquired a 5 percent stake, valued at around $250M at the time of the acquisition, in buy now, pay later (BNPL) Australian public company Afterpay Limited (Afterpay).[2] In September 2020, private BNPL company Klarna Bank AT (Klarna) announced it had raised $650M in an equity funding round, at a post money valuation of $10.65B.[3] Throughout 2020, we heard from the financial press about hopes, as yet unrealized, for an initial public offering from Affirm Holdings Inc. (Affirm), a BNPL company based in San Francisco, California.[4] Other BNPL companies—Sezzle, Splitit, QuadPay, Zip Co and others around the globe—are making their own headlines, and traditional payment processors and e-commerce platforms are launching competing products such as Amex's "Pay It Plan It," PayPal's "Pay in 4" and Shopify's "Shop Pay Installments."

It would be no exaggeration to say the past few years have seen an explosion in the BNPL industry, with providers globally competing for market share. The BNPL industry is certainly benefiting from the retail shift to e-commerce brought about by COVID-19, but that does not mean brick-and-mortar operations are not also looking to BNPL initiatives to boost in-store retail sales as they face the challenges of COVID-19.

If 2020 is a guide, retailers will continue to partner with BNPL providers at the same time BNPL providers continue to jostle for market share, roll out new products and possibly adjust their products and services to respond to any scrutiny they may attract from legislators, regulators and customer advocacy groups as the industry grows and matures. If the experience of our clients is a guide, in-house counsel will continue to see their business teams requesting support for partnerships with BNPL providers well into 2021 and beyond.

This article seeks to provide a summary of insights, in question-and-answer form, that we have gained from representing clients in BNPL transactions. The goal is to help in-house counsel and their business teams identify issues early in their negotiations with BNPL providers and to help in-house counsel bring value to the negotiations.

Q. HOW MANY BNPL PROVIDERS ARE NEEDED TO SERVE A RETAIL BUSINESS?

The first thing to know about BNPL providers is that there are multiple providers to choose from. The first question a retailer should ask is what BNPL provider can bring the most value to the retailer, or to different segments of the retailer's business. BNPL providers tend to focus on specific product and service categories and a particular provider may have strengths in certain geographic markets. One BNPL provider may focus on fashion and beauty and may limit total cart value accordingly, while another BNPL provider may be focused on luxury furniture or automotive goods and support correspondingly higher-dollar cart values. A leading BNPL provider in the United States may not be the leader in Europe or another region and vice versa.

When an in-house lawyer finds him- or herself supporting a business team focused on a specific geography or segment of the retailer's business, we recommend considering whether other teams within the retailer are operating in other geographies or segments of the retailer's business and whether they could have an alternative, preferred BNPL provider. In-house counsel may need to review the agreement to ensure that it does not inadvertently limit the ability of the retailer's teams operating in other geographic markets or segments of the company from transacting with other BNPL providers.

In-house counsel should also bear in mind that established payment service providers are increasingly providing competing products to meet retail customer demand for BNPL products and services. PayPal's "Pay in 4" product offering is an example of a BNPL service offered by an incumbent payment processing services provider. Even if a business team desires to partner exclusively with one preferred BNPL provider across their business and geographies, they may need exceptions from any agreed exclusivity terms for products and services that their incumbent payment service providers bring to market. In-house counsel should remind their teams to check agreements with existing payment service providers, including other BNPL providers, to ensure there is no potential conflict with existing contractual obligations.

[1] Dickler, J. Buy now, pay later plans are booming in the Covid economy. CNBC. December 14, 2020. https://www.cnbc.com/2020/12/14/buy-now-pay-later-plans-are-booming-in-the-covid-economy.html Accessed December 2020.

[2] Tencent buys 5% stake in Australian buy-now-pay-later firm Afterpay. Reuters. May 1, 2020. https://www.reuters.com/article/us-afterpay-equity-tencent-holdings/tencent-buys-5-stake-in-australian-buy-now-pay-later-firm-afterpay-idUSKBN22D52J Accessed December 2020.

[3] Klarna (2020). Klarna announces $650M funding round to further accelerate global growth. September 15, 2020. https://www.klarna.com/international/press/klarna-announces-650m-funding-round-to-further-accelerate-global-growth/ Accessed December 2020.

[4] Farrel, M., Lombardo, C. Affirm Postpones Its Initial Public Offering. Wall Street Journal. December 12, 2020. https://www.wsj.com/articles/affirm-postpones-initial-public-offering-sources-say-11607801619?mod=article_inline Accessed December 2020.

Q. HOW ARE BNPL PRODUCTS AND SERVICES STRUCTURED?

From the perspective of retail customers, BNPL services allow a retail customer to pay only a portion of the full purchase price at checkout and pay the remainder of the purchase price over a limited period of time, usually without fees or interest if payments are made on time. The transaction with the retail customer is often structured as a loan, but it could take other forms such as an installment contract. The choice of how to structure the retail customer's transaction is typically driven by regulatory requirements and considerations in the jurisdiction where the product is offered.

From the perspective of retailers, BNPL services typically look like payment processing services. The BNPL provider typically pays the retailer the full purchase price up front, possibly less fees (alternatively, fees to be paid by the retailer will be separately invoiced), and the BNPL provider is solely responsible for collecting future payments from the retail customer, taking the risk that the retail customer defaults. The services frequently involve a technological integration to facilitate retail customer checkout (not unlike integrations with other payment processors), access to the BNPL's customer base, joint marketing to the customers of both the BNPL provider and the retailer, and access to data insights that the BNPL provider may gain from de-identified and aggregated data across its customer base. BNPL services are increasingly coupled with other fintech products, such as mobile wallets, to enable faster and more convenient checkout.

Depending on how the BNPL product is structured, and especially if the BNPL product involves the use or issuance of either a physical or virtual card to the BNPL customer that is used to process BNPL transactions, retailers will want to understand any impacts on the retailer's existing payment card processing activities. For example, if a BNPL product is structured for the BNPL user to use a prepaid card issued to the user, and the retailer processes the transactions as "prepaid cards," that may trigger different processing pricing depending on the details of the retailer's payment card processing agreement.

As recently as this year, we have seen large BNPL providers change the structure of their products to incorporate new technologies or meet regulatory requirements in jurisdictions into which they have expanded operations. As with most fintech products, the only constant right now is change.

Q. WHAT ARE THE ELIGIBLE GOODS AND SERVICES?

When considering a BNPL provider, it is important to understand that BNPL services cannot necessarily be used with all of the goods and services that a retailer provides. BNPL providers often specialize in certain goods and services and certain sizes of retail transactions and they are likely to prohibit their services from being used in connection with certain goods and services. In some cases, these limitations (such as a prohibition on using BNPL services to purchase gift cards or other cash equivalents) may be in place to prevent undesirable retail customer behavior or fraud. In other cases, limitations may be in place to align with the BNPL's commitments to corporate and environmental social responsibility. From a logistics point of view, backordered goods and other goods not delivered immediately to customers, services and returns may present challenges depending on how the BNPL and the retailer have structured their respective operations. In all these cases, retailers will want to consider how to prevent customers from using BNPL services with BNPL-restricted goods and services while managing the customer experience.

Q. HOW WILL THE PRODUCT INTEGRATE WITH EXISTING SYSTEMS?

Clients will, of course, want to understand how BNPL services will integrate with their existing systems. Retailer websites and mobile applications will certainly integrate with the BNPL's systems and technology, but there may be other systems to consider as well. If a retailer outsources fulfillment, then it may need to involve its third-party fulfillment provider in conversations with the BNPL provider to determine how BNPL systems will integrate with the third-party fulfillment provider. A retailer will want to know in advance if it will be subject to additional fees charged by its third-party fulfillment provider to integrate with a BNPL provider and provide related services. Many BNPL providers have experience integrating with retailers' third-party fulfillment providers and may be able to provide valuable support. In addition, because there may be goods and services that the BNPL provider does not allow to be purchased using its services, in-store point of sale systems may need to prevent such transactions from being processed.

Q. WILL THE BNPL PROVIDER PROCESS ANY PERSONAL INFORMATION OBTAINED FROM THE RETAILER RATHER THAN THE RETAIL CUSTOMER? WHAT DATA WILL THE BNPL PROVIDER OWN? WHAT RIGHTS WILL THE BNPL PROVIDER HAVE TO MONETIZE INSIGHTS IT MAY HAVE INTO RETAILER SALES AND REVENUES?

If a retail customer checks out using a BNPL service, then that retail customer is a customer of both the BNPL provider and the retailer. Depending on how the BNPL provider has structured their product, it may obtain all of the retail customer's relevant personal information (as defined by applicable privacy laws) directly from the retail customer when the retail customer signs up as the BNPL provider's customer. Alternatively, the retailer may be asked to provide some amount of personal information about its customers to the BNPL provider to facilitate checkout. In-house counsel will want to ensure that they understand the product structure, technological integrations and data flows between the parties in sufficient detail and enlist the advice of privacy counsel as needed to ensure compliance with applicable privacy laws.

It is also important to recognize that BNPL providers may have a window into the retailer's sales and revenue trends, industry trends and customer behavior. Retailers will want to consider if the BNPL provider will have the ability to de-identify, aggregate and use such data and how. Retailers may want to define the extent of de-identification and aggregation required before any data related to it can be used or monetized.

Q. ARE BNPL PROVIDERS REGULATED AS PROVIDERS OF CONSUMER FINANCING?

Depending on how they are structured, and the jurisdiction in which they operate, BNPL providers may be subject to lending and consumer protection laws and regulations. While recognizing the flexibility and benefits BNPL products can offer to consumers, consumer advocacy groups have also noted the tendency of BNPL products and services to increase checkout cart sizes on average and the possibility that retail customers will turn to traditional credit to meet living or other expenses if disposable cash is used instead to make BNPL installment payments.[5] The alternative paths taken in Australia and California demonstrate how approaches can vary by jurisdiction.

Australian consumers have been early and enthusiastic adopters of BNPL products and services, and, in the past few years, we have seen several bodies in Australia, including the Australian Securities and Investments Commission (ASIC), conduct reviews and inquiries. The ASIC and a Senate Select Committee on Financial Technology and Regulatory Technology recommended the industry develop a code of conduct rather than be subject to regulation under national consumer credit laws. In response, an industry group including members such as Afterpay, Brighte, flexigroup, Klarna, Latitude, Openpay, Payright and Zip Co have prepared a draft industry code, with an updated final version expected on March 1, 2021.[6]

By contrast, in the United States, the California Department of Business Oversight (CA DBO) in 2020 required Sezzle, Afterpay and Quadpay to desist and refrain from engaging in the business of a finance lender without a license.[7] In each case, the companies and the CA DBO entered into consent orders without admitting or denying engaging in any businesses without the required license. The largest penalty in any of the consent orders was less than $100,000 and the largest refund to customers was less than $1,000,000. Given the propensity of other states to follow California's lead, we would expect all BNPL providers operating in the United States to obtain lending licenses issued by the appropriate states going forward. Given the spectacular growth of the BNPL industry, we view it as quite possible that legislators, regulators and customer advocacy groups will show increased interest in investigating industry participants. At the present, however, we expect the industry to continue to grow at breakneck speed, notwithstanding regulatory risk or the concerns of consumer advocacy groups.

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[5] Evans, P. Buy now, pay later? Instalment payment services for online shopping come to Canada. CBC. November 21, 2020. https://www.cbc.ca/news/business/instalment-payment-services-canada-1.5810207 Accessed December 2020.

[6] Australian Finance Industry Association. Buy Now Pay Later Code of Practice. 2020. https://afia.asn.au/AFIA-Buy-Now-Pay-Later-Code-of-Practice Accessed December 2020.

[7] In re Sezzle, Inc., No. 60DBO-104155 (Cal. Dep't Bus. Oversight Jan. 6, 2020) (Consent Order), https://dbo.ca.gov/wp-content/uploads/sites/296/2020/01/settlement-sezzle.pdf; In re Afterpay, US Inc. (Cal. Dep't Bus. Oversight Mar. 16, 2020) (Consent Order), https://dbo.ca.gov/wp-content/uploads/sites/296/2020/03/afterpay-settlement.pdf; In re Quadpay, Inc. (Cal. Dep't Bus. Oversight April 22, 2020) (Consent Order), https://dbo.ca.gov/wp-content/uploads/sites/296/2020/04/Quadpay-Consent-Order-Final.pdf

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ABOUT US

Hunton Andrews Kurth is a global law firm of more than 1,000 lawyers handling transactional, litigation and regulatory matters for clients in myriad industries including energy, financial services, real estate, retail and consumer products and technology. Areas of practice focus include capital markets, mergers and acquisitions, intellectual property, P3, public finance and infrastructure, and privacy and cybersecurity. With offices across the United States and in Europe, the Middle East and Asia, we're aligned with our clients' businesses and committed to delivering exceptional service.

Our retail industry lawyers represent businesses at every step, from factory floor, to retail outlet, to online store. Our extensive list of international, national and regional clients includes many well-known restaurant chains, malls, home-improvement centers, supermarkets, and media and entertainment companies, as well as manufacturers and retailers of apparel, baby products, cosmetics, electronics, fine jewelry, luxury goods, toys and other merchandise. Our retail team is composed of more than 200 lawyers who represent retailers in the Fortune 500® and virtually every retail sector.

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