

SUSTAINABLE IS THE NEW BLACK: ESG IN FASHION

The fashion industry is intrinsically evolving as the most coveted patterns and textures ebb with the tide of public opinion. While these shifts occur, the physical materials that infuse excitement on red carpets and in closets around the globe often are overproduced and subsequently wasted. A similarly unglamorous subject within the industry is the global labor force that grows, harvests, and fabricates clothing materials while enduring poor working conditions, low or unlivable wages, and loss of arable land within their communities.

State and federal lawmakers have introduced legislation aiming to enforce corporate accountability and increase sustainability within fashion. We discuss three of the existing and potential regulatory and enforcement mechanisms affecting the fashion industry in the U.S. and their implications for companies in terms of disclosure, public-facing agenda or reputation, due diligence criteria, civil liability, and potential penalty exposure.

REGULATORY TRENDS IN THE FASHION INDUSTRY

The California Garment Worker Act ("SB62")

According to a 2016 study, many garment workers make less than half of California's minimum wage at less than \$6 per hour due, in large part, to the piece-rate method of compensation.¹ Even though this pay rate must comply with minimum wage requirements of the Fair Labor Standards Act ("FLSA"), employees can be subject to payment lower than minimum wage if they work for enterprises grossing under \$500,000 or if they are classified as independent

¹ Paulina Velasco, Garment workers in America's fashion capital may make just \$6 an hour. A new law could change that, *The Guardian*, Sept. 18, 2021, <https://www.theguardian.com/us-news/2021/sep/18/california-garment-worker-protection-act-wages-pay> (citing *Dirty Threads, Dangerous Factories: Health and Safety in Los Angeles' Fashion Industry*, UCLA, 2016, https://www.labor.ucla.edu/wp-content/uploads/2016/11/DirtyThreads_FINAL_web_single.pdf).

contractors.² Accordingly, labor coalitions have been advocating, rather successfully, to secure wage and labor condition protections. To protect garment workers, the California legislature recently passed SB62 to secure state minimum wages for garment workers, provide better working conditions, and compensate individuals who were incorrectly paid by their employers.³ The law enhances the powers of the state's Labor Commissioner through joint and several liability schemes as well as other non-compliance fines to compensate injured garment workers.⁴

Any garment manufacturer, brand guarantor, or contractor in the industry doing business within the state of California is subject to California's SB62.⁵ This law goes beyond capturing international fashion retailers by holding any corporation, partnership, association, wholesaler, and individual in the garment industry accountable.⁶ Specifically, producers of apparel or accessories designed or intended to be worn by any individual such as clothing, hats, and gloves are implicated.⁷ Although shoes are not listed, this type of apparel would likely fall within the scope of the law.

Companies subject to SB62 are required to register annually and remunerate employees by an hourly rate of no less than the applicable minimum wage; piece-rate pay is prohibited under SB62.⁸ Funds are disbursed at the Labor Commissioner's determination to compensate wage violations.⁹ In addition, the law mandates employers to maintain certain records pertaining to employees for a period of 4 years.¹⁰

Entities that violate the pay rate requirements will be required to pay unpaid wages and interest,¹¹ in addition to compensatory damages of \$200 per pay period in which the complaining employee is paid piece-rate.¹² They may also be liable for attorney's fees and costs,¹³ and civil penalties.¹⁴

SB62 was signed into law on September 27, 2021, and took effect on January 1, 2022. While no enforcement action has occurred to date, companies employing garment workers in California should understand the newly imposed obligations and restrictions under this law.

² FLSA, 29 U.S.C. § 203(r)(1) (defining "[e]nterprise" to exclude activities performed by independent contractors); § 203(s)(1)(A)(ii) (defining "[e]nterprise engaged in commerce or in the production of goods for commerce" to include those "whose annual gross volume of sales made or business done is not less than \$500,000"); § 206(a) (providing that such enterprises must pay workers at least \$7.25 per hour).

³ C.A. Senate Bill No. 62, Chapter 329, effective Jan. 1, 2022.

⁴ *Id.* § 6, amending Labor Code § 2673.1(a)(1); § 7, amending Labor Code to add § 2673.2(d), (f).

⁵ *See generally id.*

⁶ C.A. Senate Bill No. 62, Chapter 329, § 4, amending Labor Code § 2671(a).

⁷ *See, e.g., id.* § 4, amending Labor Code § 2671(c), (d), (f).

⁸ *See generally id.* § 8, amending Labor Code § 2675.5(a) (referring to the registration requirement); § 7, amending Labor Code to add § 2673.2(a) (regarding the payment requirement).

⁹ *Id.* § 8, amending Labor Code § 2675.5.

¹⁰ *Id.* § 5, amending Labor Code § 2673(a).

¹¹ *Id.* § 6, amending Labor Code § 2673.1(a)(1)(A).

¹² *Id.* § 7, amending Labor Code to add § 2673.2(d). The Labor Commissioner can bring an enforcement action as well. *See id.* § 7, amending Labor Code to add § 2673.2(f).

¹³ *Id.* § 6, amending Labor Code § 2673.1(a)(1)(B).

¹⁴ *Id.* § 6, amending Labor Code § 2673.1(a)(1)(C).

The New York Fashion Sustainability and Social Accountability Act ("NY A. 08352")

New York Senate bill A. 08352 would increase and enforce the disclosure and due diligence obligations on fashion retailers and manufacturers doing business in New York with an annual receipt of \$100 million or more.¹⁵ The New York proposal would also collate the money from corporate fines into a community benefit fund for environmental conservation.¹⁶ While the current draft of the bill did not pass the Committee on Consumer Affairs and Protection this session, the bill remains in Committee and lawmakers are expected to re-word it to increase its likelihood of success.¹⁷

The New York proposal defines fashion retail sellers and fashion manufacturers as business entities which list retail trade and manufacturing, respectively, as their principal business activities in the state of New York via their tax returns, and primarily sell apparel and/or footwear.¹⁸ Only fashion retail sellers and fashion manufacturers with an annual receipt that exceeds \$100 million would be implicated by the disclosure requirement.¹⁹

The New York bill would subject companies to extensive due diligence and disclosure obligations, including, but not limited to, i) mapping their supply chains from raw material to final production; ii) making disclosures on social and environmental impacts and on due diligence programs in place to address these impacts; and iii) disclosing impact reduction targets.²⁰ For prioritized risks, disclosure obligations would include i) a "quantitative baseline" and targets on energy, greenhouse gas emissions, water, and chemical management; ii) production volume, with details on materials used, including "how much production has been displaced with recycled materials"; iii) prioritized supply chain workers' wages, as compared to the applicable minimum wage and living wage; and iv) workers' rights incentives in the supply chain.²¹

Violators may be subject to civil suits instigated by the attorney general in pursuit of injunctions, monetary damages, or performance of the requirements imposed by the law, and those who remain non-compliant after three months would face fines up to 2% of annual revenues of \$450 million or more. In addition, violators would risk private enforcement actions.²² Because the attorney general would be required to publish an annual report listing the non-compliant fashion retail sellers and fashion manufacturers,²³ these companies may face reputational risks as well.

Beyond these penalties, companies may face serious reputational and pecuniary consequences when they engage in the deceptive practice of making imprecise

¹⁵ NY A. 08352 § 2, amending N.Y. Gen. Bus. Law to add § 399-mm (2).

¹⁶ *Id.* § 3, amending N.Y. State Fin. Law to add § 97-ccc (1)-(5).

¹⁷ Kate Lisa, Lawmakers eye work on Fashion Act during session recess, Spectrum News 1, Jul. 13, 2022, <https://spectrumlocalnews.com/nys/central-ny/politics/2022/07/14/lawmakers-eye-work-on-fashion-act-during-session-recess>.

¹⁸ NY A. 08352 § 2, amending N.Y. Gen. Bus. Law to add § 399-mm (1)(c)-(d).

¹⁹ *Id.* § 2, amending N.Y. Gen. Bus. Law to add § 399-mm (2).

²⁰ *Id.* § 2, amending N.Y. Gen. Bus. Law to add § 399-mm (4)(a), (b), (d).

²¹ *Id.* § 2, amending N.Y. Gen. Bus. Law to add § 399-mm (4)(c).

²² *Id.* § 2, amending N.Y. Gen. Bus. Law to add § 399-mm (5).

²³ *Id.* § 2, amending N.Y. Gen. Bus. Law to add § 399-mm (5)(i).

claims concerning their sustainability outcomes, also known as "greenwashing."²⁴ A recent class action lawsuit against international retailer H&M illustrates the risks that players within the industry are facing regarding their sustainability claims.²⁵ In that lawsuit, claimants allege that H&M engaged in false advertising when it presented its products "as environmentally-friendly when they are not."²⁶ This case is part of a growing number of lawsuits and increasing attention from regulators on climate-related disclosures. Companies should be mindful of the implications of making false, unsubstantiated, or misleading statements about the sustainability of a product, service, or operation.

The Fashion Accountability and Building Real Institutional Change ("FABRIC") Act ("S. 4213")

Consistent with a national trend of corporate disclosure and accountability, the U.S. Senate is considering a mandate akin to SB62 to enforce corporate accountability around garment workers' wages. S. 4213 aims to consolidate the social component of ESG at the federal level, targeting wage and hour protections for garment workers.²⁷ Similar to the California law, S. 4213 would outlaw the use of piece-rate pay, and penalize employers – garment contractors or manufacturers – and brand guarantors under the joint and several liability theory.²⁸ The bill would also require that garment workers receive an hourly wage according to the federal minimum wage under section 6(a)(1) of the FLSA.²⁹ S. 4213 aims to improve garment manufacturing in the U.S. by disseminating grants to eligible entities supporting domestic garment manufacturing and workforce development.³⁰

Any company engaged in garment manufacturing as an employer – including a subcontractor – or brand guarantor should be aware of the implications of falling under the purview of the bill.³¹ The concept of doing business within the U.S. is broad, as articulated by the U.S. Supreme Court,³² such that businesses in the garment industry with sufficient commercial ties and operations in the U.S. would be subject to this law. Given the broad interpretation of "doing business" in the U.S. and the heightened liability schemes for employers under this Senate bill, garment worker employees would be able to hold employers accountable even when factory owners try to skirt FLSA mandates with independent contractor employment contracts.

This law would include companies engaged in the production of clothing, hats, gloves, and other articles "intended to be worn by an individual" (likely including shoes).³³

Companies covered by S. 4213 would be required to register annually with the Department of Labor and pay employees an hourly rate no less than the federal

²⁴ See, e.g., David Adams & Karina Bashir, SEC Begins "Greenwashing" Enforcement: A Sign of Increasing Risk to Come? Clifford Chance, May 27, 2022, <https://www.cliffordchance.com/insights/resources/blogs/business-and-human-rights-insights/2022/05/SEC-begins-greenwashing-enforcement-a-sign-of-increasing-risk-to-come.html>.

²⁵ Complaint, *Commodore v. H&M HENNES & MAURITZ LP* (S.D.N.Y. 2022) (No. 7:22-cv-06247).

²⁶ *Id.*

²⁷ FABRIC Act, S. 4213, 117th Cong. (2022).

²⁸ *Id.* § 2(a)(1), amending 29 U.S.C. § 207 to add § 8(a), (c).

²⁹ *Id.* § 2(a)(1), amending 29 U.S.C. § 207 to add § 8(b).

³⁰ *Id.* § 5.

³¹ *Id.* § 2(a)(1), amending 29 U.S.C. § 207 to add § 8(c); § 2(a)(3).

³² *International Shoe Co. v. Washington*, 326 U.S. 310 (1945).

³³ FABRIC Act, S. 4213, 117th Cong., § 2(a)(1), amending 29 U.S.C. § 207 to add § 8(f)(2).

minimum wage, discontinuing piece-rate pay.³⁴ Separate from the civil penalties for businesses that fail to comply with the registration requirements, S. 4213 would allow injured employees to recover lost wages.³⁵

While the bill has support among various worker coalitions and fashion brands,³⁶ it must pass the U.S. Senate Finance Committee, and there is little indication on any member's opinion of the bill as it stands.

CONCLUSION

The fashion industry remains an appealing and marketable place for companies to grow and explore novel trends. As ESG concerns rise to the crest of the corporate accountability wave, companies should continue monitoring new laws, and proposed legislation such as S. 4213 and NY A. 08352. Moreover, businesses would satisfy investors, consumers, and any government agency now concerned with ESG metrics by upholding honesty in their reporting and maintaining appropriate compliance mechanisms.

Our Clifford Chance experts include multi-disciplinary lawyers who stand ready to address the many questions that might arise in multiple jurisdictions as companies navigate the ever-changing ESG and human rights compliance landscape.

³⁴ *Id.* § 2(a)(1), amending 29 U.S.C. § 207 to add § 8(a)-(b); § 3(b).

³⁵ *Id.* § 2(a)(3)(A)(i).

³⁶ Ana Colon, Everything you need to know about the FABRIC Act, The First Federal Fashion Bill, Fashionista, May 16, 2022, <https://fashionista.com/2022/05/fabric-act-federal-fashion-bill-explainer>.

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