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Home Depot Appeal To Test Banks' Data Breach Footing

By **Allison Grande**

Law360, New York (July 7, 2016, 9:58 PM ET) -- Home Depot on Tuesday took the somewhat unusual step of seeking permission to bring to the Eleventh Circuit several questions of law raised by a judge's refusal to toss data breach claims asserted by financial institutions, including whether the banks have standing to sue at all, a request that if granted will determine whether banks will continue to enjoy stronger footing than consumers in these disputes.

The retailer asked U.S. District Judge Thomas W. Thrash Jr. of the Northern District of Georgia to **certify for interlocutory appeal** his May order preserving the overwhelming majority of claims brought by a proposed class of financial institutions and credit unions against Home Depot in multidistrict litigation over its 2014 data breach.

Home Depot argued that the ruling raised at least six novel questions of law that would benefit from immediate resolution, including whether financial institutions have Article III standing to assert claims arising out of a data breach, whether retailers owe banks a duty to protect against third-party criminal hacks, and whether financial institutions can bring a negligence claim premised on an alleged violation of Section 5 of the Federal Trade Commission Act.

"Home Depot has raised some good questions and is trying to stake out some new ground in a few different ways," said Kevin McGinty, a member at Mintz Levin Cohn Ferris Glovsky & Popeo PC.

A Question of Standing

One significant area where the retailer is hoping to make a splash is the question of Article III standing.

Unlike consumers, who are regularly stymied in actions over payment card breaches because their losses are covered in full by banks, financial institutions have had a good deal of success in defeating dismissal bids by pointing to the steps they've taken to cover cardholders' losses.

"Issuer banks usually have stronger claims on standing than consumers do because consumers are held harmless by fraud losses by issuer banks, who have out-of-pocket losses that they can pursue," McGinty said.

The banks in the Home Depot action fit this mold, as Judge Thrash concluded in **his May ruling** that they had pled actual injuries — including the loss of money through card reimbursement, fraudulent charges and transaction fees — that gave them standing.

But Tuesday, Home Depot argued that the banks had simply lumped together a list of their injuries in six paragraphs of a 283-paragraph complaint and that no institution had alleged its own specific injuries. The retailer also contended that the banks' decision to implement "prophylactic measures" to protect against the risk of future harm was insufficient to maintain standing.

Noting that no other court has yet ruled on the standing of financial institutions to assert claims arising out of a data breach, Home Depot urged the district court to allow the Eleventh Circuit to tackle the questions of whether named plaintiffs in class actions have Article III standing without

specifying their individual injuries, and whether prophylactic measures taken to guard against losses that may never occur can establish Article III standing.

"The legal precedents in data breach litigation are evolving, especially when it comes to Article III standing issues and the precise pleading obligations and the level of 'harm' that must be alleged to withstand a motion to dismiss," said Craig A. Newman, a partner at Patterson Belknap Webb & Tyler LLP and chair of the firm's privacy and data security group. "Here — instead of a consumer class action standing issue — Home Depot is attacking the specificity of the harm alleged by each of the financial institution plaintiffs."

If the judge approves the appeal and the Eleventh Circuit elects to decide the issue, the outcome could have a substantial effect on whether claims from financial institutions continue to thrive in the wakes of major data breaches, attorneys say.

"When financial institutions sue for data breaches involving payment cards, the bulk of the damages relate to their mitigation costs rather than their reimbursement of cardholders," Hughes Hubbard & Reed LLP data privacy and cybersecurity group co-heads Dennis Klein and Seth Rothman said in a joint email. "So if Home Depot's standing argument is successful, it could substantially reduce the size and impact of these cases and shift some of the financial risks away from the retailers and to the banks issuing the cards."

The Card Settlement Process: A Way Out?

The growing frequency of these claims and the easier path that banks have so far had in pushing their cases forward were not lost on Home Depot.

In the second paragraph of its motion, Home Depot asserted that "financial institution claims are becoming more and more prevalent in the wake of a data breach." The retailer suggested that this trend was "undoubtedly due to the difficulties consumer data breach plaintiffs have establishing standing" under the U.S. Supreme Court's 2013 ruling in *Clapper v. Amnesty International*, which held that plaintiffs need to prove they have suffered actual harm or a certainly impending injury to satisfy standing requirements.

Retailers and restaurants such as Target, Kmart and Wendy's have all faced putative class actions seeking to recoup costs borne by financial institutions in the wake of headline-grabbing data breaches. Both Target and Kmart **elected to settle the actions**, while the action against Wendy's is still in its very early stages, having only been **filed at the end of April**.

The parties in the Target case reached their \$39 million settlement, which was **announced in December**, only after a Minnesota federal court refused to toss most of the litigation and the certified a class of all financial institutions that issued cards affected by the hack.

In its bid to shut down the case, which the court largely rejected in December 2014, Target focused solely on the argument that the banks had **failed to plead sufficient facts** to establish any of their claims, electing not to challenge the financial institutions' standing to bring the suit.

The move likely stemmed from the fact that the banks involved in the Target litigation had yet to go through the card brands' settlement process to recoup any losses. But as Home Depot pointed out in its motion Tuesday, the affected banks affected by its own breach had completed this exercise, making the standing calculus different from what the Target court faced.

"Because the card settlement process played out in this case before the motion to dismiss process played out, that cast the standing issue in an entirely different light from the Target case," McGinty said. "What Home Depot is essentially saying here is, 'Okay, so now that the settlement process is complete and the fraud losses and other losses from issuing cards are addressed, what else do you got?'"

If the Eleventh Circuit agrees with Home Depot's argument, banks are likely to have a much harder time leaning on their traditional argument that the losses that they bear from consumers constitute actual, lasting harm, attorneys say.

"What a ruling could do is drive the resolution process more firmly into the card settlement process," McGinty said. "Why interpose the class action process when there's an existing process in place to resolve the issues already? That doesn't benefit anyone but plaintiffs' lawyers."

The FTC Act and Banks

Aside from the standing issue, Home Depot pressed four other dicey questions of law: whether the independent duty exception to the economic loss rule under Georgia law extends to cases involving criminal data breaches, whether retailers owe financial institutions a duty to protect against third-party criminal attacks, whether a negligence per se claim can be premised on a violation of Section 5 of the FTC Act, and whether nonconsumers such as banks fall within the category of entities protected by Section 5.

While the first two questions deal with issues that are unlikely to resonate far outside Georgia, the second pair of questions could have much broader implications, attorneys say.

Section 5 of the FTC Act empowers the commission to bring claims for unfair or deceptive trade practices against a wide range of businesses, although private parties can't wield that authority. In its motion, Home Depot is asking the Eleventh Circuit to determine whether a violation of the unfairness prong of the FTC Act can give rise to a negligence per se claim, a move that Judge Thrash supported in his recent order.

The FTC has been stepping up its enforcement in data security and privacy in recent years, particularly after the Third Circuit in August **affirmed the regulator's ability** to bring such actions in a challenge to its statutory authority mounted by Wyndham Worldwide Corp. Attorneys say a ruling that plaintiffs can use Section 5 to support their private negligence claims — and that entities like banks, which are not traditionally considered consumers that the statute is intended to protect, could participate in this exercise as well — would be significant.

"It would be a big advantage for plaintiffs if the court said that they can rely on FTC pronouncements and standards as a way to establish what the duty of care is for business," McGinty said.

However, despite the apparent clarity that could be derived from the Eleventh Circuit's taking up these issues of first impression, attorneys were quick to caution that review was not a sure bet.

"By seeking an interlocutory appeal, Home Depot wants to get the appellate court's view on a number of threshold issues before moving forward in the case," Newman said. "But we'll have to wait to see if the Eleventh Circuit wants to wade into these issues at this point."

Because the district court has only ruled on the motion to dismiss and hasn't issued a final determination in the case, Home Depot must first get permission from the lower court to appeal the ruling to the Eleventh Circuit, and then the appellate court must agree to weigh in.

While courts are typically wary of sending matters up the ladder before the dispute advances past a motion to dismiss, Home Depot contended that its request "easily satisfied" the requirements for an immediate interlocutory appeal because the challenged ruling involves controlling questions of law, there is a substantial ground for difference of opinion with respect to each question, and a quick appeal could materially advance the ultimate termination of the litigation.

"There has to be something where the party has got a strong ground to say that the trial court may have gotten something wrong here and if the appeal court corrects it, that could end the case," McGinty said. "And Home Depot seems to have made a pretty strong argument here to meet those standards."

The financial institution plaintiffs are represented by Joseph Guglielmo and Erin Green Comite of Scott & Scott LLP, Gary Lynch and Jamisen Etzel of Carlson Lynch Sweet Kilpela & Carpenter LLP and Kenneth Canfield of Doffermyre Shields Canfield & Knowles LLC, as well as W. Pitts Carr & Associates PC, Conley Griggs Partin LLP, Hausfeld LLP, Carney Bates & Pulliam PLLC, Chestnut Cambronne PA, Zimmerman Reed PLLP, Kaplan Fox & Kilsheimer LLP, Beasley Allen Crow Methvin Portis & Miles PC, Murray Law Firm, Lockridge Grindal Nauen PLLP, Heins Mills & Olson PLC, Cohen

Milstein Sellers & Toll PLLC, Gillen Withers & Lake LLC and the Finley Firm PC.

Home Depot is represented by Cari Dawson and Kristine Brown of Alston & Bird LLP.

The suit is In re: The Home Depot Inc., Customer Data Security Breach Litigation, case number 1:14-md-02583, in the U.S. District Court for the Northern District of Georgia.

--Editing by Mark Lebetkin and Brian Baresch.

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