The Honorable James L. Robart

UNITED STATES DISTRICT COURT
FOR THE WESTERN DISTRICT OF WASHINGTON
AT SEATTLE

VERIDIAN CREDIT UNION, on behalf of itself and a class of similarly situated financial institutions,

Plaintiff,

v.

EDDIE BAUER LLC,

Defendant.

NO. 2:17-cv-00356-JLR

**PLAINTIFF'S MEMORANDUM OF LAW IN OPPOSITION TO DEFENDANT'S MOTION TO DISMISS FOR FAILURE TO STATE A CLAIM**

**** ORAL ARGUMENT REQUESTED****

Plaintiff Veridian Credit Union ("Plaintiff" or "Veridian") respectfully submits this memorandum of law in opposition to Defendant Eddie Bauer, LLC's ("Defendant" or "Eddie Bauer") Motion to Dismiss Plaintiff's Class Action Amended Complaint ("Complaint" or CAC"). ECF No. 40 ("Br."). For the reasons argued, the Court should deny this motion.

## I. INTRODUCTION

For its economic benefit, Eddie Bauer accepts credit and debit cards for payment from customers at its point-of-sale ("POS") registers. ¶17.[1] In January 2016, hackers accessed Eddie Bauer's inadequately protected POS systems and installed malicious software (often referred to as "malware") that infected every single Eddie Bauer store in the United States and Canada (the "Data Breach"). ¶29. With this malware, hackers stole payment card data from Eddie Bauer's

[1] All "¶" or "¶¶" citations are to the CAC. ECF No. 36.



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systems and sold it to other individuals who made massive amounts of fraudulent transactions on those payment cards. ¶¶7, 25, 29, 32, 35-36, 96-97.

Plaintiff, like the putative nationwide class of financial institutions, issued payment cards compromised in the Data Breach and suffered significant property damage to the unique data included on the payment cards (including the effective ruination of the payment card itself) and financial loss in connection with covering customers' fraud losses and reissuing the compromised cards. ¶¶8, 22, 96-98, 135. Plaintiff alleges the Data Breach and Plaintiff's injury was the foreseeable result of Eddie Bauer's minimalistic data security measures—which were known within the company to be insufficient to protect against recognized threats—and refusal to implement industry-standard security measures because they cost too much. ¶¶39-92. Plaintiff brings this action to recover its losses caused by Eddie Bauer's negligence and violations of the Washington Consumer Protection Act ("CPA") and data breach notification law, Wash. Rev. Code ("RCW") § 19.255.020, and for equitable relief.

In its motion to dismiss, Eddie Bauer argues the Court must decide now whether the law of Washington (where Eddie Bauer is headquartered) or Iowa (where Plaintiff is headquartered) governs Plaintiff's claims. Not only is this issue premature (and should be deferred until after discovery), it is irrelevant because Eddie Bauer's arguments in support of dismissal fail under either state's law.

First, Eddie Bauer seeks dismissal of the negligence claims because it purportedly had no duty to protect Plaintiff from cyber criminals. Yet, Washington and Iowa impose a common law and/or statutory duty of reasonable care to avoid creating a risk of injury to others. In the Wendy's, Home Depot, and Target data breach litigations, which involved nearly identical malware intrusions, the courts recently construed Ohio, Georgia, and Minnesota law (respectively) to impose a duty on merchants to act reasonably to protect payment card data. Moreover, the courts in these cases found that Section 5 of the Federal Trade Commission Act ("FTC Act") imposes a statutory duty on merchants not to engage in unfair practices, which the



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Federal Trade Commission ("FTC") repeatedly has determined includes the duty to maintain reasonable data security measures. Tellingly, Eddie Bauer cites ***none*** of these cases, which are factually and legally on all fours with this case.

Second, Eddie Bauer argues the economic loss doctrine bars Plaintiff's negligence claims. While this doctrine prohibits recovery in tort for purely economic losses resulting from a breach of contract, it does not apply if a legal duty exists that is independent of any contractual duty. Plaintiff does not seek damages stemming from any purported breach of contract and is not seeking to enforce a contractual duty, but instead seeks recovery for Eddie Bauer's breach of an independent duty to not create an unreasonable risk with regard to the financial institutions' payment card data. Plaintiff never contracted (directly or indirectly) for any products or services from Eddie Bauer, nor are Plaintiff's injuries attributable to the loss of the benefit of any bargain the parties made. Moreover, Plaintiff's losses are not purely economic, but also include property damage to the financial data contained on the payment cards and, concomitantly, to the payment cards themselves, which had to be cancelled and reissued. Thus, the economic loss doctrine is inapplicable.

Third, in asserting Plaintiff has no claim under the CPA or RCW 19.255.020, Eddie Bauer ignores the Complaint's allegations. Plaintiff adequately pleads these statutory violations. Finally, Plaintiff alleges in the Complaint that Eddie Bauer's data security problems are ongoing, and therefore, has adequately alleged a case or controversy under the Declaratory Judgment Act, an imminent risk of future harm, and entitlement to equitable relief. That Eddie Bauer contests the accuracy of these allegations is no basis for dismissal.

## II. FACTUAL BACKGROUND

The Data Breach was the inevitable result of Eddie Bauer's inadequate data security measures and indifferent data security approach. ¶3. Plaintiff alleges Eddie Bauer's data security measures were so minimalistic that the most inexperienced information technology ("IT") professional could identify the measures as woefully insufficient. ¶71. Despite the well-



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publicized threat of cyber-attacks targeting payment card data through POS systems and inadequately protected computer networks (including those at merchants like Wendy's, The Home Depot, Target, Kmart, and P.F. Chang's) (¶¶45-53), Eddie Bauer refused to implement best practices and upgrade critical security systems, ignored warnings about the vulnerability of its network, and disregarded or violated industry standards. ¶¶57-59, 63-70, 74-88.

Eddie Bauer used an outdated operating system for its POS environment that was highly vulnerable to attack because the manufacturer no longer provided security or technical updates, lacked adequate firewall protection and multi-factor login authentication that would have prevented damage from any attack entirely, failed to implement safety protocols or software that would have detected the Data Breach, failed to provide timely security update patches for vital software, and failed to upgrade its payment systems to use EMV technology, which would have encrypted payment card data. ¶¶39, 57-81. According to a former Information Security ("IS") Manager, Eddie Bauer ***knew*** its data security measures were inadequate, and therefore, retained an IT consultant that evaluated Eddie Bauer's POS systems and recommended that Eddie Bauer implement point-to-point encryption and tokenization to protect the POS environment. ¶¶63-65. However, Eddie Bauer refused to implement these security enhancements in light of the increased cost. ¶¶68-70. Eddie Bauer could have prevented this Data Breach had it remedied its internally well-known data security deficiencies. ¶44.

Eddie Bauer exacerbated the harm caused by its security deficiencies by failing to identify and contain the Data Breach. ¶161. The malware remained undetected within Eddie Bauer's POS system ***for six months*** – from January 2, 2016 until July 5, 2016, when third-parties first notified Eddie Bauer that an unusual number of fraudulent transactions had taken place on payment cards used at Eddie Bauer's U.S. retail locations. ¶¶1, 3, 25.[2] Despite this notice, Eddie Bauer did not acknowledge that its payment card environment had been breached for another six weeks, when

[2] Eddie Bauer suggests Plaintiff is unable to allege that any fraudulent transactions took place after hackers stole this sensitive information. Br. at n.2. This assertion is false. Plaintiff alleges that the third-party that notified Eddie Bauer of the breach did so on the basis of "a pattern of fraud on customer cards that had one thing in common: they were all used at Eddie Bauer's American retail locations." ¶25.



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it finally announced on August 18, 2016, that the company found malware on the POS systems at all of its 370 stores. ¶27. Eddie Bauer confirmed that "cardholder name, payment card number, security code and expiration date" were compromised. ¶¶31, 35-36. Plaintiff, an Iowa-chartered credit union with more than 209,000 customers located throughout the United States, including in Washington, issued compromised payment cards and has suffered significant property damage and financial loss as a result of Eddie Bauer's deficient data security approach.[3] ¶¶8, 11, 96-98, 135; *see also* Declaration of Gregory T. Slessor ("Slessor Decl."), at ¶¶ 2-6.[4]

## III. PLEADING STANDARD

On a motion to dismiss, "a complaint must contain sufficient factual matter, accepted as true, to 'state a claim to relief that is plausible on its face.'" *Ashcroft v. Iqbal*, 556 U.S. 662, 678 (2009).[5] A claim is facially plausible when the facts alleged "allow[] the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Id*.

## IV. CHOICE-OF-LAW

### A. It Is Premature to Conduct a Choice of Law Analysis.

Washington courts regularly decline to conduct a fact-intensive choice of law analysis at the motion to dismiss stage, particularly where discovery is necessary to determine the extent of the parties' contacts. *See*, *e.g.*, *Bolling v. Gold*, No. C13–0872JLR, 2015 WL 5254140, at *7 (W.D. Wash. Sept. 9, 2015) (Robart, J.); *cf. Moussouris v. Microsoft Corp.*, No. C15-1483JLR, 2016 WL 4472930, at *7-8 (W.D. Wash. Mar. 7, 2016) (Robart, J.) (deferring decision on the extraterritorial application of Washington law to nationwide class claims until after discovery where the class's contacts were not alleged). Eddie Bauer contends that performing a choice of law analysis now would conserve resources and simplify the proceedings. Br. at 9. Plaintiff

[3] Eddie Bauer claims Veridian "tacitly concedes it cannot allege any harm with specificity." Br. at n.1. Eddie Bauer simply ignores that Plaintiff pleads it "suffered losses resulting from the Eddie Bauer Data Breach related to (a) reimbursement of fraudulent charges or reversal of customer charges" and other responsive actions. ¶97.

[4] Eddie Bauer criticizes Plaintiff for amending the Complaint, asking that dismissal be with prejudice. Br. at 3. However, "[w]here claims are dismissed under Rule 12(b)(6), the court "should grant leave to amend ... unless it determines that the pleading could not possibly be cured by the allegation of other facts." *Rispoli v. King County*, No. C14-cv-00395RSM, 2014 WL 6808996, at *2 (W.D. Wa. Dec. 2, 2014).

[5] All emphasis is added and internal citations and quotation marks are omitted unless indicated.



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supports conserving judicial and litigation resources, and to that end, advocates prioritizing discovery and addressing choice of law early in the proceedings. ECF No. 46, Combined Joint Status Report at 3-4 (proposing prioritized discovery relating to choice of law).

One of Eddie Bauer's several *ad hominem* attacks on Veridian is that it "failed" to allege where Eddie Bauer's computer servers are located. Br. at 7 & n.4. However, only Eddie Bauer, which is not a public company, knows this information. More importantly, only Eddie Bauer knows the specific information about the Data Breach, including the situs of the attack vector and the location from which the data was exfiltrated. Moreover, Eddie Bauer disputes where Plaintiff's customers are located. Presently, the relevant facts pertaining to where the injury occurred and where the conduct causing the injury occurred must be obtained through discovery, which Plaintiff is committed to conducting efficiently.[6] Thus, the Court should defer ruling on choice of law until after the parties conduct discovery. *First Choice Fed. Credit Union v. Wendy's Co.* ("*Wendy's*"), No. CV 16-506, ECF No. 80 at 5 (W.D. Pa. Feb. 13, 2017), *R&R adopted*, 2017 WL 1190500 (W.D. Pa. Mar. 31, 2017); *id.*, ECF Nos. 97, 100.

**B. Even if the Court Analyzes Choice of Law, Washington Law Applies.**

If the Court conducts a choice of law analysis, it nonetheless should apply Washington law.[7] The choice of law rules of Washington, the forum state, apply in this diversity action. *Fields v. Legacy Health Sys.*, 413 F.3d 943, 950 (9th Cir. 2005). In choosing which state's law to apply, the Court must first determine whether there is an actual conflict between Washington and other applicable state laws. *Erwin v. Cotter Health Ctrs.*, 161 Wn.2d 676, 692, 167 P.3d 1112 (2007). In the absence of a conflict, Washington law applies. *Id.* If an actual conflict exists, the Court

[6] *Carideo v. Dell, Inc.*, 706 F. Supp. 2d 1122 (W.D. Wash. 2010), and *Edifecs Inc. v. TIBCO Software Inc.*, 756 F. Supp. 2d 1313 (W.D. Wash. 2010), are inapposite where, unlike here, the contacts were easily ascertained.

[7] Contrary to Defendant's argument, the choice of law analysis is relevant only to Plaintiff's negligence claims, not to its statutory claims. Br. at 5. To manufacture a conflict, Defendant recasts Plaintiff's Declaratory Judgment Act claim into one for standalone injunctive relief (which Iowa recognizes, but Washington does not). *Id.* This is a red herring. Plaintiff's Declaratory Judgment Act claim plainly is not a standalone injunctive relief claim. And, as a federal cause of action, state law does not apply to this claim. Curiously, Defendant also argues a conflict exists between Washington and Iowa consumer protection laws. Plaintiff, however, has not alleged an Iowa consumer protection claim. Plaintiff, as a non-Washington resident, may sue under the CPA and RCW 19.255.020. *Schnall v. AT & T Wireless Servs., Inc.*, 139 Wash. App. 280, 284, 161 P.3d 395 (2007).



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must determine the forum that has the "most significant relationship" to the action to determine the applicable law. *Rice v. Dow Chem. Co.*, 124 Wn.2d 205, 875 P.2d 1213, 1217 (1994).

**1. A False Conflict Exists, and Therefore, Washington Law Applies.**

An "actual conflict" exists "between the laws or interests of Washington and the laws or interests of another state" when the various states' laws could produce different outcomes on the same legal issue. *Erwin*, 161 Wn.2d at 692. As the analysis of the substantive arguments below demonstrates, a false conflict exists because the outcome is the same under both Washington and Iowa law.[8] Thus, the Court may apply Washington law.

**2. Even If a True Conflict Exists, Washington Law Still Applies.**

Where an actual conflict of laws exists, the Court must determine which "forum [ ] has the 'most significant relationship' to the action," by the test outlined in the Restatement (Second) of Conflict of Laws §145 (1971). *Johnson v. Spider Staging Corp.*, 87 Wn.2d 577, 580, 555 P.2d 997 (1976). In making this determination, courts consider: "1) the place where the injury occurred; 2) the place where the conduct causing the injury occurred; 3) the domicile residence, nationality, place of incorporation and place of business of the parties; and 4) the place where the relationship, if any, between the parties is centered." *Brewer v. Dodson Aviation*, 447 F. Supp. 2d 1166, 1175-76 (W.D. Wash. 2006). The Court's "approach is not merely to count contacts, but rather to consider which contacts are most significant and to determine where these contacts are found." *Id.* at 1176. "Where the defendant's conduct causes harm in two or more states, the 'place where the defendant's conduct occurred will usually be given particular weight in determining the state of the applicable law.'" *Kelley v. Microsoft Corp.*, 251 F.R.D. 544, 552 (W.D. Wash. 2008).

[8] Contrary to Eddie Bauer's claims, Plaintiff is not attempting to "avoid" Iowa law. Rather, Plaintiff is bringing its claims in the very forum Eddie Bauer has selected to hear actions against it and, in doing so, is invoking the law of Eddie Bauer's home state. *See* Terms of Use, http://www.eddiebauer.com/company-info/company-info-terms-of-use.jsp (users must "irrevocably and unconditionally consent and submit to the exclusive jurisdiction of" state or federal court in Washington).



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Plaintiff alleges Eddie Bauer's misconduct emanated from Washington because ultimately the affirmative decisions regarding the security of Eddie Bauer's POS system, i.e., the decision to maintain data security measures internally known to be inadequate and deprioritize data security and reject recommended improvements to conserve costs, were made by Eddie Bauer's executives in Washington.[9] ¶¶113-15. These allegations are analogous to those in *Kelley*, where the court found "Washington is the location where 'the conduct causing the injury occurred" because "Defendant developed and launched its allegedly deceptive promotional program in Washington." *Kelley*, 251 F.R.D. at 552. Thus, the second factor weighs heavily in favor of applying Washington law. The remaining factors are neutral. Eddie Bauer's negligent acts in Washington caused injury throughout the United States. ¶¶7, 99. As a result, there is "little reason in logic or persuasiveness to say that one state rather than another is the place of injury." *Kelley*, 251 F.R.D. at 552.[10] As to the third and fourth factors, the putative class is domiciled in all states, while Eddie Bauer is domiciled in Washington, and thus, "the parties' relationship is not centered in any particular place because the parties did not contract with one another." *Id.* Thus, as in *Kelley*, Washington has the most significant relationship, and the Court should apply Washington law.

[9] Eddie Bauer's claimed conceptual difficulty in understanding how a "failure to act 'emanated' from a specific place" (Br. at 7) is specious. Corporations do not run themselves. Executives meet and make decisions to act or not act in allocating the resources of the corporation.

[10] Eddie Bauer repeatedly disputes where Plaintiff's customers are located, and thus, where its injury occurred, proffering its own evidence for the Court's consideration. Br. at 7, 8 & nn. 3 & 5; ECF No. 41. As an initial matter, this argument ignores that this is a putative nationwide class action. Where Veridian's customers are located ultimately is irrelevant because the Data Breach impacted every single Eddie Bauer store, and therefore, class-member financial institutions are likely to be located throughout the United States. Second, Plaintiff's allegations must be taken as true at this stage. *Iqbal*, 556 U.S. at 678. Third, Defendant improperly offers facts, which are incomplete, to challenge Plaintiff's allegations, and thus, its request for judicial notice of Plaintiff's website (ECF No. 41) should be denied. *Lee v. City of Los Angeles*, 250 F.3d 668, 689 (9th Cir. 2001). In any event, Veridian has thousands of customers located throughout the United States, including in Washington (because although there is an Iowa membership requirement, when members relocate to other states they are not required to relinquish their membership). *See* Slessor Decl. ¶¶4-6.



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## V. ARGUMENT

### A. Veridian Adequately States a Claim for Negligence.

#### 1. Eddie Bauer Owed a General Duty of Care to Plaintiff

"The concept of duty is a reflection of all those considerations of public policy which lead the law to conclude that a plaintiff's interests are entitled to legal protection against the defendant's conduct." *Affiliated FM Ins. Co. v. LTK Consulting Servs., Inc.*, 170 Wn.2d 442, 450, 243 P.3d 521 (2010); *accord Thompson v. Kaczinski*, 774 N.W.2d 829, 834 (Iowa 2009) ("whether a duty exists is a policy decision based upon all relevant considerations that guide us to conclude a particular person is entitled to be protected from a particular type of harm"). Washington courts decide whether to impose a duty of care by balancing considerations of "logic, common sense, justice, policy, and precedent." *Affiliated FM*, 170 Wn.2d at 449. Under Iowa law,[11] "[a]n actor ordinarily has a duty to exercise reasonable care when the actor's conduct creates a risk of physical harm."[12] *Thompson*, 774 N.W.2d at 834. Only "in exceptional cases" will this duty of reasonable care not apply. *Id*. at 835. "An exceptional case is one in which 'an articulated countervailing principle or policy warrants denying or limiting liability in a particular class of cases.'" *Id*. These duty factors support recognizing a general duty of care here, and any countervailing principle or policy does not warrant denying or limiting liability.

**Risk of Physical Harm.** The Complaint alleges Eddie Bauer had a duty to employ commercially reasonable security measures because utilizing inadequate measures creates an unreasonable risk that Plaintiff's card data (and, concomitantly, the payment cards themselves) would be compromised, rendered commercially worthless, and used to make fraudulent

[11] Eddie Bauer misstates the standard for determining whether a duty exists under Iowa law. Br. at 10. In Iowa (as in Washington), ultimately "whether a duty exists is a policy decision based upon all relevant considerations that guide [the court] to conclude a particular person is entitled to be protected from a particular type of harm." *Id*. at 834. The analysis does not depend upon the application of "three distinct and necessary elements, as Eddie Bauer suggests. *Id.*

[12] The Restatement (Third) of Torts: Phys. & Emot. Harm § 4 (2010) defines "Physical harm" as "the physical impairment of the human body ('bodily harm') or of real property or tangible personal property ('property damage')." Plaintiff alleges it suffered property damage, *i.e.*, the complete and immediate obsolescence of Plaintiff's computer data associated with the compromised payment cards, which required Veridian to cancel and reissue the payment cards and take other mitigation measures. ¶¶8, 96-98, 135.



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transactions such that Plaintiff would incur substantial costs, in part, to make repairs to and replacements of its damaged property, and to reimburse its customers for fraud losses on their accounts. ¶7-8, 96-98, 135. Eddie Bauer, for its benefit, voluntarily accepts credit and debit card payments at its stores, ¶17, 88, and thus, Eddie Bauer is aware of the need to safeguard payment card data, in light of the general practices within the payment card industry and federal data security requirements. ¶¶24, 46, 87, 90-92. As an active participant in the payment card transaction process, Eddie Bauer also is aware of the threat of cyber-attacks targeting payment card data through vulnerable POS systems. ¶¶45-53. Yet, Eddie Bauer lacked the most basic security features and knew its data security measures were inadequate but refused to implement recommended security enhancements because management decided they were too expensive. ¶¶39, 57-81. Therefore, Eddie Bauer's decisions to consciously maintain data security measures internally known to be inadequate created a risk that hackers would steal payment card data, the stolen data would be used to make fraudulent transactions, and financial institutions, like Plaintiff, would be damaged. This risk was foreseeable in light of the relationship between the parties.

**Precedent.** Eddie Bauer is wrong in stating Plaintiff has failed to allege an actionable duty. Br. at 10-14, 20-23. Numerous other courts have found the exact duty to exist in similar circumstances. *See, e.g.*, *In re The Home Depot, Inc. Customer Data Sec. Breach Litig.*, 1:14-md-2583, 2016 WL 2897520, at *3 (N.D. Ga. May 18, 2016) (Applying Georgia law to hold: "A retailer's actions and inactions, such as disabling security features and ignoring warning signs of a data breach, are sufficient to show that the retailer caused foreseeable harm to a plaintiff and therefore owed a duty in tort."); *Wendy's*, ECF No. 80 at 6-7 (Applying Ohio law to hold that merchant owed a duty to issuing banks to protect cardholder data based on a general duty of care); *In re Target Corp. Customer Data Sec. Breach Litig.*, 64 F. Supp. 3d 1304, 1309-10 (D. Minn. 2014) ("*Target (FI Track)*") (Applying Minnesota law to hold the same).[13] Like these

[13] *See also Lone Star Nat'l Bank, N.A. v. Heartland Payment Sys., Inc.*, 729 F.3d 421, 426 (5th Cir. 2013) (Applying New Jersey law, reversing dismissal of card-issuing banks' negligence claim, and finding that "Heartland had reason



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cases, the Complaint alleges that Eddie Bauer created a risk, which was entirely foreseeable, that a data breach would occur and would harm Plaintiff, and thus had a duty to act reasonably. ¶¶39-92.

**Logic, Common Sense, Justice, & Policy.** Recognizing Eddie Bauer has a legal duty fulfills the underlying purposes of negligence law – compensation and deterrence – by placing the risk of financial loss on the ***only*** entity with the ability to prevent that loss. Certainly, the public has an interest in holding merchants liable to financial institutions and consumers alike for failing to meet a reasonable standard of care when handling highly sensitive payment card data. Absent a duty to protect payment card data, a merchant, such as Eddie Bauer, has a strong incentive to cut corners, take minimum precautions, and not to place data security high enough on its mission statement, while the financial institutions that issued the cards, which have no ability to protect themselves, are damaged and forced to bear the costs. On the other hand, if a duty is imposed holding merchants legally responsible when they fail to fulfill their basic duties, they will likely implement adequate data security measures to avoid paying damages. *Home Depot*, 2016 WL 2897520, at *4; *Sovereign Bank*, 395 F. Supp. 2d at 194.

Eddie Bauer argues public policy militates against imposing a duty on retailers because the contractual allocation of risk is preferable. Br. at 13-14. Yet, Eddie Bauer admits it has no contract with Plaintiff. *Id*. at 10 n.9. Because no such contracts are before the Court, it would be inappropriate to consider them at this stage. *Banknorth, N.A. v. BJ's Wholesale Club, Inc*., 394 F. Supp. 2d 283, 287 (D. Me. 2005).[14] Further, the card brand recovery processes of MasterCard

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to foresee the Issuer Banks would be the entities to suffer economic losses were Heartland negligent"); *In re Hannaford Bros. Co. Customer Data Sec. Breach Litig*., 613 F. Supp. 2d 108, 115 (D. Me. 2009*), aff'd in part, rev'd in part on other grounds sub nom., Anderson v. Hannaford Bros. Co.*, 659 F.3d 151 (1st Cir. 2011) (Applying Maine law and holding: "when a merchant is negligent in handling a customer's electronic payment data and that negligence causes an unreimbursed fraudulent charge or debit against a customer's account, the merchant is liable for that loss"); *Banknorth, N.A. v. BJ's Wholesale Club, Inc*., 394 F. Supp. 2d 283, 286-87 (D. Me. 2005) (Applying Maine law to hold that a merchant owed a duty to issuing bank "to safeguard cardholder information from thieves"); *Sovereign Bank v. BJ's Wholesale Club, Inc*., 395 F. Supp. 2d 183, 193-95 (M.D. Pa. 2005) (Applying Pennsylvania law to hold that a merchant owed a duty of care to payment card issuer to prevent unauthorized disclosure of payment card data).

[14] Defendant's cited cases also do not support a countervailing policy interest. Br. at 13 & n.13. Both *Citizens Bank of Pa. v. Reimbursement Techs., Inc.*, No. 12-1169, 2014 WL 2738220 (E.D. Pa. 2014) and *Dittman v. UPMC*, No.



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and Visa, to which Eddie Bauer alludes, do not take into account all of the damages incurred by Plaintiff and the putative class.[15]

**Custom & Voluntary Undertaking.** Imposing a duty on Eddie Bauer is consistent with industry standards – duties Eddie Bauer voluntarily assumes. Under well-established Washington and Iowa law, a person may be held liable for the negligent performance of a voluntary undertaking. *Merriman v. Am. Guarantee & Liab. Ins. Co.*, 198 Wash. App. 594, 396 P.3d 351, 363-64 (2017); *McCormick v. Nikkel & Assocs., Inc.*, 819 N.W.2d 368, 375 (Iowa 2012). Plaintiff alleges Eddie Bauer, as an active participant in the payment card industry, assumed the duties recognized by such industry to protect payment card data. ¶¶83-87; *Target (FI Track)*, 64 F. Supp. 3d at 1310 (discounting the burden of imposing a duty on merchants because they have "voluntarily assumed similar duties"). Thus, when a company, such as Eddie Bauer, through the ordinary course of its business (and for its economic benefit) receives, gathers, and stores payment card data, it has undertaken to take action necessary for the protection of that property, and therefore has an affirmative duty to take reasonable efforts to provide security for that property. *See, e.g.*, *Merriman*, 396 P.3d at 363-64.

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GD-14-003285, 2015 WL 4945713 (Pa. C.P. Civ. Div. 2015) involve dissimilar facts that shed no light on whether a merchant owes a duty to protect the computer data that resides on payment cards, which the merchant affirmatively chose to accept (for its own economic advantage) with the knowledge that the financial institutions that issued the payment cards would suffer significant damage if the computer data was misappropriated. Furthermore, in finding no duty to safeguard personal information, the courts in *Dittman*, 2015 WL 4945713, at *4-5, and *Dig. Fed. Credit Union v. Hannaford Bros.*, No. BCD-CV-10-4, 2012 WL 1521479, at *3 (Me. B.C.D. 2012), relied (in part) on the state legislatures' decision to limit the rights of individuals for the protection of personal information. Here, the Washington legislature provides a private right of action to financial institutions that have to replace the payment cards of their Washington customers. *See* RCW 19.255.020(3)(a). The *Dittman* Court's discussion of whether a duty exists also is *dicta*, and therefore, the case is even less persuasive. 2015 WL 4945713, at *3. *In re Heartland Payment Sys., Inc. Customer Data Sec. Breach Litig.*, No. H-10-171, 2011 WL 1232352, at *2-3 (S.D. Tex. Mar. 31, 2011), also is factually distinguishable where the plaintiff financial institutions, unlike here, were in contractual privity with the defendant acquiring banks, and the relevant contracts were part of the record. Furthermore, *Heartland's* persuasiveness is diminished where the Fifth Circuit reversed the district court's dismissal of card-issuing banks' negligence claim in a companion case in the MDL, rejecting the district court's holding that card-issuing banks could not bring common law tort claims against another participant in the payment card system where, like here, the contractual relationships were unclear. *Lone Star*, 729 F.3d at 426-27.

[15] These discretionary recovery processes only include compensation for "operational" losses, which focus on partial re-issuance costs, and partial "fraud" losses. Importantly, the card brand recovery processes are not intended to provide anything close to full compensation, even for those two categories. For example, Visa's regulations state: "An Issuer in Visa Inc. or the Visa Europe Territory may recover a portion of its estimated Incremental Counterfeit Fraud losses and operating expenses resulting from an Account Data Compromise Event…." https://usa.visa.com/dam/VCOM/download/about-visa/15-April-2015-Visa-Rules-Public.pdf.



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This case is not about an unforeseeable, third-party criminal act. It is a straightforward negligence case, and the sole focus is Eddie Bauer's conduct. In failing to maintain reasonable security measures, Eddie Bauer (not a third-party criminal) created a risk of the harm that occurred and Plaintiff was the foreseeable victim of that harm. Plaintiff alleges Eddie Bauer breached its duty to implement non-negligent, commercially reasonable data security measures, enabling third-party criminals to steal payment card data and harm Plaintiff by rendering obsolete the unique data stored on the payment cards, thereby necessitating their cancellation and replacement, as well as by causing Plaintiff to incur substantial fraud loss reimbursement obligations to its customers. ¶¶93, 125-26, 131.[16]

Eddie Bauer wrongly asserts a "special relationship" must exist between it and Plaintiff to be liable for a third-party criminal act. Br. at 11-13. This is not true under Washington and Iowa law. *Parrilla*, 138 Wash. App. at 437 (rejecting argument that a duty to guard against criminal conduct may only arise when there is a special relationship); *Galloway v. Bankers Trust Co.*, 420 N.W.2d 437, 438 (Iowa 1988) (basing duty determination on foreseeability of criminal activity with no discussion of special relationship). Eddie Bauer claims it "was entitled to assume that others would obey the law and refrain from gaining unauthorized access into its computer system to steal customers' payment card information." Br. at 13. This also is wrong. *Parrilla*, 138 Wash. App. at 437 (rejecting that "criminal conduct is not unforeseeable as a matter of law"); *Galloway*, 420 N.W.2d at 440 (holding foreseeability may be based on "crimes in general"). Because Eddie Bauer's decisions deprioritizing data security exposed Plaintiff to a nearly-inevitable risk of injury, a duty existed without a "special relationship." *Parrilla*, 138 Wash. App. at 439 ("a duty to guard against a third party's foreseeable criminal conduct exists where an actor's own affirmative act has created or exposed another to a recognizable high degree of risk of harm through such misconduct, which a reasonable person would have taken into account.");

[16] "[I]n keeping with the general rule that an individual has a duty to avoid reasonably foreseeable risks, if a third party's criminal conduct is reasonably foreseeable, an actor may have a duty to avoid actions that expose another to that misconduct." *Parrilla v. King Cty.*, 138 Wash. App. 427, 437, 157 P.3d 879 (2007); *accord Tenney v. Atl. Assocs.*, 594 N.W.2d 11, 21 (Iowa 1999).



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*Galloway*, 420 N.W.2d at 438-40 (business has a duty to take reasonable steps to protect customers from criminal acts if criminal acts are reasonably foreseeable).[17] Even if a "special relationship" is required, that relationship exists because Defendant voluntarily assumed the duty to protect Plaintiff's property, *i.e.* its payment card data, and Plaintiff relied on Defendant to keep its property safe. *See, e.g.*, *Merriman*, 396 P.3d at 363-64.

**2. Eddie Bauer Owed a Statutory Duty of Care to Plaintiff**

In Washington, the breach of a statutory duty is evidence of negligence. *Mathis v. Ammons*, 84 Wash. App. 411, 418, 928 P.2d 431, 435 (1996), *as amended on denial of reconsideration* (Jan. 21, 1997). If a statute imposes a duty on a defendant, that duty is "additional to, and different from, the duty to exercise ordinary care." 84 Wash. App. at 416. Similarly, Iowa law provides that a statutory violation can support a negligence *per se* claim.[18] *Winger v. CM Holdings, L.L.C.*, 881 N.W.2d 433, 448 (Iowa 2016). Whether denominated as a violation of a statutory duty of care or negligence *per se*, the elements for establishing such a duty or claim are the same. A plaintiff must show that the statute provides a standard of conduct, the plaintiff is within the class of persons the statute was intended to protect, the interest invaded is the kind the statute was intended to protect, and the harm suffered is the kind the statute was intended to prevent. *Mathis*, 84 Wash. App. at 416; *Winger*, 881 N.W.2d at 448.

**(a) Section 5 of the FTC Act Provides a Standard of Conduct.**

Eddie Bauer incorrectly argues Plaintiff fails to allege a violation of a statutory duty of care or a negligence *per se* claim. Several cases, including two in the data breach context, have recognized a claim for negligence *per se* under Section 5 of the FTC Act. *Home Depot*, 2016 WL 2897520, at *4 (holding that the complaint adequately states a claim for negligence *per se* based on a violation of Section 5); *Wendy's*, ECF No 80 at 7-8 (same); *Bans Pasta, LLC v. Mirko Franchising, LLC*, No. 7:13-cv-00360-JCT, 2014 WL 637762, at *14 (W.D. Va. Feb. 12, 2014)

[17] Defendant's cited cases (Br. at 13 n.13, 22-23) are inapposite because, unlike here, they lacked allegations of foreseeability and were based solely on the defendant's failure to act.

[18] Washington does not recognize a negligence *per se* claim, but the allegations are relevant to whether a statutory source of duty supports Plaintiff's negligence claim.



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(ruling that the plaintiff adequately pled its claim for negligence *per se* based on an FTC rule); *Legacy Acad., Inc. v. Mamilove, LLC*, 761 S.E.2d 880, 892 (Ga. Ct. App. 2014) (same), *vacated on other grounds*, 777 S.E.2d 731 (Ga. Ct. App. 2015). Like in *Home Depot* and *Wendy's*, the Complaint adequately alleges a statutory duty of care/negligence *per se* claim based on a violation of Section 5 because Section 5 imposes a sufficiently clear standard of conduct and because Plaintiff is within the class of persons the FTC Act protects.

Eddie Bauer argues that Section 5 is vague and does not establish a "sufficiently absolute and specific standard" to which it must adhere. Br. at 15. The Third Circuit rejected this precise argument in a data security case. *FTC v. Wyndham Worldwide Corp.*, 799 F.3d 236, 255-58 (3d Cir. 2015) (holding that Section 5 "is not so vague as to be no rule or standard at all[,]" and it sufficiently "informs parties that the relevant inquiry here is a cost-benefit analysis…that considers a number of relevant factors[.]")

Like the defendants in *Wyndham*, Eddie Bauer was required to comply with industry standards and the FTC's guidelines and consent orders requiring that Eddie Bauer use reasonable measures to protect payment card data, as described in Plaintiff's Complaint. ¶¶89-92. These standards, guidelines, and consent orders provide adequate means to measure whether Eddie Bauer violated Section 5's standard of conduct. *Wyndham*, 799 F.3d at 258.

**(b) Plaintiff Is Within the Class of Persons the FTC Act Protects.**

Plaintiff falls within the class of persons the FTC Act protects. *Home Depot*, 2016 WL 2897520, at *4; *Bans Pasta*, 2014 WL 637762, at *13; *Legacy Acad.*, 761 S.E.2d at 892-93; *see also Wyndham*, 10 F. Supp. 3d at 625 (commenting on FTC's position that a violation of its standards "is likely to cause substantial consumer injury…to consumers and businesses"). Both the FTC and courts consistently have applied Section 5 to practices harming businesses.[19] The

[19] *See, e.g., FTC v. World Wide Factors, Ltd.*, 882 F.2d 344, 346-47 (9th Cir. 1989) (affirming preliminary injunction against a seller of promotional merchandise to small businesses); *Lee v. FTC*, 679 F.2d 905, 906 (D.C. Cir. 1980) (upholding order against company providing promotional services to investors); *U.S. Retail Credit Ass'n, Inc. v. FTC*, 300 F.2d 212 (4th Cir. 1962) (affirming order against corporation offering debt collection services to businesses and professionals); *U.S. Ass'n of Credit Bureaus, Inc. v. FTC*, 299 F.2d 220 (7th Cir. 1962) (modifying



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"consumer injury" element includes harm to businesses. *FTC v. Sperry & Hutchinson Co.*, 405 U.S. 233, 248 (1972). Thus, Plaintiff is within the wide scope of persons the FTC Act protects.

Further, Plaintiff is in direct contact with consumers—its own customers—and is required to notify those customers when their cards are compromised, investigate claims of fraudulent activity, and refund fraudulent charges. ¶¶8, 135. Thus, there is a significant nexus between Plaintiff and consumers injured by the Data Breach. Therefore, Plaintiff not only is itself an entity the FTC Act was intended to protect but also is inextricably intertwined with consumers whom the FTC Act also was intended to protect.

With little explanation, Eddie Bauer disputes that Plaintiff is not within the class to whom Eddie Bauer owes a duty. Br. at 21-22. However, this argument appears to be aimed at whether the alleged harm was foreseeable, which is a question for the jury. *Christen v. Lee*, 113 Wash.2d 479, 492, 780 P.2d 1307 (1989); *Thompson*, 774 N.W.2d at 835. Eddie Bauer also seeks to rely on a web of contractual relationships within the payment card industry to exculpate it from liability. Again, as stated above, the card brand recovery processes of MasterCard and Visa—the implementation of which are entirely within the discretion of the card brands—do not prohibit or prevent litigation to recover the losses Plaintiff seeks. And Defendant's argument that Plaintiff is a "sophisticated financial institution" (Br. at 21) does not change the fact that Plaintiff was not aware of Eddie Bauer's deficient data security measures—Eddie Bauer was. It is Eddie Bauer's deficient data security that caused Plaintiff and the putative class harm, and it should be held accountable.

**(c) The CPA and RCW 19.255.020 Provide a Statutory Duty of Care.**

Because the CPA is modeled on the FTC Act and Washington courts look to FTC precedent for guidance, *Panag v. Farmers Ins. Co. of Wash.*, 166 Wn.2d 27, 47, 204 P.3d 885 (Wash. 2009); RCW 19.86.920, the CPA also provides a statutory duty of care. *See* §V.B, *infra*.

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and enforcing order against provider of collection services to businesses); *FTC v. Kitco of Nev., Inc.*, 612 F. Supp. 1282, 1296-97 (D. Minn. 1985) (issuing permanent injunction entered against the seller of business opportunities).



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Section 19.255.020 requires businesses to take reasonable care to guard against unauthorized access to account information. *See* RCW 19.255.020(3)(a); 2010 Wash. Legis. Serv. Ch. 151 §1 (S.S.H.B. 1149) (West) ("[T]he legislature intends to encourage financial institutions to reissue credit and debit cards to consumers when appropriate, and to permit financial institutions to recoup data breach costs associated with the re-issuance from large businesses and card processors who are negligent in maintaining or transmitting card data."). Section 19.255.020 plainly provides a standard of conduct, Plaintiff, a financial institution, is within the class the statute intends to protect, the integrity of card data is the interest the statute was intended to protect, and losses associated with compromised payment card data is the harm the statute was intended to prevent.

**3. Eddie Bauer Proximately Caused Plaintiff's Damages.**

Defendant argues that the acts of the third-party hackers constituted a superseding cause that breaks the chain of causation. Br. at 22.[20] However, "[w]hether an act may be considered a superseding cause sufficient to relieve a defendant of liability depends on whether the intervening act can reasonably be foreseen by the defendant; only intervening acts which are not reasonably foreseeable are deemed superseding causes." *Crowe v. Gaston*, 134 Wash. 2d 509, 520, 951 P.2d 1118, 1122 (1998); *see also Hollingsworth v. Schminkey*, 553 N.W.2d 591, 598 (Iowa 1996) ("[F]or an act or force to be a superseding cause, thereby relieving a negligent defendant from liability, the intervening force ***must not have been reasonably foreseeable***."). "An intervening act is not foreseeable if it is 'so highly extraordinary or improbable as to be wholly beyond the range of expectability.'" *Crowe*, 951 P.2d at 1122. "The foreseeability of an intervening act . . . is ordinarily a question of fact of the jury." *Crowe*, 951 P.2d at 1122; *Haumersen v. Ford Motor Co.*, 257 N.W.2d 7, 15 (Iowa 1977). The data breach here was certainly not highly extraordinary or improbable. Indeed, as explained above, Plaintiff has sufficiently alleged the foreseeability

[20] Defendant's causation argument rests on an inapposite case outside the data breach context. The attenuated causal link between the defendant's conduct (the failure of parents to properly rear and supervise their children) alleged in *Smith v. Shaffer*, 395 N.W.2d 853 (Iowa 1986) and the car accident that led to the death of the plaintiff's decedent is wholly dissimilar from this case and does not advance Defendant's argument.



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(indeed, inevitability) of the data breach given Defendant's failure to adequately secure its data networks.

**4. The Economic Loss Rule Does Not Bar Plaintiff's Negligence Claim.**

Under either Washington or Iowa law, Plaintiff's claims, which are not based upon a contract and involve injury to property, are not barred by the economic loss rule. First, under Washington law, as Eddie Bauer acknowledges, courts no longer recognize an "economic loss rule," and instead apply the "independent duty doctrine." Br. at 4 (citing *Affiliated FM Ins.*, 243 P.3d at 526. Under that doctrine, "an injury is remediable in tort if it traces back to the breach of a tort duty arising independently of the terms of the contract." *Donatelli v. D.R. Strong Consulting Engineers, Inc.*, 312 P.3d 620, 624 (Wash. 2013) (quoting *Eastwood v. Horse Harbor Found., Inc.*, 241 P.3d 1256, 1256, 1262 (Wash. 2010) (quotation marks and alterations omitted). Because the doctrine's application depends on whether a duty exists *independent* of a contract, "[t]he analytical framework provided by the independent duty doctrine is only applicable when the terms of the contract are established by the record." *Donatelli*, 312 P.3d at 624. Here, Plaintiff alleges that Eddie Bauer owed it a common law duty of care in the handling of payment card data, and there are no contracts between the parties in the record.[21] Therefore, if the Court recognizes that Eddie Bauer owed Plaintiff a legal duty of care in processing and storing payment card data, Plaintiff's negligence claim is not barred by Washington's independent duty doctrine.

While Iowa recognizes the economic loss rule, it is nevertheless inapplicable to Plaintiff's claims here because of the lack of contractual privity between the parties and because the losses claimed by Plaintiff are for injury to its property, i.e., the payment card information and the payment cards themselves. In *Annett Holdings, Inc. v. Kum & Go, L.C.*, 801 N.W.2d 499 (Iowa 2011), the Supreme Court of Iowa stated that the economic loss rule bars recovery of purely economic losses in negligence actions "***[a]s a general proposition.***" *Id.* at 503. While the *Annett* Court's discussion of the rule is relevant, the plaintiff had entered into a contract pursuant to

[21] Indeed, Eddie Bauer plainly concedes that there is no alleged contractual privity. Br. at 12 n. 9 ("The Amended Complaint does not allege Veridian had any contractual agreement with Eddie Bauer."))



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which it agreed to be responsible for the exact type of losses it was seeking in its lawsuit.[22] That is not the case here.

As the Iowa Supreme Court has explained, the rationales for the economic loss rule are to prevent the "tortification of contract law", *id.*, and that "[p]urely economic losses usually result from the breach of a contract and should ordinarily be compensable in contract actions, not tort actions." *Pitts v. Farm Bureau Life Ins. Co.*, 818 N.W.2d 91, 97 n. 4 (Iowa 2012); *see also Van Sickle Const. Co. v. Wachovia Commercial Mortg., Inc.*, 783 N.W.2d 684, 692 (Iowa 2010) ("The economic loss doctrine was conceived to prevent litigants with contract claims from litigating them inappropriately as tort claims."). To the extent that the rule is intended to ensure that parties' rights and duties are controlled by their written agreement, it does not sensibly fit here because, as discussed above, Plaintiff and Eddie Bauer are not in contractual privity, nor was Plaintiff in a "contractual chain of distribution leading to the defendant" with respect to any products or services. *Annett*, 801 N.W.2d at 505; *Pitts*, 818 N.W.2d at 94 & 97, n.4 (indicating in dicta that the economic loss rule may be inapplicable when "there is no chain of contracts between [plaintiff] and [defendant]… [Defendant's] alleged negligence was the direct cause of the loss suffered by [plaintiff].").[23]

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[22] *Annett* involved a negligence claim by a trucking company parent against a defendant-convenience store stemming from the fraudulent use of a fuel credit card by a trucking company employee at one of the defendant's convenience store locations. *Annett*, 801 N.W.2d at 500–501. Notably, the plaintiff-trucking company parent in *Annett* had a written agreement with the credit card issuer, which provided that the ***plaintiff*** would be "fully responsible" for any fraudulent or unauthorized use of the fuel credit cards. *Id.* at 505. The defendant convenience store, in turn, had a written agreement with the credit card issuer. *Id.* at 501. Thus, the plaintiff's negligence claim against the defendant was based on precisely the type of unauthorized use contemplated by its written agreement with the credit card issuer, causing a loss that the plaintiff had explicitly assumed responsibility for. That is simply not the case here, as Plaintiff is not seeking to recover losses for which it contractually agreed to be responsible for in a written agreement with a third party.

[23] Although the "stranger economic loss rule," has been applied in some cases involving parties *not* in privity, *Annett*, 801 N.W.2d at 504, those cases turned on reasoning different from maintaining the separation of tort and contract law. For instance, *Nebraska Innkeepers, Inc. v. Pittsburgh-Des Moines Corp.* involved negligence claims brought by local business owners against a contractor that had allegedly built a defective public bridge, causing closure of the bridge and loss of business, wages, and investment value in the affected area. 345 N.W.2d 124, 125–26 (Iowa 1984). After reviewing similar bridge-related cases, the Iowa Supreme Court rejected the claim for several reasons, including the remote and tenuous connection between the negligent act and the resulting damages (i.e., proximate causation), *see id.* at 126–28, and reluctance to open a door to potentially unlimited liability, *see id.* at 128. Notably, the court recognized that the plaintiffs' claims would not have been foreclosed if they had suffered direct damages to property. *Id.* at 126, 128. In *Annett*, the dissenting opinion correctly noted that with respect to the holding of *Nebraska Innkeepers*, "we did not adopt the economic loss rule. We applied the proximate-cause-remoteness



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Plaintiff never contracted (directly or indirectly) for any products or services from Eddie Bauer, nor are Plaintiff's injuries attributable to the loss of the benefit of any bargain Plaintiff made with Eddie Bauer. Although both parties had contracts with the payment card brands, no such contracts are before the Court and it would be inappropriate to consider them at this stage. *See Banknorth*, 394 F. Supp. 2d at 287. Plaintiff alleges that Eddie Bauer owed it a common law duty to act without negligence in processing and storing payment card information. Plaintiff has alleged that the risks of providing inadequate data security, and the accompanying threat of a data breach, were foreseeable and well known to Eddie Bauer. ¶¶46, 52–56, 72, 83, 121. This is simply not a case where the court needs to be wary of Plaintiff attempting to enforce contractual obligations through a tort action.

The economic loss rule is also inapplicable here because Plaintiff has suffered actual property damage.[24] Plaintiff's payment card data and the payment cards holding that data have been rendered unusable because of Eddie Bauer's negligence. Payment card data—which enables the use of payment cards by consumers in the market place—is highly valuable (¶83) and absolutely integral to Plaintiff's operations. The use of unique, uncompromised payment card identifying data is Plaintiff's only means of authenticating the cardholder and authorizing a transaction. *See* Michael J. Zamorski, *Financial Institution Letters: Authentication In An Electronic Banking Environment*, FDIC.GOV (Aug. 24, 2001), https://www.fdic.gov/news/news/financial/2001/fil0169a.html. Due to Eddie Bauer's negligence, the integrity of Plaintiff's payment card data was compromised when it was improperly accessed and used to commit

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doctrine and called it the economic loss rule." *Annett*, 801 N.W.2d at 508 (Wiggins, J., dissenting). In this case, although Plaintiff and Defendant were not in contractual privity, Plaintiff's payment card data was processed and possessed by Eddie Bauer, the risks posed by inadequate protection of that data were foreseeable, and the damages suffered by Plaintiff were the direct result of the Data Breach. Thus, the reasons the "stranger economic loss rule" was applied in cases such as *Nebraska Innkeepers* do not support extending the rule to bar Plaintiff's negligence claim here.

[24] *E.g.*, *Audio Odyssey Ltd. V. United States*, 243 F. Supp. 2d 951, 961 (S.D. Iowa 2003) ("[T]he 'pure economic loss' doctrine . . . bars recovery in negligence claims absent physical harm.").



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fraudulent transactions.[25] ¶¶94–98. As a result, Plaintiff's payment card data, and the payment cards on which such data was contained, were rendered commercially useless for the purpose for which that data was intended (i.e., was damaged). Therefore, Plaintiff had to cancel its customers' payment cards and reissue them with new identifying numbers and magnetic strip information. ¶96.

Courts recognize electronically stored data to be "property" that can be "damaged," particularly in the insurance and criminal law contexts. *See Am. Guarantee & Liab. Ins. Co. v. Ingram Micro, Inc.*, No. 99- 185 TUC ACM, 2000 WL 726789, at *2 (D. Ariz. Apr. 18, 2000) ('"[P]hysical damage' is not restricted to the physical destruction or harm of computer circuitry but includes loss of access, loss of use, and loss of functionality."); *see also Se. Mental Health Ctr., Inc. v. Pac. Ins. Co., Ltd.*, 439 F. Supp. 2d 831, 837-38, (W.D. Tenn. 2006) (finding that the corruption of computer data, as result of a power outage, constitutes physical damage requirement under business interruption policy language). The Iowa and Washington state criminal codes both recognize that computer data is "property" that can be damaged or rendered useless by criminal acts. *See* Iowa Code Ann. § 702.14 ("'Property' is anything of value, whether publicly or privately owned, including but not limited to computers and computer data, computer software, and computer programs.")[26]; § 702.1A(10) ("'Loss of services' means the reasonable value of the damage caused by the unavailability or lack of utility of the property or services involved until repair or replacement can be effected."); RCW 9A.04.110(22) ("'Property' means anything of value, whether tangible or intangible, real or personal"); RCW 9A.48.100(1) (defining "physical damage" to include "impairment, interruption, or interference with the use of

[25] *See* Ioana Vasiu and Lucian Vasiu, PhD, MBA, *Break on Through: An Analysis of Computer Damage Cases*, 14 J. TECH. L. & POL'Y 158 (2014) (defining "integrity" of data).

[26] "Computer data" is further defined in the Iowa Code as "a representation of information, knowledge, facts, concepts, or instructions that has been prepared or is being prepared in a formalized manner and has been processed, or is intended to be processed in a computer. Computer data may be in any form including, but not limited to, printouts, magnetic storage media, punched cards, and as stored in the memory of a computer." Iowa Code Ann. § 702.1A(3).



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… records, information and data" as well as the "diminution in value of any property as the consequence of an act and the cost to repair any physical damage.").

Computer data that lacks integrity, and therefore is rendered unusable, also is considered "damaged property" under federal computer crime statutes. *See* 18 U.S.C. § 1030(e)(5), (8), (11). Because federal law and Iowa and Washington state law all include computer data as legally recognized property in the criminal context, the same definitions for property and property damage should apply in a civil setting. Indeed, in opining that computer data is "property" that can be "damaged," the *Ingram Micro* Court cited both federal and state criminal codes in support of its decision. *Ingram Micro*, 2000 WL 726789, at *2. As such, Plaintiff has suffered actual property damage recoverable outside the confines of the economic loss doctrine.[27] *See, e.g.*, Restatement (Second) of Torts §§ 919, 927.

**B. Veridian States a Valid Claim for Violation of the CPA.**

To prevail on a claim under the Washington Consumer Protection Act, a plaintiff must show existence of: (1) an unfair or deceptive act or practice, (2) occurring in trade or commerce, (3) affecting the public interest, (4) injury to a person's business or property, and (5) causation. *Hangman Ridge Training Stables, Inc. v. Safeco Title Ins. Co.*, 105 Wn.2d 778, 780 (1986). Defendant moves to dismiss Plaintiff's CPA claims on the grounds Plaintiff failed to plead a deceptive or unfair act. Because Defendant's data security practices put Plaintiff and other institutions that issue payment cards at substantial risk from theft of card information, and because neither Plaintiff nor consumers could reasonably avoid this risk, Plaintiff has stated a valid CPA claim.

[27] In a recent opinion, a federal district court in Colorado held that the economic loss rule applied to bar a negligence claim brought by a credit union against a restaurant chain in a factual context similar to this case. *See SELCO Comm. Credit Union v. Noodles & Co.*, No. 16-cv-2247, slip op. at 12 (D. Colo. July 21, 2017). The court in *SELCO*, however, did not analyze whether stolen payment card data constitutes physical property for purposes of the economic loss rule. *See generally id.* Instead, the court rested its decision on a finding that "Plaintiffs have … failed to direct the Court's attention to any duties of care [defendant] may have breached that differed from the duties arising out of its contracts." *Id.* at 3 (quotation marks, alternations, and citation omitted).



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The CPA prohibits unfair and deceptive business practices. RCW 19.86.020. Unfair acts alone, even acts that are not deceptive, can be the basis for a Washington CPA claim. *Klem v. Wash. Mut. Bank*, 176 Wn.2d 771, 787, 295 P.3d 1179 (2013) ("[A]n act or practice can be unfair without being deceptive…The 'or' between 'unfair' and 'deceptive' is disjunctive. . . . Our statute clearly establishes that unfair acts or practices can be the basis for a CPA action."). Often, the factual analysis as to whether an act is unfair or deceptive overlap. *FTC v. Wyndham Worldwide Corp.*, 799 F.3d 236, 245 (3d Cir. 2015).

The CPA does not define what qualifies as an "unfair or deceptive act," but directs courts to look to FTC precedent for guidance. *Panag*, 166 Wn.2d at 47; RCW 19.86.920. Additionally, courts look to the CPA's purpose—which is intended to protect the public and foster fair and honest competition—and liberally construes the provisions of the CPA to further that purpose. *Panag*, 166 Wn.2d 27, 37 (2009); RCW 19.86.920.

**1. Plaintiff Properly Alleges an Unfair Practice Because Eddie Bauer's Inadequate Data Security Practices were Likely to Cause Substantial Harm to Financial Institutions.**

Under Section 5 of the FTC Act, a "practice is unfair [if it] causes or is likely to cause substantial injury to consumers which is not reasonably avoidable by consumers themselves and is not outweighed by countervailing benefits." 15 U.S.C. § 45(n). Because a practice may be unfair if it is "likely" to cause substantial injury, the FTC Act includes actions for injuries that have not yet manifested. *In re LabMD, Inc.*, 2016 WL 4128215, at *9 (F.T.C. July 29, 2016). In determining whether a practice is "likely to cause a substantial injury," courts "look to the likelihood or probability of the injury occurring and the magnitude or seriousness of the injury if it does occur." *Id.*

Applying this standard, the FTC has found that failure to provide reasonable cyber security measures constitutes an unfair act under Section 5 of the FTC Act, 15 U.S.C. § 45. *See In re LabMD Inc.*, 2016 WL 4128215, at *32. In *In re LabMD*, the FTC found that the defendant "failed to use an intrusion detection system or file integrity monitoring; neglected to monitor



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traffic coming across its firewalls; provided essentially no data security training to its employees; and never deleted any of the consumer data it had collected." *Id.*, at *1. The FTC concluded these inadequate data security practices were "unfair" practices within the meaning of the FTC Act because they were likely to cause substantial harm, which could not reasonably be avoided by consumers, and were not outweighed by countervailing benefits. *Id.*, at *17, 21-24. Similarly, in *FTC v. Wyndham Worldwide Corp.*, 799 F.3d 236, 241, 247 (3d Cir. 2015), the Third Circuit held that the Wyndham hotel company's various inadequate data security practices, including a failure to implement adequate policies regarding the storage of payment card information, could constitute an unfair act under the FTC Act.

Like in *LabMD* and *Wyndham*, Plaintiff here sufficiently pleads that Eddie Bauer's inadequate data security measures constitute unfair practices. ¶¶155, 157-58. Plaintiff's allegations of Eddie Bauer's data security failures are nearly identical to those alleged in *LabMD* and *Wyndham* and constitute practices "likely to cause substantial injury" to financial institutions that issued payment cards to consumers, whose card information was put at unreasonable risk of theft. *See Home Depot*, 2016 WL 2897520, at *5-7 (declining motion to dismiss state consumer protection act claims, including a CPA claim, in data breach action brought by financial institutions because plaintiffs adequately alleged defendant's inadequate security practices constituted an unfair act).

Specifically, Plaintiff has alleged that Eddie Bauer failed to take proper measures to protect data security regarding its POS and data security systems, failed to implement EMV chip card technology, and failed to comply with industry security standards and PCI DSS. ¶¶5, 39, 40-42, 57-62, 71-76, 81, 82-86, 157. In light of the known risk of cyber breaches involving payment card networks and systems, it was foreseeable that the failure to take reasonable security measures to protect this data would result in harm to the payment card issuers. ¶¶8, 9, 46-51, 83. Moreover, Eddie Bauer's failure to implement a policy for notifying consumers of the Data Breach was itself an unfair act or practice because it caused foreseeable and substantial injury to



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financial institutions by worsening the injuries they suffered at the hands of Eddie Bauer's lax security practices. ¶¶6, 161.

Defendant argues that Plaintiff failed to allege an unfair practice because consumers could have avoided the risk of data theft by paying for items at Eddie Bauer with cash. This argument misses the mark. Neither Plaintiff nor consumers had any way of knowing that Defendant's data security practices were deficient, or that Defendant failed to implement appropriate and reasonable security practices. ¶159. Without notice or knowledge that Eddie Bauer's security measures were inadequate and thus, created a risk for theft of payment card information and fraud, there was no way the Plaintiff could have taken action to avoid injuries that it incurred as a result of the theft of payment card information. *Cf. In re LabMD*, 2016 WL 4128215, at *22 (finding that consumers had no ability to avoid harms caused by inadequate data security practices because they lacked any information about the deficient data security practices).

Defendant further argues that Plaintiff has not alleged an act or practice that is "likely to cause harm" because inadequate security practices do not themselves cause direct harm to consumers, but rather only cause harm when the information is stolen by third parties. This argument distorts the causation analysis under the CPA. Courts apply a "but for" proximate causation standard under the CPA, and the unfair act or practice need not be the sole proximate cause of the harm. *Indoor Billboard/Washington Inc. v. Integra Telecom of Washington, Inc.*, 162 Wn.2d 59, 82, 83, 170 P.3d 10 (2007); *see also Wyndham*, 799 F.3d at 246 (noting that risk of foreseeable harm from inadequate data is sufficient under FTC Act, and unfair act need not be the most proximate cause of an injury). Here the failure to take reasonable security measures was an unfair practice because it knowingly and foreseeably put financial institutions at a risk of harm from data theft and resulting fraudulent card activity. ¶¶24, 55, 156.



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**2. Plaintiff Properly Alleges a Deceptive Practice Because Eddie Bauer's Inadequate Data Security Practices Misled Consumers and Financial Institutions.**

Eddie Bauer argues that Plaintiff fails to allege Defendant engaged in any outward action or express representation about its data security practices, and therefore cannot state a claim under the CPA. Eddie Bauer offers no support or authority for this argument. The failure to act itself can be an unfair or deceptive act or practice. *See, e.g., Deegan v. Windermere Real Estate/Center-Isle, Inc.*, 197 Wn. App. 875, 891-92, 391 P.3d 582 (2017) (holding was error to dismiss plaintiff's CPA claims because plaintiff adequately alleged unfair or deceptive act against real estate agency for the deceptive failure to disclose material facts); *Mettler v. Safeco Ins. Co. of America*, No. C12–5163 RJB, 2013 WL 231111, at *7 (W.D. Wash. Jan. 22, 2013) (noting that "failing to adopt and implement reasonable standards for the prompt investigation of claims arising under insurance policies" and "refusing to pay claims without conducting a reasonable investigation" are established by regulation as unfair or deceptive acts or practices under the CPA).

The Washington Supreme Court has stated that "[d]eception exists 'if there is a representation, omission or practice that is likely to mislead' a reasonable consumer." *Panag*, 166 Wn.2d at 50. Plaintiff and the class of payment card issuers relied on Eddie Bauer, who chose to accept cards from consumers as payment, to keep the payment card information secure. ¶88. Eddie Bauer knew of this reliance, of its obligations to secure payment card data, and of the substantial risk inadequate data security practices posed to financial institutions. ¶¶24, 46-56, 81, 87-88, 156. *Cf. In re LabMD*, 2016 WL 4128215, at *10 ("LabMD was entrusted with patients' sensitive medical and financial information, and was obligated to put reasonable security systems in place to guard against the risk of an unauthorized release of such information.").

Eddie Bauer's failure to implement adequate security practices was likely to mislead payment card issuers, who reasonably expected Eddie Bauer to comply with its data security obligations when accepting credit card payments at its retail stores. In light of Plaintiff's



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reasonable expectation that Eddie Bauer would protect the payment card data it accepted, Eddie Bauer's failure to implement adequate data security practices was misleading and deceptive in violation of the CPA.

**3. Out-of-State Plaintiffs, Like Veridian, may bring a CPA claim against an In-State Corporate Defendant, Like Eddie Bauer.**

In *Thornell v. Seattle Serv. Bureau, Inc.*, 363 P.3d 587 (Wash. 2015), the Supreme Court of Washington considered "whether the Washington Consumer Protection Act (CPA), chapter 19.86 RCW, allows a cause of action for a plaintiff residing outside Washington [like Veridian] to sue a Washington corporate defendant [like Eddie Bauer] for allegedly deceptive acts." *Id*. at 589. The court answered this question in the affirmative, holding "the CPA does allow claims for an out-of-state plaintiff against all persons who engage in unfair or deceptive acts that directly or indirectly affect the people of Washington." *Id*. at 592. The Supreme Court explained,

> As pointed out in the briefing, unscrupulous entities might escape liability under the CPA if out-of-state citizens could not bring CPA actions against Washington entities that direct unfair and deceptive practices only to out-of-state residents. Washington businesses engaging in unfair and deceptive practices that indirectly affect others do not advance the purpose of fair and honest competition. Honest businesses could be placed at a competitive *disadvantage* competing against a business that generates revenue from unlawful acts that violate the statute.

*Id.* at 591. As demonstrated above, Plaintiff brings valid claims against Eddie Bauer, a Washington entity, under the CPA. Washington law permits out-of-state plaintiffs, like Plaintiff, to bring such claims.

**C. Veridian States a Claim for Violation of RCW 19.255.020**

Wash. Rev. Code § 19.255.020 requires businesses to take reasonable care to guard against unauthorized access to account information. Plaintiff alleges that Eddie Bauer was not in compliance with PCI-DSS standards at the time of the data breach. ¶¶41, 58, 73-75, 86-88. This is sufficient to state a claim. *See Home Depot*, 2016 WL 2897520, at *7.

The Court should reject Eddie Bauer's argument that Plaintiff fails to state a claim because it does not allege ***it*** reissued payment cards to Washington residents. Br. at 26. Plaintiff



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brings this action on behalf of a ***nationwide*** class of financial institutions. ¶99. Eddie Bauer is a Washington company with approximately 370 stores (and credit card-paying shoppers) across the United States and Canada. ¶12. Plaintiff has more than 209,000 customers throughout the United States, including Washington. ¶11; *see also* Slessor Decl. at ¶¶2-4. Plaintiff alleges the putative class canceled and reissued payment cards affected by the Data Breach. ¶8. Taking these allegations in the light most favorable to Plaintiff, it is reasonable to infer that financial institutions in the putative nationwide class reissued payment cards to Washington residents.

Violation of RCW 19.255.020 also provides a cause of action under the CPA. An unfair or deceptive act under the CPA can be based on a *per se* violation of another statute if the violation proximately caused the plaintiffs' injury and the plaintiff is within the class protected by the statute. *Dempsey v. Joe Pignataro Chevrolet, Inc*., 589 P.2d 1265, 1270 (Wash. Ct. App. 1979); *Blake v. Fed. Way Cycle Ctr*., 698 P.2d 578, 581-82 (Wash. Ct. App. 1985). Alternatively, a violation of the CPA can be shown through proof that the defendant's conduct is illegal and against public policy as declared by the legislature or the judiciary. *Salois v. Mut. of Omaha Ins. Co.*, 581 P.2d 1349, 1351 (Wash. 1978).

Plaintiff amply pleads these requirements, asserting Eddie Bauer violated RCW 19.255.020(3)(a) by failing to adequately safeguard account information; the violation proximately caused injury to financial institutions; and these institutions are within the class of persons the statute was meant to protect, allowing them to recover mitigation costs. Further, Eddie Bauer's misconduct was illegal under RCW 19.255.020(3)(a) and violated the clear public policy that customer data be protected as provided by the statute.

**D. Veridian States a Claim for Equitable Relief**

There must be '"a substantial controversy, between parties having adverse legal interests, of sufficient immediacy and reality to warrant the issuance of a declaratory judgment.'" *MedImmune, Inc. v. Genentech, Inc*., 549 U.S. 118, 127 (2007). Plaintiff asserts there is a continuing controversy regarding Eddie Bauer's ongoing data security obligations and the



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inadequacy of its current practices. ¶¶138-139, 165. Plaintiff further asserts Eddie Bauer's data security measures "remain inadequate." ¶138. Viewing the allegations in the light most favorable to Plaintiff, there is a real, immediate, and substantial risk of another breach and resultant harm that is not "hypothetical," as Eddie Bauer contends. Br. at 27. In the event of another breach, Plaintiff's legal remedies will be inadequate because the resulting injuries, such as the reputational harm that occurs each time Plaintiff notifies its customers their payment card has been compromised, are not readily quantified or provable. ¶141. Thus, Plaintiff seeks a declaration that Eddie Bauer is failing to use reasonable security measures and that, to comply with its legal obligations, Eddie Bauer must implement specified additional measures to protect payment card data. *Id.* Such allegations are sufficient at this stage. *See Home Depot*, 2016 WL 2897520, at *4-5; *Wendy's*, No. CV 16-506, ECF No. 80 at 10; *In re Sony Gaming Networks & Customer Data Sec. Breach Litig.*, 996 F. Supp. 2d 942, 999 (S.D. Cal. 2014).

Eddie Bauer's arguments are specious. First, Plaintiff does not assert a "standalone claim" for an injunction. Br. at 26. Rather, Plaintiff permissibly seeks an injunction as an ancillary remedy under the Declaratory Judgment Act. *See* 28 U.S.C. §2202; *Powell v. McCormack*, 395 U.S. 486, 499 (1969). Second, Plaintiff has demonstrated the inadequacy of legal remedies, alleging many of the injuries of a future breach may not be readily quantifiable, such as loss of good will. ¶141. To countenance Eddie Bauer's contention that a subsequent lawsuit for monetary damages would sufficiently compensate Plaintiff for any losses incurred as a result of a future data breach, *see* Br. at 26, would undermine the very purpose of the Declaratory Judgment Act, which is to prevent avoidable damages from being incurred. *See, e.g.*, *Minn. Mining & Mfg. Co. v. Norton Co.*, 929 F.2d 670, 673 (Fed. Cir. 1991). The Court should reject these arguments. *See Home Depot*, 2016 WL 2897520, at *5; *In re: Managed Care Litig.*, 298 F. Supp. 2d 1259, 1308 (S.D. Fla. 2003).

The cases that Eddie Bauer cites are easily distinguished because they do not involve a continuing controversy. For example, in *Adams v. Am. Fam. Mut. Ins. Co.*, 4:13-CV-226, 2014



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WL 11788532 (S.D. Iowa July 15, 2014), *amended*, 4:13-CV-226, 2014 WL 11636150 (S.D. Iowa Oct. 8, 2014), and *aff'd* 813 F.3d 1151 (8th Cir. 2016), the plaintiffs claimed that the defendant issued insurance policies with arbitration clauses, in direct violation of Iowa Code § 679A.1. *Id*. at *2. In that case, the plaintiffs claimed damages for the difference between what they were paid on a claim and what they would have been paid if the parties went through the proper appraisal process. However, at some point, the defendant modified its insurance policies to exclude the improper arbitration clause, which ended the controversy. *Id*. at *3. Unlike the *Adams* defendant, Eddie Bauer has not made the necessary "modification" to end this controversy. Eddie Bauer still maintains inadequate data security practices that threaten Plaintiff and a national class of financial institutions with unquantifiable future monetary and reputational damage. ¶141.

Eddie Bauer's fleeting ripeness argument is equally unavailing. Eddie Bauer argues "declaratory judgment is 'not ripe for adjudication if it rests upon 'contingent future events that may not occur as anticipated, or indeed may not occur at all.'" Br. at 27 (citing *Hodgers-Durgin v. de la Vina*, 199 F.3d 1037, 1044 (9th Cir. 1999)). In *Hodgers-Durgin*, two plaintiffs sought equitable relief prohibiting officials of the United States Border Patrol from further permitting the practice of unreasonable seizures between Arizona and Mexico. *Id*. at 1038-39. Both plaintiffs testified to having been stopped only once in ten years. *Id*. at 1039. In light of plaintiffs' infrequent exposure to the practice they sought to stop, the court found they did not establish a likelihood of future injury and that, as a result, their claim for equitable relief was unripe. *Id*. at 1044. Eddie Bauer's disregard for data privacy and risk of breach, as alleged in the Complaint and discussed at length herein, distinguishes this case from *Hodgers-Durgin*. Indeed, Plaintiff alleges Eddie Bauer still has not employed reasonable measures to secure its customers' personal and financial information, ¶139(b), and as a result, "the risk of another such breach is real, immediate, and substantial." ¶141.



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## VI. CONCLUSION

For the foregoing reasons, Plaintiff respectfully requests that the Court deny Eddie Bauer's motion to dismiss.

Respectfully submitted this 24th day of July, 2017.

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**CERTIFICATE OF SERVICE**

I hereby certify that on July 24, 2017, I electronically filed the foregoing with the Clerk of the Court using the CM/ECF system which will send notification of such filing to all parties registered on the CM/ECF system. All other parties (if any) shall be served in accordance with the Federal Rules of Civil Procedure.

DATED at Seattle, Washington, this 24th day of July, 2017.

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