Simpson Thacher

Memorandum

Citing Lack of Injury, Second Circuit Affirms Dismissal of Consumer Claims in Michaels Stores Data Breach

May 19, 2017

On May 2, 2017, the U.S. Court of Appeals for the Second Circuit affirmed the dismissal of a customer's putative class action lawsuit for damages and injunctive relief after her credit card data was compromised by a security breach at arts and crafts retailer Michaels Stores. The Court affirmed a determination that the plaintiff had failed to allege an actual injury, distinguishing the case from decisions in other circuits recognizing standing in data breach cases.[1]

Case Lessons

The case is a welcome development for companies that experience data breaches. It demonstrates that, at least in the Second Circuit, plaintiffs do not have standing to bring claims following a data breach if they do not incur fraudulent charges, reasonably expend resources to prevent fraudulent charges, or suffer some other actual injury or plausible risk of a future one.

Given that the standing issue has produced mixed results across U.S. courts in other circuits, however—and that data breaches often affect consumers in all 50 states—plaintiffs are likely to "forum shop" to maximize the chances that their claim will survive a threshold standing challenge. While companies cannot control plaintiffs' filing decisions, the *Whalen* case underscores the value of taking prompt action after any data breach to protect customers from identity theft and avoid having customers engage in self-help, such as by using their own funds to pay for credit monitoring services.

Case Summary

Plaintiff Mary Jane Whalen used her credit card to shop at a Michaels store in December 2013. Two weeks later, her credit card was presented for two payments in Ecuador. Whalen promptly cancelled her card, and she did not allege that any fraudulent charges were incurred. Ten days later, Michaels announced a potential data breach and theft of customer data and advised customers to monitor their accounts. In April 2014, Michaels publicly confirmed the breach and offered customers 12 months of identity protection and credit

[1] *Whalen v. Michaels Stores, Inc.*, 2017 WL 1556116 (2d Cir. May 2, 2017), *aff'g* 153 F. Supp. 3d 577 (E.D.N.Y. 2015). Whalen filed the lawsuit as a class action, but the case was dismissed prior to certification of the class.

monitoring services.

Whalen sued Michaels on December 2, 2014, claiming the following injuries: (i) monetary losses from fraudulent card payments; (ii) loss of time and money for credit monitoring/replacement cards; (iii) overpayment for Michaels' services, as Whalen claimed she would not have shopped there had she known of the data breach risks; (iv) lost value of her credit card information; and (v) statutory violation of NY General Business Law ("GBL") § 349, which bars deceptive business practices.

The U.S. District Court for the Eastern District of New York held that Whalen did not have standing to sue Michaels under Article III of the U.S. Constitution. The District Court noted that: (i) no fraudulent charges were actually incurred; (ii) a plaintiff cannot use his/her own spending on credit monitoring to "manufacture standing," particularly if the compromised card is cancelled; (iii) Michaels did not charge a premium on its goods to reflect data security; (iv) Whalen did not explain how her personal information had lost value; and (v) the bare assertion of a violation of NY GBL § 349 does not create standing. Further, the District Court ruled that Whalen did not face a "certainly impending" or "substantial" risk of future harm, because she promptly cancelled the compromised credit card and experienced no fraudulent charges thereafter.

Whalen in Context

Whalen follows two Supreme Court cases assessing Article III standing in the data privacy context. In 2013, in *Clapper v. Amnesty Intl*, the Court held that a data privacy injury must be "concrete and particularized" for the plaintiff to have standing. Later, in the 2016 case *Spokeo v. Robins*, the Court clarified that a technical violation of a statute due to a data breach is not necessarily a sufficient, "concrete" harm to confer standing, if the plaintiff does not suffer actual injury or "the risk of real harm."[2]

Spokeo did not prescribe what types of data breach injuries (actual or potential) are sufficiently concrete to confer standing. Since *Spokeo*, many U.S. courts have cited the decision to reach different conclusions on the question of standing. These conflicting holdings reflect differing views of the standard for actual injury or a reasonable risk of a future harm sufficient to create standing.

The Second Circuit opinion in *Whalen* did not cite *Spokeo* (although it did cite *Clapper*) and distinguished its ruling from those of the Sixth and Seventh Circuits that upheld standing, where (i) more extensive personal information was stolen or (ii) customers had actually incurred fraudulent charges and/or reasonably spent money on credit monitoring.[3] The Second Circuit did not discuss the alleged violation of NY GBL § 349, which the District Court had rejected as grounds for standing.

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[2] *See Spokeo, Inc. v. Robins*, 136 S. Ct. 1540 (2016); *Clapper v. Amnesty Int'l USA*, 133 S. Ct. 1138 (2013). *Spokeo* is currently on remand in the Ninth Circuit.

[3] *See Galaria v. Nationwide Mut. Ins.*, 663 Fed. Appx. 384 (6th Cir. 2016); *Lewert v. P.F. Chang's China Bistro,* 819 F.3d 963 (7th Cir. 2016); *Rejimas v. Neiman Marcus Grp.*, 794 F.3d 688 (7th Cir. 2015). *Galaria* was decided after *Spokeo* and cites *Spokeo* and the Seventh Circuit cases; the Seventh Circuit cases pre-date *Spokeo*.

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