UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF TEXAS
HOUSTON DIVISION

LONE STAR NATIONAL BANK, N.A., *et al*.,	§	
	§	CASE NO. 10cv00171
Plaintiffs,	§	
vs.	§	
	§	
KEYBANK NATIONAL ASSOCIATION, *et al*.,	§	JUDGE LEE H. ROSENTHAL
	§	
Defendants.	§	

DEFENDANT KEYBANK NATIONAL ASSOCIATION'S MOTION TO DISMISS PURSUANT TO FED.R.CIV.P. 12(b)(6)

Defendant Keybank National Association ("KeyBank"), pursuant to Federal Rule of Civil Procedure 12(b)(6), respectfully moves this Court to dismiss Plaintiffs' Complaint with prejudice as against KeyBank because Plaintiffs fail to state a claim against KeyBank. This Motion is supported by the following memorandum and exhibits thereto.

Respectfully submitted,

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DEFENDANT KEYBANK NATIONAL ASSOCIATION'S MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF MOTION TO DISMISS

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Defendant Keybank National Association ("KeyBank"), pursuant to Federal Rule of Civil Procedure 12(b)(6), respectfully moves this Court to dismiss Plaintiffs' Complaint with prejudice as against KeyBank because Plaintiffs fail to state a claim against KeyBank.

I. SUMMARY OF ARGUMENT

This case arises from a criminal intrusion into the computer system at Heartland Payment Systems, Inc. ("HPS"), which has also given rise to the cases consolidated before this Court in *In re Heartland Payment Systems, Inc. Data Security Breach Litigation*, Case No. H-09-MD-02046. Plaintiffs are financial institutions that issue debit and credit cards as members of the Visa and MasterCard payment-card networks. Defendant KeyBank, also a member of the Visa and MasterCard networks, contracted with HPS to acquire and process merchant payment-card transactions. Plaintiffs seek to recover from KeyBank losses they allegedly incurred as a result of the HPS intrusion.

Plaintiffs claim that they are third-party beneficiaries of the contract between KeyBank and HPS. But the contract between KeyBank and HPS contains no evidence of any intent to benefit third parties generally — or Plaintiffs specifically. Further, that contract incorporates the private rules and regulations that govern membership in the Visa and MasterCard networks. Visa's regulations expressly disclaim third-party obligations, and MasterCard reserves solely to itsself the right to enforce its regulations. The First Circuit Court of Appeals considered this issue in regard to the TJX intrusion and dismissed the issuers' third-party beneficiary claim on the pleadings.

Plaintiffs alternatively recast their contract claim under tort theories: breach of fiduciary duty, negligence, and vicarious liability. Issuers suing acquirers in regard to a data system intrusion under tort theories is nothing new. The First Circuit rejected such a tactic in regard to the TJX intrusion. The Third Circuit and Supreme Judicial Court of Massachusetts have also

evaluated and rejected such claims in regard to the BJ's Wholesale Club intrusion. All those courts dismissed the issuers' tort claims under the economic loss rule. That rule should apply with equal force in this case and bar all of Plaintiffs' tort claims. Each of Plaintiffs' tort claims fail for other reasons. Plaintiffs have failed to allege facts supporting a fiduciary duty on KeyBank. Plaintiffs are already protected from the losses they claim in this case and, therefore, the Court does not need to create the common-law duty Plaintiffs claim. And, because HPS is not KeyBank's agent, there is no vicarious liability.

In sum, Plaintiffs fail to state a claim for relief and this case should be dismissed under Rule 12(b)(6).

II. PLAINTIFFS' ALLEGATIONS

Plaintiffs are five financial institutions and members of the Visa and MasterCard payment card networks. (Compl. ¶ 1, 15-19.) Defendant KeyBank is a financial institution headquartered in Cleveland, Ohio, and also a member in the Visa and MasterCard networks. (*Id.* at ¶ 2, 20.) As a member, a financial institution may issue credit or debit cards ("payment cards") to consumers. (*Id.* at ¶ 1.) In this role, the member (or "Issuer") authorizes payment card transactions and tenders payment for purchases. The Issuer also "owns the consumer's account and assumes the risk of non-payment." (*Id*. at ¶ 34.) A member may also "acquire" merchant transactions. (*Id.* at ¶ 1) In this role, the member (or "Acquirer") contracts with merchants to process payment-card transactions accepted by the merchants. (*Id.*) Acquirers contract with merchants that wish to accept Visa or MasterCard payment cards, and bear the "risk of charge-backs, which can be significant if a merchant is unable or unwilling to honor its financial liability." (*Id*. at ¶ 42.) Members can operate as both Issuers and Acquirers. (*Id.* at ¶ 1-2.) HPS is a company that contracts with merchants and Acquirers to handle the actual processing of payment card transactions. (*Id*. at ¶ 3.)

The Visa and MasterCard networks are both governed by a separate set of private rules and regulations. (*Id.* at ¶ 39.) Each member contracts with Visa and MasterCard to enter the networks and agrees to operate in accordance with Visa and MasterCard's regulations. (*Id.* at ¶ 52.) The members, however, do not contract with each other and are not otherwise in privity with each other. (*See generally id.* at ¶ 53; *id.* at Count One, ¶¶ 117-122.)

In April 2002, KeyBank and HPS entered into a merchant processing agreement (the "MPA") under which KeyBank serves as the Acquiring bank for merchant transactions processed by HPS. (*Id.* at ¶ 59.; a copy of the MPA is attached to the Declaration of Jeffery R. Comi, which is Exhibit A hereto.)[1] The MPA expressly integrates the Visa and MasterCard regulations, and gives those regulations precedence over the MPA. (MPA, Sections 1.1(c, f, i)).

On January 20, 2009, HPS announced that criminals had entered its payment processing system and placed malicious software within the system. (Compl. at ¶ 71.) Plaintiffs assert that data stolen in this intrusion was used to make fraudulent charges on their customers' accounts, which caused Plaintiffs to incur losses from reimbursing the fraudulent charges and reissuing or otherwise monitoring compromised payment cards. (*See id.* at ¶ 156).

Plaintiffs contend that KeyBank had a duty to monitor HPS's security systems under the Visa and MasterCard rules and regulations. (*Id.* at ¶ 7.) Plaintiffs allege that KeyBank failed to properly monitor HPS. (*Id.* at ¶ 9.) Plaintiffs assert claims for breach of contract as third-party beneficiaries of the MPA, (*id.* at ¶¶ 117-122.) breach of fiduciary duty, (*id.* at ¶¶ 123-129.) negligence, (*id.* at ¶¶ 130-134.) and vicarious liability. (*Id*. at ¶¶ 135-152.)

[1] This Court may consider the MPA and the Visa and MasterCard regulations in ruling on this Motion without converting it to a motion for summary judgment, as Plaintiffs specifically refer to the MPA and the regulations as documents central to its claims. *See Ace American Ins. Co. v. Huntsman Corp.*, 255 F.R.D. 179, 187-88 (S.D. Tex. 2008) (citing *Scanlan v. Tex. A & M Univ.*, 343 F.3d 533, 536 (5th Cir. 2003)).

III. STANDARD OF REVIEW

To withstand a motion brought under Rule 12(b)(6), Plaintiffs must allege "more than an unadorned, the defendant-unlawfully-harmed-me accusation." *Ashcroft v. Iqbal*, 129 S.Ct. 1937, 1949 (2009). A plaintiff must set forth "more than labels and conclusions, and a formulaic recitation of the elements of a cause of action" to defeat a motion to dismiss. *Bell Atlantic Co. v. Twombly*, 550 U.S. 544, 555, 127 S.Ct. 1955 (2007). A complaint must "contain sufficient factual matter, accepted as true, to state a claim to relief that is plausible on its face," such that the substance of its claims go "across the line from conceivable to plausible." *See Iqbal*, 129 S.Ct. at 1949; *Twombly*, 550 U.S. at 570.

This Court has explicitly adopted the *Twombly* and *Iqbal* standards. *See Lehman Bros. Holdings, Inc. v. Cornerstone Mortgage Co.*, No. H-09-0672, 2009 WL 2900740, at *4 (S.D. Tex. Aug. 31, 2009) (J. Rosenthal).

IV. LAW AND ARGUMENT

A. Plaintiffs Fail To State A Claim For Breach Of Contract

Under Count One, Plaintiffs assert a breach of contract claim. (Compl. at ¶¶ 117-122.) Conceding that there are no contracts between KeyBank and Plaintiffs and that the parties are not in privity, Plaintiffs claim that they are third-party beneficiaries of contracts between KeyBank and "various entities." (*Id*. at ¶ 118.) However, the only contract actually identified by Plaintiffs is the MPA between KeyBank and HPS. (*See generally id.* at ¶¶ 117-122.) Plaintiffs contend that they are intended beneficiaries of the MPA. (*Id.* at ¶ 118.) By its clear terms, Plaintiffs cannot state a claim for third-party beneficiary rights under the MPA. Moreover, Plaintiffs cannot rely on the card network regulations, which are integrated into the MPA. Visa and MasterCard provide their own enforcement mechanisms and expressly preclude the third-party rights that the Plaintiffs claim.

1. The Clear Terms Of The MPA Do Not Create Any Third-Party Rights

The MPA is governed by Ohio law. (MPA ¶ 4.11.) Under Ohio law, only intended third-party beneficiaries may sue to enforce a contract to which they are not a party. *Reisenfeld & Co. v. Network Group, Inc.*, 277 F.3d 856, 863 (6th Cir. 2002) (applying Ohio law). Plaintiffs are not considered third-party beneficiaries simply because they receive a benefit from a contract. *Elite Designer Homes, Inc. v. Landmark Partners*, 2006-Ohio-4079, ¶ 68 (Ohio Ct. App. 2006) ("A third party who simply receives a benefit from the agreement, without more, is only an incidental beneficiary and may not sue under the contract.") (*quoting Bush v. Roelke*, 1990 Ohio App. LEXIS 4099 (Ohio Ct. App. 1990)). "In order to be an intended beneficiary, the '*clear terms of the contract*' must show that the parties entered the contract for the benefit of the third party." *Joest Vibratech, Inc. v. North Star Steel Co.*, 109 F. Supp. 2d 746, 749 (N.D. Ohio 2000) (emphasis added). In other words, it must be clear that the parties entered into the contract "directly or primarily" for a third party's benefit. *Reisenfeld*, 277 F.3d at 863. In addition, a contractual provision explicitly disclaiming a third party as a beneficiary will be enforced as written. *See Maghie & Savage, Inc. v. P.J. Dick Inc.*, No. 08AP-487, 2009 WL 1263965, at ** 11-13 (Ohio Ct. App. May 5, 2009).

The clear terms of the MPA fail to establish that KeyBank and HPS entered into the MPA directly or primarily for the benefit of the Plaintiffs. *See Joest Vibratech, Inc.*, 109 F. Supp. 2d at 749; *Reisenfeld*, 277 F.3d at 863. The MPA does not mention the Plaintiffs, nor does it mention card issuers even *generally*. (*See* MPA.) And Plaintiffs fail to cite a single term or provision in the MPA that would even suggest that KeyBank and HPS entered into the MPA primarily for their benefit. (*See generally* Compl. at ¶¶ 117-122.)

Rather, Plaintiffs base their third-party beneficiary claim entirely on the assertion that the MPA lacks a provision explicitly disclaiming the intent of KeyBank and HPS to create third-

party beneficiaries. (Compl. ¶ 118.) But the mere lack of such a provision is not itself enough to *create* third-party rights. A party seeking such rights must still prove that:

> recognition of a right to performance in the beneficiary is appropriate to effectuate the intention of the parties and either (a) the performance of the promise will satisfy an obligation of the promisee to pay money to the beneficiary; or (b) the circumstances indicate that the promisee intends to give the beneficiary the benefit of the promised performance.

Restatement (Second) of Contracts, § 302(1); *see also Hill v. Sonitrol of Southwestern Ohio, Inc.*, 521 N.E.2d 780, 784, 36 Ohio St. 3d 36 (Ohio 1988) (Ohio follows Section 302).

Through its integration of the Visa and MasterCard regulations, the MPA explicitly states that third-parties should *not* be given the benefit of, or the right to enforce, its terms. (MPA, Sections 1.1(c, f, i).) The Visa regulations expressly "do not constitute a third-party beneficiary contract as to any entity or person . . . or confer any rights, privileges, or claims of any kind as to any third parties." (Visa Regulations, Vol. I, § 1.2.C.)[2] Likewise, the MasterCard regulations provide that "[Mastercard] has the sole right in its sole discretion to interpret and enforce the [regulations]." (MasterCard Regulations, § 3.1.)[3]

In a similar data system intrusion case, third-party beneficiary status was denied to issuing banks that sued an acquiring bank under its contract with a breached merchant and the card networks' rules and regulations. *See, e.g.*, *In re TJX Cos. Retail Sec. Breach Litig.*, 564 F.3d 489, 499 (1st Cir. 2009), *aff'g* 524 F. Supp. 2d 83, 90 (D. Mass. 2007). The court in *TJX* noted that the defendant acquiring bank was bound by the Visa and MasterCard rules to follow certain security procedures and to contractually require its merchants to do the same. *Id*.

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[2] The Visa regulations are voluminous and can be found online at http://usa.visa.com/download/ merchants/visa-usa-operating-regulations.pdf. Those portions of the regulations cited in this brief are attached in excerpt form as Exhibit B.

[3] MasterCard's regulations are also voluminous and can be found online at http://www.mastercard.com/us/merchant/pdf/BM-Entire_Manual_public.pdf. Cited portions of the MasterCard Regulations are attached in excerpt form as Exhibit C.

Following Restatement Section 302, the *TJX* court determined that the intent of the acquiring bank and merchant was immaterial because they had "otherwise agreed" that no third-party rights would be created by their contract. *Id*. Significantly, the court noted that the card networks' regulations — *which (as here) by agreement prevailed over the contract itself* — rested the sole authority to enforce the regulations with the card networks. *Id*. The court also noted that the Visa regulations expressly disclaimed any third party rights. *Id*. (citing *CUMIS Ins. Soc., Inc. v. BJ's Wholesale Club, Inc*., 23 Mass.L.Rptr. 550, at ** 2-3 (Mass. Super. 2005); *Pa. State Employees Credit Union v. Fifth Third Bank*, 398 F. Supp. 2d 317, 323-26 (M.D. Pa. 2005)).

More recently, the Supreme Judicial Court of Massachusetts dismissed a third-party beneficiary claim on the pleadings in regard to the BJ's intrusion. *CUMIS Ins. Soc'y, Inc. v. BJ's Wholesale Club, Inc.*, 455 Mass. 458, 464-69 (Mass. 2009). The *CUMIS* court determined that the regulations' enforcement mechanisms precluded any argument that Issuers are intended third-party beneficiaries of the duties imposed on Acquirers by the network regulations. *Id*. at 468 ("[E]ven if the issuing banks were intended beneficiaries of the operating regulations, those regulations 'make clear' that only Visa and MasterCard 'can enforce their terms and thus that the issuing banks have no right to file suit to achieve that end.'") (quoting *TJX*, 524 F.Supp. 2d at 89).

Here, Plaintiffs make conclusory and unsupported allegations regarding the intent of KeyBank and HPS to benefit issuing banks such as Plaintiffs. (*See* Compl. ¶ 118-120.) Just as in *TJX*, the card network regulations clearly provide otherwise. KeyBank and HPS agreed that the networks, and only the networks, would have the right to enforce their respective regulations, which were incorporated into and take precedence over the MPA's terms. (MPA Section 1.1(i).) And those rules expressly disclaim third-party rights.

Because the clear terms of the MPA fail to establish third-party rights and, in fact, explicitly disclaim such rights by reference to the network regulations, Count One should be dismissed.

2. Plaintiffs Rely Solely on the Alleged Breach of Network Regulations, As They Cannot Identify a Provision of the MPA that KeyBank Breached That Is Not Linked to the Network Regulations

Plaintiffs have identified no provision of the MPA that KeyBank breached. In fact Plaintiffs cite only four provisions of the MPA – each imposing a duty *on HPS*, not KeyBank. (Compl., ¶ 118 (citing MPA at 1.1(e) (requiring *HPS* to conduct itself in accordance with established risk management practices "to protect *KeyBank*"), 1.2(e) (requiring *HPS* to monitor activity reports for suspicious activity), 4.3(b) (requiring *HPS* to keep data confidential), 4.5(a) (requiring *HPS* to indemnify and *hold KeyBank harmless*).))

The only contractual duties that Plaintiffs contend KeyBank breached were alleged duties "expressly and/or impliedly require[d]" by the MPA to "monitor, audit, oversee and confirm" that HPS's payment card processing system safeguards were adequate to protect confidential payment card data processed by HPS. (Compl., ¶¶ 119, 121.) These are the same alleged duties that Plaintiffs identified as arising from KeyBank's sponsorship of HPS in the card brand networks. (*Id*., ¶ 7.) But those duties appear nowhere in the MPA itself. Rather, to the extent they appear anywhere, those duties are set forth *only* in the card brand regulations that Plaintiffs contend are integrated into the MPA.

If KeyBank has any obligation to monitor HPS or otherwise ensure the security of payment card data possessed by HPS, then, that obligation arises out of the card networks' regulations and nothing else. As explained above, and as precedent makes clear, those regulations are enforceable only by the card brands themselves, not by individual members. *See CUMIS Ins. Soc'y, Inc.*, 455 Mass. at 464-69 ("[T]hose [network] regulations 'make clear' that

only Visa and MasterCard 'can enforce their terms and thus that the issuing banks have no right to file suit to achieve that end.'") Thus, Plaintiffs are barred from enforcing the regulations in this lawsuit.

B. Plaintiffs Fail to State a Claim for Breach of Fiduciary Duty[4]

Aware of failed attempts by Issuers in other data intrusion cases to sue Acquirers,[5] Plaintiffs assert a theory that KeyBank is their fiduciary. (Compl. ¶¶ 123-129 (Count Two)). That theory has no support in either the Complaint or prior decisions.

By their fiduciary duty claim, Plaintiffs essentially ask the Court to impose a common-law duty between the large, sophisticated financial institutions that voluntarily participate in complex, multi-billion dollar payment systems that are already governed by a voluminous set of private rules and regulations that already provide detailed mechanisms addressing and allocating the well-known and much publicized risks of payment card data theft stemming from data security breaches. Moreover, Plaintiffs attempt to plead this claim despite the plain and undisputed facts that Plaintiffs and KeyBank are neither in contractual privity, (Compl. ¶ 118) nor do they have *any* direct interaction in the payment card transaction process. (*See* Compl. ¶ 32 (describing "data loop," in which Acquirers and Issuers are separated by the card network – Visa or MasterCard – and, in some cases, an Issuer's third-party processor); *Id*. at ¶ 33 (describing "settlement loop," in which Acquirers and Issuers are again separated by the card network); *Id*. at Exs. A and B (pictorial illustrations of the "Anatomy" of a payment card transaction in each card association, again showing that acquirers and issuers are not directly connected in any way)).

[4] Regardless of whether this Court applies the law of Ohio (KeyBank's domicile) or Texas (the forum with the greatest connection to the facts of the case, as determined by the JPML) to Plaintiffs' tort claims, the result is the same — dismissal on the pleadings is warranted. Accordingly, the law of both Ohio and Texas is cited in Sections IV.B, IV.C, and IV.D of this brief.

[5] *See, e.g., In re TJX Companies Retail Security Breach Litigation*, 564 F.3d 489; *CUMIS Ins. Soc'y, Inc. v. BJ's Wholesale Club, Inc.*, 23 Mass. L. Rptr. 550 (Mass. Super 2005).

Further, Plaintiffs attempt to establish a fiduciary relationship (which includes a duty against self-dealing) between KeyBank and Plaintiffs, despite the fact that KeyBank is in *direct competition* with the named Plaintiffs and the *entire putative plaintiff class* in the card issuing arena, and also with the putative Acquirer Class in the merchant acquisition arena. (*See* Compl. ¶ 20 (correctly identifying KeyBank as both an Issuer and Acquirer)).

As explained below, Plaintiffs' allegations are conclusory and do not pass the *Iqbal* threshold. *See Iqbal*, 129 S.Ct. 1937. Moreover, Plaintiffs have not alleged facts sufficient to establish a fiduciary relationship between KeyBank and Plaintiffs, and they have failed to allege the elements of a joint venture under applicable law. (*See* Compl. ¶ 124 (claiming that the fiduciary relationship between Plaintiffs and KeyBank "create[s] and/or emanate[s] out of a joint venture.")) Plaintiffs' breach of fiduciary duty is also barred by the economic loss rule.

1. The Complaint Does Not Satisfy the Iqbal Standard

Plaintiffs allege that KeyBank owed them a fiduciary duty for three conclusory reasons:

1) "[b]y virtue of their membership in the Visa and MasterCard Associations," and the associations' alleged status as "joint ventures;" (Compl. ¶ 124)

2) "because [KeyBank] had knowledge of the breaches of fiduciary duties committed by Heartland, another fiduciary of Plaintiffs;" (*Id*. at ¶ 127)

3) because KeyBank "engaged in transactions with Heartland, another breaching fiduciary of Plaintiffs . . . under circumstances in which Defendants knew (or should have known) about such fiduciary breaches." (*Id*. at ¶ 128).[6]

Whether any fiduciary or joint venture relationship exists between parties requires a *legal* determination: the relationships cannot be alleged as matters of *fact*. *Twombly*, 550 U.S. at 555 (requiring "more than labels and conclusions, and a formulaic recitation of the elements of a cause of action" in order to defeat a motion to dismiss); *Iqbal*, 129 S.Ct. 1937 (reaffirming

[6] Plaintiffs assert theories (2) and (3) as alternate theories of liability "[t]o the extent that Defendants *are not fiduciaries or co-joint venturers of Plaintiffs*." (Compl. ¶¶ 127-28, emphasis added.)

Twombly and dismissing discrimination claim where factual allegations were too conclusory to defeat defense of qualified immunity).

Plaintiffs do not allege the *facts* necessary to establish a joint venture or fiduciary relationship between Plaintiffs and KeyBank, nor do they allege the *facts* necessary to establish a fiduciary relationship between Plaintiffs and HPS. The conclusory pleading in Count Two of the Complaint is exactly what the Supreme Court intended to prevent in its *Twombly* and *Iqbal* decisions. (Compl. ¶¶ 123-29.) Indeed, and as explained below, Plaintiffs' legal conclusions are not even supported by a "formulaic recitation" of the characteristics of such relationships. *Twombly*, 550 U.S. at 555.

2. KeyBank Does Not Owe a Fiduciary Duty to Plaintiffs

Plaintiffs allege that, "[b]y virtue of their membership in the Visa and MasterCard Associations," Plaintiffs and KeyBank are in a fiduciary relationship. (Compl. ¶ 124.) By this logic, *every* association member would have a fiduciary relationship with *every other member*. (*Id*.) KeyBank would owe fiduciary duties to all the other issuer/acquirers (*including the entire Acquirer Class*) with which KeyBank *directly competes*.[7] Under Plaintiffs' theory, by seeking business for themselves in the payment card industry, the 14,000 Visa member financial institutions and 20,000 MasterCard member financial institutions, all of which are bound by their respective associations' rules, would be in constant breach of their fiduciary duties to one another not to engage in self-dealing. (Compl. ¶ 28-29.)

This argument has already been rejected in the payment-card context. *Visa U.S.A., Inc. v. First Data Corp.*, No. C 02-01786, 2006 WL 516662, * 3 (N.D. Cal. Mar. 2, 2006). Analyzing the relationships between participants in the payment card networks, the court in *First Data Corp.* refused to find that "the individual members maintain a fiduciary obligation to act for each

[7] Although KeyBank is being sued by Plaintiffs in its role as an Acquirer, KeyBank is also an Issuer, (Compl. ¶ 20) and therefore is in direct competition with all the named Plaintiffs and the entire putative plaintiff class.

other's economic benefit." *Id*. Instead, the *First Data* court found that "the members of Visa *do not share a common unified economic interest and do stand in actual and potential competition with one another*." *Id*. at * 6 (emphasis added). The MasterCard network does not materially differ from the Visa network in this regard. *See generally* Complaint; Complaint at Exhibits A, B.

A fiduciary is "a person having a duty, created by his undertaking, to act *primarily for the benefit of another* in matters connected with his undertaking." *Haluka v. Baker*, 34 N.E.2d 68, 70 (Ohio App. 1941) (emphasis in original); *see also Strock v. Pressnell*, 527 N.E.2d 1235, 1243 (Ohio 1988) (citing *Haluka*); *All Star Land Title Agency, Inc. v. Surewin Invest., Inc.*, 2006 WL 3095701, 2006-Ohio-5729, ¶ 36 (Ohio App. 8 Dist. Nov. 2, 2006). Plaintiffs have not alleged that KeyBank undertook a duty to act *primarily* for Plaintiffs' benefit in connection with its merchant acquiring activities. (*See generally* Compl.) And Plaintiffs have not alleged that the contracts forming the card networks are anything other than commercial transactions negotiated at arm's length between sophisticated parties, or that any party to those contracts is in a position of power over any other party. (*Id*.) All issuers and acquirers are on equal footing, and each has its own contract with Visa or MasterCard binding it to that network's rules, neither of which make any mention of a fiduciary relationship. (Compl. ¶¶ 26, 28, 39, 52.) Any relationship that might exist between an Acquirer and Issuer is indirect at best, and by no means is it fiduciary. (Compl. Exs A, B.)

Moreover, "while a fiduciary or confidential relationship may arise from the circumstances of a particular case, to impose such a relationship *in a business transaction, the relationship must exist prior to, and apart from, the agreement made the basis of the suit*." *Schlumberger Tech. Corp. v. Swanson*, 959 S.W.2d 171, 177 (Tex. 1997) (emphasis added) *(citing Transport Ins. Co. v. Faircloth,* 898 S.W.2d 269, 280 (Tex.1995)); *see also Meyer v.*

Cathey, 167 S.W.3d 327, 331 (Tex. 2005). Plaintiffs do not allege that KeyBank stood in a fiduciary relationship – or *any* relationship – with them prior to or apart from their respective memberships in the Visa and MasterCard networks. *See* Complaint, ¶¶ 123-129.

"The fact that one business person trusts another and relies on *a promise to perform a contract* does not rise to the level of a confidential relationship for purposes of establishing a fiduciary duty." *Garrison Contractors, Inc. v. Liberty Mutual Ins. Co.*, 927 S.W.2d 296, 301 (Tex. App. 1996) (emphasis added). The only alleged wrongful act or omission Plaintiffs have attributed to KeyBank is a failure to "monitor, audit, oversee and confirm" that HPS's payment card processing system safeguards were adequate. (Compl. ¶ 126.) Plaintiffs allege that same act or omission *verbatim* to constitute a breach of KeyBank's contract with HPS, under which Plaintiffs attempt to claim third-party beneficiary status. (*Id.* at ¶¶ 119, 121.) Plaintiffs cannot bootstrap an alleged contractual obligation into the basis for a tort action.

Plaintiffs do not allege the facts necessary to establish a fiduciary relationship with KeyBank.

3. The Visa and MasterCard Networks Are Not Joint Ventures

Plaintiffs also allege that, by virtue of the their membership in the Visa and MasterCard networks, KeyBank and Plaintiffs were part of a joint venture. Plaintiffs contend that as members of the same joint venture, KeyBank owed them a fiduciary duty. This argument fails. Plaintiffs have not alleged *facts* establishing a joint venture.

A joint business venture is defined as:

> [A]n association of persons with intent, by way of contract, express or implied, to engage in the carry out a single business adventure for *joint profit*, for which purpose they combine their efforts, property, money, skill and knowledge, without creating a partnership, and agree that there shall be a community of interest among them as to the purpose of the undertaking, *and that each coadventurer shall stand in the relation of principal, as well as agent, as to each of the other coadventurers*, with an *equal right of control* of the means employed to carry out the common purpose of the adventure.

Ford v. McCue, 127 N.E.2d 209, 213 (Ohio 1955) (emphasis added). "An agreement for a *division of the profits* between the parties is also essential in a joint business adventure. A *profit jointly sought* in a single transaction by the parties thereto is the chief characteristic of a joint business adventure, and the *profit accruing must be joint and not several*." *Id*. (emphasis added); *see also, e.g., Ayco Development Corp. v. G.E.T. Service Co.*, 616 S.W.2d 184, 185 (Tex. 1981) (setting forth materially similar elements of a Texas joint venture).

Plaintiffs generally – and without reference to any agreement – allege that they have a "community of interest" and "a common purpose" with other card network members. (Compl. ¶ 26.) Plaintiffs do not, however, state what that interest or purpose is. *Id*.; *see First Data Corp.*, 2006 WL 516662, at * 6 ("The *undisputed* evidence before the Court indicates that, with respect to the function of [payment card authorization, clearing, and settlement] services, the members of Visa *do not share a common unified economic interest and do stand in actual and potential competition with one another*.") (emphasis added).

Plaintiffs also do not and cannot allege any control that any Issuer or Acquirer has over any other Issuer or Acquirer or over either card network as a whole. S*ee* Compl. ¶ 40 (admitting that Issuers "have *no control* over the majority of the interchange system").

Finally, Plaintiffs do not and cannot allege any agreed sharing of profits or losses among card network members, or that any "profit" of a payment card network is jointly accrued. *See First Data Corp*., 2006 WL 516662, at * 4 ("[T]here is no dispute that the profits and losses associated with the banks' card businesses do not end up under the same corporate mattress."). And Plaintiffs *admit* in their Complaint that certain risks and losses inherent in the payment card industry are borne by *individual* issuers or acquirers, *not* by the network as a whole. (Compl. at ¶ 34 (issuers bear the risk of cardholder non-payment); ¶ 42 (acquirers bear the risk of charge-backs).)

In sum, Plaintiffs' allegation that a joint venture exists among card network members is impermissibly conclusory, wholly unsupported, and *contradicted* by allegations in the Complaint.

4. The Economic Loss Rule Bars Plaintiffs' Fiduciary Duty Claim

Texas applies the economic loss rule not only in traditional contexts where parties are in privity or where a defective product damages itself, but also to bar recovery in negligence actions where, as here, the plaintiff's claimed injury is purely economic in nature. *See*, *e.g., Hou-Tex, Inc. v. Landmark Graphics*, 26 S.W.3d 103, 107 (Tex. App. 2000). Ohio applies the economic loss rule in a similarly broad manner. *See HDM Flugservice GmbH v. Parker Hannifin Corp.,* 332 F.3d 1025, 1029-1030 (6th Cir. Ohio 2003) (applying economic loss rule to bar tort claim in action between commercial parties); *In re Whirlpool Corp. Front-Loading Washer Prods. Liab. Litig.*, No. 08-wp-65000, 2009 WL 3712649, * 4 (N.D. Ohio Nov. 3, 2009). Moreover, courts have held in similar data-intrusion cases that losses experienced by credit-card Issuers are purely economic and cannot be recovered from an Acquirer in tort. *See In re TJX Companies Retail Security Breach Litigation*, 564 F.3d at 498-99 (affirming dismissal of Issuer's negligence claim against Acquirer); *CUMIS*, 23 Mass. L. Rptr. 550, at ** 8-9 (same); *Pa. State Employees Credit Union,* 398 F. Supp. 2d at 326 (M.D. Pa. 2005) (same, in lawsuit brought against Acquirer by one of the Plaintiffs in this case).[8]

Plaintiffs seek in this case to recover the money that they allegedly spent in notifying customers, canceling and reissuing payment cards, and absorbing fraudulent charges. (Compl. ¶ 133.) Plaintiffs have failed to allege any non-economic damages. Because Plaintiffs' fiduciary

[8] The economic loss rule is not limited to claims of simple negligence. An Ohio court dismissed a fiduciary duty claim where the plaintiff suffered only economic harm, even though the plaintiff was not in contractual privity with the defendant. *OC Property Mgt., L.L.C. v. Gerner & Kearns Co., L.P.A.*, 2008-Ohio-4709, ¶ 14 (Ohio App. 8 Dist. Sep. 18, 2008) (defendant attorney hired by buyer and seller to preside over a real estate closing failed to properly record plaintiff lender's mortgage, causing lender to lose priority status in foreclosure).

duty claim seeks purely economic damages, the economic loss rule precludes such a claim and should be dismissed.

C. Plaintiffs Fail To State A Claim For Common-Law Negligence

Under Count Three, Plaintiffs assert a common-law negligence claim against KeyBank. Plaintiffs allege that the "special relationships" between Plaintiffs and the putative class members, on the one hand, and KeyBank, on the other hand, create a duty of care from KeyBank to Plaintiffs in regard to monitoring HPS's activities. (Compl. ¶ 131.) The "special relationship" alleged by Plaintiffs arises solely from the parties' membership in the Visa and MasterCard payment-card networks. Thus, Plaintiffs are contending that, by virtue of its membership in the Visa and MasterCard payment-card networks, KeyBank owes all the other members a common-law duty of care.

But Plaintiffs' negligence claim fails as a matter of law. First, courts have repeatedly denied Issuers' attempts to pursue negligence claims against Acquirers in data-intrusion cases under the economic loss rule. That rule should apply equally in this case. Second, Plaintiffs and the putative class members already protect themselves from the risks associated with data intrusions through the Visa and MasterCard regulations, and thus there is no need for the courts to create a common-law duty to protect those interests.

As discussed above, the economic loss rule bars a negligence claim to recover purely economic damages. *See Hou-Tex, Inc. v. Landmark Graphics*, 26 S.W.3d at 105; *In re Whirlpool Corp.*, 2009 WL 3712649, * 4. Moreover, courts have held, in similar data-breach cases, that losses experienced by credit-card Issuers are purely economic and cannot be recovered from an acquirer under a negligence theory. *See TJX Companies*, 564 F.3d at 498-99 (affirming dismissal of issuer's negligence claim against acquirer); *CUMIS*, 23 Mass. L. Rptr. 550, at ** 8-9 (same); *Pa. State Employees Credit Union v. Fifth Third Bank*, 398 F. Supp. 2d

317, 326 (M.D. Pa. 2005); *Sovereign Bank v. BJ's Wholesale Club, Inc.*, 533 F.3d 162, 179-80 (3d Cir. 2008). Because Plaintiffs' alleged damages are purely economic, Count Three is barred by the economic loss rule and should be dismissed.

Plaintiffs attempt to plead around the economic loss rule by stating that the rule does not apply because (i) issuers, such as Plaintiffs and the putative class members, were not in "express contractual privity" with KeyBank or HPS and could not "protect their economic interests via express contracts," and (ii) the "basis of their indirect relationships is not a tangible product, but rather an intangible service." (Compl. ¶ 134.) But Texas and Ohio have not adopted such a limited application of the economic loss rule. In both Texas and Ohio, privity of contract between the parties is not required for the economic loss rule to apply. *See Hou-Tex, Inc.*, 26 S.W. 3d at 105; *Flugservice,* 332 F.3d at 1029-1030. In other words, the economic loss rule will bar a negligence claim seeking purely economic damages, regardless of privity between the parties. Thus, the exception alleged by Plaintiffs does not apply in this case.

But even if Plaintiff's purported exception did apply, the facts in this case would still warrant dismissal. In this case, Plaintiffs, and all card Issuers, already protect themselves against the risks of credit card data being stolen and misused through the Visa and MasterCard regulations. These regulations contain detailed provisions governing the ability of members, such as Plaintiffs, to recover their losses in the event the theft of such data was caused by a violation of those regulations.[9] Given these comprehensive recovery mechanisms, there is no need for the courts to create a common-law duty to protect those interests. Indeed, in the only reported decision on this issue in the data breach context, the court declined to create the

[9] *See* MasterCard Chargeback Guide Chapter 5 (Ex. C), http://www.mastercard.com/us/merchant/pdf/TB_CB_Manual.pdf (providing that an Issuer can file a claim *with MasterCard* for reimbursement of certain fraud losses and card-reissuing costs); Visa Operating Regulations Vol. II, generally and at Chapter 4 (Ex. B), http://usa.visa.com/download/merchants/ visa-usa-operating-regulations2.pdf. (providing the "ADCR" method by which Issuers can recover fraud losses and card-reissuing costs).

common-law duty that Plaintiffs urge this court to recognize. *See Cumis Ins. Soc'y, Inc. v. Merrick Bank Corp.*, No. 07-374, 2008 WL 4277877, at *11-12 (D. Ariz. Sep. 18, 2008) (dismissing common-law negligence claim).

For these reasons, Count Three should be dismissed. Plaintiffs have failed to state a viable claim for common-law negligence.

D. Plaintiffs Fail To State A Claim For Vicarious Liability

Because Plaintiffs cannot state a claim against KeyBank for direct negligence, Plaintiffs offer the alternate theory of vicarious liability, thereby attempting to impute the alleged acts or omissions of HPS to KeyBank. *See* Compl., ¶¶ 135-152. But the economic loss rule bars Plaintiffs' vicarious liability claim just as it does Plaintiffs' fiduciary duty and negligence claims. Moreover, Plaintiffs cannot impute HPS's actions to KeyBank, because HPS was not KeyBank's agent under the clear terms of the agreement governing HPS and KeyBank's relationship. And, finally, Plaintiffs do not state a viable claim as it relates to the alleged underlying conduct of HPS – there is, therefore, no liability to impute to KeyBank.

1. The Economic Loss Rule Bars Plaintiffs' Vicarious Liability Claim

As stated above, the economic loss rule bars tort claims that are rooted in an alleged contractual duty, even when the claimant is not in privity to the contract that creates the duty. This is just as true when the allegedly tortious conduct of one party is imputed to another under a vicarious liability claim. *See, e.g., City of Southaven v. Datamatic, Ltd.*, Case No. 2:07-cv-58, 2008 WL 3200706, * 1 (N.D. Miss. Aug. 6, 2008) (holding that vicarious liability claims are barred by the economic loss doctrine); *Flannery v. Mid Penn Bank*, Case No. 1:CV-08-0685, 2008 WL 5113437, * 7 (M.D. Pa. Dec. 3, 2008) (dismissing vicarious liability claim based on economic loss doctrine); *Anastasi Brothers Corp. v. Mass. Convention Center Authority*, No. 890867B, 1993 WL 818553, * 3 (Mass. Super. Nov. 1, 1993) (dismissing contract claim against

building authority based upon acts of its architect and stating that, had plaintiff also alleged vicarious liability against authority, economic loss doctrine would bar recovery).

As discussed in sections IV.(B)(4) and (C), Plaintiffs' claims fail under the economic loss rule. That rule should preclude Plaintiffs' vicarious liability claim as well.

2. HPS Was Not KeyBank's Agent Under the MPA

The liability of an independent contractor generally cannot be imputed to its employer. *See, e.g., Miller v. Metropolitan Life Ins. Co.*, 16 N.E.2d 447, 448 (Ohio 1938) ("The fundamental rule generally recognized is that the doctrine of *respondeat superior* is applicable to the relation of master and servant or of principal and agent, but not to that of employer and independent contractor."); *Elliott-Williams Co., Inc. v. Diaz*, 9 S.W.3d 801, 803-04 (Tex. 1999); *Bell v. VPSI, Inc.*, 205 S.W.3d 706, 718 (Tex. App. 2006) ("[T]he long-standing common-law rule in Texas, as stated in Section 409 of the Restatement (Second) of Torts, is that 'the employer of an independent contractor is not liable for physical harm caused to another by an act or omission of the contractor or his servants.'") (citing *Elliot-Williams Co., Inc.*, 9 S.W.3d at 803).

Plaintiffs allege generally that HPS was KeyBank's agent, and that KeyBank was therefore liable for HPS's actions. *See* Compl., ¶¶ 135-152. But Plaintiffs also acknowledge that KeyBank's relationship with HPS is governed by the MPA between them. (*See* Compl., ¶ 59; *see also* MPA.) Section 1.1(k) of the MPA explicitly states:

> Keybank and HPS agree that in performing their responsibilities pursuant to this Agreement, they are in the position of independent contractor. This Agreement is not intended to create, nor does it create and shall not be construed to create, a relationship or joint venture or agency or any association for profit between KeyBank and HPS. HPS is not authorized thereunder to hold itself out as an agent of KeyBank or to inform or represent that HPS has authority to bind or obligate KeyBank or to otherwise act on behalf of KeyBank.

The relationship between HPS and KeyBank is defined by the clear terms of the MPA – HPS is an independent contractor to KeyBank – and Plaintiffs cannot impute HPS's alleged

liability to KeyBank. *See Miller*, 16 N.E.2d at 448; *Elliot-Williams Co., Inc.*, 9 S.W.3d at 803; Restatement (Second) of Torts § 409. Plaintiffs therefore fail to state a claim for vicarious liability.

3. Plaintiffs Do Not and Cannot State a Claim Against HPS For Which KeyBank Could Be Held Vicariously Liable

If Plaintiffs do not state a claim against HPS, they cannot impute any liability to KeyBank. *See, e.g., Citicasters Co. v. Bricker & Eckler, LLP*, 778 N.E.2d 663, 668 (Ohio App. 2002) ("[U]nder established principles of agency law, the principal is entitled to assert any defense that the agent would be entitled to assert."); Restatement (Second) of Agency § 219, cmt. c ("In an action against the master, the [master] has all the defenses open to one defending an action of tort."); *see also Meckfessel v. Fred Weber, Inc.*, 901 S.W.2d 335, 339 (Mo. App. 1995) ("Under the doctrine of vicarious liability, the liability of the master is derived from and can be no greater than the liability of the servant."); Restatement (Second) of Judgments § 51, cmt. b, illus. 2 ("A judgment for [agent] precludes [plaintiff] from bringing an action against [principal] for his injuries").

As HPS has argued in its Motion to Dismiss (which KeyBank incorporates herein by reference), HPS has no negligence liability to issuers resulting from the data intrusion. *See generally* HPS's Memorandum in Support of Motion to Dismiss (Docket Entry 40, case no. 09-md-02046), filed October 23, 2009 (invoking, among other things, the *Iqbal* and *Twombly* pleading standard, a lack of common law duty, and the economic loss rule).

Indeed, in a case materially identical to the one at bar involving the CardSystems data intrusion, the issuers' negligence claims (asserted by a subrogee) against the acquiring bank and its processor were dismissed under Rule 12(b)(6). *See Cumis Ins. Soc'y, Inc. v. Merrick Bank Corp.*, No. 07-374, 2008 WL 4277877, at * 11-12 (D. Ariz. Sep. 18, 2008). It follows from the

ruling in *Merrick Bank* that HPS cannot be held liable to Plaintiffs. Therefore, KeyBank cannot be vicariously liable to Plaintiffs.

E. Plaintiffs' Subrogee Claims Fail

Under Count Five, Plaintiffs assert a claim on behalf of subrogees that "stand in the shoes" of proposed class members. (Compl. ¶ 154.) But Plaintiffs have not alleged that any of them are actually subrogees. And even if they did, the subrogee's claims fail for the same reasons that Plaintiffs' claims fail and Count Five should be dismissed.

V. CONCLUSION

For the foregoing reasons, KeyBank's motion to dismiss should be granted and Plaintiffs' claims against KeyBank should be denied with prejudice.[10]

Respectfully submitted,

DATED: April 9, 2010

/s/ James A. Slater

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[10] Heartland Bank has also filed a motion to dismiss (ECF ## 26, 27). To the extent Heartland Bank's arguments support dismissal of the claims against KeyBank, KeyBank incorporates Heartland Bank's arguments herein.

CERTIFICATE OF SERVICE

I hereby certify that on April 9, 2010, a copy of the foregoing was filed electronically. Notice of this filing will be sent to counsel for all parties by operation of the Court's electronic filing system. Parties may access this filing through the Court's system.

/s/ James A. Slater
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