# *United States Court of Appeals*

FIFTH CIRCUIT
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LYLE W. CAYCE
CLERK

TEL. 504-310-7700
600 S. MAESTRI PLACE
NEW ORLEANS, LA 70130

February 11, 2013

Mr. Michael Allen Caddell
Caddell & Chapman, P.C.
1331 Lamar Street
Suite 1070
Houston, TX 77010-3027

Ms. Cynthia B. Chapman
Caddell & Chapman, P.C.
1331 Lamar Street
Suite 1070
Houston, TX 77010-3027

Mr. Richard Lyle Coffman
Coffman Law Firm
505 Orleans Street
First City Building
Suite 505
Beaumont, TX 77701-0000

Mr. Cory Steven Fein
Caddell & Chapman, P.C.
1331 Lamar Street
Houston, TX 77010-3027

Mr. Joseph G. Sauder
Chimicles & Tikellis, L.L.P.
361 W. Lancaster Avenue
Haverford, PA 19041-0100

No. 12-20648, In Re: Heartland Payment Sys, et al
USDC No. 4:09-MD-2046

The following pertains to your brief electronically filed on February 8, 2013.

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Brandy C. Lemerle, Deputy Clerk
504-310-7714

cc: Mr. Michael J. Conlan
Mr. Seth Carlton Harrington
Ms. Anne E. Johnson
Mr. Brant Mitchell Laue
Mr. Neal Stuart Manne
Mr. Douglas Harlan Meal

**No. 12-20648**

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**IN THE UNITED STATES COURT OF APPEALS**
**FOR THE FIFTH CIRCUIT**

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**LONE STAR NATIONAL BANK, N.A.; AMALGAMATED BANK; FIRST BANKERS TRUST COMPANY, N.A.; PENNSYLVANIA STATE EMPLOYEES CREDIT UNION; ELEVATIONS CREDIT UNION; O BEE CREDIT UNION; AND SEABOARD FEDERAL CREDIT UNION,**

**Plaintiffs-Appellants**

**v.**

**HEARTLAND PAYMENT SYSTEMS, INC.,**

**Defendant-Appellee**

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**ON APPEAL FROM THE UNITED STATES DISTRICT COURT**
**FOR THE SOUTHERN DISTRICT OF TEXAS,**
**HOUSTON DIVISION**

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# REPLY BRIEF OF APPELLANTS

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Michael A. Caddell
Cynthia B. Chapman
**CADDELL & CHAPMAN**
1331 Lamar, Ste. 1070
Houston, TX 77010
(713) 751-0400

Richard L. Coffman
**THE COFFMAN LAW FIRM**
First City Building
505 Orleans, Ste. 505
Beaumont, TX 77701
(409) 833-7700

Joseph G. Sauder
**CHIMICLES & TIKELLIS LLP**
One Haverford Centre
361 W. Lancaster Avenue
Haverford, PA 19041
(610) 642-8500

**ATTORNEYS FOR APPELLANTS**

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## INTRODUCTION

The Financial Institutions'[1] opening brief ("FIs' Br.") explained that the New Jersey economic loss rule does not bar their negligence claim against Appellee Heartland Payment Systems, Inc. ("Heartland") because (i) the parties have never entered into (much less, negotiated) a contract, (ii) Heartland is not a member of the Visa or MasterCard networks, (iii) there is no evidence of any contract(s) between Heartland and Visa or MasterCard, and (iv) there is no contractual remedy available to the Financial Institutions vis-à-vis Heartland. *See, e.g.*, FIs' Br. at 11, 14. In its opposition brief ("Heartland Br."), Heartland fails to refute these critical points. Instead, it resorts to arguing that the parties are somehow connected by a "series of contractual relationships"[2] and a "relationship" that "arises out of contract."[3] As discussed below, Heartland's attempt to shoehorn the economic loss rule into this attenuated fact scenario is neither persuasive, nor supported by New Jersey law.

Heartland's untenable positions do not end there. Incredibly, Heartland—a payment card processor entrusted with massive amounts of sensitive financial information that Heartland claimed would be appropriately protected—contends

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[1] Appellants are also referred to in this Reply Brief as the "Financial Institutions" or the "Issuing Banks."

[2] *See* Heartland Br. at 10.

[3] *Id.* at 15.

that it "owed no common-law duty" to the Financial Institutions. Heartland Br. at 25. Heartland is wrong as a matter of law. Heartland's reliance on the *Twombly* and *Iqbal* pleading standards and attempt to defensively invoke collateral estoppel are also legally insupportable. The Court, therefore, should reverse the judgment of the district court and remand this case to the district court for further proceedings.

## ARGUMENTS AND AUTHORITIES

### A. The New Jersey Economic Loss Doctrine Does Not Bar the Financial Institutions' Negligence Claim.

While Heartland states that it has a contractual relationship with the Acquiring Banks and Merchants,[4] it does not contend that it is in direct privity with the Issuing Banks. Nor does Heartland offer any evidence or facts to refute the Financial Institutions' claim that Heartland is not a member of the Visa and MasterCard Networks. Indeed, Heartland even acknowledges that "***the Issuing Banks do not have a direct contractual remedy against non-members [of the Card Brands' networks] such as Heartland . . .***"[5]

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[4] *See id.* at 9 ("Payment card processors, such as Heartland, contract with acquiring banks and merchants to assist in the processing of authorization messages and settlement of payments to merchants.").

[5] *Id.* at 23. For this reason, the *Dynalectric* court's finding that the economic loss rule barred tort claims where the plaintiff had "another means of redress against the alleged tortfeasor" is inapposite. *Dynalectric Co. v. Westinghouse Electric Corp.*, 803 F. Supp. 985, 991 (D.N.J. 1992). *See also* FIs' Br. at 17–18 (discussing *id.*).

Heartland attempts to explain that it is connected with the Issuing Banks through a "contractual relationship" whereby (i) the Issuing Banks have a contract with Visa and MasterCard (the "Card Brands"), (ii) the Card Brands have a contract with the Acquiring Banks, and (iii) the Acquiring Banks have a contract with merchants and processors, such as Heartland. Heartland Br. at 10. Despite the attenuated connection between them, Heartland argues that Appellants' negligence claim is barred under the New Jersey economic loss doctrine because "the parties' relationship arises out of contract." *Id.* at 15.

New Jersey courts, however, do not view the economic loss doctrine so broadly. *See, e.g., Ford Motor Co. v. Edgewood Properties, Inc.*, No. 06-1278, 2012 U.S. Dist. LEXIS 125197, at *74-76 (D.N.J. Aug. 31, 2012) ("Here, Edgewood alleges contract claims against Ford and EQ, but not against Arcadis. Accordingly it cannot be said that Edgewood's recovery from Arcadis 'flows only from a contract.'") (internal citations omitted). In fact, Appellants' opening brief discussed at length another District of New Jersey case squarely holding that the absence of a direct contractual relationship between a plaintiff and a defendant specifically precludes the application of the New Jersey economic loss rule. *See* FIs' Br. at 17–19 (citing *Consult Urban Renewal Dev. Corp. v. T.R. Arnold & Assoc.*, No. 06-1684, 2009 U.S. Dist. LEXIS 56194 (D.N.J. Jul. 1, 2009)).

The *Consult Urban* court explained that the "rationale behind the economic loss doctrine is that contract law is more suitable for the adjudication of certain types of claims because the parties are able to negotiate the allocation of the risk at the outset." 2009 U.S. Dist. LEXIS 56194, at *10. Just like the case here, the plaintiff in *Consult Urban* was "at most a third party beneficiary" to a contract between others, which the plaintiff "had no opportunity to negotiate . . ." *Id.* The *Consult Urban* court concluded that in such a scenario "it makes little policy sense to apply the [economic loss] doctrine."[6] *Id.* Remarkably, Heartland's brief does not attempt to distinguish—much less, even cite—*Consult Urban*.

Instead, Heartland relies on a string of data breach cases from other jurisdictions that have applied the economic loss rule *under laws other than New Jersey*. Heartland Br. at 20 n. 9. Setting aside this material difference,[7] the data breach cases addressing the economic loss doctrine have not uniformly prohibited tort claims. In *Banknorth, N.A. v. BJ's Wholesale Club, Inc.*, 394 F. Supp. 2d 283 (D. ME. 2005), for example, an issuer bank asserted negligence and other claims

[6] The *Consult Urban* court also noted that the economic loss rule "typically applies to the sale of goods, not the provision of services," and "[w]hile some jurisdictions have chosen to extend the economic loss doctrine to services, there is no evidence to suggest that New Jersey has done so." 2009 U.S. Dist. LEXIS 56194, at *9 (citations omitted). Here, Heartland does not sell goods; it provides debit and credit card processing services. *See* Financial Institutions' Master Complaint ("MC") (Clerk's Record ("CR") 1399-1450) ¶¶ 24, 28.

[7] *See Hakimoglu v. Trump Taj Mahal Assocs.*, 70 F.3d 291, 295 (3d Cir. 1995) ("The New Jersey Supreme Court has long been a leader in expanding tort liability.").

against a merchant and its acquirer for damages arising from a data breach. The district court refused to dismiss the issuing bank's negligence claim on the basis of the economic loss rule, explaining that these arguments "hinge upon issues of fact as to the nature of the relationships between the parties that the Court may not appropriately resolve via a motion to dismiss." *Id.*, 394 F. Supp. 2d at 287. In another case cited by Heartland, the district court concluded that a credit union's financial losses from a data breach were not subject to the economic loss rule. *See Cumis Ins. Society, Inc. v. Merrick Bank Corp.*, No. 07-374, 2008 U.S. Dist. LEXIS 78451, at *21-22 (D. Ariz. Sept. 18, 2008).[8] Under controlling New Jersey precedent, and consistent with other the law of other jurisdictions, the economic loss rule does not apply here either.

**1. Heartland Owed the Issuing Banks a Duty to Take Reasonable Measures to Avoid the Risk of a Foreseeable Intrusion Into Its Computer Network and Theft of the Confidential Payment Card Data.**

Heartland contends that Appellants are asking this Court to "create a duty under New Jersey law requiring handlers of payment card data to safeguard payment card information for the benefit of issuers of payment cards." Heartland

[8] The *Cumis Ins. Society* court ultimately dismissed the plaintiff's negligence claim after concluding that the defendants did not owe a tort duty as a matter of Arizona law. *Id.*, 2008 U.S. Dist. LEXIS 78451, at *31–34. As discussed below, however, Heartland owed such a duty to the Financial Institutions under New Jersey law.

Br. at 3. Heartland claims that such a duty has "been rejected by every court that has considered the issue." *Id.* at 15.

As Appellants demonstrated in their opening brief, however, such a duty of reasonable care plainly exists under New Jersey jurisprudence. Heartland's attempt to distinguish the New Jersey Supreme Court's decision in *People Express Airlines, Inc. v. Consolidated Rail Corp.*, 495 A.2d 107 (N.J. 1985) is wholly unpersuasive. *See* Heartland Br. at 27 n. 12. The plaintiff in *People Express* was a commercial airline that suffered business interruption damages after a fire led to the release of a dangerous chemical in close proximity to the airport, thereby forcing the airline to evacuate its premises. *People Express*, 495 A.2d at 108–09.

In rejecting the defendant's argument that the economic loss rule barred the plaintiff's tort claim, the court explained that:

> [A] defendant owes a duty of care to take reasonable measures to avoid the risk of causing economic damages, aside from physical injury, to particular plaintiffs or plaintiffs comprising an identifiable class with respect to whom defendant knows or has reason to know are likely to suffer such damages from its conduct. A defendant failing to adhere to this duty of care may be found liable for such economic damages proximately caused by its breach of duty.

*People Express*, 495 A.2d at 116. The *People Express* court then distinguished the "identifiable class" from, for example, "persons travelling on a highway near the scene of a negligently-caused accident. . .who are delayed in the conduct of their affairs" and whose "presence within the area would be fortuitous . . ." *Id.* Their

claims would be barred by the economic loss rule. *See id.*

Appellants fit squarely within the class of foreseeable and identifiable victims to whom Heartland owed a duty of care under the *People Express* framework. *See, e.g.*, "MC" ¶ 101. They are analogous to the nearby airline that suffered business interruption damages; to wit, both were the foreseeable victims of the respective defendants' negligence, and the defendants knew, or had reason to know, they were likely to suffer damages. Appellants bear no resemblance to random members of the general public who fortuitously happened to be in the area where the accident occurred whose claims were barred by the economic loss doctrine. *People Express*, 495 A.2d at 116.

Even the district court found in the case against the Acquiring Banks (the KeyBank Case) that Appellants "satisfy the *People Express* foreseeability test" (CR 3364), correctly concluding that "*People Express* addresses situations in which the parties have no contractual relationship . . ." CR 3367. However, the district court's decision to nonetheless apply the economic loss rule on the premise that the "relationships among issuers, acquirers, and their contractors—such as Heartland Payment Systems—are governed by the Visa and MasterCard regulations, not tort law" (CR 3771; 3769-70) is incorrect as a matter of fact[9] and

[9] *See, e.g.*, FIs' Br. at 5–6, 14 (explaining that Heartland is not a member of the Visa and MasterCard networks, and thus, there are no contracts between the Financial Institutions and Heartland).

law.[10]

Heartland misreads *People Express* as limited to situations "where economic losses were accompanied by actual or threatened physical harm to person or property." Heartland Br. at 27 n. 12. But there is nothing in *People Express* that supports such a narrow view. *People Express*, 495 A.2d at 109 ("No physical damage to airline property and no personal injury occurred as a result of the fire.").

Moreover, the New Jersey Supreme Court subsequently explained that *People Express* stands for the proposition that "a plaintiff could bring an action for purely economic losses, regardless of any accompanying physical harm or property damage, if the plaintiff was a member of an identifiable class that the defendant should have reasonably foreseen was likely to be injured by the defendant's conduct and the plaintiff's injuries had been proximately caused by the defendant's negligence." *Carter Lincoln-Mercury, Inc., Leasing Div. v. EMAR Group, Inc.*, 135 N.J. 182, 195 (N.J. 1994) (citing *People Express*, 495 A.2d at 107). As discussed above, this describes Appellants here.

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[10] *See Consult Urban Renewal*, 2009 U.S. Dist. LEXIS 56194, at *4 (finding, as a matter of New Jersey law, that the lack of a direct contractual relationship between the plaintiff and the defendant prevented the defendant from applying the economic loss rule); *Ford Motor Co.*, 2012 U.S. Dist. LEXIS 125197, at *74–76; *Banknorth, N.A.*, 394 F. Supp. 2d at 287. *See also Anderson v. Hannaford Bros. Co.*, 659 F.3d 151, 164 (1st Cir. 2011). The fact patterns of these cases make it clear that Heartland's argument that a "special relationship" between the parties is required to recover economic losses in tort is unavailing. *See* Heartland Br. at 26.

Heartland overreaches by claiming that "[e]very court that has faced the issue whether a duty exists to safeguard card data for the benefit of payment card issuers has rejected the call to expand the common law to recognize such a duty." Heartland Br. at 27. Courts, however, in closely analogous data breach cases brought by consumers, have recognized an implied duty to take reasonable steps to protect sensitive data when a party has been entrusted with this information. *See, e.g.*, *Richardson v. DSW, Inc.*, No. 05-4599, 2005 U.S. Dist. LEXIS 26750, at *6–10 (N.D. Ill. Nov. 3, 2005).

Appellants' opening brief cited the First Circuit's observation that it would be foreseeable for a customer with a compromised debit or credit card to replace that card. *Anderson*, 659 F.3d at 164.[11] Heartland inexplicably ignores *Anderson* in its brief. Heartland also ignores *Banknorth, N.A., supra*, which rejected the defendant's argument that an issuing bank's negligence claim should be dismissed because it did not owe a duty of care *under tort law* "to safeguard cardholder information from thieves."[12] *Id*., 394 F. Supp. 2d at 286–87.

[11] *See* FIs' Br. at 2. Curiously, the district court found that the fact it is foreseeable for a consumer with a compromised debit or credit card to replace that card "further reinforces the conclusion that New Jersey law would not allow their recovery in tort law." CR 3772 n.17.

[12] *See* FIs' Br. at 23. The *Banknorth* court also rejected the defendants' argument that plaintiff's tort claims should be dismissed pursuant to the economic loss rule. *Banknorth*, N.A., 394 F. Supp. 2d at 286.

The three principal cases that Heartland claims are "directly on point" with this case (Heartland Br. at 30) are easily distinguishable—none of them, for example, applied the economic loss doctrine under New Jersey law. *See Cumis Ins. Society, Inc.*, 2008 U.S. Dist. LEXIS 78451, at *12 (Arizona law); *BancFirst v. Dixie Rests., Inc*., No. 11-174, 2012 U.S. Dist. LEXIS 1038, at *8 (W.D. Okla. Jan. 4, 2012) (Oklahoma law); *Digital Federal Credit Union v. Hannaford Bros. Co.*, No. BCD-CV-10-4, 2012 Me. Super. LEXIS 30, at *9 (Me. Super. Ct. 2012) (Maine law). As this Court has recognized, different states treat the economic loss rule differently. *See Spence v. Glock, GES.m.b.H*., 227 F.3d 308, 313 n.8 (5th Cir. 2000). *See also, Agostino v. Quest Diagnostics Inc*., 256 F.R.D. 437, 464 (D.N.J. 2009) ("States apply materially different standards of . . . economic loss requirements . . . ") (citing Joel S. Feldman, et al., *Class Certification Issues for Non-Federal Question Class Actions—Defense Perspective*, 777 PLI/LIT 35, 99 (2008)). And, as discussed above, New Jersey courts have declined to apply the economic loss rule to prohibit tort claims in closely analogous situations. *See, e.g., People Express, Consult Urban.*

Finally, Heartland's reliance on the New Jersey data breach notification statute—which "require[s] businesses holding personal information to notify the public when a breach occurs"—is a red herring. *See* CR 3773; Heartland Br. at 29–30. The principal basis for Appellants' negligence claim is that Heartland

breached its duty to exercise reasonable care in safeguarding and protecting the confidential payment card data by allowing the Data Breach to occur in the first place. *See* MC ¶ 101.[13] As such, it is irrelevant that New Jersey data breach notification requirements are triggered *after* a data breach has occurred.

In sum, Heartland's unsupported view of the law would result in the economic loss rule being expanded to bar any tort claim any time an alleged tortfeaser can point to the existence of virtually any contract, no matter how remote, that could conceivably link the parties. Such a result is directly contrary to the New Jersey Supreme Court's decision in *People Express*, the *Consult Urban* case that Heartland altogether fails to address, and other authorities interpreting the New Jersey economic loss doctrine. The district court's decision to the contrary, therefore, should be reversed.

**2. New Jersey Law Applies to Appellants' Negligence Claim.**

Heartland acknowledges that it "did not dispute" Appellants' position below that "the laws of their respective home states should not apply to their negligence claims" for purposes of the motion to dismiss.[14] It also points out that the "District

[13] While the MC also alleges that Heartland had a duty to timely disclose the data breach to consumers (MC ¶ 102), the breached duty for which Appellants seek economic damages is Heartland's failure to safeguard and protect the confidential payment card data in the first place. *Id.* ¶ 101.

[14] Heartland Br. at 7 n. 6. *See also id.* at 35.

Court had no occasion to reach th[e] choice-of-law dispute." *Id.* at 32. Yet, unable to prevail under New Jersey law, Heartland asks this Court to perform a choice of law analysis, and conclude that Texas law—rather than New Jersey law—applies to Appellants' negligence claim.

Preliminarily, the choice of law issue should be resolved by the district court—not this Court. *Boyd Rosene & Assocs. v. Kansas Mun. Gas Agency,* 123 F.3d 1351, 1353 (10th Cir. 1997) (remanding the case to the district court to conduct the choice of law analysis); *Congress Talcott Corp. v. Gruber*, 993 F.2d 315, 328 (3d Cir. 1993) ("The choice-of-law question in this case is too complex to be determined without a great deal of further analysis, which is a task for the district court, assisted by arguments of the parties, in the first instance.").

Even if this Court were to entertain Heartland's choice of law arguments, the record wholly supports the application of New Jersey law. While Heartland may have certain facilities located in Texas, it is beyond dispute that the company is headquartered in Princeton, New Jersey. Heartland Br. at 35. According to its most recent Form 10-K filed with the Securities and Exchange Commission ("SEC"), merchants in New Jersey represented 4% of Heartland's total bank card processing volume.[15] In other documents filed with the SEC, Heartland describes

[15] *See* http://www.sec.gov/Archives/edgar/data/1144354/000114435412000030/hpy1231201110k.htm.

New Jersey as one of the places from which it "obtain[s] a substantial amount of our bank card processing volume," and disclosed that it was "advised by the United States Attorney for the District of New Jersey that it has commenced an investigation . . . to determine whether there have been any violations of the federal securities laws in connection with our disclosure of the Processing Systems Intrusion . . ."[16] Heartland also litigated a securities fraud lawsuit related to the Data Breach in the District of New Jersey.[17]

To the extent Heartland makes fact-dependent arguments concerning the "principal location" of its information technology systems, security systems, "alleged improper conduct," and relevant personnel and equipment that were impacted by the Data Breach (Heartland Br. at 3, 35), such issues should be resolved after Appellants are afforded an adequate opportunity to conduct discovery to test the veracity of Heartland's claims.[18] For purposes of this appeal, the legal issues should be decided under New Jersey law, just as they were below.

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[16] *See* http://www.databreaches.net/?p=2458 (last visited Feb. 6, 2013).

[17] *In re Heartland Payment Sys., Inc. Sec. Litig.*, No. 09-1043, 2009 U.S. Dist. LEXIS 114866 (D.N.J. Dec. 7, 2009). Heartland's reliance on the decision in the securities fraud case to support its *Twombly/Iqbal* argument here is misplaced given that, *inter alia*, the case was dismissed well before the Visa and MasterCard settlements were announced on January 8, 2010 and May 19, 2010, respectively. *See* Heartland Br. at 13, 38–39.

[18] *See Hommel v. Pierce*, No. 95 Civ. 2013 (CSH), 1996 U.S. Dist. LEXIS 1218, at *1 (S.D.N.Y. Feb. 6, 1996) (recognizing that plaintiff was "entitled to some discovery on the issue of the location of the principal place of business of defendant . . .").

## B. The Complaint Satisfies the Applicable *Iqbal* and *Twombly* Pleading Standards.

Heartland next argues that the MC fails to state a claim for relief under *Ashcroft v. Iqbal*, 129 S. Ct. 1937 (2009) and *Bell Atl. Corp. v. Twombly*, 550 U.S. 544 (2007). Heartland specifically contends that the MC (i) alleges no facts that, if proven, "would show Heartland's data security practices to be negligent," (ii) largely relies on events that occurred after the Data Breach, and (iii) fails to demonstrate that Heartland's conduct actually caused Appellants' injuries. Heartland Br. at 38. Heartland further acknowledges that the district court did not specifically address the applicability of these pleading standards in its decision below. *Id*. at 37 n. 16. Each of these arguments is unpersuasive.

Rule 8(a)(2) of the Federal Rules of Civil Procedure requires that a complaint contain a "short and plain statement of the claim showing that the pleader is entitled to relief." *Id.* In *Twombly,* the Supreme Court reiterated that Rule 8 does "not require heightened fact pleading of specifics." *Twombly,* 550 U.S. at 570. While the subsequently decided *Iqbal* decision elaborated on the pleading standards set forth in *Twombly*, it did not heighten the standard of review for a motion to dismiss. *Iqbal,* 129 S. Ct. at 1953.[19] *See also Doe v. Covington*

[19] *See also Iqbal, 129 S. Ct. at 1950 ("In keeping with these principles [from Twombly] a court considering a motion to dismiss can choose to begin by identifying pleadings that, because they* are no more than conclusions, are not entitled to the assumption of truth."); *id.* at 1949 (discussing the "working principles [that] underlie our decision in *Twombly*.").

*County Sch. Dist.*, 649 F.3d 335, 342 n.13 (5th Cir. 2011) ("*Iqbal* does not require a heightened pleading standard.").

Rather, under both *Twombly* and *Iqbal*, "[t]o survive 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.'" *Id.* at 1949 (quoting *Twombly*, 127 S. Ct. at 1974)). A claim "has facial plausibility when the plaintiff pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Id.* This Court has cited *Twombly* for the proposition that "a complaint 'does not need detailed factual allegations,' but must provide the plaintiff's grounds for entitlement to relief—including factual allegations that when assumed to be true 'raise a right to relief above the speculative level.'" *Cuvillier v. Sullivan*, 503 F.3d 397, 401 (5th Cir. 2007) (quoting *Twombly*, 127 S. Ct. at 1964-65).

Heartland's contention that Appellants fail to meet the applicable pleading standards is directly refuted by the MC, which points to, *inter alia*, (i) a statement by Visa's Chief Enterprise Risk Officer that the Data Breach would not have occurred had Heartland been vigilant about maintaining its compliance with the applicable security standards,[20] (ii) an acknowledgement by Heartland's president following the Data Breach that Heartland could have done more to prevent the

[20] MC ¶¶ 61–62. And, unlike in this case where no meaningful discovery occurred, Visa and MasterCard certainly had access to many non-public facts related to the Data Breach.

breach from occurring,[21] (iii) the removal of Heartland from Visa's list of PCI-DSS compliant entities after Visa found that Heartland violated its operating regulations,[22] and (iv) fines assessed to Heartland's Acquiring Banks by MasterCard because of Heartland's failure to take appropriate security measures.[23]

Contrary to Heartland's contention, these post-intrusion admissions (and alternative security measures available to it) are not the types of subsequent remedial measures that are inadmissible pursuant to FED. R. EVID. 407. *See Fincher v. Kan. City Southern Ry*., 2009 U.S. Dist. LEXIS 6969, at *6–7 (W.D. La. Jan. 22, 2009) ("While the court agrees that subsequent remedial measures are not admissible under Rule 407, whether the defendant had alternative tools and methods at the workplace, including other available employees, at the time of the alleged injury is a factor that the jury should consider in determining negligence.") (citing *Stone v. New York Chicago & St. Louis. R.R. Co.*, 344 U.S. 407 (1953)).

Heartland's argument that the MC does not allege any facts demonstrating that its conduct actually caused Appellants' injuries should also be summarily

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[21] *Id.* ¶ 7.

[22] *Id.* ¶ 57.

[23] *Id.* at ¶ 59. *See also* Heartland Br. at 13 (describing the $59.2 million settlement reached with Visa and the $41.4 million settlement with MasterCard). Heartland's contention that any actions taken against it by Visa or MasterCard "are merely recitations by the Card Brands of the *same legal conclusion* the Issuing Banks advance here . . ." is undermined by the fact that Heartland decided to enter into settlements with both of these Card Brands to resolve these allegations. *See* Heartland Br. at 40 (emphasis in original).

rejected. *See* Heartland Br. at 41. The MC unambiguously avers in several places that Heartland's negligence and misconduct was the cause of Appellants' damages (*e.g.*, the cost of reissuing the compromised payment cards and reimbursing customers for fraudulent charges). *See* MC ¶¶ 11–19, 72, 106.

To the extent Heartland questions whether the fraudulent charges on payment cards issued by Appellants were, in fact, caused by the Data Breach or "the multitude of other ways that [unauthorized] charges can appear on card accounts" (Heartland Br. at 41), it raises a factual issue that should not be resolved in connection with a Rule 12(b)(6) motion to dismiss. *See, e.g., Page v. Postmaster Gen. & Chief Exec. Officer of the United States Postal Serv.*, No. 12-11747, 2012 U.S. App. LEXIS 22347, at *4 (11th Cir. Oct. 30, 2012) ("In adjudicating a motion to dismiss, the district court may not resolve factual disputes.") (citing *Chappell v. Goltsman*, 186 F.2d 215, 218 (5th Cir. 1950)). Appellants also cite *Anderson*—which is noticeably absent from Heartland's brief—for the proposition that it is foreseeable for consumers with compromised debit or credit cards to replace their cards.[24] It is just as foreseeable that the financial institutions that issued the compromised payment cards would also suffer related damages in the form of, *inter alia*, the hard costs to replace the compromised payment cards.

[24] *See* FIs' Br. at 2 n.1 (quoting *Anderson*, 659 F.3d at 164).

Heartland describes the factual allegations in the Financial Institutions' MC as the type of "unadorned, the defendant-unlawfully-harmed-me accusation" at issue in *Twombly* and *Iqbal*. *See* Heartland Br. at 42 (citing *Iqbal*, 129 S. Ct. at 1949). Both of these cases, however, re-affirm the time-tested standard that factual averments in a complaint should be taken as true for purposes of deciding whether the complaint states a plausible claim. *See Harold H. Huggins Realty, Inc. v. FNC, Inc.*, 634 F.3d 787, 803 n.44 (5th Cir. 2011) ("The Supreme Court's decisions in *Iqbal* and *Twombly* . . . did not alter the long-standing requirement that when evaluating a motion to dismiss under Rule 12(b)(6), a court must accept[] all well-pleaded facts as true and view[] those facts in the light most favorable to the plaintiff.") (citations omitted). Nor is the MC limited to "naked assertion[s] devoid of further factual enhancement" of the type with which the *Iqbal* and *Twombly* courts were concerned.[25] *See Iqbal*, 129 S. Ct. at 1949 (internal citations omitted).

[25] The plaintiff in *Iqbal*, a Pakistani Muslim who was detained in the wake of the September 11 attacks after being designated a person "of high interest" to the United States (and who ultimately pled guilty to fraud-related criminal charges), filed a *Bivens* action against the Attorney General of the United States and the Director of the FBI, among others. *Iqbal*, 127 S. Ct. at 1942–44. His complaint, which was held to be deficient, contained vague conclusory allegations that these high-level officials "each knew of, condoned, and willfully and maliciously agreed to subject" him to the harsh conditions of his confinement "as a matter of policy, solely on account of [his] religion, race, and/or national origin and for no legitimate penological interest." *Id.* at 1951. Similarly, the complaint the Supreme Court found deficient in *Twombly* contained conclusory allegations that the defendants had unlawfully met and conspired in violation of the antitrust laws, and pointed to parallel conduct that was also consistent with lawful behavior. *Twombly*, 550 U.S. at 551, 567.

In sum, the Financial Institutions' MC squarely meets the plausibility standard because it "pleads factual content that allows the court to draw the reasonable inference that the defendant is liable for the misconduct alleged." *Id.* at 1950. The *Iqbal* and *Twombly* pleading standards, therefore, are satisfied.

### C. None of the Financial Institutions are Collaterally Estopped from Pursuing Their Negligence Claim against Heartland.

Heartland argues that some—but not all[26]—of the Appellants are collaterally estopped from pursuing this appeal by virtue of the KeyBank Case decision, which was not appealed. *See* Heartland Br. at 43. Heartland specifically contends that because some of the Appellants asserted (and lost) the "same" negligence claim against KeyBank and Heartland Bank, they should be collaterally estopped from further pursuing their claim against Heartland. *Id*.

"[C]ollateral estoppel applies when a previously litigated issue of law or fact was ***identical*** to the present issue, actually litigated, necessary to a final judgment, and reviewed under the same standard as the present issue." *Duffy & McGovern Accommodation Servs. v. QCI Marine Offshore, Inc*., 448 F.3d 825, 829 (5th Cir. 2006) (emphasis supplied). The parties in the KeyBank Case certainly litigated the negligence claim alleged in that case. Heartland's effort to use the KeyBank Case

[26] As such, even if Heartland's collateral estoppel argument had merit—which it does not—the argument would not have any impact on Appellants that were not parties in the KeyBank Case (*i.e.*, Amalgamated Bank and First Bankers Trust Company, N.A.).

opinion as a collateral estoppel defense here, however, fails because the negligence claims in the two cases are fundamentally different. For example, in the KeyBank Case, certain of the Appellants sought relief for the Acquiring Banks' alleged negligence (not Heartland's alleged negligence) in (i) selecting and retaining Heartland to process their payment card transactions, (ii) failing "to monitor the security of the [Heartland's] database" (CR 3326), and (iii) in failing "to ensure that [Heartland] complied with the Payment Card Industry Data Security Standards." CR 3328.

On the other hand, Appellants' negligence claim against Heartland in this case is not based on Heartland's failure to properly oversee a third party's security systems. Rather, Appellants assert their negligence claim against Heartland for its failure to adequately monitor its own security systems. These fundamentally different negligence claims are not sufficiently "identical" for collateral estoppel to apply. *See Swate v. Hartwell* (*In re Swate*), 99 F.3d 1282, 1289 (5th Cir. 1996) (citations omitted) (for the doctrine of collateral estoppel to be appropriate, "the issue at stake [must be] *identical* to the one involved in the prior action …"); *Day v. Lockheed Martin Corp.*, 428 Fed. Appx. 275, 278 (5th Cir. 2011) (collateral estoppel applies where an identical issue was previously adjudicated, actually litigated, and necessary to the decision in the prior litigation) (citing *Pace v. Bogalusa City Sch. Bd.*, 403 F.3d 272, 290 (5th Cir. 2005)).

But even if the Court were to find that the economic loss issue addressed in the KeyBank Case was sufficiently identical to the economic loss issue in this case—and it is not—collateral estoppel would not apply if the Court concludes that the district court erred as a matter of law. *See Petro-Hunt, L.L.C. v. United States*, 365 F.3d 385, 397 (5th Cir. 2004) ("In this circuit, collateral estoppel applies to 'pure questions of law' only when there has been no 'change in controlling legal principles.'") (citations omitted). Under either scenario, the result is the same—Appellants are not collaterally estopped from pursuing their negligence claim against Heartland.

## CONCLUSION

For the foregoing reasons, and the reasons set forth in their opening brief, Appellants respectfully request that the Court reverse the judgment of the district court, remand this case to the district court for further proceedings, and grant Appellants such other and further relief, in law or in equity, to which they are justly entitled.

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Respectfully submitted,

By: */s/ Richard L. Coffman*

Richard L. Coffman
**THE COFFMAN LAW FIRM**
First City Building
505 Orleans, Ste. 505
Beaumont, TX 77701
Telephone: (409) 833-7700
Facsimile: (866) 835-8250
rcoffman@coffmanlawfirm.com

Michael A. Caddell
Cynthia B. Chapman
Cory S. Fein
**CADDELL & CHAPMAN**
1331 Lamar, Ste. 1070
Houston TX 77010
Telephone: (713) 751-0400
Facsimile: (713) 751-0906
mac@caddellchapman.com
cbc@caddellchapman.com
csf@caddellchapman.com

Joseph G. Sauder
**CHIMICLES & TIKELLIS, LLP**
One Haverford Centre
361 W. Lancaster Avenue
Haverford PA 19041
Telephone: (610) 642-8500
Facsimile: (610) 649-3633
JGS@chimicles.com

**ATTORNEYS FOR APPELLANTS**

## CERTIFICATE OF SERVICE

I hereby certify that the Reply Brief of Appellants was filed with the Clerk of the United States Court of Appeals for the Fifth Circuit On February 8, 2013. I further certify that a true and correct copy of the Reply Brief of Appellants also was sent to the following counsel of record, via United States mail and/or electronic mail, on February 8, 2013.

*/s/ Richard L. Coffman*
Richard L. Coffman
Counsel for Appellants

Douglas H. Meal
David T. Cohen
Seth C. Harrington
Anne Johnson Palmer
Anne Johnson Palmer
**ROPES & GRAY, LLP**
Prudential Tower
800 Boylston Street
Boston MA 02199-3600

Neal S. Manne
Erica W. Harris
David M. Peterson
**SUSMAN GODFREY, LLP**
1000 Louisiana Street, Suite 5100
Houston TX 77002-5096

**ATTORNEYS FOR APPELLEES**

## CERTIFICATE OF CM/ECF COMPLIANCE

I hereby certify that (i) required privacy redactions have been made pursuant to Fifth Circuit Rule 25.2.13, (ii) this electronic submission and all attachments are exact copies of the paper copies of such documents pursuant to Fifth Circuit Rule 25.2.1, and (iii) this submission and all attachments have been scanned for viruses with the most recent version of a commercial virus scanning program and are free of viruses.

*/s/ Richard L. Coffman*
Richard L. Coffman
Counsel for Appellants

## CERTIFICATE OF COMPLIANCE WITH RULE 32(a)

1. This reply brief complies with the type-volume limitation of Fed. R. App. P. 32(a)(7)(B) because this reply brief contains 5,358 words, excluding the parts of the brief exempted by Fed. R. App. P. 32(a)(7)(B)(iii).

2. This reply brief complies with the typeface requirements of Fed. R. App. 32(a)(5) and the type style requirements of Fed. R. App. P. 32(a)(6) because this brief has been prepared in the proportionally spaced typeface using Microsoft Word 2010 in 14-point Times New Roman type style.

*/s/ Richard L. Coffman*
Richard L. Coffman
Counsel for Appellants

Dated: February 8, 2013