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Top 10 Litigation Risks For Retailers In 2017

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With the 2017 retail season in full swing, what are the hot topics keeping retailers up at night? I have distilled this top 10 list of litigation risks and trends based on client feedback and our comprehensive Retail Industry Risk Assessment Checklist.

Data Breach/Cyber-Ransom Exposure

In 2012, FBI Director Robert Mueller said it best: "There are only two types of companies: those that have been hacked and those that will be."[1] The risk of a data breach — and how the company will respond in the event of breach — keeps many retailers on edge.

According to the Breach Level Index, the retail industry was the 4th most popular target of hackers in the first half of 2016, an increase of over 90 percent from the same period just three years earlier.[2]

In addition, we have seen the number of cyber-ransom cases increase dramatically over the last year. In a cyber-ransom attack, hackers break into a company's network, hijack critical data and threaten to destroy it if a hefty ransom is not paid within a short period of time.

Increasingly, data breach lawsuits come with a steep price tag. According to the Ponemon Institute's 2016 Cost of Data Breach Study: Global Analysis, on average, data breaches cost each affected U.S. company $7.01 million.[3] On March 17, 2017, Neiman Marcus agreed to pay $1.6 million to settle a data breach class action over exposed credit card information of approximately 350,000 customers.

On March 14, 2017, Home Depot agreed to pay over $25 million to settle data breach claims brought by a proposed class of financial institutions in the wake of a 2014 breach that affected approximately 56 million customers. (This settlement is tacked on to the $140 million Home Depot already paid to settle claims brought by credit card issuers, and another $13 million to settle consumers' claims last year.) Similarly, Target agreed to pay $39 million to settle data breach claims after over 40 million of its customers' cards were compromised.

Although many federal consumer class actions have been stymied by Article III standing challenges, the plaintiff banks in both the Home Depot and Target litigations survived Article III scrutiny. Given that these financial institution plaintiffs have survived motions to dismiss and have exacted outsized settlements, we expect that more financial institutions will pursue lawsuits against retailers in the wake of future data breaches.

To complicate matters, 47 states have enacted security breach notification laws that determine whether a breach is reportable and how quickly, to whom and in what format it must be reported. Every year, several states tweak their individual requirements, thus making it difficult to keep track of new developments.

Do Now: Consider conducting a data privacy and security audit to identify areas of vulnerability and to understand how your company collects, stores, uses, shares and disposes of personal information about your customers and employees.

You should also ensure that you have a data privacy and information security policy that you actually update and enforce, ensure that your company uses industry standard security protocols, and regularly review contracts with service providers or business partners who process or have access to your company's data.

Finally, ensure that you have a negotiated, tailored cyber-insurance policy in place. Insurance carriers may tell you that their "off-the-shelf" policies are not negotiable, but the reality is that almost everything is negotiable.

"Excessive" and "Deceptive" Shipping and Handling Fees

The next trend in class actions against retailers may focus on the shipping and handling charges for online orders. In January 2017, the same plaintiff filed substantially similar class action complaints against retailers Express LLC[4] and Electrolux Home Care Products Inc.,[5] claiming that they violated California's Unfair Competition Law and Consumers Legal Remedies Act by charging shipping and handling fees that exceeded actual shipping costs. (The plaintiff voluntarily dismissed the complaint against Express shortly after filing.)

The plaintiff admits that Electrolux offered a choice of shipping options (ranging from Ground Service for $7.99 to Next Day Air Service at $25) and disclosed the exact shipping charges that would apply before the purchase, and that he was charged the amount that he agreed to pay.

However, he claims that the shipping costs were unfair, deceptive and unethical because they exceeded both the cost of the product and the actual shipping cost, providing an improper windfall to defendant. Electrolux moved to dismiss the case on March 13, 2017. This plaintiff will likely face significant challenges to establish standing and to class certification.

Do Now: Carefully review your company's shipping procedures to ensure compliance with federal, state and local laws, and include an arbitration provision in your online ordering process to avoid costly litigation.

Strike-Through Advertising/Deceptive Pricing

We all love a bargain! Getting a cool, must-have item previously priced at $99 for $49 is exciting. But was the product ever really offered at $99? Where? And for how long? A host of federal, state and local laws prohibit deceptive pricing, including section 5(a) of the FTC Act, which prohibits "unfair or deceptive acts or practices affecting commerce."[6]

Last year, failure to adhere to pricing rules landed online retailers, off-price department stores and

luxury brand outlet stores in serious trouble with class action plaintiffs, and the suits have exacted hefty settlements, including from J.C. Penney ($50 million) and Justice ($50.8 million).

Deceptive pricing cases will remain red-hot in 2017 on the heels of a new class action suit filed against Nordstrom in February[7] and four suits by the City of Los Angeles in December against some of the largest retailers in the country: J.C. Penney, Kohl's Department Stores, Macy's and Sears Roebuck & Company.

Do Now: Carefully review your company's pricing procedures to ensure compliance with federal, state and local laws, train your staff, and keep good records to help keep the class action lawyers — and the Federal Trade Commission — at bay.

Native Advertising

Native advertising, also known as "sponsored content," is advertising designed to mimic a website/social media network's editorial look and feel. The popularity of native advertising has skyrocketed in recent years, keeping it on the hot topics list for 2017.

In 2016, both the FTC and the National Advertising Division (NAD) actively policed advertisers' unfair use of social media to dupe consumers into thinking they were viewing editorial content that was, in fact, paid advertising. For example, the FTC secured a 20-year consent decree from Lord & Taylor for its failure to disclose that it had reviewed and paid for positive editorial and influencer content.

Similarly, the NAD slammed Joyus Inc., an online shopping site, for failing to disclose that a link on People magazine's website that purported to be editorial content actually brought viewers to Joyus' shopping site.[8]

Do Now: Make sure that you clearly and conspicuously label promotional content as advertising, and beware of door openers that fail to disclose that linked content is actually advertising.

"Made in the U.S.A." Claims

We have also seen an increase in class actions over "Made in the U.S.A." claims, and judges are pushing back on settlements that do not adequately address the harm done to consumers.

For example, the litigants in Hoffman v. Dutch LLC[9] have had to appear before a judge in the U.S. District Court for the Southern District of California three times to pitch a proposed settlement, each time with an increased offering. After the court rejected their proposed settlement for a third time, the parties jointly stipulated to end the case citing the rejected settlement, as well as an amendment to California's Made in America statute that went into effect Jan. 1, 2016, as the reasons. On April 3, 2017, the judge dismissed the complaint without prejudice.

The suit alleged that Dutch falsely advertised its Current/Elliott brand of jeans on its website as being made in the United States, even though they used foreign zipper assemblies, buttons, fabric and thread. Retailers must use the "Made in the U.S.A." label with caution, and they must ensure compliance with both the FTC's standards and, if they sell goods to California residents, with California's standards.

Those standards are not the same. Retailers who have recently been slapped with a false "Made in the U.S.A." lawsuit include New Balance[10] and The Nature's Bounty Co.[11]

Do Now: Ensure your "Made in the U.S.A." claim is valid and in compliance with federal and state laws, and ensure that you have adequate documentation to substantiate the claim.

Human Trafficking/Slavery Disclosures

We have seen a spike in legislative and enforcement efforts specifically focused on ridding company supply chains of products tainted by coerced labor.

The first two of the "big three" (namely, the U.K. Modern Slavery Act and the Federal Acquisition Regulations Anti-Trafficking Provisions), place affirmative obligations on most larger businesses to evaluate the risk associated with, and disclose steps taken to end, suspected human trafficking or coerced labor in their supply chains.

Further, the enforcers have indicated their intent to continue to pursue companies who do not comply with the disclosure provisions of the California Transparency in Supply Chains Act.

Do Now: Check your supply chain for products tainted by forced or child labor.

Credit Card Truncation Laws

The Fair Credit Reporting Act and the Fair and Accurate Credit Transactions Act limit the number of credit card digits that retailers can print on receipts, and they allow for penalties of between $100 and $1,000 per violation, plus attorneys' fees and costs.

Many retailers have been hit with suits claiming that they have printed too many credit card digits on store receipts. On Oct. 20, 2016, J. Crew[12] had a suit tossed based on the U.S. Supreme Court's decision in Spokeo Inc. v. Robins, 136 S. Ct. 1540 (2016), which held that plaintiffs cannot rely on mere statutory violations to establish Article III standing, but rather, must show concrete injury.

Do Now: Double check your receipts and make sure that you are properly truncating account information.

Americans with Disabilities Act (ADA) Website Accessibility

In 2017, retailers like Calvin Klein Inc. and Pinkberry Inc. have found themselves on the receiving end of lawsuits for the alleged failure to make their websites and mobile apps accessible to persons with disabilities under the ADA and California's Unruh Civil Rights Act.[13]

These suits demand compliance with Web Content Accessibility Guidelines (WCAG) 2.0, which are a highly technical set of standards published by the World Wide Web Consortium to ensure that anyone using common assistive technology has access to the web content.

However, the Department of Justice (DOJ) has not formally adopted these, or any, web accessibility standards. And the landscape of these and other similar ADA cases has recently changed in favor of defendants.

On March 20, in Robles v. Domino's Pizza,[14] Judge James Otero of the Central District of California granted defendant's motion to dismiss all of plaintiff's ADA website accessibility claims, without

prejudice, because the court cannot enforce technical WCAG standards that have not been officially adopted by the DOJ. To do otherwise would violate defendant's right to due process.

Do Now: The best offense is a good defense — take proactive measures to make your website and apps conforming to some of the WCAG guidelines to avoid potential litigation while the DOJ gets around to adopting its own rules.

Toxic Chemical Compliance

Although California's Prop 65 warning compliance remains a reliable source of litigation in California, it is not the only chemical compliance statute that can trip up retailers who also manufacture their own goods.

A Washington statute — the Children's Safe Product Act (RCW Chapter 70.240) — requires that manufacturers of children's (anyone 12 or younger) products (clothes, toys, car seats, grooming products — essentially, anything that a child uses, wears or touches) must report to the state of Washington if their product contains "chemicals of high priority."

The state lists several dozen high-priority chemicals, which means that manufacturers of children's products sold in Washington must test their products to determine whether they must report or not. Failure to report can result in civil penalties from the state, accompanied by a press release.

Do Now: Take chemical compliance seriously. It will differ from state to state, so double check that your product meets the standards.

Bankruptcy

Finally, restructuring experts overwhelmingly identify the U.S. retail sector as the most likely industry to face financial distress this year, surpassing the oil and gas sector and the health care industry.[15]

Retailers need to know how to (i) minimize the risks presented by bankruptcy and insolvency; (ii) recognize that a competitor's bankruptcy may provide opportunities to acquire strategic assets such as intellectual property, customer lists and leasehold interests; and (iii) minimize the damage caused by the bankruptcy of a vendor or customer.

Do Now: Consult with a qualified bankruptcy and restructuring attorney to identify potential strategic acquisitions and to devise strategies to avoid being dragged into the middle of a complex restructuring.

—By Ann Schofield Baker, Perkins Coie LLP

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[1] RSA Cyber Security Conference, 2012.

[2] Breach Level Index 1st Half of 2016, Gemalto, p. 10-11.

[3] Ponemon Institute's 2016 Cost of Data Breach Study: Global Analysis, p. 2.

[4] Reider v. Express LLC, No. 2:17-cv-556 (C.D. Cal. Jan. 23, 2017).

[5] Reider v. Electrolux Home Care Prods. Inc., No. 8:17-cv-26 (C.D. Cal. Jan. 6, 2017).

[6] FTC, Guides Against Deceptive Pricing, 16 C.F.R. §§ 233.1–233.5; N.Y. Gen. Bus. Law §§ 349, 350.

[7] Keating v. Nordstrom Inc., No. 3:17-cv-00030-SLG (D. Alaska Feb. 16, 2017).

[8] National Advertising Decision vs. Joyus Inc. (NAD Case #5956, 2016).

[9] Hoffman v. Dutch LLC et al, No. 3:14-cv-02418 (S.D. Cal. Oct. 9, 2014).

[10] Dashnaw et al. v. New Balance Athletics, No. 3:17-cv-00159 (S.D. Cal. Jan. 26, 2017).

[11] Sweat v. NBTY Inc., No.3:16-cv-00940 (M.D. Fla. July 22, 2016).

[12] Kamal v. J. Crew Group Inc., No. 2:15-cv-0190 (D.N.J. Jan. 10, 2015).

[13] Robles v. Calvin Klein Inc., No. 2:17-cv-00919 (C.D. Cal. Feb. 3, 2017); Gorecki v. Pinkberry Inc., No. 2:17-cv-00912 (C.D. Cal. Feb. 3, 2017).

[14] Robles v. Domino's Pizza, No. CV 16-06599 (C.D. Cal. Mar. 20, 2017).

[15] The AlixPartners LLP's 2017 North American Restructuring Experts Survey.
