A Matter of FACTA: A Guide to Preventing and Defending the Newest Wave of Class Action Lawsuits

By John Gibson, Charles Patrizia, Joshua Hamilton and Dara Freling

INTRODUCTION

For both customer satisfaction and competitive reasons, virtually every retail business, from stores to restaurants to theaters, must allow consumers to use credit or debit cards. For economic reasons, almost all of these transactions are electronically authorized in real time. This convenience creates a risk that a customer’s credit or debit card information could be stolen and misused by identity thieves. To limit this risk, Congress passed the Fair and Accurate Credit Transactions Act ("FACTA"), which requires, among other things, that “no person that accepts credit cards or debit cards for the transaction of business shall print more than the last 5 digits of the card number or the expiration date upon any receipt provided to the cardholder at the point of sale transaction.” See 15 U.S.C. § 1681c(g).1 In our litigious society, however, plaintiffs’ class action lawyers are seeking to use the statute to extract huge attorneys’ fee recoveries by filing claims for people who have not suffered any actual damage.

Already approximately one hundred class action lawsuits have been filed in California federal courts alleging violations of the statute. These lawsuits allege that a specific retailer has “willfully” failed to comply with the statute by failing to remove all but the last five card numbers and the expiration date from the credit or debit card receipts they provide their customers. The plaintiffs allege willful violations because FACTA distinguishes between “willful” and “negligent” violations. FACTA authorizes a court that finds a willful violation to impose statutory damages of at least $100 but no more than $1,000 for each violation, even when there is no proof of actual injury. 15 U.S.C. § 1681n. By contrast, an alleged negligent violation requires proof of actual damages (i.e., proof that a consumer has had his credit card information stolen and used). 15 U.S.C. §1681o. For either type of violation, a successful plaintiff may recover attorneys’ fees.

Any business that accepts credit and/or debit card payments for the sale of goods and/or services should be keenly aware of the requirements of FACTA, and, at least until the statutory terms are authoritatively interpreted, both remove the expiration date and truncate the credit card numbers. If a business has already done this prior to the statute’s effective date, then no further action is likely required. If a business has not yet complied or is facing actual or prospective litigation for a purported violation, this client alert provides an overview of the law, suggestions for actions to limit or eliminate liability, and potential legal defenses to the claims.

UNDERSTANDING THE LAW

In 2003 Congress passed, and the President signed, FACTA requiring the truncation of credit card information from receipts. See 15 U.S.C. §1681c.2 The purpose of FACTA is to “prevent criminals from obtaining easy access to such key information.”3 The language of the statute, however, arguably is ambiguous because it may have two clear possible interpretations; i.e.: (1) the act requires both the truncation of the numbers and the deletion of the expiration date; or (2) the act requires either the truncation of the numbers or the deletion of the expiration date. The legislative history of the statute contains numerous statements concerning the need to truncate the credit or debit card numbers from receipts. However, there is no specific reference to printing expiration dates.
Damages for violating the statute are two-tiered, based on whether the violation was “willful” (in which case plaintiffs are entitled to statutory, per-violation damages) or “negligent” (in which case plaintiffs must prove actual damages – i.e., actual identity theft and use of plaintiffs’ credit). Compare 15 U.S.C. § 1581n with 15 U.S.C. § 1581o. California is plaintiffs’ current venue of choice because the governing Ninth Circuit Court of Appeals has adopted a more relaxed definition of “willful.” The Ninth Circuit defines “willful” non-compliance as including “reckless disregard” of the statute. Reynolds v. Hartford Fin. Servs. Group, Inc., 435 F.3d 1081 (9th Cir. 2006). In Reynolds, the Court held that:

“[a] company will not have acted in reckless disregard of a consumers’ rights if it has diligently and in good faith attempted to fulfill its statutory obligations and to determine the correct legal meaning of the statute and has thereby come to a tenable, albeit erroneous, interpretation of the statute. In contrast, neither a deliberate failure to determine the extent of its obligations nor reliance on creative lawyering that provides indefensible answers will ordinarily be sufficient to avoid a conclusion that a company acted with willful disregard of [the statute’s] requirement. Reliance on such implausible interpretations may constitute reckless disregard for the law and therefore amount to a willful violation of the law.” 435 F.3d at 1099.

Other circuits have interpreted “willful” to require that defendants “knowingly and intentionally committed an act in conscious disregard” of the statute. See, e.g., Philbin v. Trans Union Corp., 101 F.3d 957, 970 (3d Cir. 1996). The United States Supreme Court will soon render a decision on a uniform interpretation in Safeco v. Burr / GEICO v. Edo, Nos. 06-84, 06-100. The case has been fully briefed, and the Court heard oral argument on January 16, 2007. The state of the law, therefore, remains uncertain; the outcome of the Supreme Court decision may dictate the direction of many of the numerous pending putative class action lawsuits.

UNDERSTANDING THE RISKS

The statutory language currently has fundamental potential ambiguities that create untested defenses. The first ambiguity is what state of knowledge constitutes a “willful” violation of the statute. As discussed above, the Supreme Court is likely to make this determination in the next few months.

The second ambiguity is whether the legislature intended to require the elimination of the expiration date as well as truncating the end number. There is no discussion in the legislative history specifically concerning the expiration date. The statute would indicate that both items are prohibited if the term “either” appeared. But, it does not. In addition, a credit card transaction cannot be conducted without both the expiration date and the credit card number; if one is missing or inaccurate, the transaction will not be processed. There is thus a reasonable argument that the merchant’s own record of the transaction must have sufficient information to show proper processing, and that the danger the truncation provisions seek to prevent – identity theft – is sufficiently deterred by eliminating either the last five digits or the expiration on the customer’s receipt.

In addition to the statutory ambiguities, there are constitutional defenses that have yet to be tested fully. If their position prevails, plaintiffs’ attorneys could impose billions of dollars as damages for a class action without any proof of actual damages. As a hypothetical, if a company processes 15 million credit card transactions per year, the minimum penalty for willful violations would be approximately $1.5 billion for each year following the applicable compliance deadline, plus attorneys’ fees and costs. Such a penalty for violations of the statute calls into question whether a class action can be maintained under FACTA because of the undesirable results of astronomical penalties incurred for technical violations of a statute causing no actual damages.

Because of the number of cases already filed, the number of different judges involved, and the lack of any controlling law interpreting FACTA, there is a strong likelihood that there will be differing opinions from different courts. Some of the legal challenges have been raised in pleading practice in a few of the pending lawsuits, with little success. We are carefully following all of these cases and are counsel to defendants in several others. The burden of litigation and risk of potential liability are too significant for companies to rely on favorable court rulings or Congressional intervention; a company should immediately take steps.
to remove from its sales receipts all but the last five digits of a credit or debit card number and the expiration date. The potential recovery under FACTA is a magnet for class action suits brought by attorneys on behalf of clients who have suffered no actual injury.

**PROACTIVE PREVENTION**

**Conduct an immediate internal review**

Whether or not a lawsuit has been filed against your company, if you accept credit or debit cards as payment for the sale of goods and/or services, you should immediately conduct an internal review to ensure that all registers or tills have truncated the credit card numbers and removed the expiration date from customers’ receipts. The company must maintain its records created as part of this compliance check in case such evidence may later be needed to support the company’s efforts toward compliance. If the company maintains separate point-of-sale systems, be sure that all are checked and conform.

Thus, it is best for a company to monitor the internal review actively and work with third-party vendors who provide the point-of-sale equipment and software to make sure all machines are properly programmed. Further, a company is best served by monitoring receipts produced from purchases made through the internet as well as those made in stores.

**Determine if any third parties may be liable**

Many companies use third-party vendors to provide point-of-sale equipment, software, services and support. If the third-party vendors were responsible for programming and ensuring compliance with regulations, then the company may have claims against the third parties for breach of contract, indemnity or contribution. In addition, to the extent that the company provides receipts for Internet purchases, the company should work with the provider of its Internet operations to remove the expiration date from those receipts, as it is not clear whether such receipts are covered under FACTA.

**CONCLUSION**

The scope of FACTA is still unsettled, which has made it ripe for putative class action lawsuits preying on the uncertainty. The most prudent action is to investigate your point-of-sale practices immediately and, if necessary, redact at least all but the last five digits of the credit card number and the expiration date from all customer receipts printed electronically. This process may require working with third-party vendors to ensure that any updates are done properly. If a lawsuit has already been filed based on a company’s past practices, or an internal investigation reveals there may be violations under FACTA, the company should seek legal advice to minimize exposure.

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**If you have any questions regarding this client alert, please do not hesitate to contact any of the following Paul Hastings lawyers:**

**Los Angeles**

John S. Gibson  
213-683-6168  
johns@paulhastings.com

Joshua G. Hamilton  
213-683-3186  
joshuahamilton@paulhastings.com

**Washington, D.C.**

Charles A. Patrizia  
202-551-1710  
charlespatrizia@paulhastings.com

Dara H. Freling  
202-551-1824  
darafreling@paulhastings.com
In full, 15 U.S.C. § 1681c(g), which governs the truncation of credit card and debit card numbers, states:

1. In general. Except as otherwise provided in this subsection, no person that accepts credit cards or debit cards for the transaction of business shall print more than the last 5 digits of the card number or the expiration date upon any receipt provided to the cardholder at the point of the sale or transaction.

2. Limitation. This subsection shall apply only to receipts that are electronically printed, and shall not apply to transactions in which the sole means of recording a credit card or debit card account number is by handwriting or by an imprint or copy of the card.

3. Effective date. This subsection shall become effective –
   
   (A) 3 years after the date of enactment of this subsection [enacted Dec. 4, 2003], with respect to any cash register or other machine or device that electronically prints receipts for credit card or debit card transactions that is in use before January 1, 2005; and
   
   (B) 1 year after the date of enactment of this subsection [enacted Dec. 4, 2003], with respect to any cash register or other machine or device that electronically prints receipts for credit card or debit card transactions that is first put into use on or after January 1, 2005.

FACTA does not apply to receipts for which the sole means of recording a debit or credit card number is by handwriting or by an imprint or copy of the card because 15 U.S.C. § 1681c(g)(2) limits the application of this provision to receipts that are electronically printed.

Senate Report No. 108-166, entitled “Amending Fair Credit Reporting Act,” to accompany S. 1753 dated October 17, 2003, prepared by the Senate Committee on Banking, Housing and Urban Affairs.