Portfolio Media. Inc. | 860 Broadway, 6th Floor | New York, NY 10003 | www.law360.com
Phone: +1 646 783 7100 | Fax: +1 646 783 7161 | customerservice@law360.com

What The High Court May Not Address In Frequent Flier Case

Law360, New York (December 05, 2013, 3:08 PM ET) -- On Dec. 3, 2013, the U.S. Supreme Court heard oral argument in a case involving the scope of federal preemption of state law consumer claims against airlines under the Airline Deregulation Act of 1978 — in Northwest Inc. v. Ginsberg, No. 12-462.

The decision is expected by the end of June 2014. The vigorous questioning by the Supreme Court justices that occurred during oral argument suggests that the case is likely to resolve an important issue of whether the ADA preempts state law claims for breach of the implied covenant of good faith and fair dealing.

However, the oral argument did not cover — and the decision may not end up addressing — the equally important issue of the scope of the airline "services" that are subject to ADA preemption.

The express preemption provision in the ADA (49 U.S.C. 41713(b)) prohibits states and local governments from enacting or enforcing "a law, regulation or other provision having the force and effect of law related to a price, route or service of an air carrier" that provides air transportation.

Although many circuit courts have applied ADA preemption to immunize airlines from an array of state law claims, the Ninth Circuit has been an outlier, at times allowing disgruntled consumers to thwart congressional objectives and pursue state law claims relating to core airline functions and services that the ADA was intended to preempt.

Ginsberg arises out of Northwest Airlines' decision to terminate the membership of a customer (Rabbi S. Binyomin Ginsberg) in the airline's WorldPerks frequent flier program. The terms and conditions of the WorldPerks program granted Northwest discretion to remove individuals from the program for any improper conduct "as determined by Northwest in its sole judgment."

Northwest determined that Ginsberg's frequent complaining about his treatment by the airline supported termination of his membership in the frequent flier program.

Ginsberg filed suit, claiming that Northwest's actions amounted to breach of contract, breach of the implied covenant of good faith and fair dealing, negligent misrepresentation, and intentional misrepresentation. The district court dismissed all of Ginsberg's claims, holding that the ADA preempted them as relating to airline prices and services.

Ginsberg appealed only the district court's conclusion that the ADA preempts a claim for breach of the implied covenant of good faith and fair dealing. A three-judge panel of the Ninth Circuit reversed, stating that the "purpose, history and language of the ADA, along with Supreme Court and Ninth Circuit precedent, lead us to conclude that the ADA does not preempt a contract claim based on the doctrine of good faith and fair dealing."

Before the Supreme Court, Northwest (which is now incorporated into Delta Air Lines) claims that the Ninth Circuit's decision creates an unfounded exception that can swallow the rule by permitting disgruntled consumers to pursue cases against airlines merely by claiming that the airline breached an implied covenant to exercise good faith and engage in fair dealing in its treatment of customers — a standard that is inherently vague and ambiguous in the context of airline customer relations.

If an airline gives itself the contractual right to take a certain action solely within its unilateral discretion, that should end the matter. The airline should not have to find itself sued for allegedly failing to exercise such unilateral discussion in good faith.

The roots of Ginsberg lie in the seminal case, American Airlines Inc. v. Wolens, where the Supreme Court held that "the ADA's preemption prescription bars state-imposed regulation of air carriers, but allows room for court enforcement of contract terms set by the parties themselves."

In other words, if an airline expressly promises to do something, and fails to do it (e.g., to fly a customer from Los Angeles to Denver), then the claim for breach of that promise may not be preempted by the ADA.

Wolens involved a challenge to American Airlines' modifications of its frequent flier program. The court allowed the breach of contract claim to proceed because American had expressly made certain representations regarding its program that the plaintiffs claimed were being breached.

Ginsberg argues that Wolens allows his claim for breach of the implied covenant of good faith and fair dealing because the cause of action pertains only to the terms of the agreement between himself and Northwest, without implicating law or policy that states create and enforce.

However, Northwest maintains that a court inherently applies state law or policy when grafting the implied covenant of good faith and fair dealing upon the contractual bargain reached by the parties.

During the oral argument, the justices focused almost entirely on the issue of whether the implied covenant of good faith and fair dealing merely enforces the parties' bargain (which is not preempted) or creates an additional obligation on the airline — above and beyond that to which the airline agreed (which likely is preempted).

The justices' questions and answers during oral argument revealed a potential split among the justices. Justice Ruth Bader Ginsburg asked if an "illusory contract" would result "if the airline has an unreviewable right to terminate" the frequent flier agreement.

In addition, Justice Elena Kagan asked questions suggesting her predisposition that an airline should not withdraw frequent flier credits received by a customer, and Justice Sonia Sotomayor asked whether there was a limit to the airline's "absolute discretion."

By contrast, Justice Antonin Scalia emphasized that you cannot have a situation where you have to go through each of the 50 states and determine the intent of the parties by considering "community standards" for good faith and fair dealing. Scalia added that a claim "is obviously not an interpretation of the contract; it is an imposition of a state requirement."

A successful claim depends on the state the plaintiff is from. Similarly, Chief Justice John Roberts suggested that Ginsberg's claim would put the state supreme court's "gloss" on the term "sole discretion." In addition, Justice Stephen Breyer stated that "it might be a great idea to set airline prices "according to" the customer's "reasonable expectation, but it would be contrary to the ADA to do so.

During the oral argument, the justices paid some attention to the issue of whether Ginsberg's claim is related to airline "prices." Breyer stated: "I ... think frequent flier programs are simply price discounts." "I also think the state cannot, under the guise of contract law, regulate the prices of airlines. If you allow that, you're going to have worse than we ever had. It'll be 50 different systems, all right?"

However, none of the colloquy involved the issue of whether a frequent flier program falls within the term airline "services." Perhaps the written decision will resolve the "services" issue. However, the oral argument suggests the court may not address the "services" issue.

It would be unfortunate if the court fails to do so. In the underlying decision, the Ninth Circuit followed its prior en banc decision in Charas v. Trans World Airlines that the term "service" did not include so-called fringe benefits having nothing to do with schedules, origins, destinations, cargo or mail, and that, therefore, frequent flier programs did not constitute services under Charas.

This aspect of the lower court decision failed to reflect that the limited definition of "services" in Charas is no longer good law in light of the subsequent decision of the U.S. Supreme Court in Rowe v. N.H. Motor Transport Association — which dealt with the term "services" and its use in a statute to be interpreted in the same manner as the ADA.

The Supreme Court underscored that preemption should apply if application of state law will require provision of services different from what the market dictates.

Rowe involved a Maine statute that forbade anyone other than a licensed tobacco retailer to accept an order for a delivery of tobacco, required tobacco delivery services to use recipient verification services, and prohibited knowing transportation of tobacco unless either sender or receiver has a license.

In striking down the law, the Supreme Court relied on its ADA preemption decisions to determine that the law improperly encroached on an area subject to federal preemption.

The court reasoned that although federal laws may not preempt state laws only tenuously related to pricing and services, "if federal law preempts state regulation of the details of an air carrier's frequent flier program, a program that primarily promotes carriage, it must preempt state regulation of the essential details of a motor carrier's system for picking up, sorting and carrying goods — essential details of the carriage itself."

A contrary ruling would have allowed states to develop a range of regulations hampering the efficiency of interstate delivery systems.

The court held that Maine's statute interfered sufficiently with the services provided by the trucking industry to qualify for preemption even though the statute only regulated one kind of carrier service. The court's determination in Rowe strongly indicated that regulation of a single aspect of a carrier's service is sufficient to constitute regulation of a service under federal preemption law.

Ginsberg gives the court the opportunity to affirm frequent flier programs are "services" covered by the ADA. However, the oral argument suggests that the court may choose not to address scope of the term "services" at this time.

—By Roy Goldberg, Sheppard Mullin Richter & Hampton LLP

Roy Goldberg is a partner in the Business Trial practice group in Sheppard Mullin's Washington, D.C., office and head of the firm's aviation industry team.