Let The Frequent Flyer Beware: Airlines Can Nix Memberships

Law360, New York (April 22, 2014, 6:19 PM ET) -- On April 2, 2014, the U.S. Supreme Court decided in Northwest Inc. v. Ginsberg that the Airline Deregulation Act preempts a state law claim for breach of the implied duty of good faith and fair dealing if the claim seeks to enlarge the contractual obligations of the parties. The practical result of that ruling is that any airline can terminate a frequent flyer membership according to the terms of its frequent flyer contract, without fear of implied contractual duties being applied to it.

The Supreme Court’s ruling arose out of a dispute between Northwest Airlines and one of the members of its WorldPerks frequent flyer program. Rabbi S. Binyomin Ginsberg became a member of WorldPerks in 1999 and achieved the highest frequent flyer status available, “Platinum Elite,” in 2005. In 2008, however, Northwest terminated Ginsberg’s frequent flyer membership in reliance on a provision of the WorldPerks contract prohibiting “abuse” of the program. The high court found the facts underlying the claim of abuse important enough to include in the decision.

Apparently, over the span of approximately seven months, Ginsberg had contacted Northwest 24 separate times, nine of which were to complain about his bag arriving late at the luggage carousel. Ginsberg then would ask for compensation above Northwest’s standard guidelines. Northwest had given Ginsberg $1,925 in travel credit vouchers, 78,500 WorldPerks bonus miles, a voucher extension for his son and $491 in cash reimbursements before Northwest terminated his WorldPerks membership.

Ginsberg subsequently filed a class action complaint in the U.S. District Court for the Southern District of California, alleging that Northwest had ended his membership simply as a cost-cutting measure in the wake of Northwest’s merger with Delta. The complaint alleged four claims for relief.

First, Ginsberg argued that Northwest had breached the terms of the frequent flyer contract by revoking his Platinum Elite status without cause. Second, Ginsberg alleged that Northwest violated the implied duty of good faith and fair dealing by terminating his membership in a way that was inconsistent with his reasonable expectations about how Northwest would exercise its discretion under the frequent flyer
contract. Third, Ginsberg alleged a claim for negligent misrepresentation. Fourth, Ginsberg alleged a claim for intentional misrepresentation. Ginsberg sought damages of more than $5 million and an injunction that would both require Northwest to reinstate frequent flyer status for the class members and prohibit Northwest from terminating memberships in the future.

The California district court held that the second, third and fourth claims were all preempted by the ADA because they were "related to" Northwest's rates and services. The remaining claim for breach of contract was dismissed without prejudice because Ginsberg had not identified any material breach of the frequent flyer contract, which gave Northwest sole discretion to decide whether a member abused the program. Ginsberg chose to appeal only the dismissal of his second claim for relief for breach of the implied duty of good faith and fair dealing.

The Ninth Circuit reversed the dismissal of that claim. The circuit court held that Ginsberg's claim was "too tenuously connected to airline regulation to trigger preemption under the ADA." The court also found that such a claim did not interfere with the ADA's regulatory mandate, did not force airlines to adopt or change their prices, routes or services and did not have a direct effect on prices or services. The Supreme Court disagreed.

To explain its ruling, the Supreme Court first discussed the Federal Aviation Act and the Civil Aeronautics Board, which were in place before the ADA. Under the authority granted by the FAA, the CAB closely regulated airlines, including by controlling routes, rates and services. At that time, airlines were also regulated by the states. Congress enacted the ADA in 1978 and included a preemption provision to ensure that the states would not undo federal deregulation with regulation of their own.

Before Ginsberg, the Supreme Court twice had considered the preemption clause of the ADA. In Morales v. Trans World Airlines Inc. (1992), the high court held that the ADA preempted state consumer protection laws from being applied to airline advertising. There, the Supreme Court held that a claim "relates to rates, routes or services" — such that it would be preempted — if the claim has "a connection with, or reference to" airline rates, routes or services.

In American Airlines Inc. v. Wolens (1995), the Supreme Court later held that the preemption clause of the ADA also barred claims under an Illinois consumer fraud statute where the claims challenged an airline's devaluation of frequent flyer miles by imposing blackout dates and limits on the number of seats that could be purchased with frequent flyer miles. Wolens held, however, that the ADA did not preempt a breach of contract claim in that case. Contracts between airlines and passengers "are privately ordered obligations" and do not amount to state action within the meaning of the ADA.

This language suggests that if Ginsberg could have identified a provision of Northwest's frequent flyer contract that it breached, his first claim for relief would have survived.

Against this background, the Supreme Court first considered whether the ADA preemption provisions can be applied to common law claims, like breach of the implied duty of good faith and fair dealing, as opposed to state legislation. The Supreme Court concluded that it can be.
The Court next analyzed whether Ginsberg's claim for breach of the implied duty of good faith and fair dealing "relates to" rates, routes or services. It does. Ginsberg's claim sought reinstatement in Northwest's frequent flyer program, which Ginsberg conceded provided valuable benefits, including flight upgrades, accumulated mileage and more. Because the program awards mileage credits that can be redeemed for tickets and upgrades, the Supreme Court concluded that it is connected to airline rates.

The primary issue, then, was whether Ginsberg's single claim on appeal was one based on a state-imposed obligation — which would be preempted — or based on an obligation that the parties voluntarily undertook, which would not be preempted. To answer this question, the Supreme Court turned to an analysis of the nature of the implied duty of good faith and fair dealing.

The Supreme Court noted that different jurisdictions treat the duty as having different origins in the law; but under controlling Minnesota law, the implied duty is considered a state-imposed obligation that cannot be contracted around. "When the law of a [s]tate does not authorize parties to free themselves from the covenant, a breach of covenant claim is preempted under the reasoning of Wolens." Because the implied duty applies to every contract in Minnesota, ADA preemption prohibits Ginsberg's claim for breach of that duty.

The Supreme Court did not go so far as to say that the ADA prohibits any claim for breach of the implied duty of good faith and fair dealing, however. If the law of a state allows parties to contract around the implied duty, and the airlines choose not to do so, then the ADA would not prohibit a claim for breach of the duty to go forward.

The lesson for airlines in the wake of the Ginsberg decision is that their frequent flyer contracts should have language to avoid the imposition of the implied duty of good faith and fair dealing for all states that allow such avoidance by contract. In all other jurisdictions, the ADA preemption clause will do the work for the airlines.

The Supreme Court was not concerned that frequent fliers like Ginsberg might be left without recourse as a result of its ruling. The high court specifically identified other options available to consumers. For example, complaints can be filed with the U.S. Department of Transportation and passengers can choose to do business with airlines that are reputed to treat their frequent fliers more fairly. (The second option, though, ignores the practical difficulty that many passengers will not have a realistic choice of which airline to fly, depending on their point of origin and destination).

Perhaps more tellingly, the Supreme Court questioned why Ginsberg did not appeal the dismissal of his claim for breach of contract. That claim would not be preempted, and could have proceeded on the merits. The single claim that Ginsberg did appeal — for breach of the implied duty of good faith and fair dealing — seeks to enlarge the contractual duties of Northwest and, as a result, is preempted by the ADA.

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