1994

Federal Airline Deregulation Act Not Preempted by State Claims for Breach of Contract

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negligence. They recognized the need for a higher standard of liability in order to attract high quality officers and directors. Moreover, the court observed that two subsequent attempts to modify the statute and replace the gross negligence standard with a standard of simple negligence failed.

Taken together, the court found that the legislative history of FIRREA is consistent with its interpretation that the plain language of the statute establishes a gross negligence standard of liability for officers and directors of failed financial institutions.

**Seventh Circuit Finds Precedent for Preemption**

In further support for its holding, the Seventh Circuit found the United States Supreme Court's decision in *City of Milwaukee v. Illinois*, 451 U.S. 304 (1981) (*Milwaukee II*), required a finding of preemption in the case at bar. In *Milwaukee II*, the issue before the Court was whether the Federal Water Pollution Control Act Amendments of 1972 preempted an existing federal common law action for abatement of a nuisance caused by interstate water pollution. The Court held that the 1972 amendments preempted federal common law as Congress occupied the field, establishing a comprehensive regulatory scheme to supervise and administer the activities of federal banking agencies to require insured financial institutions. For example, FIRREA broadened the power of federal banking agencies to require officers and directors, subject to a “cease and desist” order, to make restitution or provide reimbursement if they were unjustly enriched by reckless disregard for the law or regulations.

Second, the court found that FIRREA created several expert agencies to supervise and administer the comprehensive regulatory scheme. In addition, FIRREA also created the RTC to assist failed thrift institutions.

From its analysis of the plain language of Section 1821(k), its legislative history, and the Supreme Court’s decision in *Milwaukee II*, the Seventh Circuit concluded that Congress intended to preempt federal common law and establish a gross negligence standard of liability for officers and directors of failed federally chartered financial institutions. However, the court emphasized that it chose not to address the issue of whether Section 1821(k) preempts state law. In so doing, it noted that federalism concerns require greater evidence of congressional intent to preempt state law than federal common law and that a court must start with the assumption that federal statutory law cannot supersede a state’s police power in the absence of clear and manifest congressional intent.

Joyce E. Raupp

**Federal Airline Deregulation Act Not Preempted by State Claims for Breach of Contract**

In *Wolens v. American Airlines, Inc.*, 626 N.E.2d 205 (Ill. 1993), the Supreme Court of Illinois held that state law claims for breach of contract based on an airline’s retroactive modification of a frequent flier program are not preempted by the Federal Airline Deregulation Act, 49 U.S.C. Section 1305(a)(1) (1988) (*Deregulation Act*). The court found the plaintiffs’ state law claims for money damages to be too removed from airline activities to invoke Section 1305(a)(1), which prohibits a state from enacting or enforcing a law relating to the rates, routes, or services of an air carrier. Nonetheless, the plaintiffs’ attempt to obtain an injunction to prevent the airline from retroactively modifying the rules of the frequent flier program fell within the constraints of the Deregulation Act and was preempted.

**American Offers Frequent Flier Program**

American Airlines offers discounted flights and other travel benefits to customers participating in their “AAdvantage” frequent flier program. This marketing device encourages greater use of American’s services by the general public and by frequent fliers. Benefits are awarded to participants based upon accumulated mileage credits, which a member earns by flying on American or by doing business with one of American’s affiliates.

Prior to May 18, 1988, AAdvantage members were entitled to redeem their travel award certificates for free air travel on any available date and on any available seat in the class of service provided. As of May 18, 1988, however, American retroactively altered the terms of its AAdvantage program by instituting various restrictions on previously earned AAdvantage credits.

**Class Action Filed**

In response to the changes in the frequent flier program, plaintiffs, representing AAdvantage members, filed a class action in the Circuit Court of Cook County. The complaint alleged that American’s retroactive modification of the rules of the AAdvantage program constituted a breach of contract with members who joined the frequent flier program prior to May 1988. The complaint also claimed violations of the Illinois Consumer Fraud and Deceptive Business Practices Act, Ill. Comp. Stat. ch. 815, para. 505/1 (West 1987), (Consumer Fraud Act). The plaintiffs, who sought
money damages and an injunction, did not challenge American's right to alter or restrict the AAdvantage program prospectively. Instead, the plaintiffs contended that American did not reserve the right to make changes retroactively as to diminish the value of previously earned AAdvantage credits.

The trial court denied American's motion to dismiss, holding that Section 1305(a)(1) of the Deregulation Act does not preempt the plaintiffs' claims. The trial court did, however, grant American's motion for certification for interlocutory review.

**State Damage Claims Not Preempted**

The Illinois appellate court considered the plaintiffs' attempt to enjoinder American from application of its retroactive rules as an attempt to regulate the service of an airline. Such action is preempted by Section 1305(a)(1) of the Deregulation Act. The court concluded, however, that the plaintiffs' state damages claims were not preempted by the act. Furthermore, the appellate court permitted immediate review of these issues by the Illinois Supreme Court.

The Illinois Supreme Court affirmed the decision of the appellate court, barring the claim for injunctive relief as preempted by Section 1035(a)(1), but allowing the claim for money damages based on breach of contract. Subsequently, American petitioned the United States Supreme Court for review. The Supreme Court vacated the decision of the Illinois Supreme Court and remanded the cause for further consideration in light of the recently decided case of *Morales v. Trans World Airlines, Inc.*, ___ U.S. ___, 112 S.Ct. 2031 (1992).

Upon remand, the Illinois Supreme Court held that its previous decision, denying plaintiffs injunctive relief, was consistent with *Morales*. The court then addressed whether the plaintiffs' state damages claims for breach of contract and violation of the Consumer Fraud Act were preempted by Section 1305(a)(1) of the Deregulation Act.

**American's Retroactive Changes Constitute Breach of Contract**

American argued that plaintiffs' claims were preempted by Section 1305(a)(1) of the Deregulation Act, in that the state breach of contract action sought to regulate the services of an airline. The plaintiffs contended that American did not reserve the right to make changes to the frequent flier program retroactively and that the changes made served to diminish the value of previously earned AAdvantage credits, thus constituting a breach of contract. The court determined that a contractual relationship exists between American and the members of the AAdvantage frequent flier program. The court held that American's actions in changing the program constitute a breach of contract, a state remedy that the plaintiffs are entitled to pursue.

**Illinois Supreme Court Finds Deregulation Act Connection Too Tenuous**

The Illinois Supreme Court analyzed the language of Section 1305(a)(1) of the Deregulation Act, which provides that "no state shall enact or enforce any law, rule, regulation, or standard having the force and effect of law relating to rates, routes, or services of any air carrier..." The court concluded that American's frequent flier plan was unnecessary and peripheral to the operation of an airline and indicated that the plaintiffs' claims did not seek to accomplish anything that Section 1305(a)(1) prohibits. In other words, the court found that the plaintiffs' claims did not attempt to establish rates, determine routes, or to dictate the services that an airline must provide.

The supreme court also relied on the United States Supreme Court's analysis of Section 1305(a)(1) in *Morales*, where the Court stated that in spite of the broad meaning of the phrase "relating to," all state laws would not be preempted. The Supreme Court concluded that some state actions may affect airlines in too tenuous or remote a manner to have a preemptive effect.

The Illinois Supreme Court, adopting the *Morales* analysis, reasoned that the plaintiffs' breach of contract claims, which are brought pursuant to state law, are not preempted by Section 1305(a)(1) of the Deregulation Act. The court held that plaintiffs' state law claims for money damages based on the AAdvantage program bear only a tangential relation to American's rates, routes, and services. Because this connection is too tenuous in relation to the areas covered by the Deregulation Act, the plaintiffs' claims are not preempted by federal law. Therefore, the Illinois Supreme Court affirmed the appellate court's denial of American's motion to dismiss.

**Justice McMorrow Dissents**

In her dissent, Justice McMorrow deemed the majority's preemption analysis as too narrow. She supported a more expansive and sweeping definition of the "relating to" language in Section 1305(a)(1) of the Deregulation Act, finding the plaintiffs' state law claims to have a connection and relation to American's rates and services. Justice McMorrow found that based on this connection, Section 1305(a)(1) should preempt the plaintiffs' state law claims.

Justice McMorrow considered the plaintiffs' claims, reduced to their simplest terms, to be based on deceptive inducements relating to fares and services, both of which are preempted by the Deregulation Act. She concluded that the plaintiffs' claims were not too tenuous or remote for Section 1305(a)(1) preemption because a state court adjudication in this case would give the plaintiffs an enforceable right to receive certain fares or services from American. Justice McMorrow also disagreed with the majority's statement that American's actions actually constituted a breach of con-
Newly Acquired Autos 
Do Not Automatically Qualify as “Covered Autos” Under Preexisting Policies

In *Farm & City Ins. Co. v. Anderson*, 509 N.W.2d 487 (Iowa 1993), the Supreme Court of Iowa held that a newly acquired vehicle was covered 
under an owner's pre-existing policy only if the insured requested coverage for the vehicle within the 30-day period after the insured became the owner.

**Farm and City’s Policy Provision**

Appellee Anderson had a pre-existing insurance policy with appellant Farm & City Insurance Company. The policy only applied to “covered autos,” which it defined as any vehicle shown in the declaration, or any vehicle acquired during the policy period “only if...[the owner] ask[s] [Farm & City] to insure it within 30 days after...becom[ing] the owner.”

**Accident Involves Newly Acquired Auto**

Anderson acquired a broken down 1982 pickup truck from his father in December 1991. After Anderson repaired the truck, his father transferred the certificate of title to Anderson on April 16, 1992. Anderson began driving the truck on April 23, but he never asked Farm & City to insure the truck. On May 16, Anderson collided with another car which had two occupants, both of whom claimed damages for injuries resulting from the accident.

Farm & City denied Anderson coverage on the truck, claiming it was not a “covered auto” under the policy since Anderson never requested specific coverage for it. Farm & City filed an action seeking a declaratory judgment that it did not have a duty to defend Anderson or indemnify him for any damage claims by the occupants of the other car involved in the accident. Both Anderson and Farm & City moved for summary judgment.

The district court granted Anderson’s motion for summary judgment, reasoning that the policy covered newly acquired vehicles for 30 days whether or not the insured requested coverage, and the accident happened within 30 days of the date Anderson obtained title. On appeal, Farm & City claimed that its policy required notice within 30 days in order for the truck to be covered, and thus the truck was not a “covered auto” under the policy. The Supreme Court of Iowa agreed, and reversed the district court’s decision.

**Court Rejects Automatic Coverage**

The Iowa Supreme Court determined that there are two views on the issue of whether a policy automatically extends to newly acquired automobiles. The majority view holds that coverage automatically passes to a newly acquired vehicle for 30 days without notice and subsequently becomes void after the 30-day period if notice is not given. The rationale for the majority view is that a reasonable person reading the policy would conclude that a new car was covered for 30 days without notice. A further basis for this view is that “automatic coverage” would not be automatic if notice was required, thus a reasonable person would not expect to have to give notice.

The Supreme Court of Iowa, however, rejected the majority view, preferring the opinion that coverage must be requested within the 30-day period after the insured becomes the owner. The court noted that the majority view was based on the decisions of three courts, none of which were dealing with the issue of notice during the automatic coverage period. Further, the court questioned the validity of the majority view, pointing out that many subsequent courts have accepted it without conducting an independent analysis of the issue.

The court was not persuaded by the reasoning used to justify the majority view. It did not agree that the policy provision at issue in this case was ambiguous. An insured’s request for coverage is a condition that must be met in order for the newly acquired vehicle to be a “covered auto” under the policy. The court failed to see how a reasonable person could conclude that notice was not required for coverage under this policy.

Finally, the court rejected the argument that its interpretation destroyed the automatic nature of the coverage. Coverage for newly acquired vehicles is still automatic in the sense that the insurer is not at liberty to deny coverage on the basis that the vehicle is not listed in the policy. Moreover, the policy would still be effective retroactively to the date of ownership if the insured gave notice within 30 days, even if notice was given after an accident occurred. This provision assures coverage for an accident occurring during the notice period provided notice is given.

**Insured Remains Liable**

Thus, the Iowa Supreme Court held that Anderson’s Farm & City insurance policy clearly required him to give notice in order for his newly acquired auto to be covered during the 30-day notice period. Since Anderson failed to give Farm & City notice that he owned the truck within 30 days after obtaining it, the truck did not qualify as a “covered auto” under his insurance policy. Additionally, the Farm & City policy did not cover liability arising from the use of an “uncovered auto” owned by the insured; therefore, Anderson was also not insured for any potential liability to the occupants of the other car involved in the accident. As a result,