NOTE

DIVIDED COURT PERMITS AIRLINE TO RELY ON THIRD-PARTY VENDOR'S ARBITRATION CLAUSE BASED ON EQUITABLE ESTOPPEL

Herrera v. Cathay Pacific Airways Lt

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Introduction

The Ninth Circuit's divided decision in *Herrera v. Cathay Pacific Airways* Lt[1] underscores a significant expansion of arbitration clauses' reach via the doctrine of equitable estoppel. This case highlights emerging tensions between arbitration enforcement and consumer protection, particularly in contracts involving intermediaries like travel agencies. By allowing a non-signatory airline to compel arbitration based on a third-party vendor's terms, the court's ruling raises critical questions about the obligations of non-signatories and the scope of equitable estoppel in consumer contracts. The court's divided ruling has far-reaching implications for consumer protection and contract enforcement, especially in the context of international air travel.

Facts

Winifredo and Macaria Herrera purchased international round-trip tickets on Cathay Pacific (Cathay) via the third-party booking platform ASAP Tickets, operated by International Travel Network, LLC (ITN). The Herreras agreed to ASAP's Terms and Conditions (T&C). ASAP's T&C stipulated that if an airline fare's rules allowed for refunds or exchanges, ASAP would charge a $250.00 fee per ticket to process any refunds or exchanges. The agreement also included a binding arbitration clause requiring any dispute or claim arising under ASAP's T&C be resolved through small claims court or arbitration. The tickets issued by Cathay incorporated Cathay's General Conditions of Carriage for Passengers and Baggage (GCC). Article 10.2 of Cathay's GCC provided that "except as otherwise provided by the Warsaw Convention or the Montreal Convention or applicable law," Cathay's GCC dictates how Cathay should issue a refund after Cathay cancels a flight. Under Article 11.1.1 of Cathay's GCC, Cathay is entitled to issue a refund to the person named on the ticket or whoever paid for the ticket after they provide satisfactory proof of payment.

Cathay canceled the Herreras' international return flight during their trip due to "operational reasons." At the airport, a Cathay agent assured the Herreras that they would receive a refund for the unused portion of their tickets and recommended the Herreras purchase a return flight through another airline. Following this advice, the Herreras purchased a return flight with another airline. Cathay later instructed the Herreras to contact ASAP for the refund. The Herreras made multiple requests to ASAP, resulting in only temporary travel vouchers that would expire within months of issuance. The Herreras rejected this offer due to ongoing COVID-19 travel restrictions. Cathay stated that the airline never received a refund request from the Herreras or ASAP on behalf of the Herreras.

The Herreras sued Cathay, alleging breach of contract under the GCC. Cathay moved to compel arbitration, invoking the arbitration clause in ASAP's T&C through equitable estoppel. The district court denied Cathay's motion to compel arbitration because the Herreras breach of contract case stemmed from Cathay's GCC, not ASAP's T&C. Cathay filed an interlocutory appeal seeking reversal of the district court's denial of its motion to compel arbitration and either dismissal or a stay of the action pending arbitration of the Herreras' breach-of-contract claim.

Holding

The Ninth Circuit held that Cathay, though a non-signatory, could enforce ASAP's arbitration clause under the doctrine of equitable estoppel. The court reasoned that the Herreras' claims were "intimately founded in and intertwined with" ASAP's T&C, justifying arbitration. Judge Forrest dissented, arguing that the Herreras' breach-of-contract claim was independent of ASAP's T&C, making equitable estoppel inapplicable.

Analysis

Equitable estoppel allows a non-signatory to compel arbitration if the claims are intertwined with a contract containing an arbitration clause. Under the relevant caselaw, a non-signatory to a contract may enforce an arbitration provision under the doctrine of equitable estoppel when "the claims are 'intimately founded in and intertwined with' the underlying contract."[2] The court focused on whether Herreras' breach-of-contract claim was intimately founded and intertwined with ASAP's T&C, which included the arbitration clause. To determine whether equitable estoppel applies to the Herreras' claim, the court looked at the" relationship between the parties and their connection to the alleged violations."[3] Because the court concluded that the Herreras' allegations that Cathay breached the GCC were "intimately founded in and intertwined with" ASAP's alleged conduct under its T&C, Cathay was justified in seeking to enforce the arbitration clause contained in the T&C.

Judge J. Clifford Wallace, writing for the majority, emphasized that the Herreras' claims were intertwined with ASAP's T&C. The court found that resolving the breach-of-contract claim required analyzing ASAP's role in processing refunds and the arbitration clause within ASAP's agreement. The court drew parallels to *Franklin v. Cmty. Reg'l Med. Ctr.,* where claims against a non-signatory were linked to an employment contract.[4] In *Franklin*, a nurse entered into a travel-nurse-assignment contract with a staffing agency. This contract contained a provision that stipulated any claims or disputes under the contract would be handled with arbitration.[5] The staffing agency assigned the nurse to a hospital where she worked for several months.[6] The nurse sued the hospital to recover her unpaid wages.[7] Although her claims were directed at the hospital, a non-signatory to the nurse's contract with her staffing agency, the court compelled arbitration because her claims for unpaid wages were closely related to her contractual relationship with the staffing agency.[8] Because the staffing agency was responsible for reviewing the nurse's timekeeping records, approaching the hospital with any discrepancies, and paying her wages, the staffing agency and its contract with the nurse would be implicated in the nurse's suit against the hospital.[9] Since the nurse's claims against the hospital were dependent on the staffing agency's performance under its contract, the nurse's claims against the hospital were found to be "intimately founded in and intertwined with" her employment contract with the staffing agency and the nurse was found to be equitably estopped from avoiding arbitration of her claims against the hospital.[10]

Similarly, the court in *Herrera* found that the Herreras' claims against Cathay are connected to ASAP's T&C, which included an arbitration clause. Just as *Franklin* highlighted the "substance" of the claims rather than simply who was named in the contract, the court here observed that the Herreras' allegations depended on the obligations and processes set by ASAP's T&C.[11] Applying equitable estoppel to enforce the arbitration clause within ASAP's T&C was fair and appropriate, even though Cathay Pacific was not a direct signatory to the contract between the Herreras and ASAP. The doctrine of equitable estoppel allows a non-signatory to compel arbitration if the claims are intimately connected to the agreement containing the arbitration clause. The court found that the Herreras' breach-of-contract claims against Cathay were "intimately founded in and intertwined with" ASAP's performance under its T&C, particularly around the issues of requesting and processing refunds. The majority dismissed the Herreras' argument that federal regulations precluded arbitration, interpreting the regulations narrowly.

For these reasons, the court concluded that the district court erred in denying Cathay's motion to compel arbitration based on the doctrine of equitable estoppel. The district court's decision was reversed. The Ninth Circuit remanded the case back to the district court with instructions to either dismiss or stay the action pending arbitration of the Herreras' breach-of-contract claim, depending on whether all the suit's issues could be handled during the arbitration.

Implications and Impact

The decision in *Herrera v. Cathay Pacific Airways Ltd.* has significant implications for applying equitable estoppel in arbitration contexts, particularly when a non-signatory seeks to enforce an arbitration agreement embedded in a third-party contract. By upholding the arbitration clause, the court signaled that even if a party, like Cathay, isn't directly part of the original agreement, it can still compel arbitration if the claims are "intimately founded in and intertwined with" a contract that included an arbitration clause. This means that courts may now be more willing to enforce arbitration clauses when a case is indirectly related to a contract, even if the main contract dispute is with a different party. The court's reliance on cases like *Franklin v. Community Regional Medical Center* highlights the shift toward focusing on the core issues of the claims, rather than simply who signed the contract.

The decision also reinforces arbitration's reach over consumer claims, even when those claims are directed at a party that does not have a signed arbitration agreement with the consumer. This interpretation could undermine consumer protections by blurring the line on when arbitration applies, allowing companies to exploit indirect contractual ties to compel arbitration. As a result, consumers could find it harder to take their disputes to court if businesses increasingly use arbitration clauses in agreements with third-party intermediaries to avoid lawsuits. Due to ASAP's role as a middleman, the decision may impact how courts view the role of intermediaries in contractual disputes. The court's holding suggests that parties engaging with consumers through third-party platforms might be able to enforce arbitration even if they do not directly hold arbitration agreements with those consumers. Consumers and companies will need to be more cognizant of the provisions within the terms and conditions they consent to with intermediaries because it can expose the consumer or the company on a broader scale.

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Judge Danielle J. Forrest began her dissent by immediately disagreeing with the outcome reached by the majority. She emphasized that the doctrine of equitable estoppel prevents parties from circumventing arbitration agreements by suing non-signatories for issues "intimately founded in" or "intertwined with" an existing contract.[12] Judge Forrest argues that the Herreras case does not meet this threshold because their refund claim hinges solely on Cathay's obligations, not on ASAP's T&C. The dissent argued that Herreras' claim is narrowly focused on Cathay's failure to issue refunds per their own GCC. This is crucial because the claim does not involve interpreting and enforcing the agreement with ASAP but rather is concerned with a separate contractual obligation between Cathay and its passengers under its GCC.

Equitable estoppel does not apply where the plaintiff "would have a claim independent of the existence of the [contract containing the arbitration agreement]."[13] In *Kramer v. Toyota Motor Corp,* the court concluded that consumers' product-defect claims were not intertwined with their retail purchase agreements.[14] Even though the claims would not have arisen had the consumers not purchased the product, their claims did not rely on the actual terms of the purchase agreement.[15] In contrast, *Franklin* dealt with a nurse who brought claims for wages and overtime pay for unrecorded time against the hospital where she worked.[16] In that case, resolving the issue involved knowing whether the staffing agency paid her.[17] This is what made her claims "intertwined."

Judge Forrest focuses on the fact that the Herreras' claims rested on a simple theory: Cathay breached its ticket contract by not issuing them a refund following the cancellation of their flight. The claim is framed as an alleged breach by Cathay of its own obligations under the GCC. Thus, the underlying facts do not inherently implicate ASAP's T&C. For this reason, Judge Forrest concludes that the doctrine of equitable estoppel should not be applicable in this case.

The dissent also refuted the majority's view that ASAP's role as a middleman bound Cathay to the arbitration agreement in ASAP's Terms. If Cathay was required to issue any refund owed to ASAP instead of to the Herreras directly, then Cathay's obligation to ASAP would be independent of any downstream obligation that ASAP owed to the Herreras. Judge Forrest viewed these as two distinct obligations within two contracts involving separate parties. The majority also noted that the two obligations are intertwined because ASAP violated its own T&C by creating refund restrictions that formed a basis for the Herreras' claim. The dissent argued that when analyzing intertwined-with-contract claims, the question is not what the defendants assert but what plaintiffs plead in their complaint.[18] In this case, the Herreras specifically claimed that they were entitled to a refund from Cathay.

To conclude that ASAP violated its T&C by denying the Herreras a refund, one must first establish that Cathay was not obligated to provide the refund to the Herreras. In *Franklin*, the case could not be resolved without the nurse's information about her pay rate and terms of employment contained in the third-party contract.[19] The Herreras' claim that Cathay owed them a refund, however, could have been resolved without any information about their relationship with ASAP. Because Cathay has not shown any basis for which equitable estoppel should apply, Judge Forrest argues that the district court's denial of Cathay's motion to compel arbitration should be affirmed.

Judge Forrest's dissent argues that the claims against Cathay were independent of ASAP's T&C. She highlighted that the Herreras' refund entitlement stemmed from Cathay's GCC, not from ASAP's obligations, making equitable estoppel inappropriate. The dissent cautioned against broadening arbitration clauses to cover disputes unrelated to the contract's terms, emphasizing consumer protection concerns.

Conclusion

The Ninth Circuit's decision in *Herrera v. Cathay Pacific Airways Ltd*. exemplifies the court's expansive interpretation of equitable estoppel in the context of arbitration agreements. By allowing Cathay Pacific, a non-signatory, to enforce an arbitration clause contained in ASAP's Terms and Conditions, the court has potentially set a precedent that could significantly impact consumer contract disputes. The ruling emphasizes the importance of the relationship between parties and the interconnectedness of claims, signaling a broader reach for arbitration contracts.

However, Judge Forrest's dissent highlights the potential dangers of this expansive interpretation. One such potential danger is that applications of equitable estoppel such as this could undermine consumer protections by compelling arbitration even when claims appear to be independent of the third-party agreements. Her concerns underscore the tension between facilitating arbitration and preserving access to judicial remedies for consumers.

For businesses, *Herrera* underscores the strategic advantage of leveraging intermediary agreements to extend arbitration clauses, which could serve as a shield against litigation. For consumers, it serves as a cautionary tale, emphasizing the importance of understanding the implications of agreeing to third-party terms. As arbitration clauses increasingly permeate consumer transactions, this decision may prompt further scrutiny from courts and policymakers seeking to balance efficiency with fairness in dispute resolution.

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1 104 F.4th 702 (9th Cir. 2024). https://law.justia.com/cases/federal/appellate-courts/ca9/21-16083/21-16083-2024-03-11.html
2 Kramer v. Toyota Motor Corp., 705 F.3d 1122, at 1128—29 (9th Cir. 2013), quoting Goldman v. KPMG, LLP, 173 Cal. App. 4th 209, at 221 (2009).
3 Franklin v. Cmty. Reg'l Med. Ctr., 998 F.3d 867, 875 (9th Cir. 2021).
4 *Id.* at 869.
5 *Id.*
6 *Id.*
7 *Id.*
8 *Id.* at 875—876.
9 *Id.*
10 *Id.* at 876.
11 *See id.* at 875.
12 *Kramer,* 705 F.3d at 1128—29.
13 *Id.* at 1131.
14 *Id.* at 1131—32.
15 *Id.*
16 *Franklin*, 998 F.3d at 875—76.
17 *Id.*
18 *Franklin,* 998 F.3d at 875.
19 *Id.*