



AIRCRAFT MANAGEMENT COMPANIES AND OTHER SERVICE PROVIDERS: MANAGING DEBT FROM AIRCRAFT OWNERS

-By Brendan Collins-

As we have seen, owners of corporate aircraft are not immune from economic hardships. As a result, in today's economic environment it is more important than ever for those providing aviation services or products - such as aircraft management companies, fuel providers, and parts and labor providers - to recognize that even seemingly stable, long-standing customers may face financial burdens that create insolvency or necessitate their filing for bankruptcy. While there may be nothing that one can do to prevent a customer's reorganization or liquidation in bankruptcy, there are important steps that you can take to minimize the risk that you experience significant financial losses as a result of such an insolvency.

One obvious concern is when your customer fails to pay its bills. What steps can be taken to maximize your ability to recover unpaid invoices? Also problematic are attempts by a debtor or its bankruptcy trustee to recover payments made to you during the "preference period" (i.e., 90 days prior to the bankruptcy filing). This article illustrates some steps that you can take to minimize or eliminate those risks.

The simplest way to avoid becoming a creditor in a bankruptcy action is not to provide goods or services to a customer without having been paid in advance or without having a pre-funded retainer in place. Of course, in many instances, this may be an impractical way to do business. Nonetheless, more and more companies are opting to take this route. By doing so, there will be no outstanding claims in the event the owner of an aircraft to whom you have provided goods or services files for bankruptcy.

If payment is made at the time of or before providing the goods or services at issue, no creditor relationship exists and the payments are not made on account of a pre-existing debt owed before the payment was made. Thus, advance payments also should be immune from attempts by debtors or bankruptcy trustees to recovering payments made within the preference period.



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More commonly, goods or services are provided on credit or advance retainers are insufficient to reimburse for the aviation services or products provided. In the event of bankruptcy filing, general unsecured creditors often recover only a small percentage of the amount owed by the debtor. Accordingly, steps should be taken to attempt to “secure” your claim so as to provide priority over the claims of other creditors.

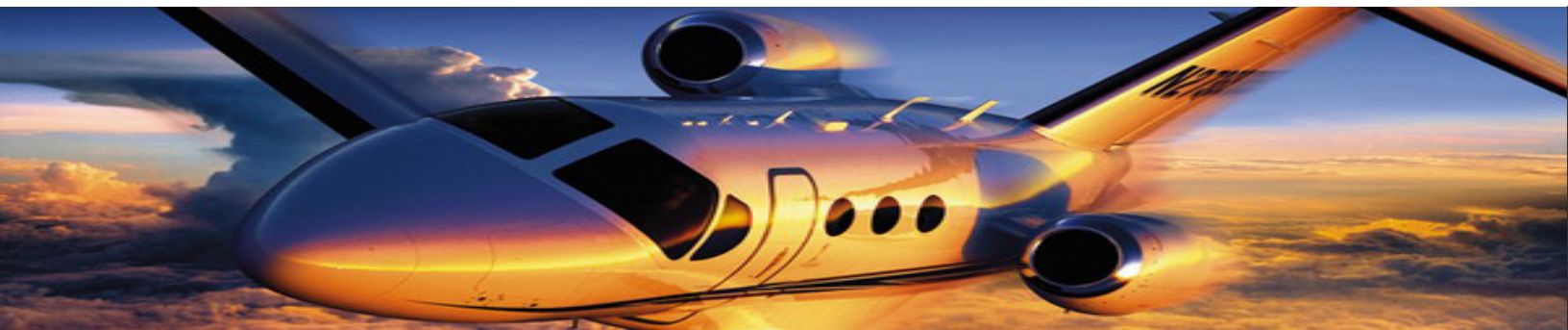
Ordinarily in a bankruptcy proceeding, the automatic stay prevents a secured creditor from repossessing the debtor’s collateral. Chapter 11 carves out an exception for secured creditors with a security interest in aircraft, aircraft engines and spare parts. This article does not address the scope of that exception.

By the enactment of the Federal Aviation Act, Congress established a single national filing system for the recordation of documents evidencing title and security interests in civil aircraft. The Code of Federal Regulations provide that all notices of liens, including mechanic’s liens against aircraft, engines and spare parts are conveyances subject to mandatory FAA recording requirements. In promulgating these filing requirements, however, Congress did not override state laws that would otherwise govern priorities between perfected security interests.

Thus, in determining the validity of a security interest, one must look not only to federal law but also to state law to ensure compliance with statutes governing such a creditor’s rights. Some states provide that a mechanic’s lien securing the value of material and labor used to enhance or restore property is invalid unless it is filed with the FAA, as well as in some cases, the clerk of the county where the aircraft was located when the labor, services, fuel or material was provided. Other states, however, have statutes that require that the person providing repair or maintenance services retain possession of the aircraft or spare parts in order to perfect its lien. Under those statutes, possession of the goods perfects the lien, rather than a written document.

The FAA has determined that it will not accept filing of a mechanic’s lien from states where possession of the aircraft or spare parts perfects the lien. Most importantly, close attention must be paid to FAA and state law requirements in order to ensure one maximizes the ability to recover in the event of insolvency. State laws may be traps for the unwary. Among the issues that one must assess are whether the mechanic must retain continuous possession of the aircraft in order to maintain the validity of the lien and whether the consent of the owner of the aircraft is required before a mechanic can establish a lien against the property.

State statutes differ as to the type of services that may be subject to a mechanic’s lien. State laws and courts interpreting those laws have differed as to the extent to which a mechanic’s lien may apply to various services provided by aviation service providers. There is virtual unanimity that liens cover repairs for aircraft and/or engines. Differences arise, however, as to whether liens properly may attach to money owed for fuel purchased on credit or for similar supplies. While some courts have held that such liens are valid, other courts have ruled that fuel, oil and oxygen provided by an aviation center are not “materials” under statutes creating liens in favor of those who furnish materials for aircraft.



Before filing a lien or taking possession of a customer's assets, consideration must be given as to the effect it will have on your relationship with that customer. Filing a lien could trigger a default in an aircraft owner's loan documents. This could lead to a management company being terminated or the aircraft owner utilizing another vendor for fuel or future repairs. Under certain circumstances, however, such steps must be taken in order to protect your interests. A lien may not force the owner of an aircraft to pay you until the aircraft is sold, but in the event of a bankruptcy filing, a properly recorded lien may be the difference between having your claim paid in full and only receiving pennies on the dollar.

Many critical steps can be taken to limit exposure and maximize recovery by aircraft management companies or those providing fuel and/or parts and labor for aircraft. If you are interested, GKG Law attorneys can assist with these planning alternatives. Please feel free to contact Brendan Collins by telephone at 202/342-6793 or by email at bcollins@gkglaw.com.

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Brendan Collins is a litigator with expertise in bankruptcy and transportation-related matters. Mr. Collins was a trial lawyer for more than 10 years with the U.S. Department of Justice specializing in bankruptcy and interstate commerce. He represented the United States' interest in numerous bankruptcies involving billions of dollars worth of claims, including airline bankruptcies such as US Air and Aloha Airlines.

