

FAA Notice of Proposed Policy Clarification for the Registration of Aircraft in Owner Trusts

February 14, 2012

On February 10, 2012 the FAA published a Notice of Proposed Policy Clarification for the Registration of Aircraft in Owner Trusts. The main focus is aircraft registered in the name of trustees with non-US citizen trustors/beneficiaries. A link to the 46 page Notice is: <http://www.regulations.gov/#!documentDetail;D=FAA-2012-0012-0001>. Comments on the Notice are due to the FAA by March 31, 2012.

Summary

Some of the items of most interest to trustors/beneficiaries at this time are:

- Owner trustees will be required to have additional information from each trustor/beneficiary.
 - A letter agreement whereby the trustor/beneficiary agrees to provide the required information to the owner trustee may be required for existing trusts.
 - The trustor/beneficiary may be required to send periodic updates on aircraft operations to the owner trustee.
- The FAA wants to see all documents affecting the relationship between the owner trustee and the trustor/beneficiary. This includes any sideletters and operating agreements.
 - If none of these documents exist, an affidavit should be provided stating this.
 - Operating agreements may become standard for future owner trusts, but it is uncertain what will be required for existing owner trusts.
 - Whether these documents are to be filed of record with the FAA still seems to be an open issue.
 - The existence of an operating agreement with language leasing the aircraft from the owner trustee to the trustor/beneficiary should be reviewed for any tax issues.
- The ability of the owner trustee to resign (without locating a replacement trustee) and/or to de-register the aircraft due to trustor/beneficiary non-compliance or tardy compliance will become stronger. The FAA expects updated information from owner trustees on very short (2-5 US business day) time-frames.
 - Resignation of the owner trustee or de-registration of the aircraft could negatively affect a lender's security interest in the aircraft so lenders may amend their loan documents also.
- At this time, the trustor/beneficiary may only terminate the owner trustee for cause. Cause will probably be defined in the future to only include gross negligence or intentional misconduct.

It is not currently known what, if any, impact the proposed policy may have on existing owner trusts. However, it seems likely that the final policy may affect existing owner trusts.

Overview of Notice

The Notice is divided into several sections. Pages 1-4 address the recent history of the issue of owner trusts (non-citizen trusts or "NCT"). Next, the Notice describes the US FAA's responsibility under the Chicago Convention for aircraft registered in the US (the "State of Registry"). These obligations involve issuing licenses for crew members, issuing certificates of

airworthiness and overseeing the continuing airworthiness of aircraft. In its review of NCT's, the FAA has determined that the basing and operation of such aircraft outside the US frequently gives rise to problems in execution of the FAA's oversight responsibilities.

The Notice also addresses an aircraft owner's responsibilities, including the regulatory obligations of owners of US registered aircraft generally. For example, an application for an airworthiness certificate must be submitted by the owner. The regulations also impose certain maintenance responsibilities on owners as well as with operators. Airworthiness Directives are also sent to registered owners, not operators.

Section 3 describes an owner's regulatory compliance obligations. The FAA treats all "owners" the same with respect to the obligations for regulatory compliance, whether that owner is an owner-trustee or an individual or an entity that operates the aircraft.

Section 4 addresses the due diligence reviews of the trustors/beneficiaries of NCT's. Most owner trustees already perform due diligence on the trustors/beneficiaries under the USA Patriot Act. The Notice states that "Those reviews do not however, necessarily meet the needs of the FAA with regard to protecting U.S. interests concerning aviation safety inasmuch as they do not consider the technical aviation issues that drive a safety oversight system." The FAA expects that owner trustees will have information about the identity and whereabouts of the actual operators of the aircraft as well as the location and nature of the operations of the aircraft and that this information is updated on an ongoing basis. Commentators, in response to the prior request for comments from the FAA, suggested that the owner trustee should not be required to identify the operator or be able to insure quick contact with the operator. The FAA specifically rejects these suggestions in the Notice. The FAA does not just want the owner trustee to provide the FAA the contact information of the trustor/beneficiary. The FAA wants the owner trustee to obtain any requested information from the trustor/beneficiary to then provide that information to the FAA.

Section 5 addresses the FAA policy clarification for information requirements. The FAA has not been as successful in accessing information necessary for it to carry out its State of Registry obligations for aircraft registered to owner trusts where the aircraft is primarily or exclusively operated outside the US. The FAA expects that within 2 business days an owner trustee will be able to provide to the FAA:

- The identity of the person normally operating or managing the aircraft;
- Residence or principal place of business of that person;
- Location of maintenance and other records; and
- Location of aircraft's normal base and operations.

Within 5 business days, an owner trustee is to be able to provide to the FAA:

- Operator, crew and aircraft operations on specific dates;
- Maintenance and other aircraft records; and
- Current airworthiness status of the aircraft.

The FAA may request information more quickly in an emergency situation. Although the FAA may not require all prior trusts to be amended, the owner trustee will be required to have

additional information, updated periodically, from each trustor/beneficiary, even from existing trusts, so it seems that, at a minimum, a new letter agreement whereby the trustor/beneficiary agrees to provide the required information in a timely manner, will probably be required to be entered into with the owner trustee. Periodic updates on aircraft operations will also probably be required to be sent to the owner trustee. Currently most owner trustees do not require initial or updated information, such as any leases, management agreements, charter agreements, etc., but that may change.

The next section of the Notice is a policy clarification related to NCT's and the registration process. The FAA wants to see all documents affecting the relationship between the owner trustee and the trustor/beneficiary. This includes any sideletters and operating agreements. If none of these documents exist, an affidavit must be provided stating this. Operating agreements may become standard for all future owner trusts, but it is uncertain what will be required for existing owner trusts. Whether these documents are to be filed of record with the FAA also still seems to be an open issue. There is currently no FAA form for an operating agreement. The existence of an operating agreement with language leasing the aircraft from the owner trustee to the trustor/beneficiary may give rise to state sales/use tax issues.

The next topic addressed by the Notice is removal and resignation of the owner trustee.

FAR 47.7(c)(3) currently states:

If persons who are neither U.S. citizens nor resident aliens have the power to direct or remove a trustee, either directly or indirectly through the control of another person, the trust instrument must provide that those persons together may not have more than 25 percent of the aggregate power to direct or remove a trustee. Nothing in this paragraph prevents those persons from having more than 25 percent of the beneficial interest in the trust.

The FAA is concerned that most current trust agreements do not adequately limit the ability of a non-US citizens to remove an owner trustee. Many current trust agreements allow owner trustees to be removed for cause without specifying what constitutes sufficient cause. The FAA will now require that the trust agreement describe with specificity what is sufficient cause for removal of an owner trustee. The trustor/beneficiary will not have the ability to fire the owner trustee, except for cause, which may be a standard such as gross negligence or intentional misconduct. The FAA will require that the trustee state in writing in the trust agreement, trustee affidavit of citizenship or elsewhere how and why it is that the non-citizens will not be able to exercise more than 25% of the aggregate power to direct or remove a trustee.

The Notice states that the non-citizen trustor/beneficiary is not restricted from terminating a trust in accordance with its terms. The Notice also states that the FAA expects the effect of such a trust termination, not involving removal of the owner trustee, would be to end registration or render the registration ineffective.

The Notice points out that the FAA does not have any restrictions on the ability of an owner trustee to resign without first being replaced by a successor trustee. The FAA expects the effect of such a trust termination, not involving removal of the owner trustee, would be to end

registration or render the registration ineffective. The ability of the owner trustee to resign (without locating a replacement trustee) and/or de-register the aircraft due to trustor/beneficiaries non-compliance or delayed compliance will likely become stronger. There may be some state law issues that arise if the owner trustee tries to resign on short notice.

The Notice also proposes adding a statement to the trust agreement recognizing that it is the owner trustee's duty to expeditiously communicate emergency airworthiness directives concerning the aircraft to the trustor/lessee.

The Notice also includes a sample revised form of trust agreement which shows language the FAA will want to be included.

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