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Aircraft Lessor and Lender Liability: Implications of the Settlement of the Air Philippines Accident

On April 19, 2000, Air Philippines Flight 541 crashed into a 577-foot mountain in Samal Island in the Republic of the Philippines, killing all passengers and crew members. An independent committee appointed by the President of the Philippines to investigate the incident determined that the pilots' loss of situational awareness while attempting to land caused them to inadvertently steer the aircraft into the mountain.

On March 10, 2008, Nolan Law Group issued a press release[1] following the US$165 million settlement of a resulting litigation, *Layug v. AAR*.[2] The case was a class action brought against AAR Parts Trading, Inc., the prior owner/lessor, and Fleet Business Credit, LLC, the owner/lessor at the time of the crash.

The press release quoted Donald J. Nolan of Nolan Law Group, lead counsel to the plaintiffs, as stating, "[t]hese companies should never have leased the decrepit airplane to Air Philippines, an under-funded and unsafe start-up airline", and that lessors have "a duty to provide oversight to ensure that passengers fly on airliners with the latest equipment, the best maintenance and finest training available."

If Nolan's statement were accurate, then aircraft lessors should be concerned that the provision of the Federal Aviation Act (49 U.S.C. §44112) generally viewed as providing aircraft lessors and other financing parties with protection from liability in circumstances such as the Air Philippines crash does not provide sufficient protection from such potential liability. Although the *Layug* settlement highlights the fact that imprecise language in §44112 has allowed certain courts, such as the *Layug* court, to narrow the protections under §44112, we believe that the Nolan press release is inaccurate in a number of respects and that the *Layug* settlement does not represent an undermining of the protections under §44112.

The circumstances behind the settlement in *Layug* are fact specific and do not mean, explicitly or implicitly, that aircraft lessors have legal liability for aircraft crashes

In considering the *Layug* settlement and the Nolan press release, it is important to note a number of issues. First, the Nolan press release is a publicity paper designed to gain notoriety for its authors. It does not provide an accurate description of the status of the *Layug* case, nor does the release address the protections afforded to lessors and other financiers by Congress and by recent case law.

Second, the circumstances behind the settlement in *Layug* are fact specific and do not mean, explicitly or implicitly, that aircraft lessors have legal liability for aircraft crashes. In *Layug*, Air Philippines' insurance carriers, faced with a series of very plaintiff favorable procedural decisions by the trial court, agreed to a settlement before any substantive hearing on the plaintiffs' allegations.

Finally, the last procedural decision made by the *Layug* court was weak in a number of respects. While the decision clearly spurred Air Philippines' insurers to settle the case, various aspects of the decision render it of minimal importance for future litigation regarding lessor liability.

The Layug Case

Layug was settled very early into the court proceedings. After a procedural argument as to whether the Philippines or Illinois was the proper forum, the case was set to be litigated in Illinois.

Prior to the commencement of substantive litigation, the defendants filed a motion to dismiss the case on the grounds that the plaintiffs' state law claims were preempted by §44112. Section 44112 states that:

"[a] lessor, owner, or secured party is liable for personal injury, death, or property loss or damage on land or water *only when* a civil aircraft, aircraft engine, or propeller is in the actual possession or control of the lessor, owner, or secured party..."[3]

The intention of §44112 is to protect from civil liability owner/lessors and other parties who provide financing for aircraft acquisitions but do not operate such aircraft.[4] This intent reflects the long-standing public policy of encouraging the financing of strategic assets, such as aircraft, and the concomitant belief that imposing liability on financing parties for aircraft accidents would discourage such financing. Disregarding such public policy considerations (and the clear language of §44112), the *Layug* court denied the motion to dismiss, allowing the case against AAR and Fleet to continue.

Notwithstanding the strong policy argument for respecting the language of §44112 (which the *Layug* court clearly did not find compelling), a closer analysis of the two technical legal issues at point in the case show that these two defendants should have been, and likely were, protected by §44112 from liability arising out of the crash. The two relevant issues are: first, whether this provision of the Federal Aviation Act preempts state law claims; and second, which type of aircraft lenders, owners, lessors or secured parties are meant to be protected by the statute.

Preemption

The *Layug* court held that §44112 did not preempt the plaintiffs' state law claims. In doing so, the court relied on *Retzler v. The Pratt & Whitney Company, et.al.*,[5] a decision which has been criticized by several courts in subsequent cases.[6]

Criticism of *Retzler* has focused on the fact that there is no provision in the Federal Aviation Act which could impose liability upon aircraft lessors, owners or secured parties. Because there is no potential liability for such financing parties within the Federal Aviation Act, §44112 must be intended to protect such financing parties from potential liability outside of the Federal Aviation Act. The only such potential liability is for state law claims. In decisions subsequent to *Retzler*, other courts have noted that the *Retzler* court offers no counter-argument to such reasoning and have held that §44112 preempts state law claims against financing parties.[7] In following *Retzler,* the *Layug* court failed to note the criticisms of *Retzler*.

Based on such criticisms, and the thoroughly reasoned decisions in which courts have found that §44112 does indeed preempt state law claims against financing parties, there is strong support for the view that, on appeal, the *Layug* decision would have been overturned.

Protected parties under §44112

The second recurrent issue in decisions regarding §44112 is the question of which parties in an aircraft financing are protected under §44112. The plain language of §44112 provides protection for secured parties, owners and lessors. Notwithstanding such plain language, the recent decision in *Coleman v. Windham Aviation Inc.*[8] held that owner/lessors were not protected by the statute, which was intended to protect only secured parties. The *Coleman* court noted that §44112 is a recodification, and not a substantive alteration, of a prior statute that provided only such limited protections. The *Coleman* court determined that the original codification did not include owners and therefore a reading of the recodification to include owners would impermissibly extend the scope of the statute.[9] Courts that follow the *Coleman* decision may hold that lessors who own aircraft are not covered by the statute, even though such lessors do not maintain possession or control over their aircraft.

The decision in *Coleman* has been criticized and contradicted subsequently in *Mangini v. Cessna Aircraft Co*.[10] The *Mangini* court explicitly held that aircraft owners can indeed take advantage of §44112 if all other requirements of the provision are met. In response to the *Coleman* court's reasoning regarding the recodification, the *Mangini* opinion noted that "it is far more likely that Congress overstated the general purpose of recodification than Congress inadvertently inserted a precise and unequivocal definition of "owner" and specifically stated that the limitation on liability extended to such well-defined owners."[11]

Conclusion

Since its enactment in 1948, §44112 and its predecessor statute have protected aircraft lessors and other financing parties from liability arising out of aircraft accidents. There is no disputing that aircraft lessors and other financing parties should note and consider the rulings issued by the *Layug* court that ultimately forced settlement by the airline's insurers, as well as other court decisions narrowing the protections of §44112. Such decisions demonstrate that the imprecise language in §44112

remains susceptible to narrow interpretation by plaintiff-friendly courts limiting the protections provided thereunder.

The Nolan press release implies that the settlement in the *Layug* case evidences a major shift in how United States courts interpret and apply §44112 and, consequently, a greater risk for lessors of liability in circumstances such as the Air Philippines crash. However, the rulings by the *Layug* court have minimal value as precedent and the facts and circumstances of the settlement do not support the implications of the press release. Notwithstanding *Layug* and other cases in which courts have narrowed the protections of §44112, the plain language of the statute and better reasoned court decisions should continue to protect lessors and other financing parties from liability arising out of aviation incidents.

[1]*American Leasing Companies Pay $165 Million to Settle Philippines Crash*, March 10, 2008, available at: http://press-release-depot.com/pr/american-leasing-companies-pay-165-million-to-settle-philippines-crash.html.

[2]No. 00 L 9599 (IL Cook Co. Cir.).

[3]49 U.S.C. §44112(b) (emphasis added). Before the recodification, the statute was found at 49 U.S.C. §1404.

[4]See H.R. Rep. No. 802091 (1948) ("Provisions of present Federal and State law might be construed to impose upon persons who are owners of aircraft for security purposes only, or who are lessors of aircraft, liability for damage caused by the operation of such aircraft. This bill would remove this doubt by providing clearly that such persons have no liability under such circumstances. . . It is the conviction of this committee that the bill should be passed to remove one of the obstacles to the financing of purchases of aircraft.")

[5]723 N.E.2d 345 (Ill. App. 1999).

[6]*See e.g. In re Lawrence W. Inlow Litigation*, 2001 U.S. Dist. LEXIS 2747 (S.D. Ind. 2001). The *Inlow* court stated that "the plain language of §44112 establishes that it preempts state common law claims against covered lessors" and that the *Retzler* court "did not acknowledge or consider the district court's decision in *Matei*," the case upon which *Retzler* relied. The *Inlow* court also noted that *Retzler's* analysis "strayed from the statutory language and ultimately gives §44112 no effect."

[7]*See e.g. In re Lawrence W. Inlow Litigation*, 2001 U.S. Dist. LEXIS 2747 (S.D. Ind. 2001) ("Federal common law generally does not provide a remedy for those injured in aircraft accidents. The word "only" could have effect only if the statute preempts claims against lessors arising under state law."); *Rogers v. Ray Gardner Flying Service, Inc.,* 435 F.2d 1389 (5th Cir. 1970), *cert. denied*, 91 S.Ct. 155 (1971) ("This provision appears clearly and forthrightly to preempt any contrary state law which might subject holders of security interests to liability for injuries so incurred.").

[8]2005 R.I. Super. LEXIS 119 (R.I. Super. 2005).

[9]It is unclear why the *Coleman* court chose to ignore clear language in the prior statute that covers lessors and why the legislative history of the prior statute referenced by the *Coleman* court justifies the exclusion of lessors.

[10]2005 WL 3624483 (Conn. Super. 2005).

[11]*Mangini*, 2005 WL 32624483 at *5.

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