Global Transportation Finance Newsletter

December 2018

In This Issue

Federal Safe Harbor from Liability Expanded for Aircraft Lenders and Lessors

After many years of congressional stalemates, the long awaited five-year reauthorization for the Federal Aviation Administration (the FAA) became federal law when signed by President Trump on October 5, 2018 (the Reauthorization Act).[1] Although the Reauthorization Act addresses a myriad of items of interest to the aviation industry, one such item should be of particular interest to aircraft lessors, lenders, and investors. Specifically, the Reauthorization Act modifies and expands the essential federal safe-harbor preempting these passive owners and interest holders from liability under the strict liability laws of most states.

"Dangerous Instrumentalities" Under State Law

Liability is an inherent transactional risk to parties leasing, financing, or investing in aircraft. As background, some states, such as Florida, impose vicarious liability on parties merely because they own or have an interest in "dangerous instrumentalities."[2] This "strict" liability, if imposed, would make owners and other interest holders legally accountable for personal injury and property claims relating to an aircraft accident or incident, even if it neither possessed nor controlled the operation or other matters relating to that aircraft. The legislative justifications for holding passive parties responsible for injury and property claims is to assure that there is a creditworthy party to cover the claims of citizens of that state who suffer harms from this dangerous instrumentality, and perhaps to promote conduct by passive interest holders intended to avert these potential harms. As there is no federal aviation law imposing tort liability, the liability laws of the relevant state are applied unless preempted by a federal statute.

Vedder Price Global Transportation Finance Team Welcomes Shareholder John F. Imhof Jr.

John F. Imhof Jr. joined the firm as a Global Transportation Finance Shareholder in New York. Mr. Imhof focuses his practice on maritime and transportation finance. He has more than twenty-five years of experience advising lenders, lessors, investors, borrowers and lessees in the domestic and cross-border financing of transportation and logistics assets, including ships, shipping containers, aircraft, railroad rolling stock and related infrastructure. His experience involves a variety of facilities and financing techniques, including syndicated senior secured loan facilities, mezzanine and subordinated loan facilities, letter-of-credit facilities, single-investor leases, leveraged leases, sale-leaseback transactions and restructurings. Prior to joining Vedder Price, Mr. Imhof was a partner at Seward & Kissel LLP. He earned his Juris Doctor degree, *cum laude*, from Syracuse University College of Law, and his Bachelor of Science degree from Duke University.

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However, in certain circumstances, Congress has from time-to-time passed federal laws that preempt state laws as to matters involving a compelling national interest.[3] When doing so, Congress makes a determination that the national interests are better served by overriding the state law to the extent it is inconsistent with the preemptive federal law. Congress created such a preemptive protection against the referenced state vicarious liability laws back in the 1940s when establishing the first comprehensive federal aviation laws.[4] This statutory protection, often referred to as the "safe harbor statute," was originally passed by Congress in 1948 as 49 U.S.C. § 1404 of the Federal Aviation Act and has been re-codified, most recently in 1994 as 49 U.S.C. § 44112.

Federal Preemption

Section 44112, in its original and recodified iterations, effectively provided that lessors, secured lenders and other interest holders are liable for injury and property claims relating to aircraft[5] *only* if these interest holders are in control or possession of the aircraft. The Congressional intent for enacting this safe harbor, and including it in the later recodifications, was to facilitate the availability of aircraft financing for businesses in the United States. By removing this strict liability risk as an impediment to aircraft leasing or financing, it became especially helpful for smaller businesses without access to large amounts of capital. If applied as intended by Congress, the statute should preempt state tort laws imposing liability upon any lessor, financier, or investor for damages caused during operation of the aircraft, so long as such interest holder had neither possession of, nor control over, the aircraft operations at the time of the accident.

Unfortunately, some courts have struggled with the application of § 44112 by finding ambiguities in the current statute and its legislative history. State and federal courts have interpreted the scope of § 44112 differently, resulting in confusing and somewhat contradictory holdings among those courts when asked to consider its application to the facts and circumstances presented in that specific case.[6]

Efforts lead by the Equipment Leasing and Finance Association (ELFA), GE Corporate and Vedder Price[7] resulted in amendments to the safe harbor statute intended to award future misapplication of the statute.

Shareholder Edward K. Gross played a key advisory role in the drafting of the newly passed FAA Reauthorization Act of 2018, signed into law on October 5, 2018. The bill reauthorizes the Federal Aviation Administration's programs and funds the programs through 2023, the longest such authorization since 1982.

Honors & Awards

RANKED IN Chambers UK 2019 Vedder Price

Chambers UK 2019 Asset Finance: Aviation Finance—UK-Wide ranks Vedder Price **Band 2**. Gavin Hill and Neil Poland are ranked Band 2, Derek Watson is ranked Band 4 and Dylan Potter is recognized as Up and Coming.

LEGAL MEDIA GROUP EUROMONEY

Shareholder Mark J. Ditto received "Best in Aviation" award at *Euromoney Legal Media Group's* inaugural Americas Rising Star Awards on October 1, 2018.

Vedder Price is pleased to announce that Global Transportation Finance Shareholder Francis X. Nolan, III has been named as one of the Top 10 Maritime Lawyers globally as part of *Lloyd's List's* "2018 Top 100 Most Influential People in Shipping" series. *Lloyd's List* has been an authority on maritime news since 1734. Mr. Nolan is one of only three Americans named.

The Statute

Prior to the amendment, 49 U.S.C. § 44112(b), stated, in part:

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, and the personal injury, death, or property loss or damage occurs because of - (1) the aircraft, engine, or propeller; or (2) the flight of, or an object falling from, the aircraft, engine, or propeller.

Section 44112 also defines those parties whose civil liability could be limited by this section as follows:

(1) "lessor" means a person leasing for at least 30 days a civil aircraft, aircraft engine, or propeller.

(2) "owner" means a person that owns a civil aircraft, aircraft engine, or propeller.

(3) "secured party" means a person having a security interest in, or security title to, a civil aircraft, aircraft engine, or propeller under a conditional sales contract, equipment trust contract, chattel or corporate mortgage, or similar instrument.[8]

While a number of courts have held that the federal safe harbor preempts state tort liability law,[9] the courts in two landmark cases, *Storie v. Southfield Leasing*[10] and *Vreeland v. Ferrer*,[11] disagreed. In *Storie*, the Michigan Court of Appeals considered the preemption issue in connection with a wrongful death case brought by the estate of a passenger in an aircraft owned and leased by the defendant to the passengers' employer. The appellate court, relying on a prior, but essentially similar version of the statute, held that the statute did not preempt a Michigan vicarious liability law.[12] The court reasoned that the plaintiff's injury did not occur *on the surface of the earth*, and, accordingly, per the plain language of the statute, was not covered by its scope.[13]

Similar to *Storie*, the *Vreeland* case rests on a strict reading of the "*on land or on water*" element of § 44112.[14] In *Vreeland*, the surviving beneficiary of a passenger killed in an aircraft accident sued the aircraft lessor who had leased the aircraft to a third-party lessee, in control of and operating the aircraft at the time of the accident.[15] The plaintiff argued that, "as owner of the aircraft, [lessor] was liable and responsible for the negligence of [the pilot] in the operation and inspection of the aircraft."[16]

After the trial court denied the plaintiff's vicarious liability claim by deeming it to be preempted by § 44112, the Florida Supreme Court considered, upon appeal by the plaintiff, whether the trial court had erred as to its application of the preemption.[17] The Florida Supreme Court, relying on a strict construction analysis, reversed the district court of appeals' decision, holding that § 44112 could only preempt liability under Florida's dangerous instrumentality laws "[t]o the extent that the [laws] applie[d]

Honors & Awards

(continued)

U.S. News—Best Lawyers, a publication of *U.S. News & World Report*, distinguishes Vedder Price as "Law Firm of the Year" for Equipment Finance in its annual "Best Law Firms" rankings. In addition, Vedder Price achieved 20 National Rankings and 26 Metro Rankings. The Global Transportation Finance team is especially pleased with the recognition of our Maritime, Banking and Equipment Finance practice areas:

National Tier 1
- Admiralty & Maritime Law
- Banking and Finance Law
- Equipment Finance Law

Metropolitan Tier 1
- New York
  Admiralty & Maritime Law
  Equipment Finance Law
- Washington, DC
  Equipment Finance Law

Metropolitan Tier 2
- Chicago
  Equipment Finance Law

Vedder Price is ranked in the 2018 *Legal 500 United Kingdom Asset Finance and Leasing Guide*. In addition, Dylan Potter is named a Next Generation Lawyer while Gavin Hill and Neil Poland are individually recommended.

to injuries, damages or deaths that occur[ed] on the surface of the earth."[18] However, "because the death of [the passenger] occurred while he was a passenger in a plane that crashed – not on the ground beneath the plane – the wrongful death action" was not preempted by § 44112.[19] The Appellate Court also reasoned that because there existed a separate statute addressing injuries to aircraft crew and passengers who were in the aircraft at the time of the incident, Congress specifically intended the predecessor to § 44112 to preempt state law with regard only to "injuries that occurred on the surface of the earth."[20]

Similar to the holding in *Storie*, and as expanded in the dissent in *Vreeland*, the majority's opinion "defied reality."[21] Citing the lower court's opinion, the dissent noted that the majority's "reasoning [did] not 'explain why an airplane crash does not cause an injury on the surface of the earth regardless of whether the injured person was in the airplane or standing on the ground.'"[22] According to the majority, the passenger "was not 'on land or water' at the time of the crash", even though the passenger "was in the aircraft when it hit land . . . [and] his death occurred 'on land,' not in the aircraft prior to contact with the land."[23]

The impact of cases like *Storie* and *Vreeland* is that they encourage Plaintiff's counsel in aircraft accident cases to forum shop, by selecting one of the jurisdictions with precedent most favorable to their clients' cases. The vulnerability of § 44112 to those and other cases challenging the extent of the preemption was the motivation for the industry advocacy team to pursue the recent amendments. Members of our advocacy team met frequently, especially after *Vreeland*, with various members of Congress, pertinent committees and staffers seeking amendments to the statute in future legislation. Achieving effective legislation change is extremely challenging, but based on the advice of our advocacy professionals from ELFA and GE Corporate,[24] the team's strategy was to propose amendments that were simple, straight-forward, essential, and non-controversial to any constituency. After many dozens of these Hill meetings over the past seven years, and by sticking to our strategy, sponsors in the House and Senate agreed to include the amended safe harbor statute reflecting our changes in the Reauthorization Act in section 514, titled "Aircraft Leasing." The statute now states, in part:[25]

> A lessor, owner, or secured party is liable for personal injury, death, or property loss or damage only when a civil aircraft, aircraft engine, or propeller is in the actual possession or *operational* control of the lessor, owner, or secured party, and the personal injury, death, or property loss or damage occurs because of –
>
> (1) the aircraft, engine, or propeller; or
>
> (2) the flight of, or an object falling from, the aircraft, engine, or propeller.

- Shareholder Edward K. Gross and Associate Erich P. Dylus's article from the April 2018 GTF Newsletter "Aircraft Lender Not Responsible for Customer's Structuring Strategy" was reprinted in the Fall 2018 issue of ABA's *The Air & Space Lawyer*. The article reviews a recent case between a guarantor of an aircraft acquisition loan and a lender whose outcome serves as an important reminder to lenders, and other financing providers, that they should generally refrain from providing structural and/or ownership advice to their customers beyond financing.
- Shareholder Edward K. Gross recently co-authored "Leases" in the Fall 2018 edition of *The Business Lawyer*. The survey covers a number of cases decided in 2017-2018 involving disputes between parties to equipment financing transactions or with third parties regarding the transactions or the related equipment.

The amendments to the statue include striking "on land or water" and inserting "operational" before "control." The deletion of "on land or water" was intended to nullify judicial decisions, such as *Vreeland*, where interpretation of those words allowed courts to justify their refusal to apply the preemption. Specifically, this amendment will make it difficult for a court to replicate the *Vreeland* opinion in which a victim must actually be underneath the aircraft, "defy[ing] reality," as the dissent noted. Second, the insertion of "operational" before "control" aims to curb interpretations that may broaden the definition of "control." The intention here is that a court would look to FAA regulations and interpretations and have a more precise scope of what constitutes "operational control."[27]

Conclusion

The risk that federal preemption might not be applied by a court based on its narrow interpretation of § 44112 has had a chilling effect on prospective lessors and other aircraft investors and financiers. The amendments pursued and achieved by our industry advocacy team should reduce the likelihood that a court will refuse to apply § 44112 due to an evenly narrow interpretation, and in turn, give some comfort to lessors and other aircraft investors and financiers that their liability risk may have been somewhat diminished. Nonetheless, lessors and financing parties should still require the typical transactional protections. Among other things, the lease or loan documents should include indemnifications and legal compliance provisions and, most importantly, liability insurance coverage pursuant to policies from reliable credit-worthy insurers and with acceptable policy scope, coverage amounts, breach of warranty, and other lender/lessor endorsements, terms, and conditions.

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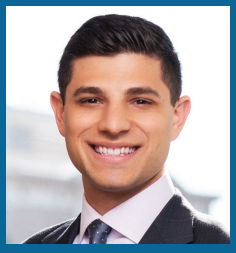

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Recent Speaking Engagements

September 18-19, 2018
17th Annual Marine Money Week Asia, Singapore

Shareholder Ji Woon Kim moderated the panel **Traditional Shipping Banks Change Direction**. Panelists discussed the decreasing shipping exposure of European banks since 2008 as the banks deal with nonperforming loans and de-risk their lending books. Panelists further discussed the reorientation of traditional shipping banks toward catering to key clients and their shipping and banking requirements.

October 1-2, 2018
Revolution.Aero 2018, San Francisco, CA

Shareholder Edward K. Gross moderated the panel **Risky Business? Insuring the New Revolution**, which investigated how insurers look at new technology and whether the aviation market can underwrite new risks.

Shareholder David M. Hernandez moderated **Build It and They Will Fly**, which examined how to make money building aircraft and what is needed to manage relationships with regulators.

October 14-15, 2018
National Business Aviation Association's Tax, Regulatory, & Risk Management Conference, Orlando, FL

Shareholder David M. Hernandez presented **Introduction to FARs & Permissible Operating Models**, discussing what makes certain flight operations legal from an FAA perspective.

October 16, 2018
Equipment Leasing and Finance Association's 57th Annual Convention, Phoenix, AZ

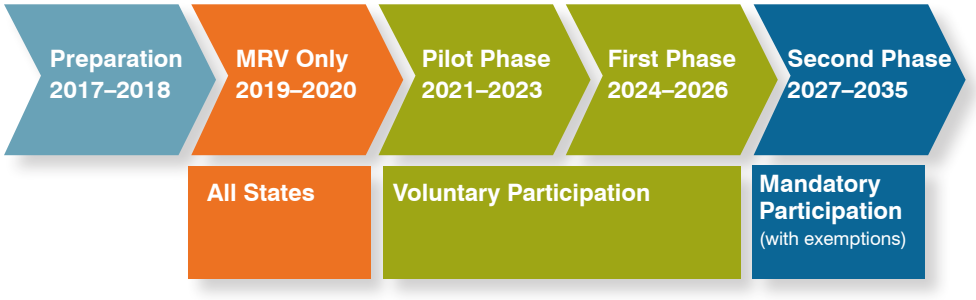
Shareholder Edward K. Gross led **Making Business Move: Transportation Leasing and Finance**, a roundtable discussion of the current market approach to transportation finance transactions.

ICAO CORSIA Update: Compliance Complexities Under ICAO's New Carbon Offsetting Scheme

Airlines and airline associations have broadly welcomed ICAO's new carbon offsetting scheme, scheduled to commence on January 1, 2019. However, the scheme's Standards and Recommended Practices (the **SARPs**) impose an immediate compliance obligation on international airlines and raise a number of potential risks for aircraft financiers and lessors.

In June 2016, the 39th Assembly of the International Civil Aviation Organization (**ICAO**) agreed to adopt a global market-based measure to control aviation carbon dioxide (CO_2) emissions,[1] This scheme is referred to as the Carbon Offsetting and Reduction Scheme for International Aviation (**CORSIA**). On June 27, 2018, ICAO's Council adopted the First Edition of Annex 16, Volume IV, which details the international SARPs for CORSIA[2] Ultimately, over 700 aircraft operators[3] (**Operators**) worldwide will be compelled to comply with various aspects of the scheme.

Commencing on January 1, 2019, all Operators not otherwise exempt from CORSIA[4] with annual emissions exceeding 10,000 metric tons of CO_2[5] will be required to record and report emissions data for their international flights on a yearly basis. Operators will also be required to submit an emissions monitoring plan by February 28, 2019. Annual emissions reports and Emissions Monitoring Plans must be submitted by an Operator to its ICAO Contracting State regulator even if the Contracting State[6] has opted not to participate in the voluntary phases of CORSIA. The reported data will form the baseline for calculating compliance requirements during the upcoming voluntary and compulsory phases of the scheme occurring during the periods indicated in the following timeline:



CORSIA timeline—Under the Monitoring, Reporting and Verification (**MRV Only**) Phase (2019–2020), all aircraft operators are required to submit an Emissions Monitoring Plan[7] no later than 28 February 2019 and report their 2019 and 2020 emissions to their ICAO state regulator by 31 May 2020 and 31 May 2021 respectively.

Recent Speaking Engagements

(continued)

October 16, 2018
20th Annual Marine Money Greek Ship Finance Forum, Athens

Partner Dylan Potter moderated **IMO 2020: The Views of Greek Shipping**. The panel examined the opinions of Greek shipping on the impacts of the IMO 2020 requirements and the action being taken by the industry to prepare for and address them.

October 16-18, 2018
NBAA Business Aviation Convention & Exhibition, Singapore

Shareholder David M. Hernandez presented **Knowing Your Customers: How to Avoid Dealing with Bad Actors**, in which he and co-presenters examined the increasing importance of properly vetting transactions given the common presence of middlemen.

October 17, 2018
Airline Economics Growth Frontiers New York 2018, New York, NY

Shareholder Kevin A. MacLeod spoke on a panel entitled **The Aviation ABS and the Future of Aviation Securitizations**, which discussed current trends in the aviation ABS market and the outlook for its growth and development.

October 17-18, 2018
Ishka's 2018 The Aviation Investival: New York, New York, NY

Shareholder Kevin A. MacLeod moderated a panel on the topic of **Will a Deeper Secondary Market Help Grow the Aviation Capital Markets?** He and his co-panelists offered a breakdown of trading activity and volumes in the secondary market, as well as answered the following questions: How do investors differentiate between the creditworthiness of different types of issuers, and is this reflected in pricing? What is needed to create more secondary trading and price transparency in deals?

Given these impending deadlines, from a practical standpoint, Operators need to be well into the process of developing and implementing their international aviation emissions monitoring plans in order to ensure compliance.

ICAO expected most of its 192 Member States to implement the SARPs[8] into their respective national laws without modification. CORSIA Contracting States were given until October 22, 2018 to file disapproval of the SARPs and were also required to file any differences to ICAO in transcribing the SARPs into their national laws by December 1, 2018. On November 21, 2018, the EU Council instructed EU Member States to file differences to ICAO concerning the lack of time available to transcribe the SARPs into EU law and also that certain differences currently exist between EU Directive 2003/87/EC and detailed rules adopted by the EU Commission, on the one hand, and CORSIA, on the other hand, particularly with respect to MRV requirements and to offsetting requirements.[9] This has created widespread concern that the SARPs will not be universally adopted, transcribed or fully implemented by each Contracting State. This could potentially result in a patchwork of different sub-rules, regulations and enforcement measures that may apply, and some Contracting States may even simply fail to adopt, regulate and/or enforce CORSIA at all.

CORSIA therefore raises a number of potential and unforeseen credit, political and reputational risks, not only for Operators but also for aircraft owners[10] and lessors. ICAO has yet to determine the types of carbon offset units that will be eligible under the scheme and whether grandfathering of existing offsets will be permissible.[11] Any restriction concerning the type or vintage of eligible offsets may increase the cost of compliance and thus create an economic burden for many Operators under CORSIA. The expected bottom-line impact of CORSIA compliance for airlines has caught the attention of international credit rating agencies such as Moody's, who suggested in a recent report that

> *"[g]rowing carbon offset costs have the potential to become significant relative to operating profit…carbon costs have the potential to lower operating income by between 4% and 15% by 2025, and by between 7% and 35% by 2030, all else being equal."*[12]

CORSIA compliance will present aircraft owners with several commercial and legal risks and challenges. One such challenge is identifying who will be responsible for compliance under the scheme where the operator of a flight has not been identified. The first line of inquiry is the ICAO designator,[13] followed by the aircraft registration mark and holder of an Aircraft Operator Certificate (AOC). If the ICAO designator and AOC holder cannot be readily established, CORSIA compliance will then will fall to the aircraft owner identified in the aircraft registration documentation.[14] Should an Operator fail to submit an emissions monitoring plan and annual emissions reports, its CORSIA Contracting State

Recent Speaking Engagements

(continued)

October 29-31, 2018
Airline Economics Growth Frontiers Hong Kong 2018, Hong Kong

Shareholder Cameron A. Gee spoke on **Current Developments in Aircraft Pre-Delivery Payment Financing Transactions**.

Shareholder Ji Woon Kim moderated a panel on **Supported Finance—ECAs and Alternatives (AFIC and Beyond)**.

November 12-14, 2018
Corporate Jet Investor Miami 2018 Conference, Miami, FL

Shareholder Edward K. Gross moderated the panel **Business Jet Finance 2019**, discussing how the industry has changed over the past 10 years and whether financiers are adjusting properly to competition.

November 14, 2018
Marine Money 19th Annual Ship Finance Forum, New York, NY

Partner Dylan Potter moderated **Alternative Asset Managers—Flexible Capital for the Right Situations**, discussing preferred equity, asymmetric scrap deals, credit products and finding niche sectors.

may not be able to identify the operator of an aircraft's international flight activity or, consequently, the responsibility for its emissions from such activity, and therefore CORSIA compliance obligations would automatically be attributed to the aircraft owner. Any such risk may become compounded for aircraft lessors and investors in asset-backed finance portfolio transactions.

The fact that ICAO has no legal rights to enforce the CORSIA SARPs creates risk that local governments and regulators may hold an aircraft owner responsible for CORSIA non-compliance. Each individual Contracting State is responsible for transcribing CORSIA into its domestic law. While it remains unclear as to exactly how (if at all) and when each Contracting State will do so, the possibility certainly exists for states to pass laws allowing relevant government entities to impose a lien on, and seize and potentially sell, an aircraft pending cancellation of sufficient emissions offsets for the operator's entire fleet—similar to the Eurocontrol fleet lien and applicable regulations in certain jurisdictions under the European Union's Emissions Trading Scheme (EU ETS)—notwithstanding the rights of the aircraft owner or mortgagee.[15] In addition, legal and financial consequences may arise should an Operator fail to cancel a sufficient quantity of eligible emissions offset units to cover its existing obligations following an insolvency declaration.

Furthermore, current lease and loan documentation practices need to be reconsidered in light of the differences between compliance under EU ETS and compliance under CORSIA. EU ETS runs on an annual reporting and emissions allowance surrender cycle. In contrast, while CORSIA will have an annual emissions reporting cycle, cancellation of emissions unit offsets will, starting in 2020,[16] be subject to a three-year compliance cycle. This longer cycle is likely to cause aircraft owners to accumulate a much greater credit risk exposure. Requiring an Operator, as a condition precedent under a lease or loan agreement, to deliver a CORSIA "Letter of Authority" permitting the relevant regulator to disclose the Operator's emissions obligations as a means for a lessor or mortgagee to monitor this credit exposure will likely have little if any effect. It is presently unknown to what extent, if any, Contracting State regulators will honor such letters of authority, as CORSIA allows aircraft Operators to request regulators to keep commercially sensitive emissions data confidential.[17] Moreover, until the end of the three-year compliance cycle expires, the CORSIA regulator will not be able to confirm the level of an Operator's compliance and financial liability, by which point the damage (and potential exposure for the lessor or mortgagee) may be irreversible. Also, the price of eligible emissions units under CORSIA (measuring the cost of compliance) will not be known until the time of purchase by the Operator, unless an Operator hedges its CORSIA exposure through a forward contract with a carbon broker.

Recent Events

GTF Holiday Dinner

Our Global Transportation Finance team hosted our aviation finance clients at our annual holiday dinner in New York City. Many of our clients and friends attended the event along with attorneys from our offices around the country. Thanks to all who joined!

Should the EU decide to transcribe CORSIA[18] as an annex to EU ETS, then the existing enforcement measures for non-compliance, being a statutory penalty of €100 per ton of CO_2[19] plus additional local fees, penalties and the rights of aircraft seizure, detention and sale may apply. Meanwhile, the UK is scheduled to exit the EU ETS in March 2019[20] and is currently considering its options, including whether to seek to negotiate with the EU to opt back into EU ETS, or alternatively set up its own ETS or UK aviation carbon offset scheme for domestic and intra-European Economic Area (EEA) flights. The UK remains fully committed to CORSIA for international flights outside the EEA. Meanwhile, the uncertainties surrounding CORSIA could create challenges in disclosing climate change-related risks, trends or factors in publicly listed leasing and finance company annual financial reports[21] and offering memoranda for securitization transactions that require a credit rating.[22]

In sum, given the plethora of potential risks and uncertainties under CORSIA, it is important that aircraft owners and financiers understand the basic functions of the scheme, keep an eye on the evolving landscape of requirements and consequences of non-compliance, and consider implementation of risk mitigation measures in lease and loan documentation. While there is considerable momentum for commencing and implementing CORSIA as a global method for reducing aviation emissions, the scheme still presents many unknowns and risks, but few clear solutions.

Vedder Price can advise on developing CORSIA-related provisions in aircraft lease and loan agreements. Avocet Risk Management is positioned to provide CORSIA risk management and mitigation solutions to aircraft owners and financiers.

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Drones—Rise of the Basic Regulation

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Last summer we reported on the UK Government's proposals to regulate the use of drones in the UK (https://www.vedderprice.com/necessary-regulation-or-the-uk-government-droning-on). Since then, competency for the regulation of drones has been transferred to the EU, and the new EASA Basic Regulation (EU) 2018/1139 (the Basic Regulation) covering their regulation has been published in the Official Journal, and came into force on 11 September 2018.[1]

Prior to the adoption of the Basic Regulation, drones lighter than 150kg that were operated in the United Kingdom were under the jurisdiction of the UK authorities, and operators and manufacturers would be subject to differing design and safety requirements from elsewhere in the EU.

The Basic Regulation aims to create a common regulatory framework for manufacture, design and operation of drones. Many of the proposals discussed in our article relating to the UK Government's proposals for operators are included in the Basic Regulation—the Basic Regulation sets the groundwork for establishing rules that will require all users of drones weighing 250g and above to register their drones and ensure they are marked for identification. New rules will make it clear that (i) drones must be used in a way that does not put people at risk and (ii) operators must know the rules governing their flights and demonstrate the ability to operate a drone safely.

[1] It should be noted that the Basic Regulation does more than introduce the new regulatory framework for drones, but this was one of the principal reasons behind the introduction of the new regulation.

Federal Safe Harbor from Liability Expanded for Aircraft Lenders and Lessors.

1 *FAA Reauthorization Act of 2018*, Pub. L. No. 115-254, 132 Stat. 3186 (2018).

2 *See Southern Cotton Oil Co. v. Anderson*, 86 So. 629 (Fla. 1920) (holding that an automobile is a dangerous instrumentality and its owner's liability extends to the automobiles, use by anyone with the owner's consent).

3 *See Abdullah v. Am. Airlines, Inc.,* 181 F.3d 363 (3d Cir. 1999) (holding that federal aviation regulations constituted implied field preemption of state law air safety regulations).

4 49 U.S.C. § 1404 (current version at 49 U.S.C. § 4412 (2006))

5 Note that the statute also affords the referenced liability safe harbor to lessors, lenders and other passive parties having an interest in aircraft engines or propellers, and that you may assume that each reference in this article to "*aircraft*" may also be read as "*aircraft, engine* or *propeller,*" as appropriate.

6 Among the issues that have been decided differently among these cases, are the extent to which the federal exculpation preempts state law imposing liability, the meaning of "possession or control" in the context of this statute, and whether it covers all types of aircraft interest holders.

7 The advocacy team consisted primarily of representatives from ELFA (Andy Fishburn and his predecessor, Richard Shanahan), GE Corporate (Darby Becker), together with the co-authors of this article (Edward Gross and Jonathan Rauch).

8 49 U.S.C. § 44112 (2006) (emphasis added).

9 *Mangini v. Cessna Aircraft Co.*, 2005 Conn. Super. LEXIS 3387 (Conn. Dec. 7, 2005) (holding that owners are entitled to the same limitation of liability that Section 1404 extended to security holders); *In re Inlow Accident Litig*. No. IP 99-0830-C H/G, 2001 U.S. Dist. LEXIS 2747 (D. Ind. Feb. 7, 2001) (holding that § 44112 prevents the imposition of liability on lessors that are not engaged in some concrete fashion in the operation of the aircraft); *Matei v. Cessna Aircraft Co.*, 35 F.3d 1142 (7th Cir. 1994) (holding that aircraft owner who leased aircraft to corporation, who had operational control when the aircraft crashed, was preempted from liability, in part, by § 1404); *Rogers v. Ray Gardner Flying Serv., Inc.*, 435 F.2d 1389, 1394 (5th Cir. 1970) (holding that liability of aircraft owner preempted when aircraft leased to fixed-based operator and crashed in their control); *Rosdail v. W. Aviation, Inc.*, 297 F. Supp. 681, 684-85 (D. Colo. 1967) (holding that no persons who merely have a security interest in aircraft or who are lessors for thirty days or more shall be liable for property or personal damages caused by an aircraft unless those persons are in actual possession or control at the time of such injury).

10 *Storie v. Southfield Leasing, Inc.*, 90 Mich. app. 612 (1979).

11 *Vreeland v. Ferrer,* 71 So.3d 70 (Fla. 2011).

12 *Storie*, at 615 (citing 49 U.S.C. § 1404 "No person . . . shall be liable . . . for any injury to or death of persons, or damage to or loss of property, on the surface of the earth (whether on land or water) caused by such aircraft)."

13 *Id.*

13 *Id*. at 72.

14 This point of impact element had been revised from "on the surface of the earth (whether on land or water)" in § 1404 to just "on land or water" in § 44112 as then codified.

15 *Id.*

16 *Id* at 72.

17 *Vreeland v. Ferrer,* 71 So.3d 70, 75 (Fla. 2011).

18 *Id.* at 84.

19 *Id.*

20 *Id.* at 80

21 *Id.* at 85

22 *Id.*

23 *Id.*

24 *See supra* note 7.

25 49 U.S.C. § 4412 (2006).

26 *Vreeland v. Ferrer,* 71 So.3d 70, 85 (Fl. 2011).

26 14 C.F.R. § 1.1 *("Operational control,* with respect to a flight, means the exercise of authority over initiating, conducting or terminating a flight.").

ICAO CORSIA Update: Compliance Complexities Under ICAO's New Carbon Offsetting Scheme

1 *See* https://www.icao.int/Newsroom/Pages/Historic-agreement-reached-to-mitigate-international-aviation-emissions.aspx.

2 *See* https://www.unitingaviation.com/publications/Annex-16-Vol-04/#page=1

3 ICAO's CORSIA uses the term "Aeroplane Operator."

4 Operators subject to CORSIA's technical exemptions being those (i) with annual emissions of less than 10,000 t/CO_2, (ii) operating humanitarian medical and firefighting flights, (iii) operating military and State flights (Presidential, customs, police, etc.), and (iv) operating helicopters.

5 10,000 metric tons of CO_2 is approximately equivalent to 4,000,000 liters (1,000,000 US gallons) of JET-A aviation fuel. Source UK Department of Transport.

6 The terms "Contracting State" and "Member State" are used interchangeably by ICAO.

7 An "Emissions Monitoring Plan" is a collaborative tool between the state and the aircraft operator that identifies the most appropriate means and methods for CO_2 emissions monitoring on an operator-specific basis, and facilitates the reporting of required information to the state.

8 The first edition of ICAO's SARPs (Annex 16, Volume IV), was adopted on June 27, 2018. Such parts of the SARPs that are not disapproved by more than half of the total number of Contracting States on or before October 22, 2018 became effective on that date and will become applicable on January 1, 2019.

9 http://data.consilium.europa.eu/doc/document/ST-14330-2018-ADD-1/en/pdf.

10 CORSIA uses the term "Aeroplane Owner" as the scheme is only applicable to fixed wing aircraft and excludes rotor wing aircraft.

11 Particularly Carbon Reduction Emissions offset units created under the United Nations' Clean Development Mechanism

12 *See* Moody's "Passenger Airlines—Global: Pricing power, route mix to determine credit implications of carbon transition" (April 2018). https://www.moodys.com/research/Moodys-Carbon-transition-risk-varies-by-airline-with-international-carriers--PR_382486?WT.mc_id=AM%7eRmluYW56ZW4ubmV0X1JTQl9SYXRpbmdzX05ld3NfTm9fVHJhbnNsYXRpb25z%7e20180418_PR_382486

13 Being the three (3) letter call sign, should the aircraft operator have such a call sign. See clause 1.1.3 of the CORSIA SARPs, https://www.unitingaviation.com/publications/Annex-16-Vol-04/#page=1

14 *See* clause 1.1.4 of the CORSIA SARPs, https://www.unitingaviation.com/publications/Annex-16-Vol-04/#page=1

15 For example, under the UK's Greenhouse Gas Emissions Trading Regulations, the UK Civil Aviation Authority has the right of seizure, detention and sale of aircraft in the event of persistent EU ETS aviation non-compliance. However, liens are not applicable where an aircraft is owned by a lessor and liens are not transferable to a new operator of an aircraft subject to penalties (i.e., "follow the metal").

16 The first CORSIA emissions credits are scheduled to be cancelled on January 31, 2025.

17 ICAO's SARPs (Annex 16, Volume IV) Chapter 2.3.16/2.3.17.

18 Depending on whether the EU considers that CORSIA meets the terms of Bratislava Declaration.

19 EU Directive 2008/101/EC, includes provision of an excess emissions penalty of EUR 100 applies for each ton of carbon dioxide equivalent emitted for which the aircraft operator has not surrendered allowances. Payment of the excess emissions penalty does not release the operator or aircraft operator from the obligation to surrender an amount of allowances equal to those excess emissions when surrendering allowances in relation to the following calendar year. Potentially a similar penalty regime may also apply for CORSIA.

20 But will require aircraft operators reporting to the UK regulator to continue to comply with EU ETS for the 2019 emissions compliance year.

21 At least 40 countries, including all EU Member States currently have mandatory emissions reporting programs in place, World Resources Institute, https://www.wri.org/blog/2015/05/global-look-mandatory-greenhouse-gas-reporting-programs

22 Credit risk arising from CORSIA should be a factor in future rating agency modelling.

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Global Transportation Finance

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