Recordation: Treatment of Instruments With Proprietary Information Intentionally Omitted; Legal Opinion

AGENCY: Federal Aviation Administration (FAA), DOT.

ACTION: Notice of legal opinion.

SUMMARY: This notice of legal opinion is issued by the FAA Chief Counsel to advise interested parties of the treatment of instruments, including leases, with certain proprietary information intentionally omitted, when they are submitted to the Civil Aviation Registry for recordation as conveyances.

ADDRESSES: Information concerning this opinion may be requested from the Assistant Chief Counsel for the Aeronautical Center, P.O. Box 25082, Oklahoma City, OK 73125–4904.

FOR FURTHER INFORMATION CONTACT: Joseph R. Standell, Assistant Chief Counsel for the Aeronautical Center, address above, or by calling (405) 954–3296.

SUPPLEMENTARY INFORMATION: Section 503(a)(1) of the Federal Aviation Act of 1958 (49 App. U.S.C. 1403(a)(1)) requires the Secretary of Transportation to establish and maintain a system for the recording of conveyances which affect title to, or any interest in, civil aircraft of the United States.

Under section 101(20) of the Federal Aviation Act (49 App. U.S.C. 1301(20)), a "conveyance" means a bill of sale, contract of conditional sale, mortgage, assignment of mortgage, or other instrument affecting title to, or interest in, property. Consistent with that definition, aircraft leases are treated as conveyances.

Leases and other conveyances are frequently submitted for recordation to the Civil Aviation Registry (the Registry). Prior to submitting documents to the Registry, law firms will often request the opinion of the FAA Assistant Chief Counsel for the Aeronautical Center with respect to questions concerning registration or recordation. In the last several years, when submitting such documents, law firms have typically asked the Assistant Chief Counsel a question similar to this:

> We hereby request your opinion that the Lease Amendment, with (i) Exhibit B (Table of Stipulated Loss Values), (ii) Exhibit C (Table of Basic Rents) and (iii) Exhibit D (End of Term Buyout Percentage) intentionally omitted from the FAA filing counterpart thereof as containing confidential information, is eligible for recordation under section 503(a) of the Act.

The Assistant Chief Counsel typically responds by permitting recordation with such omissions. Airlines and other parties that record conveyances involving large aircraft strongly favor continuation of such permission.

Now, the editor of the "Commercial Aviation Report" and persons who appraise the market value of large aircraft oppose continuation of such recordations and request that the Registry record only complete documents. Their position is set out in the Locke Parnell Rain Harrell (hereinafter, Locke Parnell) law firm's letter of September 1, 1993.

Following receipt of the Locke Parnell letter, the views of interested persons were solicited. This option addresses the concerns of all interested parties and states the agency position with respect to the recordability of conveyances with redactions and omissions.

Accordingly, consistent with 5 U.S.C. 552(a)(1)(D), the FAA publishes its response to Locke Parnell in the Appendix to this document.

Issued in Washington, D.C., September 16, 1994.

John H. Cassady,

Deputy Chief Counsel.

Appendix—Text of Locke Parnell Letter

Bruce K. Packard, Esquire, Locke Parnell Rain Harrell, 2200 Ross Avenue, #2200, Dallas, TX 75201–6776.

Treatment of Instruments With Proprietary Information Intentionally Omitted

Dear Mr. Packard: Thank you for your letter of September 1, 1993, in which, on behalf of your client, "Commercial Aviation Report," you object to the Federal Aviation Administration (FAA) permitting air carriers and lessors to submit purchase, sale, and lease documents to FAA for recordation with certain financial information deleted.

You say that the omitted information includes lease rates, maintenance reserves, amortization schedules and debt loans. You argue that FAA's permitting the nondisclosure of such information is contrary to the public interest because the deleted information is essential in making fair and accurate assessments of a carrier's financial status, its safety and maintenance reserves and meaningful debt analysis.

You request FAA to immediately stop its policy of permitting recordation of incomplete document, or, in the alternative, to initiate formal rulemaking procedures allowing for public comment.

As your know, your letter was distributed as an attachment to FAA's letter of September 27, 1993, which requested advice from interested persons concerning the legal and policy issues. We received responses from 17 concerned parties including attorneys, airlines, appraisers, the Air Transport Association, and the editor of "Commercial Aviation Report." Twelve responses favored continuation of the FAA policy of permitting omissions. Five responses opposed it. Their positions will be discussed herein.

Based on review of the comments and our reconsideration of the issues, we have decided to continue permitting the recordation of documents with limited omissions or redactions.

As set out in your letter of September 1, 1993, and letters from Rocklin D. Lyons and Associates; Jack B. Feir and Associates; Aircraft Information Services, Inc.; Avitas Aviation; and "Commercial Aviation Report," principal arguments in support of FAA acceptance of only complete instruments are the following:

It is urged that obtaining capital to finance transactions involving transport aircraft is highly competitive. In making decisions, lenders rely heavily on information concerning financial health of an airline, as well as the real market value of aircraft. The market value is frequently determined by appraisals which are based on recent comparable transactions. A principal source of information about comparables is found in the Registry's aircraft records. If financial and other information considered proprietary is permitted to be deleted, market value appraisals become more speculative. As a result, conservative investors are less likely to back transactions where the real value of the collateral is not reliable. It is urged that will hurt the aviation industry.

Additionally, it is urged that the overall financial situation of an airline is often discernible from a review of recorded transactions. As an example, one commenter pointed out that although a particular airline, as a public company, had filed all documents required by the Security and Exchange Commission (SEC) and Department of Transportation (DOT), it was only through a thorough review of the Registry's aircraft record that the "true extent of its financial woes" became known. The resulting publication of the "carrier's precarious condition" allegedly resulted in financial institutions withdrawing from transactions with the airline.

The same commenter pointed out that SEC and DOT do not provide current information and retain such information only for a limited time.

With respect to legality, an attorney suggests that a document with schedules deleted is not a "conveyance" because in defining a contract, Black's Law Dictionary says: the writing " " " contains the agreement of the parties with the terms and conditions" " ".

He argues that:

A written instrument that contains less than the total of the terms cannot, by definition, be "the" conveyance.

He further points out that the filing system under the Uniform Commercial Code as adopted in the various states, is totally dissimilar from the filing system under section 503 of the Federal Aviation Act.

He also says that the leading court cases which discuss the purposes of the Federal aircraft recording system do not factually involve the issue of whether proprietary information may be omitted.

The case for permitting documents to be recorded with deletions is set out in letters from Pegasus Capital Corporation; Crowe and Dunlevy; American Airlines; USAir; AINA Holdings, Inc.; British Aerospace, Inc.; Milbank, Tweed, Hadley and McCloy; United Airlines; Paul, Hastings, Janofsky, and Walker; Federal Express; Air Transport Association; and McAfee and Taft.

In regard to policy issues, practically all persons supporting FAA's recording documents with omissions or redactions have mentioned the significant harm which would befall airlines if confidential financial information were required to be released. They assert that the harm comes not only as a result of the advantage to other airlines in knowing proprietary information about the competition, but also in the weakened negotiating position of airlines if lenders are aware of financial concessions in previous agreements. Moreover, it is urged that foreign airlines and nonaviation businesses would have a distinct advantage in competing for capital.

Several airlines point out that there is a significant amount of information concerning airline fitness already available to the public. In any event, they say that the Registry was never intended as a database for financial information which even airlines' stockholders can't obtain.

Several commenters suggest that full disclosure does not benefit the public at la but only parochial interests.

With respect to legal issues, practically pro-omission commenters point out that there is no statutory or regulatory basis to require disclosure of confidential financia information. By reference to legislative history, case law, and "plain meaning" of section 503 of the Federal Aviation Act, th point out that the Registry was established a clearing house solely to allow interested persons to check on interests in aircraft.

An attorney in Oklahoma City argues th FAA's position with respect to permitting omissions has not really changed since 19 He alleges that neither FAA nor its predecessor, Civil Aeronautics Authority, ever required a promissory note with underlying financial information be filed with a chattel mortgage. He also alleges th the Registry has historically accepted security agreements which contain blanks representing financial terms.

Several commenters analogize the FAA recording system to that established in each of the states based on the Uniform Commercial Code's model. One airline suggests that the FAA recording system would pass legal muster even if it were on a "notice system." A law firm says a "bare-bones conveyance" is recordable with "superfluous information in an unrecorded document."

Four commenters have pointed out that since 5 U.S.C. 552(b)(4) exempts release of commercial or financial information under the Freedom of Information Act, the Regist should not disclose such information. An airline says that under section 1104 of the Federal Aviation Act of 1958 (49 App. U.S. 1505), disclosure of information obtained b FAA is not permitted if such disclosure would "adversely affect the competitive position of any carrier in foreign air transportation."

Two law firms say that FAA should not b in the business of determining the validity instruments since that is reserved to the states under section 506 of the Act.

An Oklahoma City attorney says that Congress' intent in creating the FAA recording system can be gleaned from sectio 503(g) of the Act (49 App. U.S.C. 1503(g)) which authorizes FAA to issue regulations providing for endorsements upon certificate of registrations "as may be necessary to facilitate the determination of the rights of parties dealing with civil aircraft " " "."

The same attorney suggests that a recordable "conveyance" is simply whateve the Registry will accept under § 49.33(a) of the Federal Aviation Regulations (14 CFR 49.33(a)).

In answer to Locke Parnell's assertion tha permitting documents to be recorded with omissions requires rulemaking action by FAA, a commenter says that the "policy" or "rule" which permits omissions is exempte from rulemaking by the Administrative Procedure Act, 5 U.S.C. 553(b)(A) because it is an interpretative rule.

All comments have been reviewed. We now begin discussion by considering the statutory language.

In pertinent part, section 503(a)(1) of the Act (49 App. U.S.C. 1503(a)(1)) provides

The Secretary of Transportation shall establish and maintain a system for the recording of * * * any conveyance which affects the title to, or any interest in, any civil aircraft of the United States.

Under section 101(20) of the Act (49 App. U.S.C. 1301(20)), a "conveyance" means:

A bill of sale, contract of conditional sale, mortgage, assignment of mortgage, or other instrument affecting title to, or interest in, property.

(The Registry has historically treated aircraft leases as instruments affecting an interest in property.)

There is nothing in the language of section 503 of the Act, or by way of legislative history to the Act of 1958 and predecessor Civil Aeronautics Act of 1938, to suggest that section 503 of the Act mandates disclosure of confidential financial information. The purpose of section 503 of the Act is "* * * to create a central clearing house for recordation of title so that a person, wherever he may be, will know where he can find ready access to the claims against, or liens, or other legal interests in an aircraft." *Aircraft Trading And Services* v. *Braniff, Inc.* 819 F.2d 1227 at 1231 (2nd Cir. 1987), quoting language in *Philko Aviation, Inc.* v. *Shacket*, 462 U.S. 406 at 411 (1983), which language comes from house hearings leading to passage of the Civil Aeronautics Act of 1938.

To our knowledge, there is no case law that indicates that section 503 of the Act either requires disclosure of financial information or that a legislative purpose of section 503 of the Act was to provide information concerning financial fitness or safety of airlines.

In the FAA Assistant Chief Counsel's letter of September 27, 1993, he posed the question whether a document with schedules omitted is a "conveyance." That question is relevant because under section 503 of the Act, FAA records only "conveyances" as defined in section 101(20) of the Act.

Only a few commenters responded to the question. As previously noted, one attorney argued that a document which is anything less than the complete agreement of the parties is not a conveyance.

However, other commenters say that such a document may be a conveyance:

1. * * * so long as the provisions relating to the conveyance of title or interest are not redacted * * *.

2. Because a conveyance is similar to an enforceable sale of goods under UCC 2–201 which requires only a writing sufficient to show a contract of sale.

3. Because a "bare-bones conveyance" is sufficient.

4. Because such a conveyance is considered "acceptable by the Administrator."

We believe that such a document with certain, limited omissions or redactions is a conveyance. It would be difficult to explain why a 30-page, original lease signed by the parties is not a conveyance simply because a schedule showing stipulated loss values has been intentionally omitted. The fact that the parties to such a lease may also have reached agreement as to stipulated loss value (which they are unwilling to disclose) does not, in our judgment, make the lease submitted for recordation any less a conveyance.

The regulations which implement section 503 of the Act are set out in part 49 of the Federal Aviation Regulations (14 CFR part 49); § 49.1 is a restatement of section 503 of the Act. Section 49.31 is a restatement of the definition of "conveyance" in section 101(20) of the Act and includes release, cancellation, and discharges as authorized in section 503(b) of the Act.

Section 49.33 states the eligibility requirements of recording conveyances. As pertinent to this discussion, §49.33(a) provides that a conveyance must be "in a form prescribed by, or acceptable to, the Administrator for that kind of conveyance."

Determinations of what are "* * *acceptable to the Administrator." can be found in the Registry's Examination Guidelines, and in opinions of the Assistant Chief Counsel for the Aeronautical Center. There are no FAA guidelines which presently speak to the issue of recordability with omissions and redactions.

During the last 5 years law firms have routinely sought favorable opinions concerning the redaction of schedules containing confidential financial information. The Assistant Chief Counsel frequently finds such redactions acceptable.

Therefore, it appears, as one of the commenters has suggested, that certain redacted conveyances when submitted for recordation are in a form which has been found and continues to be found acceptable.

Section 49.33(c) provides that a conveyance must be an original or duplicate original document. As discussed earlier, there is no indication that a Congressional purpose would be defeated by allowing the withholding of certain financial information. Nor for that matter, does § 49.33(c) require that an original document or duplicate original document contain such information when no Congressional purpose would be served. Therefore, we regard an allowably redacted conveyance with ink signatures to meet the requirement for an "original or duplicate original document."

Based on the foregoing discussion, we believe that the recording of documents with limited redactions or omissions is not contrary to statute, regulation, or other directive.

We next turn to Locke Parnell's claim that rulemaking action is necessary in order to continue the practice of recording documents with omissions or redactions. Such action would include general notice of proposed rulemaking and the public's opportunity to participate in accordance with the Administrative Procedure Act, 5 U.S.C. 553 (b) and (c).

The Air Transport Association (ATA) has commented that: FAA has informally construed the Part 49 regulations to allow conveyance transactions to be recorded without certain sensitive information * * *.

ATA suggests that what FAA is doing is in the nature of interpreting section 503(a) of the Act and that "interpretative rules" are exempt under 5 U.S.C. 553(b)(A) from formal rulemaking requirements. ("General statements of policy" are also exempt under 5 U.S.C. 553(b)(A).)

Federal courts have applied various tests, singly or in combination, to attempt to distinguish between interpretative and legislative rules (e.g., "substantial impact;" "deference to agency label;" "legal effect;" "binding norm"). See Administrative Conference of the United States, A Guide To Federal Agency Rulemaking, 55–68 (2d ed. 1991), pages 55 through 68. More recently, in determining whether rules are either legislative or interpretative, courts have focused on the legal effect of the rules. See *e.g., American Min. Congress* v. *MSHA*, 995 F.2d 1106 (D.C. Cir. 1993). "A statute or legislative rule that actually establishes a duty or right is likely to be relatively specific (and the agency's refinement will be interpretative), whereas an agency's authority to create rights and duties will typically be relatively broad (and the agency's actual establishment of rights and duties will become an amendment merely because it supplies crisper and more detailed lines than the authority being interpreted). If that were so, no rule could pass as an interpretation of a legislative rule unless it were confined to parroting the rule or replacing the original vagueness with another." *Id.* at 1112. Consequently, the FAA's delineation of section 503(a) as permitting the continued recordation of conveyances with omissions or redactions of financial data is interpretative and not legislative in nature.

Finally, we note that a commenter suggests that the FAA should adopt a UCC-like approach and only require that a filed document indicate that a party has conveyed title to or has an interest in a civil aircraft. By this opinion, we intend only to affirm the continuation of permitting schedules containing confidential, proprietary information to be redacted or omitted from otherwise recordable documents. With respect to particular documents, the advice of the Assistant Chief Counsel for the Aeronautical Center should be sought.

Sincerely,

John H. Cassady,

Deputy Chief Counsel.

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