

Tentative Position Paper

USE OF VOTING TRUSTS

for purpose of

ESTABLISHING CITIZENSHIP STATUS UNDER § 101(16) OF THE FEDERAL AVIATION ACT

to facilitate

CORPORATE REGISTRATION OF CIVIL AIRCRAFT OF THE UNITED STATES

INTRODUCTION

This Paper provides a statement of those evaluation factors being now considered by the FAA Aircraft Registry in its review of any voting trust tendered to support corporate citizenship as a prerequisite to U.S. aircraft registration. It contains the current view of the FAA on this complex technique. Such views are subject to further refinement, due to the presentation in the future of unique trust provisions and to new variations in the relationships of parties to a voting trust.

The concept of using a voting trust to achieve corporate U.S. citizenship is relatively new in the aviation industry and is undergoing constant changes. Changes in aircraft ownership, use, financing, and international liaison necessitate a continuing reconsideration of alien interests in and use of U.S. registered aircraft. The FAA Aircraft Registry must therefore continuously reevaluate (on a case by case basis) the use of voting trusts as a means to achieve corporate U.S. citizenship. Of underlying concern to the FAA are the true independence of the U.S. citizen-trustee and the good faith of the trust transaction. Therefore, this Tentative Position Paper must be read as being in transience, subject to periodic change and development.

It represents only the current evaluation criteria and is necessarily subject to revision, as new public and federal concepts emerge.

I. BACKGROUND

Flight in an unregistered aircraft is unlawful. An aircraft is eligible for U.S. registration under § 501(b) of the Federal Aviation Act of 1958, as amended (49 U.S.C. 1401(b)) (hereinafter: the "Act"), if--

"(1)(A) it is --

(i) owned by a citizen of the United States or by an individual citizen of a foreign country who has lawfully been admitted for permanent residence in the United States; or

(ii) owned by a corporation (other than a corporation which is a citizen of the United States) lawfully organized and doing business under the laws of the United States or any State thereof so long as such aircraft is based and primarily used in the United States; and

(B) it is not registered under the laws of any foreign country; or

(2) it is an aircraft of the Federal Government, or of a State, territory, or possession of the United States or the District of Columbia or a political subdivision thereof.

For purposes of this subsection, the Secretary of Transportation shall, by regulation, define the term 'based and primarily used in the United States'."

Section 47.9 of the Federal Aviation Regulations (14 C.F.R. 47.9) defines the term "based and primarily used in the United States." Essentially, it means that 60 percent of total flight hours of the aircraft must be accumulated within the United States during each 6-calendar month period. Registration of aircraft by this category of applicant is not within the scope of this Paper.

A recurring situation is one involving a corporate applicant (for a Certificate of Aircraft Registration) that does not wish to have to restrict the operation of the aircraft as required by Section 47.9 and meets all the requirements of § 101(16) of the Act, except that 75 percent of its voting interest is not owned or controlled by other citizens of the United States. To remedy this obstacle to registration eligibility, proposals are sometimes being made to place "control" of foreign-owned stock in a voting trust, utilizing trustees who are citizens of the United States.

The statutory criteria of control of 75 percent of the "voting interest" is elusive. It is not defined in Title V or VI of the Act. The term does appear in Title IV ("Air Carrier Economic Regulation") where, for those purposes only, Section 413 indicates that "it is immaterial whether such control is direct or indirect." Nor has the Civil Aeronautics Board, which administers Title IV, defined "control" in its regulations, although the term is used (see, e.g., 14 C.F.R. § 287.1(e)). In Ronson Corporation CAB Dockets 25583 and 25603, an Administrative Law Judge of the Board in 1974 held that a voting trust was not effective for purposes of the citizenship requirement for air carriers in the absence of an overriding public interest factor. Nevertheless, the FAA for several years has approved the use of some voting trusts to achieve corporate citizenship for aircraft registration purposes.

II. FACTUAL SITUATIONS

Situations suggesting the use of voting trusts fall into two categories:

I. The stock of an existing U.S. corporation is acquired by a foreign corporation.

II. A domestic corporation, owned by a foreign corporation, is created specifically for the purpose of owning one or more aircraft holding U.S. registration, but does not wish to register the aircraft under the provisions of § 501(b)(1)(A)(ii) of the Act.

This Position Paper makes the following factual assumptions:

(1) That most or all of the stock of the domestic corporation is owned by an alien (usually a corporation);

(2) That the applicant corporation is duly organized under the authority of a State, territory, or possession of the United States, and is regular in all respects as to its organization;

(3) That the president and two-thirds of the board of directors and other managing officers of the applicant corporation are U.S. citizens;

(4) That the quantum of the voting interest to be placed under control of voting trustees is such that--when added to the quantum of voting interests owned or otherwise clearly controlled by U.S. citizens--the aggregate quantum totals at least 75 percent of the voting interest;

(5) That the voting trustees are themselves citizens of the United States within the definition of § 101(16); and,

(6) That no problem exists with whether or not the applicant is to operate as an air taxi or other entity for which operating authority is to come from the FAA.

III. THE REGULATORY STANDARD OF "GOOD FAITH"

FAR § 47.43(a)(4) [49 C.F.R. Part 47] in effect requires that the applicant for an aircraft registration certificate holds title in good faith, and is not a "Man-of-Straw" holding title simply to avoid compliance with the citizenship requirements of the Act. If an applicant for aircraft registration withholds from the FAA information which makes him ineligible to obtain a registration certificate, and the FAA Aircraft Registry issues the requested certificate in ignorance of the undisclosed fact, the certificate may be declared invalid ab initio. The risk to an applicant in failure to make an open-hands disclosure of all citizenship facts thus involves the following hazards:

(a) Aircraft operation may become subject to an FAA civil penalty for each flight without a valid registration certificate;

(b) The applicant may be liable to criminal action for a false representation that he is a citizen within the scope of § 101(16) of the Act;

(c) Insurance policies on the aircraft may be voided for failure to operate within the FARs.

In Situation I (the alien acquisition of the stock of an existing domestic corporation owning an aircraft) there may be no ^{DAD FAITH} malafide transaction under FAR § 47.43(a)(4), but the total acquisition of the corporate voting stock by the new, alien parent may have terminated the domestic corporation's prior qualification as a citizen under the statutory definition. Such aircraft should be reregistered in some cases.

However, in Situation II (where a domestic corporation is specially created for the sole purposes of holding title to the aircraft and of obtaining a Certificate of Aircraft Registration) it may be necessary also to question the transaction as to its good faith.

In both situations, if voting trusts are used as a corrective measure, a common problem exists: whether the voting interest of the stock of the corporate applicant has been so placed in the hands of U.S. citizens as voting trustees that the trustees have a valid, independent, and bona fide control of the voting interest. Section 47.8 of the Federal Aviation Regulations (14 C.F.R. Part 47) sets forth the requirements for a voting trust.

IV. MINIMUM GUIDELINES FOR PREPARING A VOTING TRUST

There are many nuances in determining what constitutes "good faith". Each case must be judged on its own merits. The following guidelines should assist the counsel who undertake to prepare a voting trust instrument which will meet both (1) the statutory standard and (2) the regulatory "good faith" requirement.

A. VOTING INTEREST

The voting trust must identify the "voting interest", as that phrase appears in § 101(16) of the Act. Customarily, the common stock, which has the traditional voting privileges, is placed in trust. However, the appropriate amount of any type of corporate stock having a voting privilege must be placed in trust.

B. TRUSTEE(S)

The usual practice is to use individual trustees whose status and function is clearly independent of both corporations. The trustee may not be a director, attorney, banker, officer, or employee of the domestic corporation, or of its alien/parent corporation. Alternatively, a corporate trustee is sometimes used, but caution must be exercised. Use of the bank, major supplier, or other business associate of either the applicant or of its alien stockholder raises serious doubts as to the economic independence of the corporate trustee. Since the selection of the trustee(s) is pivotal, the use of a representation, in the form of an affidavit, (see attachment A) as an assurance of trustee independence is required by Section 47.8(a)(2) of the Federal Aviation Regulations.

C. BUSINESS PURPOSE

The applicant corporation should be organized for a profit-making purpose and not set up for the sole purpose of holding title to aircraft for registration purposes. It may be organized for the purpose of leasing or otherwise dealing in aircraft, but must have an ordinary business purpose.

D. INSTRUMENT

The voting trust must bind the U.S. trustees, the applicant corporation, and the alien stockholders, as well as all other parties (if any) to the transaction. It may not be executed by employees whose authority to bind their respective corporation is dubious.

E. VOTING CONTROL

Powers given to the trustee(s) must be bona fide, not pro forma.

Broadly stated, the trustees must be given wide authority to exercise their duties with independence, totally free from economic or other subtle or indirect forms of dominance by either the applicant corporation or the alien stockholder. Nor should the trustee(s) serve mainly as a mere conduit, whose principal function is to pass on the dividends to the holders of the beneficial interests.

F. CLASSES OF STOCK

The trustee(s) must have control of the appropriate quantum of all voting interests, not just of the common stock or of only one class of stock if more than one class of stock has voting rights. The voting interest control may not change in the event of future stock splits, reissuance, or new issues or classes of stock, or exercise of subscription rights.

G. TERM

The duration of the voting trust should be for a long term, preferably to the extent permitted by State law. Voting trusts limited to only 2 or 3 years raise doubts as to the bona fides of the arrangement. It must be remembered that when the term of the voting trust ends, this terminates the corporate registrant's status as a citizen and the registration certificate then also terminates. Operation of the aircraft with an invalid registration certificate is unlawful.

If the term of the voting trust may be shortened by unilateral act of the parent corporation, exercise of this power should be conditional on notice to the FAA Aircraft Registry.

H. SUCCESSION

The trust must provide for succession of a voting trustee in the event of death, disability, resignation, termination of citizenship, or any other event leading to the replacement of voting trustee. The replacement voting trustee shall immediately submit to the FAA Aircraft Registry the affidavit referred to in IVB. and required by Section 47.8(a)(2) of the Federal Aviation Regulations (14 C.F.R. Part 47).

V. PERMISSIBLE PROVISIONS

A. The voting trust may allow the appointment and replacement of trustees with or without cause. Replacement must be eo instanti.

B. The trust may be revocable. If the trust be revoked, the FAA Aircraft Registry must be notified immediately, since without a functioning trust, ownership and control of the stock of the corporate owner would not be a U.S. citizen, therefore the U.S. registration would be invalid, and operation of the aircraft may be illegal.

C. Any number of individual trustees are permissible, but each trustee must be a U.S. citizen.

D. The trustee may be individual or corporate. The corporate trustee must qualify in its own right as a citizen within the FAA Act. If a corporate trustee is selected, the life of the trust may not exceed the life of the corporate trustee.

E. Trustee(s) may be relieved of all liability in connection with the exercise of their voting rights. However, such a provision will be considered with other elements of the voting trust in considering whether the trustee's control is acceptably real, or--on the contrary--merely nominal.


F. Each trustee may be proscribed from selling his interest, if any, giving proxies, or otherwise disposing of it without the consent or direction of the beneficial owners.

G. The trust may impose duties to issue voting stock certificates, certificate scrip, or other instruments for insuring dividend distribution. The inclusion or omission of such duties is not germane to the statutory requirements.

H. Trustee resignation is permissible. However, the trust must provide for succession of a voting trustee.

I. The trust instrument must require submission of the required affidavit to the FAA upon the substitution or succession of trustees.

J. Voting Trustees may not act through a proxy.

 K. Provisions relating to operation and management of the applicant corporation are usually omitted, as not germane to the powers of the trustees, the scope of the voting interest, or status of the applicant as a citizen.

VI. HAZARDOUS CLAUSES

Various clauses have been found in voting trusts previously reviewed which tend to limit the independence of the voting trustees. Taken alone, a single such clause may not be so malafide in itself such as to cause disapproval of the proposed trust. When several appear in the trust agreement they may tend collectively to show that the trustee does not have true, actual and unfettered "control of the voting interest" with sufficient independence to satisfy the implied requirements of the Act, and to avoid the prohibition of Section 47.43(a)(4) of the Federal Aviation Regulations.

Accordingly, an application for an aircraft registration certificate, supported by a voting trust (needed to qualify for citizenship), will normally be disapproved if it contains two or more of the following clauses, no matter how actually worded:

A. A prohibition that the trustee may not incur expenses in connection with the exercise of his voting interest.

B. A requirement that the trustee give notice to either corporation or the holders of the beneficial interest before exercising his voting interest.

C. A requirement that the trustee seek the advice of the holder(s) of the beneficial interests before exercising the voting interest.

D. A requirement that the trustee follow the instructions of the holder(s) of voting certificates.

E. Any prohibition which blocks the trustee from obtaining sufficient corporate fiscal or operational data upon which to formulate a voting decision.

F. A limitation on the trustee to seek independent counsel, or any enticement on the trustee to use counsel contemporaneously serving the applicant corporation or the alien stockholder.

G. Unfettered power of the trustee to appoint a proxy to exercise the trustee's powers.

VII. USE OF PROXIES IN LIEU OF TRUSTS

A question is sometimes raised under § 101(16) of the Federal Aviation Act as to whether or not the giving of standard proxies (if permitted by State corporate law and by corporate charter) is a permissible technique

for achieving the voting control necessary to create citizenship for U.S. aircraft registration purposes. The question is answered in the negative.

In voting trust agreements, the independent voting interest customarily reposes in the trustee on a long term basis, in exchange for voting trust certificates issued to the holders of the beneficial interests. This leaves a clear and continuing control of voting interest in U.S. trustees.

However, in the typical proxy arrangement, a different situation prevails:

1. Proxies are customarily, if not by legal restrictions, limited to a specific voting episode, rather than an indefinite period.

2. Proxies are revocable, even if declared irrevocable or coupled with an interest (cf. 19 Am. Jur. 2nd Corporations, § 669 et seq.).

3. The validity of corporate proxies varies considerably according to the various State laws.

4. The arrangement for giving of proxies is not amenable to an assurance that the proxy receiver is a citizen of the United States, or to an assurance that the proxy is not under the dominance of the applicant corporation or of the alien stockholder.

5. After a proxy is exercised, the control of the voting interest reverts back to the alien stockholders.

6. The quantification of the proxies actually used is usually unclear until after the proxies are utilized and their validity ends.

For these reasons, the FAA Aircraft Registry is unwilling to issue a Certificate of Aircraft Registration where the applicant corporation seeks

to qualify as a citizen registrant based merely on the issuance of proxies by an alien stockholder.

VIII. SUGGESTED PROCEDURES

A. A true copy of the executed voting trust must accompany the Aircraft Registration Application (ARA) when submitted for approval by the FAA Registry.

B. Applicants who submit voting trusts to qualify as registrants should understand that the FAA reserves the right to make an investigative inquiry at any time into all aspects of the corporate and trust activities in order to determine the bona fides of its operations. Upon a finding that the terms of the trust are being violated, or not being adhered to in good faith, the FAA may decline to issue a registration certificate or--if issued--may declare the certificate invalid upon the grounds of citizenship ineligibility.

C. The FAA Aircraft Registry provides a retention system for such voting trusts.

D. Because of the complexity of the voting trust technique, requests for expedited approval cannot be honored. Review of an application, when supported by a voting trust, usually involves detailed administrative and legal consultation within the FAA.

E. Applications for Aircraft Registration supported by a voting trust should be sent to:

FAA Aircraft Registry
P.O. Box 25504
Oklahoma City, Oklahoma 73125

Aeronautical Center Counsel
Mike Monroney Aeronautical Center
P.O. Box 25082
Oklahoma City, Oklahoma 73125
(405)686-2296

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Original issuance: August 13, 1976

Updated issuance: July 1, 1980

Enclosure
Attachment A

of my totally independent judgment as a voting trustee under said
Voting Trust Agreement.

Dated this _____ day of _____, 19__.

Subscribed and sworn to before me this ____ day of _____,
19__.

Notary Public