TRANSACTIONS GONE BAD:
LITIGATION BETWEEN BUYERS AND SELLERS OF AIRCRAFT

By:

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by Mark Pierce, Austin, Texas

When a multi-million-dollar jet aircraft does not meet its buyer's expectations, the unhappy owner is likely to want legal advice. A commercial litigator consulted by such a buyer (or lessee) has an array of considerations to discuss with the client. The initial inquiry, and the focus of this article, will include the following assessment: (1) the types of parties involved in such litigation; (2) potential causes of action; and (3) available remedies.

This article does not adopt a "plaintiff' or "defense" perspective because the original defendant may find itself prosecuting a counterclaim, a third-party action, or both. The plaintiff's lawyer (who may regret having a standard contingency fee agreement in the case) sometimes gets to play defense too. The practice of law in this demanding field requires the flexibility to adapt seamlessly to the role of plaintiff or defense.

A. PARTIES

For business and tax reasons, few aircraft (particularly turbine-powered aircraft) are owned by individuals. Regardless of who is involved in the negotiation of the transaction, ultimately the registered owner, fractional-share owner, or lessee is likely to be a corporation or limited liability company (LLC).

This tends to diminish the plaintiff's usual advantage before juries in consumer-type cases. Jurors who might readily identify and empathize with the individual buyer of a "lemon" car will have higher expectations about the sophistication and bargaining position of high-end aircraft operators. Further, as discussed below, some states limit the application of their consumer protection statutes to individual persons, and some courts refuse to apply federal law governing warranty protection to cases involving airplanes altogether—regardless of who the buyer may be.

Both plaintiff and defendant will also want to sort through the possible targets for additional or third-party claims, which can include brokers, sales agents, consultants, manufacturers, distributers, parts suppliers, lenders, mechanics, prior owners, and pre-purchase inspectors. Thus, what at first may seem to be a straightforward case of buyer-against-seller can become a legal quagmire involving multiple parties and claims. As in other areas of aviation law, business litigation involving aircraft transactions is rarely simple and straightforward.

B. CAUSES OF ACTION

When an aircraft transaction goes bad, it can give rise to a number of potential causes of action. Some of those most often asserted are set out below.

1. UDAP Statutes

Each of the 50 states has at least one statute commonly referred to as UDAP—the acronym for "unfair or deceptive acts or practices," which is a phrase lifted from Section 5(a)(1) of the Federal Trade

Commission Act, 15 U.S.C. §45(a)(1), (FTCA)—and some states even have two. The FTCA does not itself provide for private enforcement, but the statutes it spawned provide significant state and private remedies for a wide range of prohibited practices involving misrepresentation, concealment of material information, and other questionable business practices.

Some conduct is specifically enumerated as unlawful, while other actions (in most states) are more generally described as unfair, unconscionable, or deceptive acts and practices. Iowa's UDAP, which does not expressly provide a private remedy, is the lone exception. The Iowa Supreme Court has denied the existence of an implied private right of action, except to the extent that the alleged conduct is a criminal offense. *Hall v. Montgomery Ward & Co.*, 252 N.W.2d 421 (Iowa 1977). UDAP statutes typically provide an easier cause of action to prove than common law fraud (often by eliminating requirements of fraudulent intent or knowledge), as well as a vehicle for recovery of a prevailing plaintiff's attorney's fees and an opportunity in most states for some form of enhanced damages.

Despite the existence of a Uniform Deceptive Trade Practices Act, many states have not adopted it or have significantly amended their UDAP statutes over time. Each state's UDAP will be different from the others to some degree. Therefore, a practitioner involved in a UDAP case must study the applicable statute of the state whose substantive law governs the lawsuit.

Some states may require exhaustion of administrative remedies as a prerequisite to filing a UDAP lawsuit. Other states require a pre-suit notice letter to a potential defendant with an opportunity to tender a settlement offer; failure to make such an offer can cause a lawsuit to be abated or dismissed or result in the offending party being denied attorneys' fees and costs.

Some courts have found their states' UDAP statutes inapplicable in transactions between individuals, thereby excluding from the scope of the statute any transaction that involves a non-merchant seller. Because the "buyer" or "consumer" in a large aircraft transaction is likely to be a corporate entity, an LLC, or some other legal construct rather than a natural person, some states exclude such parties from the protection of the UDAP statute—particularly in those states where application of the statute is limited to products intended for "personal, family, or household use."

Texas, in fact, has gone one step further. Even though a corporate entity, an LLC, or a partnership can be a "consumer" under the Deceptive Trade Practices—Consumer Protection Act, the Texas statute specifically excludes from protection those buyers with more than $25 million of assets or transactions that involve total consideration over $500,000. TEX. BUS. & COMM. CODE §§17.45 (4), 17.49 (2015).

2. Federal Warranty Law

The Magnuson-Moss Warranty Act, 15 U.S.C. §§ 2301-2312, is a federal statute which regulates the content of written

consumer warranties and creates a federal right of action for breaches of express and implied warranties. The Act provides for attorney's fees and actual damages for breaches of written warranties, express warranties, which can be made orally, and "service contracts," which are often commonly referred to as "extended warranties." It does not make any distinction between new and used goods.

There is confusion about whether aircraft are included within the scope of Magnuson-Moss. Because the Act only applies to transactions that involve a "consumer product," which is defined as "any tangible personal property which is distributed in commerce and which is normally used for personal, family or household purposes," courts have struggled with the question of whether an airplane may be considered a consumer product.

The Federal Trade Commission (FTC) has influenced the courts' interpretation of the term "consumer product" in the aviation realm by initially listing "small aircraft" (without defining the term) as an example of a consumer product covered by Magnuson-Moss in 1975. However, the FTC dropped "small aircraft" from the list one year later—after the General Aviation Manufacturers Association (GAMA) wrote a letter asking the FTC to reconsider its initial decision. *See* 40 C.F.R. 25,722 (1997); 41 C.F.R. 26,757 (1976).

The 1976 revision of the rule referred to GAMA's request for reconsideration, then recited that "(t)he data available to the Commission indicates that no appreciable portion of new aircraft are sold to consumers, for personal, family, or household use." The rule change did not make any specific reference to the data in GAMA's request for reconsideration. It also does not appear that the FTC consulted or relied on any source of information other than GAMA's letter when it changed its mind.

The FTC's change of heart proved persuasive to a Georgia appeals court, which, in *Patron Aviation, Inc. v. Teledyne Industries Inc.*, 267 S.E. 2d 274, 278 (Ga. App. 1980), addressed the question of whether the sale of an aircraft engine was within the scope of Magnuson-Moss and concluded (with more than a little hyperbole) that "(i)t would stretch the greatest of imaginations to hold that an aircraft engine is normally used 'for personal, family, or household purposes.'

A decade later, a federal district court in Kansas cited *Patron* as support for its conclusion that "the protections afforded by the Magnuson-Moss Act are not designed to encompass the purchase of a $3,000,000 jet"—despite the fact that Magnuson-Moss does not put a price limit in its definition of "consumer products," *CAT Aircraft Leasing, Inc. v. The Cessna Aircraft Co.*, 1990 WL 171010 (D. Kan. October 3, 1990). The court in *CAT Aircraft* mistakenly asserted that the Georgia court in *Patron* had "considered the issue of whether a jet aircraft engine was covered by the Act." In fact, the *Patron* case involved the issue of whether Teledyne Continental was obligated to provide a major overhaul, or merely a top overhaul, for a defective piston engine.

Following the same line of reasoning as *Patron*, a district court in Illinois rejected a buyer's argument in *Cinquegrani v. Sandel Avionics, Inc.*, 2001 WL 649488 (N.D. Ill. Jue 8, 2001) that Magnuson-Moss should apply because a new Mooney M20M had been purchased by a corporation for the sole stockholder's personal use. According to the *Cinquegrani* court, in considering whether Magnuson-Moss applies to the sale of aircraft, one has to look broadly at general customer use; only if "personal, family, or household purposes" are "not uncommon" would Magnuson-Moss apply. Without making any attempt to distinguish among types or uses of aircraft, the court simply held that a buyer of a "small aircraft" did not fall within the protection of Magnuson-Moss. *Id.*

In a related opinion involving the parties in *Cinquegrani*, the Seventh Circuit found fault with the conclusion that "an airplane cannot be a consumer product" because "airplanes" is "too large a category for analysis." In *Waypoint Aviation Services Inc. v. Sandel Avionics, Inc.,* 469 F.3d 1071, 1072 (7th Cir. 2006), the court reasoned that "(j)ust as personal cars are consumer products even though 60-passenger busses (sic) are not, single-engine airplanes used for personal transport or recreation may be consumer products even though Antonov 225s and skycrane helicopters are not."

The court of appeals also noted that times change, and without citing any data asserted (probably incorrectly) that "more consumers fly personal airplanes now than they did 30 years ago." It did not, however, provide any guidance as to how a plaintiff might prove that a particular airplane's use for personal, family, or household purposes is common enough to bring the plaintiff's claim within the scope of Magnuson-Moss.

In *Balser v. Cessna Aircraft Co*., 512 F. Supp. 1217 (N.D. Georgia 1981), the U. S. District Court changed the analysis by deciding that the determining factor is the actual use of the product by the purchaser; thus, if the airplane were to be "normally" used by that buyer for personal, family, or household purposes, Magnuson-Moss would apply. In doing so, the court found the FTC's dropping of "small aircraft" from its enforcement list to be unpersuasive as to the court's independent duty to interpret the statute.

The airplane at issue in *Balser* was a Cessna 340 purchased by a trustee for use by the trust's sole beneficiary, who was also a named plaintiff. Under the *Balser* analysis, application of the statute would depend on the buyer's subjective intention on how the airplane was to be used. *Balser* stands alone as authority for this approach, and it has been criticized as being "based on an erroneous application of the test" to determine personal use. *Cinquegrani*, 2001 WL 649488. It should be noted that the *Cinquegrani* court was criticized for its handling and analysis of the case in *Waypoint*, 469 F.3d at 1073.

Because interests in most U.S.-based aircraft—large and small—are owned by corporations or LLCs for tax and business reasons, it may be difficult for a plaintiff to persuade a court that Magnuson-Moss warranty protection extends to a company-owned aircraft. However, the *Waypoint* and *Balser* opinions leave open the possibility that an owner of even a large turbine aircraft

can find a way to obtain Magnuson-Moss protection. It is certainly not inconceivable in the era of light jets, Light Sport Aircraft, and VIP-configured Boeing 727s, that an aircraft of any size could be commonly used for the "personal purposes" contemplated by Magnuson-Moss.

3. The Uniform Commercial Code

Like Magnuson-Moss, the Uniform Commercial Code (UCC) applies to the sale of both new and used goods. In cases involving leases rather than outright purchases, UCC Article 2A governs the relationship between lessor and lessee (except in Louisiana).

A case originating out of a "deal gone bad" will almost always be affected by the UCC. The application of the UCC among those states enacting it and the courts enforcing it, however, is far from "uniform." This is demonstrated, for example, by opinions issuing out of Alabama and Texas courts that raise doubts as to whether the implied warranty of merchantability applies to used goods, even though the other 48 states—not to mention the plain language of the UCC itself and the drafters' comments adopted upon enactment—clearly assert that it does. See e.g. *Bagley v. Creekside Motors, Inc.*, 913 SO.2d 441 (Ala. 2005); *Southerland v. Northeast Datsun, Inc*., 659 S.W.2d 889 (Tex. App.—EI Paso 1983, no writ).

In light of the possibility that Magnuson-Moss will not apply to transactions involving aircraft, it is important to understand the UCC provisions that are likely to affect an aircraft transaction.

a. Express Warranties

Under the UCC, express warranties are created in virtually all transactions. UCC 2-313 establishes the existence of express warranties on the basis of "an affirmation of fact or promise," by a description of the goods, or by display of a sample or a model.

Express warranties can be created even if the seller did not intend to create a warranty and even if they are not in writing. If any such warranty is part of the "basis of the bargain" (note that this phrase does not include reliance) and if it is breached, the buyer will have a claim for relief.

b. Implied Warranty of Merchantability

UCC Section 2-314 provides that "unless excluded or modified, a warranty that the goods shall be merchantable is implied in a contract for their sale if the seller is a merchant with respect to goods of that kind." The term "merchantable" is not explicitly defined in the UCC, but, under Section 2-314(2), goods must meet certain minimum criteria.

With regard to aircraft (new or used), the provision most likely to apply is that the aircraft be "fit for the ordinary purposes for which such goods are used." In essence, this means that the aircraft must be able to do its job (fly) with reasonable safety, efficiency, and comfort. As noted above, in Alabama and Texas, the implied warranty of merchantability may only exist with regard to new aircraft.

c. Implied Warranty of Fitness for a Particular Purpose

Section 2-315 of the UCC provides for the existence of this warranty if the seller has reason to know that the buyer has a "particular purpose" for the goods in mind, the buyer actually relies on the seller's skill or judgment in selecting the goods, and the seller has reason to know of the buyer's reliance.

d. Exclusion or Disclaimer of Warranties

The implied warranty of merchantability and the implied warranty of fitness for a particular purpose can be disclaimed—essentially waived by the buyer—if done precisely in accordance with the UCC's protocols. To waive the implied warranties, the UCC require specific language and conspicuous presentation. It is not uncommon in aircraft transactions for a seller to insist on language to the effect that the buyer is taking the aircraft "as is" and "with all faults."

Other critical language may be required, such as the specific reference to "merchantability" if the implied warranty of merchantability is to be effectively disclaimed. A seller may also gain some protection from insisting on a pre-sale inspection, a common practice for those accustomed to buying and selling aircraft.

It should be noted, however, that even an "as is" clause and a pre-purchase inspection may not shield a seller from all liability. As the Texas Supreme Court said in *Prudential Ins. Co. v. Jefferson Associates, Ltd,* 896 S.W.2d 156, 162 (Tex. 1995):

> A buyer is not bound by an agreement to purchase something "as is" that he is induced to make because of a fraudulent representation or concealment of information by the seller. A seller cannot have it both ways: he cannot assure the buyer of the condition of a thing to obtain the buyer's agreement to purchase "as is," and then disavow the assurance which procured the "as is" agreement. Also, a buyer is not bound by an "as is" agreement if he is entitled to inspect the condition of what is being sold but is impaired by the seller's conduct. A seller cannot obstruct an inspection for defects in his property and still insist that the buyer take it "as is." In circumstances such as these an "as is" agreement does not bar recovery against the seller.

4. Racketeer Influenced and Corrupt Organizations Act (RICO)

The federal Racketeer Influenced and Corrupt Organizations Act, 18 U.S.C. §§1961-1968 (RICO), and similar state statutes, originally created to fight organized crime, contain broad language providing for civil liability for certain abusive or dishonest acts and practices by an "enterprise" that may not necessarily be associated with "organized crime." By its own terms, the federal statute is to be "liberally construed to effectuate its remedial purposes," although many federal courts have attempted to limit its scope. Under appropriate circumstances, a RICO

claim, which provides for treble damages as well as attorneys' fees and costs, should be fully explored.

5. Common Law Claims

In addition to the statutory causes described above, all available common law causes of action need to be considered. Fraud, negligent misrepresentation, breach of

contract, civil conspiracy, money had and received, unjust enrichment, deceit, constructive trust, and rescission remain viable avenues to pursue under the right facts.

C. REMEDIES IN BUSINESS LITIGATION

Unlike bodily injury and death cases, business litigation often involves more than just a one-sided claim for money. For example, a disgruntled buyer may elect to pursue a claim for rescission or a revocation of acceptance under the UCC because the buyer not only does not want to continue to pay for a defective or nonconforming aircraft, but he may want to return it to the seller. Sometimes a buyer will not wait for a ruling from a court to "rescind" and a seller may find an unwanted airplane on its ramp.

It is not unusual to see claims for equitable relief: restraining orders and injunctions are sometimes necessary to preserve the status quo while claims are being litigated. For lawyers who are accustomed to the pace of tort litigation in the courts, it can come as a shock to find that a restraining order, written discovery, depositions, and a preliminary injunction hearing —often the functional equivalent of a trial on the merits—can all occur within the first 30 to 45 days of the filing of a lawsuit.

In breach of contract and UCC warranty claims, plaintiffs may seek benefit-of- the-bargain damages, loss of use and enjoyment of the aircraft, as well as cost of repair and some other incidental or consequential damages. Parties may also find themselves arguing about liquidated damages or contractual limitations on damages.

In cases arising under Magnuson-Moss, RICO, or state UDAP statutes, claims for attorneys' fees can be expected, and in some cases statutory enhanced or exemplary damages may be in issue.

This discussion touches on only some of the issues confronting the client on either the buying or selling side of a transaction in which one or more parties are unhappy. Concerns about a variety of other issues—such as arbitration clauses, insurance coverage, bankruptcy and solvency concerns, and choice of law—will require both plaintiff and defense attorneys to bring

the full arsenal of legal resources to the litigation.

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