

LEGAL EVALUATION OF PARTS TRANSACTIONS GONE AWRY

2019 ASA Annual Conference

Workshop L

CASE STUDY NUMBER ONE

Steven Suspect is the holder of a commercial pilot certificate and an aircraft mechanic certificate. In 2006, the FAA issued an emergency order revoking both of Mr. Suspect's certificates. The Order stated that the FAA had determined Mr. Suspect had tampered with maintenance records for helicopter rotor blades. The FAA's investigation revealed that Mr. Suspect had whited out inspection entries designating the blades as unrepairable scrap and replaced it with information claiming the blades had thousands of hours of green time remaining.

Mr. Suspect sold the blades to a buyer, who installed them on his helicopter. When the buyer was unable to balance the blades for takeoff, he had another inspection performed. That inspection revealed the fraudulent documentation.

While Mr. Suspect was appealing the Order, the FAA and Mr. Suspect settled and the FAA issued an amended order revoking Mr. Suspect's mechanics certificate—and not his pilot certificate—for one year.

Five years later, Mr. Suspect was convicted of criminal fraud under 18 U.S.C. § 38 for the sale of the blades. Based on that conviction the FAA issued a new order in 2013 permanently revoking both of Mr. Suspect's certificates: mechanic and pilot.

Mr. Suspect appealed the permanent revocation of his certificates claiming that the FAA was precluded from revoking his certificates because the issue had already been adjudicated based on the 2006 settlement.

CASE STUDY NUMBER TWO

In 2005, Euro Aviation contacted Coolguys, a company that supplies aircraft parts, to inquire about purchasing a vapor cycle air conditioning ("VCAC") system. Euro expressed its intention to purchase a VCAC system for which Coolguys holds an STC.

Install Co. is a company that develops aerospace technology and provides manufacturing and maintenance services for aircraft. In 2007, Euro asked Install Co. to install a VCAC system in one of its aircraft. Euro wanted Install Co. to purchase a standard VCAC system from Coolguys, and have Coolguys customize the VCAC unit to certain specifications. Install Co. contacted Coolguys in 2007 on behalf of Euro to purchase the modified system. Thereafter, Coolguys communicated with Install Co., rather than Euro, about providing the VCAC system.

Later that year Coolguys sent a technical representative to Install Co. to inspect the aircraft upon which the VCAC system was to be installed. Coolguys advised against the modified system requested by Install Co. on behalf of Euro because it would likely not provide the desired cooling for the designated areas of the aircraft. For this reason, Coolguys requested a waiver acknowledging the fact of this possible shortcoming.

Before the modified VCAC system could be installed on the aircraft, it needed to be approved by the FAA because the customized VCAC system was not covered by Coolguys's STC for the standard system. Coolguys notified Install Co. of this fact, and warned that the FAA approval process would be time consuming, especially given the specific modifications requested by Install Co. However, because Install Co. wished to proceed, Coolguys informed Install Co. that it would obtain FAA approval for the modified system.

On February 6, 2008, Coolguys finalized the order for the modified VCAC system, when it received a waiver from Install Co. acknowledging that the customized VCAC system would not provide the desired cooling. Coolguys made initial contact with the FAA on February 21, 2008, to begin the approval process. Coolguys continued to respond to requests for information from the FAA after that point.

According to Install Co., on February 7, 2008, it sent Coolguys the total payment for the VCAC system, amounting to a total of \$112,805, which included payment for the travel to its location. Coolguys disputed this date, and stated that it received that sum by April 3, 2008. It also disputed that it has received full payment under the contract because of estimated expenses incurred in procuring EASA certification for the modified system.

On December 2, 2010, Install Co. sent a letter to Coolguys canceling their contract because Coolguys had failed to deliver the VCAC system. Despite this cancellation, Install Co. responded to Coolguys's request for information needed by the FAA to continue the approval process on December 8, 2010. Coolguys asserts that it did not receive the cancellation letter until April 2011. Coolguys never delivered a modified VCAC unit to Install Co.

CASE STUDY NUMBER THREE

Dr. J decided to start an air-taxi business and was looking to purchase several small aircraft. Dr. J contacted Alabaster Aircraft expressing interest in its four-seat, two-engine plane. Dr. J visited Alabaster's facility and received an extensive presentation about the plane, during which he learned that the engines relied on a new technology and were manufactured by a different company, Emerald Engines. Because the engines were new technology, they would require frequent inspections and maintenance. Alabaster explained that the engines would be covered by Emerald's warranty, "parts and labor prorated over 2400 hours or 12 years" with replacement in full at prorated cost if replacement was necessary before 2400 flight hours.

While Dr. J was negotiating to purchase five aircraft from Alabaster's authorized dealer (while Alabaster personnel stayed heavily involved in discussions), another aircraft became available. Dr. J purchased the aircraft for \$600,000. Two weeks later, Emerald declared bankruptcy and voided its engine warranties. Left without engine warranties, Dr. J sought to trade his aircraft to Alabaster for a new plane equipped with Alabaster's recently developed engines. Alabaster refused and Dr. J sued.

Dr. J claimed that Alabaster had made representations regarding the length and reliability of the engine warranty, had endorsed Emerald as a reliable company, had prepared a break-even analysis stating the engines would not require overhaul until 2400 hours, and that he had relied on Alabaster's representations about Emerald in deciding to purchase the plane.

Dr. J further claimed that Alabaster's sales personnel stated that they had negotiated extensive warranties with Emerald because of the new technology and that Alabaster's personnel had ensured him that the warranty would protect the engine and that he could rely on it.

Finally, Dr. J identified during discovery an email indicating Alabaster knew of Emerald's pending insolvency, which read, "Wow, good news on the Emerald stock--he'll be bankrupt soon! Oh wait, we aren't finished with our engine what will we do now? Quick get the our engine certified. . . . or maybe we will take over Emerald, but then we have to carry his warranty obligations. What do we do now? Oh well! Main thing is that Emerald is dying. Might kill us too, but we WIN!"

CASE STUDY NUMBER FOUR

Weekly Wings is a commercial air carrier that operates several aircraft types. Awesome Aero furnishes parts for those aircraft pursuant to a long-term agreement, which provides for net-30 day payment on all invoices.

During the relationship, Weekly's payment of invoices was inconsistent. Weekly routinely paid invoices to Awesome outside the net-30 day terms of the Agreement and often paid multiple invoices with one check.

In January 2014, Weekly began having financial difficulties. In March 2014, Weekly notified Awesome by phone that it would no longer be purchasing parts. Later that month Weekly sent a letter to Awesome and other suppliers notifying them of its plan to rework its supply and maintenance agreements in an effort to increase profitability. The letter also stated that Weekly intended to pay suppliers up front for new parts and to pay off old accounts within 60 days of receiving new financing. Weekly indicated it expected new financing to come through later in 2014.

In late March 2014, Awesome sent a letter to Weekly addressing Weekly's "continuing failure to maintain its accounts receivable" and Weekly's plans to revise its supplier agreements. Awesome stated that in order to supply Weekly in the future it would require the payment by Weekly of all outstanding invoices and accounts receivable. Weekly made ten payments to Awesome totaling \$1.4 million in satisfaction of over 200 outstanding invoices.

In November 2014 Weekly filed a petition for Chapter 11 Bankruptcy. In the 90 days preceding its bankruptcy filing, Weekly made nine payments to Awesome totaling \$782,000. During that same 90 days, Awesome provided \$165,000 in additional parts to Weekly.

The bankruptcy trustee sent letters to each company that had received payment from Weekly in the preceding 90 days requesting a return of those payments totaling \$782,000.

The bankruptcy trustee has threatened to file a complaint against Awesome seeking to avoid the nine payments (and ultimately require Awesome to return the money to the Weekly bankruptcy estate) if the payments are not returned to the bankruptcy estate, now.

CASE STUDY NUMBER FIVE

ABC is in the business of manufacturing, distributing, marketing, and selling aircraft parts, including pneumatic products, propeller products, pneumatic de-icers and components, and other aircraft parts. GHI is a distributor of aircraft parts.

ABC received approval from the FAA to manufacture de-icing products for different types of aircraft. Until ABC received this approval, Ice-Co was the only manufacturer of de-icing products in the general aviation market. Distributor GHI was interested in entering the de-ice market and had attempted to become a distributor for Ice-Co. Failing to have done so, ABC and GHI began negotiations to allow GHI to become a worldwide distributor of the ABC de-ice product line. These negotiations led to a Distributor Agreement between ABC and GHI.

Under the Distributor Agreement, ABC appointed GHI as the distributor for its ice shield pneumatic de-icers and components, and ice shield propeller de-icers and components. The parties negotiated and agreed to the following performance figures.

A. Distributor GHI will be required to maintain inventory and sell products during the term of the agreement as follows:

Effective Date	Min. Inventory Level at Distribution Cost	Annual Sales Attainment
Year 1	125,000.00	n/a
Year 2	250,000.00	1,000,000.00
Year 3	500,000.00	4,000,000.00

According to the Distributor Agreement, ABC and GHI agreed that all invoices would be paid within thirty days and any invoices not timely paid would be subject to a late payment of one and one half percent per month. Additionally, GHI agreed to collaborate with ABC to develop an annual market plan and forecast for products under the Distributor Agreement.

Pursuant to the Distributor Agreement, ABC provided GHI with aircraft parts from for the first two years of the Agreement. GHI paid for the products that it received until November 1 of year two, but failed to pay for the products it received from November of year two until February of year three. ABC contends that the balance owing, excluding interest and attorney's fees is \$ 77,295.00. In April of year three, ABC informed GHI that GHI was in material breach of the Distributor Agreement, and ABC made a demand for payment.

According to ABC, in the Fall of year two, GHI allegedly reduced its efforts to promote actively and sell ABC products. By February of year three, GHI had entered into an agreement with Ice-Co to distribute Ice-Co's de-ice product line.

ABC brought breach of contract claims against GHI and GHI counterclaimed. GHI alleged that before executing the Distributor Agreement, GHI and ABC made mutual mistakes concerning the scope and depth of the market for replacement de-icing and propeller products and their ability to capture a market share in the short period of time provided for in the agreement. GHI also alleges that ABC failed (1) to collaborate with GHI in developing an annual marketing plan and forecast for the territory and markets covered by the Distributor Agreement; (2) to provide GHI with sales literature, product specific literature, training material and other information; (3) to provide GHI with technical support and training to deal with customers; (4) to schedule dates for delivery of the products; (5) to provide a certificate of insurance for product and general liability insurance; (6) to achieve FAA certification for the number, type, and kind of de-icing products to be used on specific aircraft (thereby limiting the number of aircraft for which GHI could sell de-icing replacement products); and (7) to refrain from direct competition with the GHI sales force. As a result, in May of year three, GHI terminated the Distributor Agreement. GHI seeks \$ 500,000.00 in damages against ABC for lost sales and profits, lost marketing costs, lost inventory carrying costs, consequential "and/or" incidental damages.