



# News from the Hill

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## Lien Laws You Need to Know

Last month, we touched on some basic strategies for ensuring your right to get paid for the work you perform. This month, we will examine lien laws as a general tool that can be used to help accomplish that goal.

Lien laws vary from state to state. Although this article examines certain state laws as examples, it is not meant to take the place of a thorough understanding of the state and federal laws that apply to your transaction. Please do not hesitate to seek the advice of your local lawyer on these subjects, and you should also feel comfortable reading the laws yourself, so you know all of the ins-and-outs that your lawyer might forget to mention!

### Prologue

I was speaking with Al Michaels, recently. Many in the aviation industry know Al as the FAA's parts and helicopter guru, but it is less commonly known that before Al was an FAA Maintenance National Resource Specialist, he owned two different repair stations—first one in Pittsburgh and then one in Indianapolis.

I enjoyed learning more about the way the repair business evolved though the '70s and '80s (Al got into the repair biz after serving as a helicopter pilot in Vietnam). Then the topic turned to business relationships with customers. I asked Al how he made sure his clients paid him when he was in business.

"Ohhhh," he began, "Back in the

'70s and '80s, business just wasn't as vicious. You did business on a handshake. No one ever signed the work orders—you just dropped the ship off and everyone expected that the work would be done and that they would pay for it."

Al works frequently with repair stations on airworthiness issues and he hears all of the dirt. With a shrug, he sums the modern industry up by ex-

ally, the lien entitles the lien holder to sell the property in question (often at a judicial auction) in order to raise all or part of the money owed by the borrower. Such sales are only used when the borrower fails to pay the lender according to the terms and conditions of the transaction.

Repair stations find themselves acting in the role of creditor frequently. In fact, every time a customer picks

*Using liens, a repair station can protect its right to get paid (in case the alleged check never arrives).*

plaining "Today is just different."

We all know that the industry is a different place, today. Some customers are slow to pay; some demand extensive credit terms; others look for every loophole to avoid payment. Bankruptcies have become so common that Congress recently enacted legislation designed to discourage unnecessary bankruptcies (see last month's *Avionics News* article for details). We can't all become regulators, so repair stations today (and their personnel) need a higher level of assurance of payment from their customers.

### What Is a Lien?

A lien is a legal right established against a piece of property. Liens are often established where one party, the lender, lends money or extends credit to another party, the borrower. Usu-

ally, the lien entitles the lien holder to sell the property in question (often at a judicial auction) in order to raise all or part of the money owed by the borrower. Such sales are only used when the borrower fails to pay the lender according to the terms and conditions of the transaction.

All types of property can have liens placed against them. When you buy real estate, the bank from which you get your mortgage will usually establish a lien against the property to serve as security against your payment of the mortgage. Liens can be established against personal property; for example, when an aircraft is used as security for a bank loan, the bank establishes a lien against the aircraft that can be used to secure the bank's interest in getting repaid (and it is filed in Oklahoma City ... more on this topic later in the article).

As a general rule, liens that are use-

ful to AEA members can be divided into “liens by law”—liens that can be established pursuant to a law that provides guidance on when the lien can be used, how it is established, and how it is enforced—and “liens by agreement”—which encompasses liens that are established based on an agreement among the parties, and that may be subsequently ‘perfected’ and enforced according to the terms established under state law.

### **Liens By Agreement**

The most basic form of lien is the lien by agreement. As the name connotes, this sort of lien is generally the product of an agreement between the debtor and the creditor, in which the debtor pledges an asset as collateral against the possibility that the debtor may fail to repay the loan or other credit extended by the creditor.

Generally speaking, a lien by agreement is reflected in two documents, although it is possible to merge the two documents into a single document that encompasses both sets of data.

The first document is the security agreement. A security agreement is a contract that pledges the item (asset) as collateral to secure a debt owed to the creditor. Although the security agreement establishes the right to a lien between the parties, it does not establish that right with respect to third persons. In order to do that, the lien must be ‘perfected’—usually by filing the lien (but occasionally through other means)—a topic covered in more depth later in this article.

The second document is the financing statement. The financing statement includes:

- Names and addresses of lien holder and debtor
- Description of secured item (consistent with Security Agreement)
- Date of service provided

- Dollar amount of lien claim
- Signature of the debtor (for best results, get this before you start the work, or at least get it before the customer takes back his aircraft or appliance)

There is a standard for financing statements, called a “UCC-1.” This form is standard for many types of transactions, and its use is mandated as the filing document of choice in some states; but the UCC-1 is not mandatory in all states, and the common law of financing statement simply requires them to include the required element of information. Despite the fact that the UCC-1 is a standard form in aviation, it is often NOT used in aviation transactions, for reasons discussed below in the FILING section of the article.

### **Liens By Law**

In many states, there are laws that give repair stations and mechanics the right to establish liens against aircraft or components on which they have worked. These sort of laws vary widely from state to state, so you need to check your state’s laws carefully before you try to assert one of these liens.

The most common liens by law that may be asserted by repair stations are repairman’s liens. In many states, any person who has performed work on an item of personal property (such as an aircraft or avionics component) and in doing so adds value to the property, may assert a lien against the item of personal property. This should not be confused with a mechanic’s lien, which in most states refers to a comparable lien levied against real property (e.g. a mechanic’s lien may be levied against a home by a carpenter who has done carpentry work on the home). Often, a repairmen’s lien needs to be filed in an appropriate office (more on this in the next section) in order to be effective.

Other laws found in some states in-

clude aircraft-specific liens. In some cases, a state might have one set of laws that apply to liens against aircraft and another set of laws that would apply to aircraft components. Where more than one set of lien laws could potentially apply to a transaction, the repair station may use any of the parallel laws as the basis for establishing the lien, so long as the formalities associated with that particular law are followed. Some laws require that a filing be made, either to make the lien effective against the owner, or (more commonly), to make the lien against subsequent owners of the property (so that it becomes a negative factor on the title of the property in question). Other laws might make such a filing unnecessary—often, where there is no requirement of filing, the person asserting the lien may need to hold onto the asset. The reason that the filing becomes unnecessary is because no one can take possession from the owner while it is in the lienor’s possession, so there is no need to make a public filing.

Some state laws require seizure of the asset (aircraft) in question, and those states that permit this differ on whether the repair station that has relinquished control over an aircraft can reassert a lien if they regain actual possession or control of the aircraft.

One of the difficulties in a lien by law is determining the value of the lien. Past precedent has been that the lien is good for the agreed-upon sum as discussed by the parties. Because there may be no written agreement between the repair station and the customer as to the fee, it may be difficult to ascertain the actual value of the lien. Where there is clear agreement (or where there was clearly no agreement as to the price), the lien by law is permitted to be filed for the fair market value of the work performed.

*Continued on page 45*

## NEWS FROM THE HILL

Continued from page 27

### Filing Your Liens

Why do you need to file your liens? In order for a lien to be effective against any party, it must comply with the Constitutional doctrine of due process. One of the elements of due process is notice—no one can have a legal action taken against them without some notice of the action; however notice does not need to be ‘actual,’ there is a doctrine of constructive notice that suggests that we are all responsible for knowing anything that has been properly established by the government. Thus, we are all subject to constructive notice of all of the laws in our jurisdiction even if we have never bothered to read them (you may have heard that “ignorance of the law is no excuse”). A properly established lien by agreement may be effective against the present aircraft owner (who signed the security agreement), but it may not be effective against the next owner when the aircraft is sold (thus the lien becomes extinguished upon sale). This is the reason that filing the lien is important. Filing a lien with the appropriate authority provides the world with ‘constructive notice’ of the existence of the lien, and the lien may therefore be enforced against anyone, even if ownership of the asset is transferred.

The appropriate authority in most cases is a state or county office in which liens are typically filed (exact office varies from state to state). The rule of thumb for filing is that you file where the asset is located. So if you are filing a lien against an inventory of aircraft parts, you would file in the county or state where the warehouse full of parts was located (depending on the exact requirements of the law of that state).

Aviation is the exception to the rule when it comes to filing a lien. One reason that aviation reflects an exception

is because aircraft are easily moved from one state to another, so without a 50-state review of all lien registry offices, it might be impossible to determine whether any liens were asserted against the aircraft (an important issue when one is considering purchasing an aircraft). For this reason, Congress established a registry office within the FAA. For certain aviation liens, the filing must be made with the FAA Registry Office in Oklahoma City. The FAA accepts the filings for 1) U.S.-registered aircraft, 2) aircraft engines of 750 or more rated takeoff horsepower, and 3) propellers able to absorb 750 or more

states, like California, absolutely require that you file a UCC-1 (other forms will be rejected). Aviation represents the major exemption to the financing statement rule of thumb. For transactions filed with the FAA, though, the security agreement must be filed. This is the reason that it is not uncommon to see the financing statement and security agreement residing in a single document in the aviation industry. This is also the reason that UCC-1s are used less frequently in aircraft transactions ... because the security agreement, and not the UCC-1, is what is filed at the FAA.

***For AEA members who want to use liens as a means of ensuring their right to get paid for their work, it is possible to make a lien agreement a standard part of your work order.***

rated takeoff shaft horsepower. The FAA will also accept filings for aircraft engines, propellers, appliances or spare parts maintained by or for a certificated air carrier and expected to be installed/used by that air carrier.

There are federal cases that make it clear that a filing with the FAA, for those items accepted for filing by the FAA, supercedes any state-level filing. Many states (Virginia is one) have laws on the books that reinforce this doctrine.

Thus a repair station with a lien against an aircraft would file it with the FAA. A repair station doing work on a TCAS Processor for a general aviation client would file a UCC-1 in the state in which the TCAS Processor is located at the time of filing (usually the state where the owner can be found). But a repair station that performs work on a TCAS Processor for an air carrier may be able to file its lien with the FAA Registry Office.

What do you file? In most cases, you file the financing statement. Some

Filing a lien is also called ‘perfecting the lien.’ A lien must be perfected to be enforceable. There are other ways to perfect liens, but they are outside the scope of this article.

For AEA members who want to use liens as a means of ensuring their right to get paid for their work, it is possible to make a lien agreement a standard part of your work order. This is useful for shops that make the customer sign the work order before beginning work. Many states also have very favorable laws permitting the repair station to retain possession of an aircraft until payment is rendered (an unhappy customer under these circumstances may be willing to sign a security agreement and financing statement guaranteeing payment in order to regain actual possession of the aircraft, so don’t overlook this as a possible tactic when dealing with non-paying ‘customers’).

Have a great story about how you used a lien to secure your right to get paid? Send it to me by email: Jason@washingtonaviation.com. □