Bankruptcy Law - Third Circuit Applies Section 1110 of Bankruptcy Code to Sale-Leaseback Transactions

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BANKRUPTCY LAW—THIRD CIRCUIT APPLIES SECTION 1110 OF BANKRUPTCY CODE TO SALE-LEASEBACK TRANSACTIONS

In re Continental Airlines (1991)

I. INTRODUCTION

Under the automatic stay provision of the Bankruptcy Code (the Code), creditors are prohibited from repossessing or collecting assets from bankrupt debtors. The increasing number of airlines facing bankruptcy, however, prompted Congress to enact section 1110 of the Bankruptcy Code. Section 1110 protects financiers of aircraft while also allowing airlines to increase their capital at a lower interest rate.

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   (a) Except as provided in subsection (b) of this section, a petition filed under section 301, 302, or 303 of this title . . . operates as a stay, applicable to all entities, of—
      (1) the commencement or continuation, including the issuance or employment of process, of a judicial, administrative, or other action or proceeding against the debtor that was or could have been commenced before the commencement of the case under this title, or to recover a claim against the debtor that arose before the commencement of the case under this title;
      (2) the enforcement, against the debtor or against property of the estate, of a judgment obtained before the commencement of the case under this title;
      (3) any act to obtain possession of property of the estate or of property from the estate or to exercise control over property of the estate;
      (4) any act to create, perfect, or enforce any lien against property of the estate;
      (5) any act to create, perfect, or enforce against property of the debtor any lien to the extent that such lien secures a claim that arose before the commencement of the case under this title;
      (6) any act to collect, assess, or recover a claim against the debtor that arose before the commencement of the case under this title;
      (7) the setoff of any debt owing to the debtor that arose before the commencement of the case under this title against any claim against the debtor; and
      (8) the commencement or continuation of a proceeding before the United States Tax Court concerning the debtor.

Id. This automatic stay provision generally operates to preclude the creditor from removing any property in the bankrupt debtor's possession, including property that has been leased. Id.; In re Continental Airlines, 932 F.2d 282, 283 (3d Cir. 1991).

2. Continental, 932 F.2d at 290-91. The legislative history of § 1110 states that the purpose of this section is to "encourage new financing in the transportation industry and to promote modernization of the industry by protecting equipment financiers." Glenn S. Gerstell & Kathryn Hoff-Patrinos, Aviation Financing Problems Under Section 1110 of the Bankruptcy Code, 61 AM. BANKR. L.J. 1, 7 (1987) (footnote omitted).

(880)
cifically, section 1110, which is based on sections 77(j) and 116(5) of the previous Code, provides an exemption from the automatic stay for certain aircraft which are in the possession of an airline involved in bankruptcy proceedings. The exemption is limited to "(1) a holder of a

3. Sections 77(j) and 116(5) of the previous Bankruptcy Code were precursors to § 1110 of the current Bankruptcy Code. Continental, 932 F.2d at 290 (citing 11 U.S.C. §§ 205(j), 516(5) (1976) (repealed)). Section 77(j), enacted in 1935, gave special protection to financiers of certain railroad equipment which allowed investors to recover their property during a railroad’s bankruptcy proceeding. Id. at 289. Section 77(j) provided:

The title of any owner, whether as trustee or otherwise, to rolling stock equipment leased or conditionally sold to the debtor, and any right of such owner to take possession of such property in compliance with the provisions of any such lease or conditional sale contract, shall not be affected by the provisions of this section.

11 U.S.C. § 205(j) (1976) (repealed). Under this provision, railroads financed transportation equipment separately from other assets of the railroad through a form of financing called a “railroad equipment trust.” Continental, 932 F.2d at 289. The railroad equipment was “placed in a trust and leased or conditionally sold to the railroad.” Id. The trustees of the equipment usually had priority over the other creditors of the railroad. Id. This special protection was given to financiers of railroad equipment "because the high cost and long life span of rolling stock, combined with the railroads’ frequently precarious financial situations, made such equipment an extraordinarily risky investment. Such risks were magnified if the secured property could not be recovered promptly in bankruptcy proceedings.” Id. at 289 (citing Gerstell & Hoff-Patrinos, supra note 2, at 5-6).

Section 77(j) was extended to the airline industry in 1957 by the enactment of § 116(5) of the Bankruptcy Act. Id. at 290 (citing 11 U.S.C. § 516(5) (1976) (repealed)). Section 116(5) provided in pertinent part:

[T]he title of any owner, whether as trustee or otherwise, to aircraft . . . leased, subleased, or conditionally sold to any air carrier . . . and any right of such owner or of any other lessor to such air carrier to take possession of such property in compliance with the provisions of any such lease or conditional sale contract shall not be affected by the provisions of this chapter if the terms of such lease or conditional sale so provide.


(a) The right of a secured party with a purchase-money equipment security interest in, or of a lessor or conditional vendor of, whether as trustee or otherwise, aircraft, aircraft engines, propellers, appliances, or spare parts . . . that are subject to a purchase-money equipment security interest granted by, leased to, or conditionally sold to, a debtor
purchase-money equipment security interest (PMESI) in aircraft or a
conditional vendor of aircraft and (2) a lessor of aircraft." Section
1110 therefore allows lessors of aircraft which are leased to an air carrier
to repossess the aircraft if the lessee air carrier files for bankruptcy,
although the air carrier can prevent repossession by curing its defaults
within sixty days.6

—that is an air carrier . . . to take possession of such equipment in compliance
with the provisions of a purchase-money security agreement, lease, or conditional sale contract, as the case may be, is not affected by
section 362 or 363 of this title or by any power of the court to enjoin
such taking of possession, unless—

(1) before 60 days after the date of the order for relief under
this chapter, the trustee, subject to the court’s approval, agrees to
perform all obligations of the debtor that become due on or after
such date under such security agreement, lease, or conditional sale
contract, as the case may be; and

(2) any default, other than a default of a kind specified in
section 365(b)(2) of this title, under such security agreement, lease, or
conditional sale, as the case may be—

(A) that occurred before such date is cured before the ex-
piration of such 60-day period; and

(B) that occurs after such date is cured before the later
of—

(i) 30 days after the date of such default; and

(ii) the expiration of such 60-day period.

Id. Section 1110 provides that the right of lessors to repossess their leased air-
craft is not affected by the automatic stay provision of § 362. Louis B. Goldman,
et al., Repossessing the Spirit of St. Louis: Expanding the Protections of Sections 1110 and
1168 of the Bankruptcy Code, 41 Bus. Law. 29, 42 (1985). Additionally, a court
may not enjoin lessors from repossessing their aircraft unless the airline can
cure its defaults within the 60-day cure period. Id.

5. Gerstell & Hoff-Patrinos, supra note 2, at 2. A “purchase-money equip-
ment security interest” (PMESI) is not defined in the Bankruptcy Code, but it is
similar to a “purchase money security interest” (PMSI), which is defined in Arti-
cle 9 of the Uniform Commercial Code (U.C.C.). Id. at 10-11; see also U.C.C. § 9-
107 (1977). The legislative history of § 1110 suggests that it should be inter-
preted in accordance with state law under the U.C.C. Gerstell & Hoff-Patrinos,
supra note 2, at 10. Section 9-107 of the U.C.C. provides:

A security interest is a “purchase money security interest” to the
extent that it is

(a) taken or retained by the seller of the collateral to secure all or part
of its price; or

(b) taken by a person who by making advances or incurring an obliga-
tion gives value to enable the debtor to acquire rights in or the use of
collateral if such value is in fact so used.


6. Continental, 992 F.2d at 284. This cure period was added to § 1110 “to
soften the effect of the prior law, which was considered ‘harsh in [its] appli-
cation.’” Id. at 290. If the debtor cures its defaults within 60 days, the lessor
cannot repossess the aircraft. Gerstell & Hoff-Patrinos, supra note 2, at 2-3. The
debtor can cure its defaults by agreeing “to perform all its obligations under the
relevant security agreement, lease or conditional sale contract according to its
pre-bankruptcy terms.” Id. at 3.

Additionally, the lessor cannot repossess the aircraft unless it has provided
for a right to repossession in the lease or security agreement for the aircraft. Id.
Airlines finance their aircraft and aircraft equipment in several ways. Airlines finance aircraft that are newly constructed, used aircraft that are new to the airline, and aircraft which are neither newly constructed nor new to the airline. This third category of aircraft includes "lease renewals, sale and leaseback transactions, and the use of aircraft previously owned by an airline free-and-clear as collateral for financing." Aircraft in this category are generally referred to as non-acquisition financing because they do not result in the addition of new aircraft to the airline. Commentators have suggested that section 1110 clearly applies to newly constructed aircraft and used aircraft new to the airline, but have questioned the application of the section to non-acquisition financing of used aircraft previously owned by the airline, such as aircraft subject to a sale-leaseback transaction.

The Third Circuit recently addressed the issue of whether section 1110 applies to sale-leaseback transactions or only to acquisition financing. In In re Continental Airlines, the Third Circuit resolved this uncertainty when it held that section 1110 applies to sale-leaseback transactions.

If such a provision exists, a court may not enjoin the financier from repossessing the aircraft. Id. at 3-4.


8. Id. For a discussion on how Continental financed its fleet, see infra notes 21-22 and accompanying text.

9. Giddens & Schick, supra note 7, at 123.

10. Id. The first two categories of aircraft, newly constructed and used aircraft, are referred to as acquisition financing because they result in the addition of new aircraft to the airline. Continental, 932 F.2d at 284.

11. Giddens & Schick, supra note 7, at 123 (noting that "[i]t is reasonably clear that the first two types of transactions—those involving new aircraft, or aircraft new to the airline—are within section 1110, but it is not so clear with respect to the third type"). Other commentators, however, have come to the opposite conclusion. See, e.g., Gerstell & Hoff-Patrinos, supra note 2, at 25-26 (suggesting that sale-leaseback transactions are covered under § 1110).

12. Continental, 932 F.2d at 282. A sale-leaseback transaction occurs when an air carrier sells aircraft to a financier and then immediately leases it back. Gerstell & Hoff-Patrinos, supra note 2, at 24. These transactions “are widely used in the airline industry as a means of raising working capital.” Continental, 932 F.2d at 284. Sale-leasebacks may also be part of a “package deal” in which the airline buys new aircraft from a manufacturer, then enters into a sale-leaseback transaction with a financier. Id. According to Continental, these “package deals” are acquisition transactions because “they result in the addition of aircraft to the fleet.” Id. As discussed supra note 10, acquisition financing occurs when an airline acquires newly constructed aircraft or used aircraft which is new to the airline.

For a discussion of whether sale-leaseback transactions are covered under § 1110, see Gerstell & Hoff-Patrinos, supra note 2, at 24 (addressing issue of whether sale-leaseback transactions should qualify for § 1110 protection); Giddens & Schick, supra note 7, at 123 (suggesting that it is unclear whether sale-leaseback transactions fall within § 1110).

transactions. The Continental court reached the same result as two
other jurisdictions that previously decided the issue. As a result of this
Third Circuit decision, financiers of aircraft will be able to repossess air-
craft subject to sale-leaseback transactions where the debtor air carrier is
unable to cure its default within the sixty-day statutory period. This
bright line rule will have the effect of making financiers more willing to
engage in these transactions, thereby helping ailing airlines.

II. DISCUSSION

A. Facts and Procedural History

On December 3, 1990, Continental Airlines, Inc. (Continental) filed
for bankruptcy under Chapter 11 of the Bankruptcy Code. The credi-
tors in this case had entered into sale-leaseback transactions with Conti-
nental and wanted to repossess their leased aircraft pursuant to section
1110. On January 16, 1991, Continental filed a motion seeking a dec-
laration that certain aircraft which it leased were not subject to section
1110 of the Bankruptcy Code.

Continental, like many other commercial airlines, leases a majority
of its aircraft. The leases consist of acquisition leases, under which
Continental acquires new aircraft through standard leasing agreements,
and non-acquisition leases, under which Continental sells its own air-
craft to a financier and then immediately leases it back. Continental
argued that section 1110 applies only to acquisition leases and not to
sale-leaseback transactions. The bankruptcy court agreed and granted

14. Id. at 287. For a discussion of the holding of Continental, see infra notes 67-72 and accompanying text.
15. See In re Pan Am Corp., 125 B.R. 372 (S.D.N.Y.), aff’d per curiam, 929 F.2d 109 (2d Cir. 1991); In re Braniff, Inc., 110 B.R. 980 (Bankr. M.D. Fla. 1990). For further discussion of these cases, see infra note 29 and accompanying text.
16. Continental, 932 F.2d at 284.
17. For further discussion of the impact of this decision in the Third Cir-
cuit, see infra notes 71-72 and accompanying text.
18. Continental, 932 F.2d at 283.
19. In re Continental Airlines, 125 B.R. 399, 400 (D. Del.), aff’d, 932 F.2d 282 (3d Cir. 1991). Amicus curiae were filed in support of creditors’ position by five other solvent airlines and the American Association of Equipment Lessors. Id.
20. Continental, 932 F.2d at 283-84. This motion was opposed by financiers of the leased aircraft, who served as appellees in this case. Id. at 284.
21. Id. Two-thirds of Continental’s current fleet of aircraft consists of leased aircraft. Id.
22. Id. Continental has 211 aircraft operating under acquisition leases and
104 aircraft operating under non-acquisition leases. Id. For further discussion of sale-leaseback transactions, see supra note 12 and accompanying text.
23. Continental, 932 F.2d at 285. Continental made a separate argument in
the bankruptcy court that $1110 “was intended to apply only to ‘true’ leases.” Id. Continental argued that under § 1110 certain transactions that are called leases are actually “disguised security interests,” which are not covered under
the exemption of § 1110. Id. Neither the bankruptcy court nor the district
Continental’s motion. The district court, however, reversed the order of the bankruptcy court. The district court concluded that sale-leaseback transactions are included within section 1110, and therefore the creditor is entitled to repossess all aircraft operating under non-acquisition leases. Continental appealed this decision to the United States Court of Appeals for the Third Circuit.

B. Analysis

The Third Circuit addressed the issue of whether the word “lease” in section 1110 of the Bankruptcy Code applies to both acquisition and non-acquisition leases by examining the plain language of the statute and its legislative history. The court noted at the outset that this identical question had been answered by two other federal courts, both of which held that sale-leaseback transactions were covered under section 1110.

The district court, however, reached this issue. Id. The Third Circuit held that § 1110 applies only to “true” leases, but left open the question of whether Continental’s leases are true leases or disguised security interests. Id. For further discussion of this issue, see infra notes 63 & 71 and accompanying text.

24. In re Continental Airlines, 123 B.R. 713 (Bankr. D. Del.), rev’d, 125 B.R. 399 (D. Del.), aff’d, 932 F.2d 282 (3d Cir. 1991). The bankruptcy court held that the term “lessor” in the statute applied only to acquisition leases because the terms “PMESI” and “conditional vendors,” which accompany the term “lessors” in the statute, both refer to acquisition devices. Id. at 713. The court suggested, however, that a sale-leaseback transaction could be part of an acquisition transaction if, for example, Continental arranged to buy aircraft from a manufacturer and in the same transaction sold that same aircraft to a financier, then leased it back. Id. Thus, the bankruptcy court held that Continental’s sale-leasebacks of aircraft were not subject to § 1110 unless those leases were part of a “package deal” in which the airline also acquired new aircraft. Continental, 932 F.2d at 285.

25. Continental, 125 B.R. at 411. The district court, after determining that it had jurisdiction to hear the appeal, discussed the doctrine of noscitur a sociis. Id. at 403-06. The court held that the doctrine did not apply because the term “lessor” in § 1110 was intended to have a meaning separate from its adjoining terms “PMESI” and “conditional vendor.” Id. at 406. For a discussion of how the Third Circuit applied this doctrine, see infra notes 40-44 and accompanying text.

The district court then examined the legislative history of § 1110 and concluded that Congress did not explicitly exclude sale-leaseback transactions. Continental, 125 B.R. at 410. Therefore, the district court reversed the decision of the bankruptcy court and held that sale-leaseback transactions were covered under § 1110. Id. at 411.

26. Continental, 125 B.R. at 411. The district court concluded that “the legislative history here does not demonstrate a Congressional purpose at odds with a literal reading of the statute.” Id. Thus, it was “compelled to find that Congress meant what it said, and h[e]ld that non-acquisition leases are entitled to § 1110 protection.” Id.

27. Continental, 932 F.2d at 283.

28. Id. at 286-87. The Third Circuit recognized that the appeal involved “a straightforward question of statutory interpretation.” Id. at 286.
The Third Circuit ultimately reached the same conclusion.\textsuperscript{30} The \textit{Continental} court first examined whether it had jurisdiction to hear the appeal.\textsuperscript{31} In the Third Circuit, "when the bankruptcy court issues what is indisputably a final order, and the district court issues an

\textsuperscript{29} Id. at 287; see \textit{In re Pan Am Corp.}, 125 B.R. 372, 380 (S.D.N.Y.) (holding that only true leases are protected under § 1110), aff'd per curiam, 929 F.2d 109 (2d Cir. 1991); \textit{In re Braniff, Inc.}, 110 B.R. 980, 985 (Bankr. M.D. Fla. 1990) (concluding that leased aircraft need not be newly acquired to be protected by § 1110).

In \textit{Pan Am}, the sole issue on appeal was whether lessors involved in "non-acquisition sale/leaseback transactions" with the debtor airline qualified as "lessors" within the meaning of § 1110. \textit{Pan Am}, 125 B.R. at 373. \textit{Pan Am} argued that § 1110 applied only to lessors who "lease[d] aircraft and related equipment which are new to the airline." \textit{Id.} The lessors argued that the term "lessor" applied to any true lessor, and maintained that the legislative history did not support the position that § 1110 was only intended to apply to aircraft new to the airline. \textit{Id.} at 374. The \textit{Pan Am} court examined the plain language of § 1110 and the legislative history and concluded that if Congress had intended the section to apply only to acquisition leases, it would have qualified the word "lease" to apply only to newly acquired aircraft. \textit{Id.} at 379. Thus, "[i]f the lease is a true lease, rather than a disguised loan, and meets all other elements of the statute—e.g., qualified equipment, qualified air carrier, repossession clause in lease—the lessor is protected by § 1110." \textit{Id.} at 380. In an appeal by \textit{Pan Am}, the Second Circuit affirmed. \textit{In re Pan Am Corp.}, 929 F.2d 109 (2d Cir. 1991) (per curiam).

In the \textit{Braniff} case, Braniff Airways, Inc. (Airways) set up a subsidiary (Braniff) to operate domestic flights while Airways was involved in a Chapter 11 reorganization. \textit{Braniff}, 110 B.R. at 981. Braniff entered into leases for aircraft with a liquidating trust established by Airways, then subsequently filed for bankruptcy. \textit{Id.} at 982. Braniff sought to prevent the lessors of the aircraft from repossessing the leased aircraft by arguing that the leases did not fall under § 1110 because the aircraft were not new to the airline. \textit{Id.} For the same reasons the Second Circuit used in \textit{Pan Am}, the \textit{Braniff} court held that "[§] 1110 is not limited to leases that permit aircraft to be newly acquired by the lessee." \textit{Id.} at 985. Furthermore, the court concluded that Braniff’s leases were subject to § 1110 even though the aircraft were not new to the airline. \textit{Id.}

\textsuperscript{30} \textit{Continental}, 932 F.2d at 287 ("The ‘identical’ question has been considered in two other cases, where the position now taken by \textit{Continental} has been rejected. We reach the same result." (citations omitted)).

\textsuperscript{31} Id. at 285. Under the United States Code, circuit courts of appeals have jurisdiction over final orders of the district courts. 28 U.S.C. § 158(d) (1988). The Third Circuit first decided that the order of the bankruptcy court, which held that \textit{Continental}’s aircraft could not be repossessed by certain lessors, was a final order. \textit{Continental}, 932 F.2d at 285. In order to determine if the order of the bankruptcy court was final, the Third Circuit looked at "the impact of the issue on the assets of the bankruptcy estate, the necessity for additional fact-finding on remand, the preclusive effect of a decision on the merits, and furtherance of judicial economy." \textit{Id.} Because the order of the bankruptcy court "deprived the lessors of the ability to repossess their aircraft or force rental payments," the Third Circuit held that the order was final. \textit{Id.; see also United States v. Nicolet, Inc.}, 857 F.2d 202, 206 (3d Cir. 1988) (order denying relief from automatic stay is generally appealable). It was unclear, however, whether the order of the district court reversing the decision of the bankruptcy court was appealable because the district court must still determine the issue of whether \textit{Continental}’s leases should be characterized as leases or disguised security interests. \textit{Continental}, 932 F.2d at 285-86. When further fact-finding on remand is necessary, courts are hesitant to find that an order is final. \textit{Id.} at 286.
order affirming or reversing, the district court's order is also a final order." Consequently, the court concluded that it had jurisdiction to hear the appeal.

The remainder of the court's opinion focused on statutory interpretation of section 1110 of the Bankruptcy Code.

1. Plain Language

When interpreting a statute, the Supreme Court of the United States has held that "[t]he plain meaning of legislation should be conclusive, except in the 'rare cases [in which] the literal application of a statute will produce a result demonstrably at odds with the intention of
its drafters.' 35 The Continental court indicated that the plain language of a statute can be overcome only by clear extrinsic evidence presented by the party seeking a contrary meaning. 36

In the present case, Continental attempted to show that the word "lease" in section 1110 was intended to encompass only acquisition leases, as opposed to non-acquisition leases. 37 First, Continental argued that Congress should have qualified the word "lease" in the statute to cover only acquisition leases. 38 The court, however, concluded that the language of the statute can be qualified only if applying the statute to non-acquisition leases would contradict the intent of the drafters. 39

Using the doctrine of noscitur a sociis, Continental next argued that the term "lease" could be "discerned only by reference to the other words that surround it." 40 Because section 1110 refers to "conditional

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35. United States v. Ron Pair Enters., 489 U.S. 235, 242 (1989) (quoting Griffin v. Oceanic Contractors, 458 U.S. 564, 571 (1982)). The Supreme Court held that it is unnecessary to look beyond the plain language of the statute "as long as the statutory scheme is coherent and consistent." Continental, 932 F.2d at 287 (quoting Ron Pair, 489 U.S. at 240-41).

36. Continental, 932 F.2d at 287. The "plain meaning" rule does not preclude the use of extrinsic aids when interpreting a statute. Id. (citing Watt v. Alaska, 451 U.S. 259, 266 (1981) (quoting Boston Sand & Gravel Co. v. United States, 278 U.S. 41, 48 (1928))); see also Train v. Colorado Pub. Interest Research Group, 426 U.S. 1, 10 (1976) (suggesting that extrinsic evidence may be used to determine meaning of statute); United States v. American Trucking Ass'ns, 310 U.S. 534, 543 (1940) (noting that "[w]hen [the plain] meaning has led to absurd or futile results ... this Court has looked beyond the words to the purpose of the act"); Smith v. Fidelity Consumer Discount Co., 898 F.2d 907, 910 (3d Cir. 1990) (holding that court should follow plain meaning rule unless that would be against purpose of statute).

37. Continental, 932 F.2d at 288. Section 1110 "plainly refers to 'lessors' of aircraft that are 'leased' to an airline." Id. at 287. Sale-leaseback transactions used by Continental are recognized as valid leases in other legal contexts. See, e.g., Frank Lyon Co. v. United States, 435 U.S. 561 (1978) (sale-leaseback transactions valid under Internal Revenue Code); In re Fashion Optical, Ltd., 653 F.2d 1385, 1389 (10th Cir. 1981) (bona fide sale-leaseback not fraudulent conveyance under Bankruptcy Code); Gordon v. Motel City "B" Assocs., 403 F.2d 90 (2d Cir. 1968) (sale-leasebacks valid under New York Bulk Sales Law); In re Chateaugay Corp., 102 B.R. 335, 343 (Bankr. S.D.N.Y. 1989) (sale-leasebacks valid under Bankruptcy Code § 365).

38. Continental, 932 F.2d at 288.

39. Id. Accepting Continental's argument would require the court to qualify the plain meaning of the statute. Id. According to the court, it could "only do so if the application of § 1110 to non-acquisition leases would produce a result 'demonstrably at odds with the intention of its drafters.'" Id.

40. Id. The term noscitur a sociis literally means "that a thing may be known by its associates." In re Continental Airlines, 125 B.R. 399, 403 (D. Del.), aff'd, 932 F.2d 232 (3d Cir. 1991). Under this doctrine, the "meaning of an ambiguous statutory term may be derived from the meaning of accompanying terms."
sale contracts" and "PMESIs," which are two types of acquisition devices, Continental argued that the term "lease" was intended to apply only to acquisition leases. The court, however, pointed out that Congress had intended to treat the term "leases" differently from "conditional sale contracts" and "PMESIs" because it separated the terms with the conjunction "or." Furthermore, the court noted that the doctrine's utility decreases when it is used to qualify the plain meaning of a statute. Thus, the court concluded that the doctrine of noscitur a sociis was not applicable to this case because Continental sought to qualify a word in an unambiguous statute, rather than clarify language that "plainly encompasses more than one meaning."

Continental, 932 F.2d at 288. For examples of how this doctrine is applied, see generally Jarecki v. G.D. Searle & Co., 367 U.S. 303, 307 (1961) (applying doctrine where "word is capable of many meanings in order to avoid the giving of unintended breadth to the Acts of Congress"); 2A SUTHERLAND STATUTORY CONSTRUCTION § 47.16 (Norman Singer ed., 5th ed. 1992) (suggesting that doctrine should be used only when "meaning of a statute is not clear").

When the meaning of a statute is unclear, the meaning of ambiguous words may be interpreted by reference to their relationship with other associated words and phrases. 2A SUTHERLAND STATUTORY CONSTRUCTION, supra, § 47.16. "Thus, when two or more words are grouped together, and ordinarily have a similar meaning, but are not equally comprehensive, the general word will be limited and qualified by the special word." Id. Hence, Continental argued that "PMESIs" and "conditional sale contracts," which are acquisition devices, are "special words" that limit and qualify the term "lessor" to apply only to acquisition devices. Continental, 932 F.2d at 288. For a discussion of why the Continental court rejected this argument, see infra note 42 and accompanying text.

41. Continental, 932 F.2d at 288. For a discussion of PMESIs, see supra note 5.

42. Continental, 932 F.2d at 288. "When Congress has separated terms with the conjunction 'or,' it is presumed that Congress intended to give the terms 'their separate, normal meanings.' " Id. (quoting Garcia v. United States, 469 U.S. 70, 73 (1984)). Thus, the Continental court rejected the argument that the term "lease" should apply only to acquisition leases because it is associated in the statute with other acquisition devices. Id.

43. Id. The Supreme Court has held:

That a word may be known by the company it keeps is . . . not an invariable rule, for the word may have a character of its own not to be submerged by its association. Rules of statutory construction are to be invoked as aids to the ascertainment of the meaning or application of words otherwise obscure or doubtful. They have no place . . . except in the domain of ambiguity. Moreover, in cases of ambiguity the rule . . . is not exclusive. The problem may be submitted to all appropriate and reasonable tests, of which noscitur a sociis is one.

Id. (quoting Russell Motor Car Co. v. United States, 261 U.S. 514, 519 (1923)); see also Donovan v. Anheuser-Busch, Inc., 666 F.2d 315, 327 (8th Cir. 1981) (refusing to use doctrine of noscitur a sociis "when there is no ambiguity, to defeat the legislative intent and purpose, to make general words meaningless, or to reach a conclusion inconsistent with other rules of construction").

44. Continental, 932 F.2d at 288. The court explained that a court is never barred from enlisting the aid of this or any other extrinsic tool, but noscitur a sociis is more useful when the statutory language plainly encompasses more than one meaning. Continental seeks to employ this rule to qualify language that Congress has left unqualified,
2. Legislative History

The court next examined the legislative history of section 1110 to determine the meaning of the term "lease" in the statute.\textsuperscript{45} The court reviewed the House Reports, which explained the rationale for providing protection to financiers who lease or conditionally sell aircraft to airlines.\textsuperscript{46} According to the court, the legislative history did not indicate congressional intent to exclude non-acquisition financing from the protection of section 1110.\textsuperscript{47} Rather, the legislative history of section 1110 is "consistent with an intent to facilitate the procurement of low-cost capital in general."\textsuperscript{48} The court concluded that the inclusion of both acquisition and non-acquisition leases under section 1110 would further the statute's purpose of increasing the availability of working capital at a decreased cost.\textsuperscript{49} Moreover, the court agreed with the argument made by several solvent airlines, serving as amici, that the denial of adequate protection to the financiers of sale-leaseback transactions would be det-
Continental then argued that its sale-leasebacks are the functional equivalent of general mortgages, which the House Reports state are not protected under section 1110. The court rejected this argument by noting that sale-leasebacks are different from secured loans, and that a lessor involved in a sale-leaseback transaction bears a greater risk than a party to a secured loan such as a general mortgage. Specifically, the lessor of the aircraft retains economic ownership of the property when the lease expires, while the holder of the security interest does not retain any interest in the property once the security interest lapses. Therefore, the court found that aircraft lessors bear a substantial risk because they rely in part on the residual value of the aircraft for their profits. Accordingly, the court concluded that the legislative history distinguished between leases and security interests, and afforded protection only to leases because "title to the property [leased] remained with the lessor."

Other provisions of the Code recognize sale-leaseback transactions

50. Id. Because sale-leasebacks are widely used in the airline industry, airlines would have difficulty finding financiers for their aircraft if sale-leaseback transactions were not protected under § 1110. Id.

51. Id. Continental argued that its "leases" were not covered under § 1110 because "its sale-leaseback transactions are the functional equivalent of general mortgages on specific pieces of equipment." Id. The court, however, did not believe that Congress, by excluding general mortgages from the reach of § 1110, intended to explicitly deny protection to sale-leaseback transactions. Id. The court specifically stated that "the words 'general mortgage' could refer to a general mortgage attaching to after-acquired assets, rather than a mortgage attaching to a specific piece of equipment." Id. Even if Congress was referring to loans on specific pieces of equipment, the court did not believe this reference demonstrated an intent to exclude sale-leaseback transactions from the reaches of § 1110. Id.

52. Id.

53. Id. The court noted that "[t]he factor of economic ownership reveals the superficiality of any resemblance between the sale-leaseback transaction and a secured loan. Where the resulting lease is a true lease, a genuine change in ownership, evidenced by a transfer of residual risk, has taken place." Id. (quoting Gerstell & Hoff-Patrinos, supra note 2, at 25).

54. Id. The lessor of aircraft bears the risk of a "fluctuation in the residual value of the equipment." Gerstell & Hoff-Patrinos, supra note 2, at 23. If the lease is intended to be a security interest, however, the lessor intends there to be "no significant residual value beyond the end of the lease term." Id. The Uniform Commercial Code has "distinguished a lease from a security interest in holding that the lease is entitled to section 1110 protection." In re Air Vermont, Inc., 44 B.R. 446 (Bankr. D. Vt. 1984) (using U.C.C. to distinguish lease from security interest and giving lease § 1110 protection); see also U.C.C. § 1-201(37) (1977) (defining security interest).

55. Continental, 932 F.2d at 292-93. The court further noted that "title to leased property also implies residual economic ownership and its associated risks, which are still important concerns." Id. at 293. Furthermore, "Congress distinguished between leases and security interests, andrationally could have limited protection of security interests to acquisition devices, while contemplating no such limitation for leases." Id.
and treat them in the same manner as other leases. In fact, the legislative history of section 1110 indicates that the term "lease" should be interpreted consistently throughout the Code. Because Congress presumably knows how to differentiate between types of leases, the Continental court concluded that Congress would have qualified the term "lease" in section 1110 if it had intended the term to apply only to acquisition leases.

The Continental court also recognized that "accepting Continental's position would result in arbitrary distinctions and further uncertainties." For example, if Continental sold aircraft to a financier and immediately leased it back under a sale-leaseback transaction, the lease would not be subject to section 1110. If, however, the same aircraft was leased by a different air carrier, the lease would be subject to section 1110. The court believed that the purpose of the statute—to provide a "quick and predictable remedy that encourages potential financiers to be forthcoming"—would best be achieved by following the plain language of the statute and applying it to all true leases.

Other sections of the Code do not distinguish between sale-leaseback transactions and other types of leases. See, e.g., In re Fashion Optical, Ltd., 653 F.2d 1385, 1388-91 (10th Cir. 1981) (noting that provisions relating to fraudulent conveyances treat sale-leasebacks same as other leases); In re Chateaugay Corp., 102 B.R. 335, 343 (Bankr. S.D. N.Y. 1989) (noting that § 365 does not distinguish between sale-leasebacks and other leases).

The Second Circuit has recognized the possibility of further ambiguity in interpreting § 1110 if the section were to apply only to acquisition devices. See, e.g., In re Pan Am Corp., 125 B.R. 372, 378 (S.D.N.Y.) (suggesting that future litigation is likely if courts limit protection under § 1110 to acquisition leases), aff'd per curiam, 929 F.2d 109 (2d Cir. 1991).

Because the latter transaction has the same effect as a sale-leaseback transaction, the court declared that it would be arbitrary to make a distinction between these two types of transactions. The court maintained that the purpose of the statute does not support treating the sale-leaseback transaction differently from a situation in which aircraft are sold to a financier and then leased back to a different air carrier.

The Third Circuit further held that § 1110 applies only to true leases, as opposed to disguised security interests, noting that under the U.C.C. and other statutes, "the term 'lease' includes only true leases." This interpretation of the term "lease" has been applied to § 1110 and other Code provisions. See, e.g., In re PCH Assocs., 804 F.2d 193 (2d Cir. 1986) (interpreting "lease" under §§ 365(d) and 502(b)(6)); Pan Am, 125 B.R. at 380 (interpreting "lease" under § 1110); In re Chateaugay Corp., 102 B.R. 335, 343-44 (Bankr. S.D.N.Y. 1989) (interpreting "lease" under § 365). The difference between security interests and true leases "has long been accepted in commercial and tax law." Continental, 932 F.2d at 294. The Third Circuit noted that the question of whether Continental's leases would be characterized as leases or security inter-
3. Judge Becker’s Concurrence

In a concurring opinion, Judge Becker was doubtful that the meaning of section 1110 was “plain.” He concurred, however, with the majority opinion because he found Continental’s position underwhelming. In particular, Judge Becker explained that Continental’s arguments were unsuccessful because the legislative history of section 1110 provided evidence “(1) that the sale-leaseback device had long been used for non-acquisition financing; and (2) that Congress had long been concerned with the general cost of capital in various transportation industries and was not just focusing on acquisition financing.”

III. Conclusion

Commentators dispute whether sale-leaseback transactions are subject to the exemption from the automatic stay in bankruptcy under section 1110 of the Bankruptcy Code. The Third Circuit’s decision in Continental, however, is consistent with the two other federal courts that
have decided the issue. Moreover, the Continental court’s interpretation of the term “lease,” based on its plain meaning and legislative history, support the decision. Congress must now decide whether section 1110 needs to be rewritten to qualify the term “lease” so that it only applies to newly acquired aircraft.

The court’s opinion in Continental clarifies the situations in which financiers can repossess their leased aircraft when an air carrier to which they are leasing goes into bankruptcy. Specifically, reposition will be possible when an air carrier enters into a sale-leaseback transaction with a financier, goes into bankruptcy, and then fails to cure its defaults within the statutory cure period. A remaining problem, which may be the source of further litigation, is the question of whether Continental’s leases should be characterized as “true leases” under the Bankruptcy Code. The Third Circuit was unclear about what factors a court must consider in characterizing Continental’s leases.

This decision will have an impact on both airlines and aircraft financiers. First, financiers will be more willing to enter into lease arrangements with smaller and newer air carriers because they will be assured that they will be able to repossess their aircraft if the air carrier should become unable to pay its debts. Second, air carriers will be able to get the financing they need to increase their working capital because financiers will be less hesitant to enter into sale-leaseback transactions with them. A disadvantage of the operation of section 1110 is that it may interfere with the debtor’s business if a majority of its aircraft are repossessed in the event of bankruptcy proceedings. The Continental court

66. See In re Pan Am Corp., 125 B.R. 372, 380 (S.D.N.Y.) (holding that § 1110 applies to sale-leaseback transactions), aff’d per curiam, 929 F.2d 109 (2d Cir. 1991); In re Braniff, Inc., 110 B.R. 980, 985 (Bankr. M.D. Fla. 1990) (same). For further discussion of these cases, see supra note 29 and accompanying text.

67. For further discussion of the legislative history of § 1110, see supra notes 45-61 and accompanying text.

68. For a discussion of § 1110 and the statutory cure period, see supra notes 4 & 6 and accompanying text.

69. As previously stated, only true leases, as opposed to disguised security interests, are covered under § 1110. Continental, 932 F.2d at 285. Simply calling a financing arrangement a lease does not necessarily make it a true legal lease. Whether the arrangement is a lease or a security interest will depend upon the definition of those terms under the applicable state law as well as the specific terms of the lease agreement. Id. at 294. Thus, a court may have to examine Continental’s alternative argument that some of its leases are disguised security interests. For a discussion of Continental’s alternative argument, see supra note 23.

70. Continental, 932 F.2d at 294. For a further discussion of the court’s treatment of the “true” lease issue, see supra note 23 and accompanying text.

71. For further discussion of how this impact is consistent with the legislative history of § 1110, see supra notes 46-50 and accompanying text.

72. The problem with § 1110 arises when an air carrier goes into bankruptcy and is unable to cure its debts within the 60-day statutory cure period. In such a situation, the financier is entitled to repossess the aircraft if the lease arrangement provides for such a remedy. Gerstell & Hoff-Patrinos, supra note 2,
did not address this issue in its opinion. Nevertheless, this decision seems to effectuate Congress' purpose behind section 1110, which is to allow airlines to meet their equipment needs at a decreased cost.

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at 4. This benefit to financiers becomes a detriment to other creditors and to the continuing business of the air carrier. Id.