

UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF INDIANA  
INDIANAPOLIS DIVISION

In re:

ATA HOLDINGS CORP. a/k/a  
ATA AIRLINES, INC.,

Case No. 04-19866-BHL-11  
CHAPTER 11

Debtor.

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**MEMORANDUM OF LAW IN SUPPORT OF GREATER ORLANDO AVIATION  
AUTHORITY'S MOTION TO COMPEL DEBTORS TO SEGREGATE  
AND REMIT PASSENGER FACILITY CHARGES**

The Greater Orlando Aviation Authority ("GOAA"), a public body existing under the laws of the State of Florida, respectfully submits this Memorandum of Law in Support of its Motion to Compel Debtors to Segregate and Remit Passenger Facility Charges ("Memorandum").

**ISSUES PRESENTED**

Whether Passenger Facility Charges ("PFC's") collected from the traveling public, and held in trust by the air carrier for the benefit of public agencies such as GOAA, must be remitted to the public agencies as required by statute and regulations.

Effective December 12, 2003, what are the new statutory requirements, post petition, for airline debtors since the enactment of 49 U.S.C. § 40117(m)?

**INTERVENTION**

ATA Airlines ("Debtors") have, as required by statute and by regulations, collected PFC's. PFC's were established under federal statute, 49 U.S.C. §40117, and are governed by detailed federal regulations, 14 C.F.R. §158. The amount collected by Debtor is held in trust for GOAA, and as such is property in which Debtor has a bare possessory interest and does not have an equitable interest.

## **STATUTORY AND REGULATORY HISTORY OF THE PFC PROGRAM**

During the late 1980's, the nation's airport system required additional funding sources to meet the traveling public's demands for increased capacity, safety, security, noise reduction, and competitiveness in air transportation. In 1990, Congress responded by enacting the Aviation Safety and Capacity Expansion Act (the "Act") to allow public agencies controlling airports to charge enplaning passengers a facility charge. 49 U.S.C. §40117. The Act restricts the collection and use of such charges and specific responsibilities for the public authorities who use the funds for airport-related projects, the air carriers who collect the fees, and the Department of Transportation (the "Department") who administers the overall program. In accordance with the Act, the airports, after consulting with the carriers serving their facilities, apply to the Department for authority to finance PFC funded projects which meet specified statutory criteria. 49 U.S.C. §40117. The Department may approve applications, if, among other things, (1) the proposed passenger facility fee produces revenue that is not more than needed to finance the project; and (2) the project preserves or enhances the capacity, safety, or security of the national air transportation system, reduces airport noise, or enhances competition. 49 U.S.C. §40117(d).

The Department promulgates regulations on the procedures for handling and remitting the money collected, and ensures that the carriers pay the funds promptly, less a reasonable collection fee, to the public agency on whose behalf the funds are collected. 49 U.S.C. §40117(I).

## **THE REGULATORY SYSTEM**

In accordance with Congress' explicit mandate to promulgate such regulations, the Department engaged both the airport and air carrier communities, requested industry data (55 Fed. Reg. 47,483, Nov. 14, 1990), published a Notice of Proposed Rulemaking (56 Fed.Reg.

4678, Feb. 5, 1991), and held a public hearing to define the terms, conditions, and procedures that would apply to the collection and use of PFC revenues.

Following publication of the proposed rule, some expressed concern that, in the event of an airline's bankruptcy, the PFC revenues would "become subject to bankruptcy proceedings" and airports would be "denied access to the funds." 56 Fed. Reg. 24,254, 24,269 (1991). Separate escrow accounts were proposed to avoid this problem. The airlines, on the other hand, were concerned that such an accounting system would be an unnecessary and expensive administrative burden. *Id.*

Significantly, the Airport Operators Council International, the American Association of Airport Executives (both representing airport interests), and the Air Transport Association of America (representing air carrier interests) filed joint comments. The joint comments reflected a consensus of the respective airport, airport executive, and airline memberships. Although the air carriers had concerns regarding the impracticality and costs of setting up a separate escrow account for PFC revenues, they agreed that "they would, in fact, be collecting such funds for the benefit of the airports, and that such funds [were] not to be considered airline funds." Joint Comments in the Matter of Proposed Rulemaking: 91-4, Passenger Facility Charges, FAA Docket 26385, at 19 (March 18, 1990).

Accordingly, the Department adopted a final rule that sought to balance the burden and cost concerns of the airlines with the bankruptcy treatment and accountability concerns of the airports. The final rule permitted a commingling of PFC's with the carriers' other sources of revenue, subject to various requirements, including separate accounting of PFC revenue by carriers, disclosure of PFC amounts as trust funds in financial statements, and additional reporting, record keeping, and auditing requirements. 14 C.F.R. §§158.49, 158.65, and 158.69.

See also 56 Fed.Reg. 24,254, 24,268-69 (1991). Most important, however, was the requirement for trust fund treatment of the PFC revenues.

The PFC revenues that are held by an air carrier or an agent of the carrier after collection of a PFC constitute a trust fund that is held by the air carrier or agent for the beneficial interest of the public agency imposing the PFC. Such carrier or agent holds neither the legal nor the equitable interest in the PFC revenues except for any handling fee or retention of interest collected on unremitted proceeds as authorized in 158.53

14 C.F.R. §158.49(b)<sup>1</sup>

In the Federal Aviation Administration Authorization Act of 1996, Congress specifically reiterated the trust fund status of PFC's:

Passenger facility revenues that are held by an air carrier or an agent of the carrier after collection of a passenger facility fee constitute a trust fund that is held by the air carrier or agent for the beneficial interest of the eligible agency imposing the fee. Such carrier or agent holds neither legal nor equitable interest in the passenger facility revenues except for any handling fee or retention of interest collected or unremitted proceeds as may be allowed by the Secretary.

Federal Aviation Reauthorization Act of 1996, Pub. L. No. 104-264, §1202, 100 Stat. 3213.

As the legislative history to the 1996 Act demonstrates:

[t]his provision clarifies Congress' intent in authorizing the Passenger Facility Charge program in 1990 that PFC's collected by airlines and their agents are held in trust for the local agencies imposing those fees. FAA's current regulations implementing the PFC statute accurately reflect the trust fund nature of the airlines' collection and remittance of PFC funds from their passengers. In certain recent and current airline bankruptcy cases, courts have appeared erroneously not to accept the trust fund nature of the collection process; PFC proceeds should not be treated as other funds of the bankrupt carrier.

H.R. Rep. No. 104-848 (1996).

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<sup>1</sup> The Department's selection of a trust instrument as a way to safeguard the PFC revenue is a reasonable approach by the agency charged by statute with establishing measures of the PFC program. The Department's procedures are entitled to deference. *Chevron v. Natural Resource Defense Council, Inc.*, 467 U.S. 837 (1984).

## **ACCOUNTING REQUIREMENTS FOR THE PFC TRUST**

In order to ensure that PFC proceeds, even if temporarily commingled, did not lose their identity, the Department prescribed detailed accounting, handling and auditing requirements. 56 Fed. Reg. 24254-75 (1991).

Airlines, including Delta, are responsible for collecting the PFCs from each enplaning passenger at airports with an approved PC project, subject to specific limitations. 49 U.S.C. § 40117(i)(2)(A); 14 C.F.R. §158(a)(3). After collection, airlines are required to remit the PFC revenues monthly to each airport involved. Payment is not due later than the last day of the following calendar month that the PFCs are collected (or if that date falls on a weekend or holiday, the first business day thereafter). 49 U.S.C. § 40117(i)(2)(B); 14 C.F.R. §158.51.

Each airline is required to file a quarterly report with the airport for which it is collecting funds, to account for funds collected and remitted. 14 C.F.R. §158.69(a).

Part 158 also required that an airline, such as Debtor, “establish and maintain a financial management system to account for PFC’s in accordance with the Department of Transportation’s Uniform System of Accounts and Reports (14 C.F.R. Part 241).” 14 C.F.R. §158.49(a). The pertinent provisions of Part 241 require that Debtor list in its balance sheet Account 2190 (“Other Current Liabilities”) current and accrued liabilities, including amounts payable collected as an agent that are not provided for in other specified accounts. 14 C.F.R. Part 241, Section 6 - Objective Classification of Balance Sheet Elements, Account 2190. Debtor was required to file its Balance Sheet, including PFC’s within Account 2190—40 days after the close of the quarter. 14 C.F.R. Part 241, Section 22, Due Dates of Schedules in Form 41 Reports. Pursuant to 14 C.F.R. 158.51, all PFC’s collected must be remitted to GOAA no later than the last day of the following calendar month.

Thus, as designed by Congress and the Department, the PFC trust has several characteristics:

Clear trust relationships: The air carrier serves as the trustee and is responsible for collecting the PFC's, accounting for them, and remitting them – less handling costs – on a timely basis, and the public agencies serve as the beneficiaries of the trust.

Segregation not required: To address the concerns of the carriers, the PFC trust established does not require segregation of the trust corpus in a separate account. In a PFC trust, the PFC amounts collected can be commingled with other corporate funds.

Accounting and Reporting Requirements: Carriers are subjected to detailed PFC record – keeping, auditing and reporting requirements to ensure that, despite commingling, PFC funds maintain their integrity as trust proceeds.

**THE PFC TRUST IS INDISTINGUISHABLE  
FROM THE TRUST FUND TAXES IN *BEGIER***

The PFC regulations create a trust in a dollar amount, i.e., the amount of PFC revenue collected, and as such, the PFC trust is not subject to common-law tracing rules. *Begier v. United States*, 496 U.S. 53, 110 S. Ct. 2258 (1990).

In *Begier*, the debtor used its general operating funds to pay withholding and excise taxes (known as “trust-fund taxes”) owed to the IRS. The trustee later sought to avoid the payments as preferences. The Supreme Court held that the payments did not constitute property of the estate, but rather, they were trust funds of the Government under 26 U.S.C. §7501.

Section 7501 provides that the amount of tax collected or withheld “shall be held to a special fund in trust for the United States.” 26 U.S.C. §7501. According to the Supreme Court, the trust under §7501 was created at the time the appropriate amount of money was collected or withheld, even though the debtor was not required to segregate the money.

In analyzing whether the funds paid to the IRS were trust property, the Court concluded that tracing rules useful in following the res of a common law-trust were inapposite to the type of trust created under §7501. The Court explained that “[u]nlike a common-law trust, in which the settler sets aside particular *property* as the trust res, §7501 creates a trust in an abstract ‘amount’ – a dollar *figure* not tied to any particular assets...” *Begier*, 496 U.S. at 62 (emphasis in original). Since common-law tracing rules were inapplicable, the Court simply required the IRS to demonstrate some connection between the funds collected and those paid to the IRS.

The PFC trust is on all fours with the trust-fund tax created under §7501. Like §7501, the PFC regulations do not require segregation of PFC revenue. Even if the Debtor commingled the PFC’s with its other revenues from the moment the PFC’s were collected. Indeed, in an effort to reduce the carrier’s cost of collection and handling, the regulations contemplate that the air carrier will move PFC’s to various accounts to earn interest or other investment return on the revenue prior to remittance to the public agency. 14 C.F.R. §158.53(b); 56 Fed. Reg. 24,269 (1991).

The PFC regulations create a floating trust where: (1) PFC’s are collected by a carrier on a daily basis as passenger tickets are issued; (2) commingled with the carrier’s other sources of revenue; and (3) paid out monthly to public agencies. Unlike a common-law trust, the carrier, under the PFC regulations, does not set aside particular property as the trust res; rather, the PFC regulations create a trust in a dollar amount, i.e., the amount of PFC revenue collected by the carrier. Accordingly, common-law tracing rules are inapplicable here. Under *Begier*, the PFC claimant here simply must show some connection between the trust and the assets sought to be applied to the trust obligation. *Begier*, 496 U.S. at 65-67. Moreover, “reasonable assumptions” apply in determining whether sufficient nexus exists. *Id.* at 65-67. The nexus requirement is

easily satisfied here. Accordingly, the amount collected and held by Debtor is not property in which the estate has an equitable interest and must be segregated from and treated separately from the assets available for use by the Debtor.

To maintain the integrity of the trust account, the PFC regulations specify detailed accounting and reporting requirements so that the amount owed to public agencies can be identified by all parties. Here, it is our understanding that Debtor collected PFC funds, held them in trust, and maintained detailed accounting records showing the amounts owed to the Public Agencies. Only the remittance of those funds remains undone.

**PASSENGER FACILITY CHARGES ARE TRUST FUNDS UNDER  
FEDERAL LAW AND ARE NOT PROPERTY OF THE ESTATE**

Pursuant to Bankruptcy Code §541(d), no lien can be asserted over the PFC's in the Debtors' possession or in any PFC's collected by the Debtors because Debtors collect and hold the PFC revenue in trust for the benefit of GOAA; therefore, the PFCs are not property of the Debtors' estates. See 11 U.S.C. §541(d). Section 541(d) excludes that property from a debtor's estate in which the debtor holds "only a legal and not an equitable interest" at the commencement of its case. Id. "Because the debtor does not own an equitable interest in property [it] holds in trust for another, that interest is not "property of the estate." *Begier v. United States*, 496 U.S. 53, 59 (1990). Accordingly, no lien can attach.

By enacting §541(d), Congress expressed its intent that "when a debtor is a mere conduit for funds to travel from one party to another, it lacks an equitable interest in the monies." *Official Committee of Unsecured Creditors v. Columbia Gas Systems, Inc. (In re Columbia Gas Systems, Inc.)*, 997 F.2d 1039, 1059 (3<sup>rd</sup> Cir. 1993), cert. denied, 510 U.S. 1110 (1994). Here, because the Debtors acted as a mere conduit through which PFCs flowed from the traveling public to GOAA, the Debtors had no interest in the PFC revenue. Rather, they held the PFCs in trust for GOAA.

In *Columbia Gas Systems*, the Third Circuit held that a debtor had no equitable interest in surcharges it collected from its customers for the benefit of a non-profit research organization pursuant to federal regulation. 997 F.2d at 1062. The debtor tracked the charges in a separate “paper account,” pursuant to federal regulation, but did not segregate the funds from the general operating budget. *Id.* The research organization performed no service for the debtor and the debtor did not owe the organization any money until it actually collected the charges. *Id.* Furthermore, the debtor paid no interest to the organization during the time in which it retained the surcharges. *Id.* The debtor thus held the surcharges in trust for the research organization. *Id.*

The Debtors’ secured lenders’ (“Lenders”) interest in property is wholly derivative of the Debtors’ interest. The Lenders have no interest in or claim to PFCs, or any other user fees, that never belonged to Delta and never became part of the estate. No proceeds in the possession or under the control of the Debtors, which are impressed with the PFC trust funds, should be pledged and/or distributed to another creditor. See *Universal Bonding Ins. Co. v. Gittens & Sprinkle Enters., Inc.*, 960 F.2d 366, 272 (3d Cir. 1992) (“[Bankruptcy Law] simply does not authorize a trustee to distribute other people’s property among a bankrupt’s creditors.”) (quoting *Perlman v. Reliance Ins. Co.*, 371 U.S. 132, 135-36 (1962)). Indeed, to do so frustrates the congressional purpose underlying the creation of PFCs, which is to finance needed airport capital improvement. The PFCs collected from the traveling public were not intended to enrich an airline, let alone its creditors.

### **DEPARTMENTAL PFC ENFORCEMENT**

The Department of Transportation and the Federal Aviation Authority may enforce PFC and other various regulations through administrative, civil, and criminal sanctions. The failure to remit timely PFC’s collected from passengers to the airports may constitute an unfair and

deceptive trade practice and an unfair method of competition under 49 U.S.C. §41712. The failure to remit the money to airports not only deceives passengers – who paid the fee for the express purpose of financing airport projects – but also creates an unfair competitive advantage for the carrier over other carriers that are complying with the law. Violation of §41712 carries a civil penalty of up to \$1,000.00 for each day of the violation. 49 U.S.C. §46301(a).

**DEBTOR'S NEW FINANCIAL MANAGEMENT OBLIGATION FOR  
PASSENGER FACILITY CHARGES PURSUANT TO 49 U.S.C. § 40117(m)**

Effective December 12, 2003, Congress enacted additional protection for the collection of PFC's including: (i) recognition of the evolving case law that placed such fees as trust funds; (ii) providing the commingling of PFC's shall not defeat their trust fund status; and (iii) prohibiting the granting of a security interest in the PFC revenue. Most particularly, this statute was directed toward "covered air carriers." A covered air carrier is defined as,

An air carrier that files for Chapter 7 or Chapter 11 of the Title 11 bankruptcy protection, or has an involuntary Chapter 7 of Title 11 bankruptcy proceeding commenced against it, after the date of enactment of this subsection [enacted December 12, 2003].

*See* 49 U.S.C. §40117(7).

**CONCLUSION**

PFC's collected by the Debtors must be remitted pursuant to the new statutory scheme set forth in 49 U.S.C. §40117(m) and the detailed federal regulations in 14 C.F.R. § 158.

Dated this 26TH day of October, 2004.

BROAD AND CASSEL  
Roy S. Kobert, P.A.  
390 North Orange Ave., Suite 1100  
Orlando, Florida 32801  
Post Office Box 4961  
Orlando, Florida 32802  
Telephone: (407) 839-4200

Fax: (407) 650-0927  
Florida Bar No. 777153  
rkobert@broadandcassel.com  
orlandobankruptcy@broadandcassel.com  
(*Pro Hac Vice* Application to be filed)

and

/S/ RANDY C. EYSTER

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Randy Eyster, Esquire  
Feiwell & Hannoy, P.C.  
251 N. Illinois Street  
Suite 1700  
Indianapolis, Indiana 46204-4302  
Phone: - (317) 237-2727  
Fax - 317-237-2722  
reyster@feiwellhannoy.com