

The Cape Town Convention and Aircraft Protocol lands in the United Kingdom

In anticipation of the Cape Town Convention and related Aircraft Protocol (together, the "Treaty") coming into force for the UK on 1 November 2015 (the "Effective Date"), this briefing¹ highlights key consequences and considerations going forward for parties entering into aircraft leasing and financing transactions involving UK obligors, UK registered aircraft objects and/or English law governed agreements.

UK Implementing Regulations

The [International Interests in Aircraft Equipment \(Cape Town Convention\) Regulations 2015](#) (the "Regulations") implement the Treaty in the UK² and

also come into force on the Effective Date, from which point the Regulations will have direct effect in the UK courts and be binding as a matter of national law³.

Treaty remedies

Regulations 19 to 25 set out the remedies available to an international interest holder, including termination of the relevant lease, possession and sale or lease of the aircraft object and interim relief measures (such as grounding and safe-guarding of the aircraft). The UK has made the "self-help declaration"⁴ allowing any extra-judicial Treaty remedies to be exercised without court approval.

Creditors should recall that the Treaty imposes certain conditions on the scope and exercise of its remedies.

The consent of the debtor is required in respect of the remedies of a chargee (although this may be given at any time, including in the security agreement); a chargee must give at least ten working days' prior written notice of a proposed sale or lease to

any interested persons; and any Treaty remedy must be exercised in a commercially reasonable manner.

De-registration and export

A creditor may exercise the practical remedies of de-registration and export under Regulation 22 and, as the UK has made the "IDERA declaration"⁵, the UK Civil Aviation Authority (the "CAA") is under an obligation to record a valid IDERA submitted by the debtor provided it is substantially in the prescribed form and to co-operate expeditiously with the authorised party exercising its remedies.

Alternative A insolvency regime

The UK has adopted⁶ the Treaty's special insolvency regime with a waiting period of 60 days. Accordingly, under Regulation 37, if a debtor enters into insolvency proceedings in the UK⁷ or an

¹ This briefing assumes the reader is familiar with the scope and framework of the Treaty, including its registration system, priority rules and remedies available to a creditor on a debtor default; our previous briefings, including [Cape Town Convention and Aircraft Protocol – an Outline, March 2007](#) and [Cape Town Convention and Aircraft Protocol – UK Government Response – Adoption of Alternative A: Lex Situs rule clarification](#), provide further details and background. Certain terms, including "Contracting State", "international interest", "aircraft object", "chargee", "debtor" and "creditor", are as defined in the Treaty and/or Regulations, where applicable.

² The Treaty is an EU Treaty under the European Communities Act 1972 which provides for implementation of the UK's obligations by regulation. The Regulations reflect the UK's specific Treaty declarations.

The UK's ratification of the Treaty extends to the Cayman Islands, the Island of Guernsey and Gibraltar (subject to each territory's specific declarations). Implementation of the Treaty in each territory is subject to its domestic legislation.

³ The Regulations extend to England and Wales, Scotland and Northern Ireland. This briefing is limited to the effect of the Regulations as a matter of English law and in the English courts.

⁴ Convention Article 54(2)

⁵ Protocol Articles XIII and XXX(1)

⁶ The UK did not make the "Alternative A declaration" pursuant to Protocol Articles XI and XXX(3); instead it has amended its domestic insolvency laws in respect of aircraft objects to reflect the relevant Treaty provisions. Existing UK insolvency laws applicable to other assets and arrangements falling outside of the Treaty will not be affected.

⁷ Parties should consider that Regulation 37 may apply not only to a UK incorporated debtor but to a debtor with a UK "centre of main interests" ("COMI"), for the purposes of EC Regulation on Insolvency Proceedings 1346/2000 (or, for proceedings opened after 26 June 2017, of EU

insolvency-related event (as defined in Regulation 37) otherwise occurs, then the insolvency office holder must either return the aircraft object to the creditor at the earlier of the end of the waiting period or the date on which such creditor is otherwise entitled to possession; or cure all defaults (other than the default constituted by the commencement of the insolvency proceedings) and agree to perform all continuing obligations under the relevant agreement. In the meantime, the insolvency office holder is required to preserve the aircraft object and maintain its value in accordance with the relevant agreement and the creditor may apply for interim relief.

The open-ended moratorium on enforcement of security over the debtor's property and repossession of any property under a hire-purchase arrangement with the debtor which automatically applies on a UK corporate administration will not apply after the end of the waiting period and the court's power to order disposal of such property by the administrator is excluded⁸. At the end of the waiting period, a court order for possession will not be required. UK insolvency rules relating to antecedent transactions, such as avoidance of transactions as a preference, will still apply.

The CAA is under an obligation to make available the remedies of de-registration and export no later than five working days after notification by the creditor of its entitlement to exercise such remedies.

The above Alternative A creditor protections are only available in

⁸ Regulation No 2015/848 (recast)) Insolvency Act 1986, Schedule B1, paragraphs 43, 71 and 72, as disapplied by Regulation 37(12)

respect of registered international interests over aircraft objects⁹.

Liens and statutory detention rights

Regulation 17 specifies certain non-consensual rights and interests ("**NCRIs**") which have priority over registered interests, without registration. These are possessory liens arising under English common law for work undertaken on the aircraft object and statutory detention rights, including the powers of the CAA or other authority to detain an aircraft for non-payment of charges for air navigation, airport or other public services, regardless of whether such NCRIs are created before or after the UK's ratification (therefore, future statutory detention rights are covered). The application of the so-called Eurocontrol "fleet lien" in the UK remains unaffected by the UK's adoption of the Treaty¹⁰.

⁹ Regulation 36 provides that an international interest is effective in insolvency proceedings against a debtor only if such interest was registered under the Treaty prior to the commencement of such proceedings. Therefore, registration on the International Registry goes to perfection in insolvency as well as to priority generally. The other Treaty default remedies are available to an international interest holder regardless of registration.

¹⁰ Our June 2010 client briefing "[Aircraft fleet liens: no leniency for lessors](#)" summarises the English court's decision relating to the Eurocontrol fleet lien in *Global Knafaim Leasing Limited & CGTSN Limited vs. The Civil Aviation Authority and BAA Limited (Eurocontrol, NATS and Secretary of State for Transport as interested parties)* [2010] EWHC 1348 (Admin)

Recognition of international interest; express displacement of Blue Sky rule

Under Regulation 6(1), an international interest as provided for by the Convention is effective in law. The international interest is an *independent* interest, separate from any interest arising under existing domestic law, and is constituted under the Convention and recognised between Contracting States. From the Effective Date, this new proprietary interest in an aircraft object will be recognised in English law and by the English courts.

Regulation 6(3) further provides that the international interest has effect where the Treaty conditions are satisfied, with no requirement to determine whether a proprietary right has been validly created or transferred pursuant to the common law *lex situs* rule. This is an English choice of law rule which prescribes that the validity of a grant or transfer of a proprietary interest (including a security interest) in a tangible movable asset is to be determined by the *lex situs*, the law of the place where the asset is physically located at the time such grant or transfer takes effect.

The court in the Blue Sky case¹¹ confirmed that the *lex situs* rule applied to the question of the validity of a mortgage expressed to be governed by English law (an "**ELM**") and taken over an aircraft. The "Blue

¹¹ *Blue Sky One & Ors v Mahan Air*. the case was heard in two phases, [2009] EWHC 3314 (Comm) and [2010] EWHC 631 (Comm). The court further held that this reference to *lex situs* is to the domestic law of the place of location and not to its entire law, which would include the choice of law rules of the *lex situs*.

Sky rule" involves unique challenges for cross-border secured aircraft financings, given the highly movable nature of aircraft, the parties' different locations and the operational requirements of airlines and other users. Regulation 6(3) expressly displaces the Blue Sky rule when determining whether an international interest has been validly constituted.

English law International Interest Agreements

Parties should note that the same English law governed agreement may create a mortgage and/or charge over the relevant aircraft object under domestic law and a *parallel* international interest under the Convention, assuming the Convention conditions are met. For the purposes of this briefing, we refer to such security agreement as an "English Law International Interest Agreement" (an "ELIIA"), when entered into by a UK debtor and/or in respect of a UK registered aircraft¹².

From the Effective Date, a creditor under such ELIIA, wherever the aircraft is located at the time the security comes into effect, should have the benefit of an international interest, regardless of whether the parallel domestic law security interest is valid under the *lex situs*. Further, an equivalent analysis should apply to an ELIIA entered into by any Contracting State debtor and/or over an aircraft registered in any Contracting State; for example, an ELIIA entered into by a debtor incorporated in the Cayman Islands or in Ireland.

¹² The UK has not made the declaration excluding "internal transactions" so an ELIIA granted by a debtor to a creditor, each with its COMI in the UK, over a UK registered aircraft will still fall within the Regulations

Blue Sky may still be relevant: domestic law interest and other exceptions

Domestic law security interest

Regulation 6(3) only applies in respect of the constitution of an international interest. So, for example, if a party is seeking a valid ELM over the aircraft (whether granted in parallel under an ELIIA or separately), then the Blue Sky rule should still be considered¹³.

For example, the rights and remedies available to a mortgagee or chargee under English law, as distinguished from the Treaty remedies available to a holder of an international interest (which will be subject to the specific declarations of the relevant Contracting State), are well-established and may be of equal importance and value to a financier, regardless of whether it also has the benefit of an international interest¹⁴.

It is common for mortgages to be drafted to extend to "any and all proceeds of the aircraft". The international interest in an aircraft object extends to proceeds but these are defined narrowly as proceeds arising out of the loss, destruction or

¹³ English law recognises the concept of equitable security interests, including an equitable mortgage (as distinguished from a legal mortgage) and a charge (which is always equitable). A secured party may be comfortable with an equitable interest over the aircraft, particularly when coupled with a valid international interest.

¹⁴ Regulation 23 makes clear that additional remedies under the applicable law, including any contractual remedies agreed between the parties, may be exercised to the extent they are not inconsistent with mandatory provisions of the Regulations or the Treaty.

requisition of the aircraft, so while insurance proceeds from a total loss or government compensation amounts would be covered, it is unlikely that the holder of an international interest alone could claim for proceeds arising out of a disposal or a conversion of the aircraft. In contrast, an ELIIA may be drafted to give a financier the benefit of a domestic law charge over such wider proceeds.

We anticipate these widely drafted ELIIAs may dispense with the need for New York law or Irish law mortgages granted by Contracting State debtors (e.g. in the Cayman Islands or Ireland), especially where there is no other obvious New York law nexus.

Engines; non-Treaty cases

If the transaction involves the financing (or leasing) of an engine owned by (or leased) to a non-Contracting State debtor, then, whether or not the aircraft is registered in a Contracting State, an international interest will not arise under the relevant agreement in respect of the engine¹⁵. Secured parties may mitigate against this, for example, by structuring deals with aircraft owning entities incorporated in a Contracting State, such as Ireland or the US, which can satisfy the debtor connecting factor and grant an international interest over the relevant engines.

Where neither the location of the debtor nor the registration of the aircraft is in a Contracting State, the requisite Treaty connecting factor will

¹⁵ The aircraft registration connecting factor only brings the relevant airframe within the Treaty, not the engines which are treated as separate aircraft objects. This connecting factor is therefore also not relevant for individual engine transactions.

not be met so the secured financier will not be able to rely on an international interest. In such cases, the availability of an ELM or any equivalent local law security interest (in the jurisdiction of the debtor and/or state of registration) will be of greater significance.

Sales of aircraft objects

The orthodox position as a matter of English conflict of laws is that, for tangible movables, the *lex situs* rule applies to the validity of an outright transfer of title, as it does to a title transfer by way of security (i.e. a mortgage)¹⁶ and to a transfer of any other proprietary interest in the asset. Thus, an English court, if determining the proprietary effect of a sale of an aircraft object where the bill of sale or other title transfer instrument is expressed to be governed by English law, would refer to the law of the place where the object was physically located at the relevant time¹⁷.

Pre-existing interests

The Regulations will not apply to any pre-existing interests which will retain their priority under domestic law prior to the Effective Date, without the need for any registration on the International Registry. Existing security and leasing arrangements

involving a UK debtor and/or a UK registered aircraft will not fall within the scope of the Treaty, unless a new international interest were to be created after the Effective Date (for example, if the lease is novated or a new security interest is granted).

Companies Charges Registration – UK incorporated companies

The Companies Act 2006 establishes a system of registration for all "charges" (unless expressly excluded), including mortgages and security assignments, created by a UK incorporated company over any property. Registration goes to perfection of the security: if a registrable charge is not registered in accordance with the requirements (which include a 21 day time limit), it is void against the liquidator or administrator and any other creditor of the company. Further, failure to register renders the secured debt immediately payable.

The holder of an ELIIA granted by a UK company is therefore advised to register in accordance with the Companies Act, in order to avail itself of any domestic law remedies for secured creditors and to avoid acceleration of the debt¹⁸.

CAA Aircraft Mortgages Registration – UK registered aircraft

The CAA administers a register for mortgages over aircraft registered on the civil aircraft nationality register. Registration establishes priority: a registered mortgage has priority over subsequent registered mortgages and unregistered mortgages¹⁹. Registration also serves as notice to the world. Further, the CAA will not de-register an aircraft without the consent of the registered mortgagee.

The CAA Aircraft Mortgage Register will remain open after the Effective Date. Mortgages registered prior to the Effective Date ("**pre CAA mortgages**") will retain their priority without further registration. However, the priority of mortgages registered with the CAA after the Effective Date ("**post CAA mortgages**") will be subject to the priority rules in Regulation 16.

IDERAs and CAA registered mortgages

We understand that if a request is received under a properly recorded IDERA, the CAA will require the consent of the mortgagee under any pre CAA mortgage to de-register the aircraft but will not require the consent of the mortgagee under any post CAA mortgage.

Notwithstanding the above changes, registration with the CAA is still advisable to ensure that priority of the mortgage under an ELIIA over a UK registered aircraft is not adversely affected as a matter of domestic law.

¹⁶ An ELM involves the owner transferring title to the aircraft to the mortgagee, subject to an obligation to re-transfer ownership upon satisfaction of the secured obligation (known as the "equity of redemption").

¹⁷ The Aircraft Protocol extends certain Convention provisions to outright sales of aircraft, such as its registration and priority rules, but Articles 2 and 7 which provide for the constitution of an international interest are not applicable to sales. The Regulations also apply to sales but only to a limited extent (see Regulation 38); it is uncertain whether Regulation 6(3)'s express displacement of the *lex situs* rule is carried over to outright sales.

¹⁸ Schedule 5 of the Regulations at Part 2, paragraph 9, provides that S859A of the Companies Act 2006 is excluded for "a charge which is an international interest". The prudent view is that the effect of this consequential amendment is that the effectiveness of the international interest (and the availability of the Treaty remedies) does not require registration under the Companies Act but non-registration may invalidate the domestic law interest.

¹⁹ Other than pre-October 1972 mortgages registered before 31 December 1972 (when the register was established) – Mortgaging of Aircraft Order 1972. N.B. "mortgage" includes a fixed charge over the aircraft for the purposes of the Order.

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