

BEST PRACTICES FOR LAWYERING UNDER THE CAPE TOWN CONVENTION

*African Regional Seminar on the Cape Town Convention
and its Aircraft Protocol, and cross-border transferability
of aircraft*

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1. CONTRACT PRACTICES ISSUES

- **Contract Issues List:**
 - (i) Freedom to Contract
 - (ii) Cross-border Contracts
 - (iii) Alternative A/1110–Type Provisions
 - (iv) Lessee/Borrower Issues
 - Possible Registrations in favour of Lessee/Borrower
 - Possible Limitation of CTC Remedies

1. CONTRACT PRACTICES ISSUES *(cont'd)*

- (v) Connecting Factors in Contract
 - Contracts of Sale
 - Aircraft Engines
 - Aircraft Spare Parts
- (vi) Collateral Descriptions
- (vii) Necessary/Advisable CTC Registrations
- (viii) Pre-Existing Deals/Non-CTC Transactions
- (ix) Additional Local Registrations
- (x) Other Registration Issues
 - IDERAs
 - Prospective Interests
- (xi) Legal Opinions

2. TREATY BACKGROUND HIGHLIGHTS

- Joint sponsorship by Unidroit/ICAO with full IATA support when Treaty and Aircraft Protocol signed at Cape Town, South Africa on 16 November 2001
- Rare Debtor (IATA) and Creditor (AWG) unanimous agreement on key law reform points

2. TREATY BACKGROUND HIGHLIGHTS (*cont'd*)

- *IATA 2002 Annual Report:*

“This [Cape Town] achievement crowns many years of effort by IATA... the benefits should be felt soon. Those benefits are: reduced risk of credit financing and therefore diminished costs of financing aircraft, greater access to financing...and improved ability to dispose of used aircraft.”

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2. TREATY BACKGROUND HIGHLIGHTS *(cont'd)*

- Cape Town provides enhanced enforceability of contracts and party autonomy (to agree contractually on creditor and debtor rights)
- Freedom to contract – to be within purposes of Treaty
- Purposes of the Treaty are to “facilitate financing” of mobile equipment “in an efficient manner” and to provide “economic benefits for all interested parties”

2. TREATY BACKGROUND HIGHLIGHTS *(cont'd)*

- Why do we need this revolutionary new Treaty?
- Airlines, contrary to popular belief, sometimes default!

3. CROSS-BORDER CONTRACT CONSIDERATIONS

- **Search Contracting State Declarations when drafting defaults/remedies**
 - Contract defaults/benefits if Declarations change?
 - ASU Benefits (even if non-ECA financing)?
 - Compliance Project score?
 - Declarations affect later amendments, subleases and assignments
- **Most Important Mandatory Declaration Is:**
 - Self-Help (whether any remedies require leave of local court)

3. CROSS-BORDER CONTRACT CONSIDERATIONS *(cont'd)*

- **Most Important Opt-Out Declaration is:**
 - Speedy remedies (whether CTC expedited remedies require leave of local court)
- **Most Important Opt-In Declarations Are:**
 - Alternative “A” of Protocol
 - Cooperation of Foreign Courts in enforcing Alternative “A”

3. CROSS-BORDER CONTRACT CONSIDERATIONS (*cont'd*)

- Non-consensual interests not requiring registration to obtain priority
- Non-consensual interests requiring registration to obtain priority
- CTC not to affect local law rights of seizure and detention
- Limitation of local court discretion (time limits for speedy relief remedies)
- Contractual choice of law

3. CROSS-BORDER CONTRACT CONSIDERATIONS (*cont'd*)

- IDERA (the Irrevocable De-registration and Export Authorization)
- Qualifying Declarations for ASU Discount in their entirety

3. CROSS-BORDER CONTRACT CONSIDERATIONS (*cont'd*)

- **Declaration re Insolvency Proceedings:**
 - Alternative A (enhanced 1110-type with waiting period, eg. 60 days)
 - Alternative B (limited court discretion with waiting period, eg. 60 days – basically status quo in many jurisdictions)
 - Status Quo

4. INSOLVENCY ENFORCEMENT

Alternative A = enhanced version of U.S. Section 1110:

- Requirement to maintain aircraft objects per terms of contract
- Requirement to preserve value of aircraft objects
- anti-cramdown
- limits priorities
- triggered by more than just insolvency – includes inability to enforce due to “government action”

4. INSOLVENCY ENFORCEMENT

(cont'd)

- Alternative B does not prevent cram-downs under local law
- To date, most Contracting States have selected Alternative A (U.S. did not do so because 1110 already part of local law and ASU benefits were not available in the U.S.)
- New Representations and Warranties/Opinions:
 - that deal qualifies for CTC benefits (if applicable)
 - that deal qualifies for Alternative A (1110-type) protections (if applicable)

4. INSOLVENCY ENFORCEMENT (*cont'd*)

- “1110” is now an international concept
- New Covenants:
 - Further Assurances – should include CTC filings/advisable contract amendments
 - That debtor will never assert that deal not entitled to CTC, including Alternative A, protections (if applicable)
- In most standard aircraft mortgages and leases, Debtor already agrees to CTC-type remedies

5. LESSEE/ BORROWER ISSUES

A. Possible Lessee Registrations

- Purpose of the Treaty is to ensure enforceability of agreed terms and to facilitate speedy and effective enforcement in the event of default
- Contracts should not be entered that impair these objectives
- Registrations by Lessee (eg., subordinations (re quiet enjoyment) or purchase options) should not be consented to by Lessors as will impair re-possession and re-marketing on default

5. LESSEE/ BORROWER ISSUES *(cont'd)*

B. Possible Limitation of CTC Remedies

- Blanket exclusion contrary to Treaty intent
- Introduces uncertainty
- Debtor should identify specific problem issues (yet to be done!)

6. TECHNICAL ISSUES

A. Connecting Factors:

- When Aircraft is registered or is an agreement to register (for Chicago Convention nationality purposes) in a Contracting State; or

A. Connecting Factors (*cont'd*)

- When Debtor is “situated” (located = main place of business or legal seat) in a Contracting State (Creditor/Assignor/Buyer location not relevant)
- and -
- When Lease/Mortgage/Conditional Sale Agreement creates International Interest (which should always be the case)

A. Connecting Factors (*cont'd*)

- **Criteria are:**
 - agreement in writing
 - relates to Aircraft Object for which Chargor/Conditional Seller/Lessor has “power to dispose”
 - enables Aircraft Object to be specifically identified by manufacturer, model type and serial number
 - for a Security Agreement, enables secured obligations to be determined (without need to state a sum or maximum sum secured)

A. Connecting Factors (*cont'd*)

- and -

- When the International Interest is created or provided for after entry into force of Cape Town Convention for that Contracting State
- Contract reps/warranties?

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A. Connecting Factors (*cont'd*)

- **CONTRACTS OF SALE**

- Protocol makes CTC applicable to Aircraft/Engine Sale Agreements
- In effect, International Registry serves as an aircraft/engine title registry that preserves chain of title on public record
- Seller located in a Contracting State (Buyer location not relevant)
- Seller is registered as “Debtor”
- Buyer is registered as “Creditor”

A. Connecting Factors (*cont'd*)

- **AIRCRAFT ENGINES**

- Debtor situated in a Contracting State (Seller for sales – Manufacturer for Engines purchased by Manufacturer for sale to customers)
- When an Engine is replaced and Cape Town applies, a new International Interest must be created and registered – and the contract should so provide
- Exception – Helicopter Engines (are Parts – no separate legal status – except when off-wing)

A. Connecting Factors (*cont'd*)

- This does not apply to engines when the only connecting factor is registration of the airframe and not the location of the debtor or seller of the engine (should be registered in any event)
- When a lease is made by a debtor in a Contracting State which is the grantor of a mortgage or is the lessee under a lease of an aircraft object during the term, the lease or sublease should be registered if Cape Town applies – and the contract should so provide

A. Connecting Factors (*cont'd*)

- **AIRCRAFT SPARE PARTS**

- Re installed parts, local law (eg., re accessions /automatic title transfer) will continue to govern
- In most cases, contracts should use title transfer for spare parts and title tracking for engines

B. Collateral Descriptions

- **In Contract:**

- Describe Aircraft Object using customer specific/upgraded model designator and in accordance with “generic” model description contained in drop-down menus of International Registry (and requirements of FAA if different and applicable)
- Eg., “Boeing 777-275ER (Generic Airframe Model 777-200)”/ “GE90-115B (Generic Engine Model GE90-115B)”

C. Other New Contract Terms

- In contracts each party should agree to be registered as a TUE, and to authorize registration of the international interests, assignments and sales, either prospectively or on closing
- In contracts each party should agree to appoint a PUE to register the interests, and to agree upon the order of registration

7. REGISTRATION ISSUES

A. Necessary/Advisable CTC Registrations

- **Three potential registration scenarios to be provided for in contracts:**

(i) **CTC applies:**

- application to all parties/Aircraft
- International Registry searches and registrations must be made

A. Necessary/Advisable CTC Registrations (*cont'd*)

(ii) CTC applies in part:

- eg., not applicable to one or more parties or Aircraft
- advisable that registrations (concerning all parties/Aircraft) be made

(iii) CTC does not apply at all:

- eg., no connecting factor to any party or the Aircraft
- advisable that registrations (concerning all parties/Aircraft) be made

A. Necessary/Advisable CTC Registrations (*cont'd*)

- Registrations are inexpensive
- Airlines will/should have authorized Administrators/TUEs/PUEs
- avoids risk of missing required perfection registrations
- will save airline legal costs re analysis of whether CTC registrations are required

A. Necessary/Advisable CTC Registrations (*cont'd*)

- practical actual or constructive notice to third - parties/trustees in fact or under local law in and out of bankruptcy
- “perfection” to extent possible in many jurisdictions
- starts Title/International Interest chain from initial sale

B. NON-CTC TRANSACTIONS

- Precautionary International Registry registrations may be made for non-CTC transactions
- Precautionary registrations for future deals advisable for above reasons

C. TRANSITIONAL PROVISIONS – DOES CTC APPLY TO PRE-EXISTING DEALS?

- Pre-existing deals are all deals where the interest was created “or provided for” prior to March 1, 2006, for initial Contracting States, or prior to the entry into force of CTC for subsequent Contracting States
- CTC does not apply to pre-existing deals*
- Precautionary filings may be made in International Registry for pre-existing deals

*subject to Contracting State Declarations

C. TRANSITIONAL PROVISIONS (*cont'd*)

- Precautionary filings for pre-existing deals advisable in many cases (eg., in jurisdictions where perfection of leases/mortgages not possible)
- Post-CTC Aircraft Objects Security Agreement (AOSA), effectively a new “second charge”, can be used to bring pre-CTC transactions into CTC
 - short three-page standard form agreement
 - eliminates the need for amending and restating existing transactions

D. ADDITIONAL LOCAL REGISTRATIONS

- Inappropriate unless provide hard legal benefit not covered by IR registrations
 - UCC/PPSA registrations cover “ancillary” collateral covered by financing agreement that cannot be protected under Cape Town such as:
 - Disposition Proceeds
 - Loose Equipment

E. OTHER REGISTRATION ISSUES

- **IDERAs**
 - IDERAs always required in contracts if IDERA Declaration was made by Contracting State where aircraft is registered
 - Contracts should provide for which Creditor controls, and parameters for use
 - Contracts should provide for termination/re-grant

E. OTHER REGISTRATION ISSUES

(cont'd)

- **Prospective Interests**
 - Effective pre-registration of International Interests
 - Most OEMs do not permit Prospective Interests
 - Prospective Interests are usually made where possible to make closings more efficient, but due to potential changes in engines close to closings, are often not made weeks or even days before closing

8. LEGAL OPINIONS

- Opinion practice regarding the Convention is parallel and does not replace current opinion practice regarding domestic registry and other local filings and priorities
- See Annotated Legal Opinion Form (updated 2018) in AWG Legal Advisory Panel (www.awg.aero) Practitioner's Guide.

9. PRACTICAL RESOURCES

- Must buy *Official Commentary on Convention on International Interests in Mobile Equipment and Protocol thereto on Matters Specific to Aircraft Equipment*, UNIDROIT (Third Edition, 2013), by Professor Sir Roy Goode of Oxford
- For information on the International Registry, see www.aviareto.aero
- Best online source for Cape Town Convention (and other AWG projects) is Aviation Working Group website at www.awg.aero

G. PRACTICAL RESOURCES

(cont'd)

- The Convention and the Protocol are available to be downloaded for personal use only from www.unidroit.org
- The Aviation Working Group Legal Advisory Panel (“LAP”) has published: (i) a book on Contract Practices under the Cape Town Convention; (ii) a second volume on Advanced Contract Practices and Legal Opinions; and (iii) its online Practitioner’s Guide to the Cape Town Convention and the Aircraft Protocol (which is available for free on the AWG website)

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