1. Advantages to aircraft financiers/lessors

For a financier or lessor (each a creditor), the virtues of the 2001 Cape Town Convention and its Aircraft Equipment Protocol (together Cape Town) are that it aims to:

- bring speed, certainty and cost savings to repossession, deregistration and export of aircraft, helicopters and aircraft engines (aircraft objects) on an insolvency or other default where the aircraft object is in a country whose laws would otherwise not be creditor-friendly; and

- protect creditors’ interests in aircraft objects by:
  - providing for the registration of “international interests” in those aircraft objects at a single, web-based, "International Registry" that is open 24/7;
  - subjecting those interests to a simple priority regime whose main principles are:
    - registered international interests beat unregistered ones;
    - earlier registrations beat later registrations; and
  - the parties can vary priorities by agreeing and (for increased protection) registering subordination arrangements at the International Registry.

In this guide, we go into more detail about these benefits and how to take advantage of them.

For airlines and other aircraft operators, Cape Town's virtues are that improved creditors' rights can translate into better pricing. For example, airlines in states that have implemented Cape Town's Alternative A insolvency regime – with a "waiting period" of 60 days – have achieved impressive pricing on their capital markets financings of aircraft. For more on Alternative A and the waiting period, see section 12 (Insolvency regime declarations).

2. What are international interests?

These are certain title, security and other rights in aircraft objects that can be registered at the International Registry. To be international interests, they must be given to a:
In addition:

- the agreements documenting the above transactions must be in writing;
- the lessor, chargor or seller respectively under those agreements must have the legal power to dispose of the aircraft object in question; and
- a Cape Town "connecting factor" must apply to the agreement — for an explanation of connecting factors, see section 4 (Connecting factors – to what transactions does it apply?).

Cape Town also allows the buyer under a bill of sale issued in connection with an aircraft purchase agreement or engine contract to register its interest in those engines at the International Registry as if the sale were an international interest.

3. Which aircraft, helicopters and engines are covered?

Cape Town only applies to high-value aircraft objects in civilian use. So there will be no Cape Town international interest or sale in an aircraft object unless it meets these criteria:

- airframes (when fitted with engines) must be type certified to carry at least eight persons or goods in excess of 2,730 kg;
- helicopters must be type certified to carry at least five persons or 450 kg; and
- engines must have:
  - if jet-propelled, at least 1,750lb of thrust (or its equivalent);
  - if turbine-powered or piston-powered, at least 550 take-off shaft horsepower (or its equivalent).

4. Connecting factors – to what transactions does it apply?

Cape Town will apply to a lease, hire purchase agreement, conditional sale agreement, security agreement or bill of sale when the agreement has a Cape Town connecting factor. There will be a connecting factor when, on execution of the relevant agreement, the:

- lessee under an aircraft lease or hire purchase agreement;
- security provider under an aircraft mortgage, charge or other security agreement over an aircraft object;
- buyer under a conditional sale or hire purchase agreement of an aircraft object; and
• seller under an aircraft purchase agreement or engine contract,

• is situated in a state in which Cape Town is in force – see section 5 (*In which states does it apply?*) for a list, and a link to a world map showing the location, of these states.

A party is situated for these purposes in the state, among others, where it is incorporated, or has its place of business, registered office or centre of administration. The state(s) in which the other parties to the documents listed above are situated have no effect on whether Cape Town applies.

There is an alternative connecting factor. This one only applies to airframes and helicopters (not engines) and applies when, on execution of the relevant document:

• the parties have agreed in writing that the aircraft or helicopter in question will be registered on the civil aircraft register in one of those states; or

• that aircraft or helicopter is actually registered on the civil aircraft register in one of those states.

5. *In which states does it apply?*

This world map shows all states in which Cape Town was in force as at 11 July 2016.

As at that date, those states are: Afghanistan, Albania, Angola, Aruba, Australia, Bahrain, Bangladesh, Belarus, Bhutan, Brazil, Burkina Faso, Cameroon, Canada, Cape Verde, Cayman Islands, China, Colombia, Congo, Cuba, Curaçao, Denmark, Egypt, Ethiopia, the European Union (the EU's ratification does not bring Cape Town into force in any given state, but does restrict the declarations an EU state may make should it choose to ratify), Fiji, India, Indonesia, Ireland, Ivory Coast, Jordan, Kazakhstan, Kenya, Kuwait, Latvia, Luxembourg, Madagascar, Malawi, Malaysia, Malta, Mexico, Mongolia, Mozambique, Myanmar, New Zealand, Nigeria, Norway, Oman, Pakistan, Panama, Russia, Rwanda, San Marino, Saudi Arabia, Senegal, Singapore, Saint Maarten and the Caribbean Netherlands, South Africa, Spain, Sweden, Tajikistan, Tanzania, Togo, Turkey, UAE, Ukraine, United Kingdom, United States of America and Vietnam.

6. *What to do about pre-Cape Town transactions*

For the most part, there is little to do if Cape Town comes into force in a jurisdiction where the lessee, security provider or conditional buyer under an existing transaction is situated. This is because a fundamental rule of Cape Town is that it does not affect pre-existing rights and interests or their priorities. In other words, Cape Town does not apply retrospectively.

Ratifying states can partially depart from this rule when or after ratifying. They may do so, broadly, by declaring that, the priority of rights arising under certain transactions will be subject to the Cape Town regime.

However, its declaration in this regard needs to be made at least three years in advance of its taking effect. And the declaration only applies Cape Town's priority rules retrospectively. It does not retrospectively make Cape Town's default remedies available (more on default remedies in section 13 (*Transaction documents*)).

So far, the vast majority of ratifying states have not made the declaration necessary to make Cape Town apply to pre-existing deals.

There are two other overlapping situations in which Cape Town could affect an existing financing or leasing. These are
where the documents:

- contain a Cape Town further assurance clause; or
- are amended, extended, novated, supplemented or replaced in ways that create interests to which Cape Town applies.

7. Further assurance – obligations to re-document

In the mid 2000s, some documents would provide that the parties would enter into new agreements, and take other actions, if Cape Town came into force in a state relevant to the transaction. This was to provide the creditors with rights under Cape Town, such as Cape Town self-help repossession remedies.

If creditors invoked these clauses, any international interests the new documents created would be registrable at the International Registry. Among other things, this would protect the priority of the international interests they created (more on this in section 15 (Registrations should reflect the agreed priority position). The new transaction documents themselves would also need to be drafted to take the maximum advantage of Cape Town that the commercial deal permitted (for more on certain Cape Town drafting issues, see section 13 (Transaction documents)).

In practice, however, creditors seldom invoked these clauses, preferring instead to rely on the protection given by Cape Town’s priority rules not applying retrospectively. And such clauses are now very rare. Among other things, re-documenting older transactions to create international interests may re-start insolvency hardening periods, have adverse tax consequences or involve the need to obtain central bank or other licences without any obvious benefit in doing so.

8. Further assurance – amending, extending, novating or supplementing existing transaction documents

The more common form of further assurance obligation, broadly, requires that the lessee/security provider or conditional buyer take all steps that are necessary or desirable to give the creditors the fullest benefit potentially available to them under the transaction documents if Cape Town becomes applicable to the transaction. Subject to the detailed drafting of actual clauses, this sort of generally worded clause would not normally require that the transaction be re-constituted by executing new documents.

However, if Cape Town comes into force in a state that is relevant to an existing transaction and, for whatever reason, transaction documents are amended, novated or supplemented in ways that create international interests, then this sort of further assurance clause would require that those interests be registered at the International Registry.

There are too many permutations as to what changes to transaction documents will or will not create an international interest. It is best to analyse, and take legal advice on, individual cases as they arise. However, to give a couple of examples:

- extending the term of a lease would tend to create an international interest for the period of the extension;
- amending the maintenance or insurance covenants in a lease would not normally create an international interest.
9. Default remedies

Where Cape Town is in force in states relevant to a transaction, for the creditors to obtain the fullest benefit of Cape Town’s remedies:

- the states that are relevant to the transaction need to have adopted (via contracting state declarations – see section 11 (Contracting state declarations)) the most creditor-friendly version of Cape Town;
- the transaction documents need to specify which Cape Town remedies will be available and what events will be defaults triggering that availability – see section 13 (Transaction documents);
- the documents should also provide for the granting of an IDERA and its being recorded at the civil aviation authority on whose register the aircraft or helicopter is or will be registered – see section 10 (IDERAs); and
- the parties need to contract out of those parts of Cape Town which are optional and which do not reflect their commercial deal. The parties can exclude Cape Town’s quiet enjoyment provisions, for instance.

10. IDERAs

Civil aircraft cannot legally fly unless registered at the civil aircraft register of a state pursuant to the Chicago Convention. But an aircraft may only be registered in one state at a time. Given this, a creditor’s ability to re-lease or sell a repossessed aircraft will be restricted if it cannot procure the aircraft’s de-registration from the aircraft register in the state in which it is habitually based. Creditors often take a de-registration powers of attorney from the entity entitled to deregister “their” aircraft to try to solve this problem. However, the local aircraft register may not act on de-registration powers of attorney – or local law may allow the donor to revoke any power of attorney it has granted even if it is expressed as irrevocable.

For these reasons, Cape Town allows ratifying states to declare that their aircraft registry and other authorities must act on IDERAs to allow the holder of the IDERA to de-register and export an aircraft from their territory on a default. IDERA is short for irrevocable de-registration and export request authorisation.

11. Contracting state declarations

When states ratify Cape Town (and sometimes after they have ratified), they can pick and choose between certain provisions they want to adopt, provisions of which they prefer diluted versions and their own laws.

Key choices include:

- what remedies will be available on default;
- whether those remedies can be exercised without going to court;
- what, if any, interim remedies (for example, a court order immobilising the aircraft or for its sale and the application of the sale proceeds) will be available pending the outcome of any court proceedings that are required;
- whether the ratifying state’s aviation authority and other authorities must act on an IDERA; and
- whether a state or private entity will have rights in respect of unpaid taxes, fines, fees or charges (e.g. for landing fees or engine repair charges) to an aircraft object that rank ahead of registered international interests and whether...
12. Insolvency regime declarations

Cape Town also gives ratifying states a choice of three insolvency regimes relating to aircraft objects – Alternative A, Alternative B or (for states choosing neither) sticking with their own insolvency laws. States can also choose whether to apply any given regime to all or a type of insolvency proceedings.

Under Alternative A – broadly: if the insolvency officer or debtor is unable to cure all defaults and agree to perform all future obligations within a "waiting period" (the ratifying state specifies on ratification), the administrator or debtor must give the creditor the opportunity to take possession of the aircraft by the end of the waiting period. The ratifying state’s court has no power to stay the enforcement. In the meantime, the insolvency officer/debtor must preserve the aircraft and maintain it and its value.

Alternative B is broadly similar to Alternative A, but the crucial difference is that the local courts regulate whether, when and on what terms the creditor can take possession of the aircraft at the end of the waiting period.

If the ratifying state opts to keep its own insolvency laws, creditors’ rights on insolvency will depend on how pro-creditor that state’s insolvency laws are. Many common law jurisdictions, for example, are very creditor-friendly jurisdictions. Many civil law countries are more debtor-friendly, sometimes requiring, for example, that security over aircraft can only be enforced by lengthy public auction process, and forbidding self-help repossession.

13. Transaction documents

This section deals with some of the points the documents should cover on remedies. The parties need to agree what events will be defaults and trigger the availability of Cape Town’s remedies if they happen. They then need to agree which of those remedies will be available in their transaction. Broadly, if they do not agree to a Cape Town remedy being available, then that remedy is not available unless available under applicable law.

However, as noted above (section 11 (Contracting state declarations)), the documents can only select from those Cape Town remedies that are allowed for in the contracting state declarations made by the states where the relevant debtors in their transaction will be based, or the airframe or helicopter registered.

The main Cape Town default remedies that parties should consider adopting are:

- a mortgagee or chargee of an aircraft object being able to:
  - take possession or control of it;
  - sell or grant a lease of it;
  - collect or receive income or profits arising from its management or use; or
  - take ownership of it in or towards satisfaction of the secured obligations – all interested parties need to agree to this last remedy;
  - a lessor or seller under a conditional sale or hire purchase agreement (or an assignee of any of those people) being able to terminate the lease, conditional sale or hire purchase agreement and repossess or take control of the aircraft object;
  - the ability to procure the aircraft’s deregistration and export or physical transfer from the territory in which it is such claims need to be registered.
located using an IDERA recorded at the civil aircraft registry in that territory; and

- pending the outcome of any court proceedings following the default giving rise to the above remedies, a creditor being entitled to apply to court for orders in respect of the aircraft object for its:
  - preservation;
  - possession, control or custody;
  - immobilisation; or
  - leasing or management or its sale and the application of its proceeds.

The documents should also provide for the issue of a Cape Town IDERA, for its recordation at the relevant aviation authority and for the IR registrations (including amendments, assignments and discharges to registrations) that could be required to give effect to the title, security, priority and other arrangements contemplated by the commercial deal.

Related to this, the documents should adopt or exclude Cape Town’s quiet enjoyment rules.

Including a further assurance clause, and costs and enforcement indemnities, would also be prudent.

14. The International Registry (the IR)

Anyone with an internet-connected PC with a current browser and a recent version of Java can search the register on the IR site.

Before a party can make, amend or discharge an entry on that register, however, it, its counterparty and any lawyers either wants to use for this purpose must all be authorised and registered users of that site.

This is because the IR is purely electronic. Its officials will not register anything on the basis of documents, telephone calls, emails, faxes, letters or powers of attorney. Instead the website itself will only allow registered users to register interests if all relevant parties give their prompt electronic consent on the IR itself to such registrations.

The parties' lawyers can give that electronic consent where the transaction parties have given their previous electronic consent on the IR to their lawyers doing so.

The IR requires that the first person from any entity applying to be a site user be that entity's "administrator" in relation to the IR. The administrator is responsible for all dealings with the IR by the entity for which it is the administrator – though the administrator can delegate the ability to register, etc.

All registered users have to download a unique digital signature to their PC once the IR has accepted their application to become a user. This means that a registered user can only work on the IR via the computer to which they have downloaded their digital signature. The IR may permit the digital signature to be transferred to another computer in limited circumstances. Unfortunately, these circumstances do not include ad hoc administrative convenience.

The administrator can allow others within his or her organisation to become registered IR users and deal with the IR on the entity's behalf. Those people will also have to contact the IR from a computer that meets the specification mentioned above, download a digital signature to their PC and carry on using that PC alone for all of their dealings on the IR.

If a party wants to delegate all the Cape Town filings on a transaction to its lawyers, then those lawyers must first
15. Registrations should reflect the agreed priority position

Many Cape Town priority questions are decided by the order in which registered interests appear on the IR. It may be easier for parties to get this order right if they take advantage of the ability to register prospective international interests. These are registrable before the international interests they seek to protect exist.

Once the actual interests are created by execution of the transaction documents, the prospective international interests automatically become full blown international interests – though their priority dates back to the moment when the prospective international interests were registered.

In practice, search results make no distinction between prospective and actual international interests.

If the order of registrations does not reflect the initial deal on priorities, or if that deal is changed during the life of the financing or leasing, the parties can amend the priority of registered international interests by executing a subordination agreement. Once registered at the IR, this is effective under Cape Town to re-order the parties’ priorities and bind third parties.

Recently, the IR has introduced a "closing room" facility. Using this facility can also help ensure the registrations for a transaction appear on the register in the right order. However, the closing room facility is somewhat cumbersome and time-consuming to use. Parties with an eye on costs may prefer the option of all parties (apart from aircraft object manufacturers and other outright sellers) appointing a single law firm to effect all agreed registrations on behalf of all such parties in an agreed order.

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