



Enforcement of
Security over an
Aircraft

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ENFORCEMENT OF SECURITY OVER AN AIRCRAFT

Introduction

In the current economic climate the possibility of defaults under loans secured on aircraft is an increasing concern for aircraft financiers. It is of course important to note that a security package will vary depending on the context of the particular aircraft financing transaction, and may include security documents such as an aircraft mortgage, a charge over the aircraft's maintenance reserves, a charge over shares in the borrower, a charge over shares in the guarantor for the borrower, an assignment of airframe and engine warranties in favour of the financier and an assignment of insurances to the benefit of the financier.

This paper provides a brief overview of some important considerations in the context of a financier with a security interest as mortgagee acknowledging the challenges posed by the multi-jurisdictional nature of the aviation industry to the enforcement of a financier's security over an aircraft. A financier wishing to enforce its security following such a default will typically need to consider the following:

-  Review of the loan agreement and aircraft mortgage
-  Notice of default, locating the aircraft and repossession
-  Liens and other prior interests
-  Sale of the aircraft and deregistration
-  Foreign jurisdictions
-  The Cape Town Convention

Review of the Loan Agreement and Aircraft Mortgage

The first step will be to review the loan and security documents to ensure that an event of default has occurred and to identify which relevant clause(s) can be relied upon by the financier to enforce its security. The 'Events of Default' clause(s) will describe the circumstances in which a financier can terminate its loan early and enforce its security and will typically include circumstances such as (a) a failure by the borrower to pay principal and interest under the loan, (b) breach of representation or warranty by the borrower, (c) breach of covenant by the borrower, (d) insolvency of the borrower or any guarantor, (e) failure by the borrower to pay airport charges or other operational costs when due, (f) arrest, confiscation or seizure of the aircraft, (g) failure to maintain or insure the aircraft and (h)

occurrence of a materially adverse change in the business, operations or financial condition of the borrower or in the value of the aircraft.

It is important to ensure that the loan and security documentation fully and accurately describe the 'aircraft', and refer to the airframe, engines, manuals and technical records. The aircraft mortgage should also be reviewed to confirm that the mortgage is enforceable following a demand for repayment of the loan being made on the borrower which the borrower has not met.

Legal opinions obtained at the time of the creation of the mortgage should be considered, e.g. legal opinion in (a) the borrowers' jurisdiction, (b) the jurisdiction of any guarantor or other third party providing security, (c) the jurisdiction of registration of the aircraft and, (d) if *lex situs* issues apply, the jurisdiction where the aircraft was located at the effective time of the creation of the mortgage. It is important to note that such legal opinions are only valid on the date on which they are provided and should reflect the position as of the date of the legal opinion.

Notice of Default, Locating the Aircraft and Repossession

Having established that an event of default has occurred, a notice of default clearly and accurately specifying the relevant events of default and noting the financier's intention to enforce its security (i.e. the aircraft mortgage) should be served on the borrower. Such notice must be served in compliance with the terms, addresses and method(s) provided for in the loan documentation.

If possible, a consensual repossession of the aircraft should be sought. In the absence of the cooperation of the borrower, a forced repossession will be necessary. Before the aircraft can be repossessed, the location of the aircraft must first be established by:

- (a) contacting the Central Flow Management Unit of EUROCONTROL, in the case of a jet operating in the EUROCONTROL area; or
- (b) in the case of a non-jet aircraft, contacting the control tower at the base of the aircraft; or
- (c) contacting the Air Traffic Organisation, in respect of aircraft that is or may have been recently in the United States; or
- (d) obtaining the services of an aircraft repossession services company.

Typically, under Irish law, it is not necessary for a court order to be obtained in order to repossess all aircraft. However, a financier may opt to do so should the actual occurrence of an event of default be questionable or where it is foreseeable that difficulties may arise due

to potential uncooperative behaviour on the part of the borrower with respect to the resale of the aircraft. It is also important that adequate insurance be put in place to cover the aircraft immediately upon repossession, regardless of the method of repossession chosen.

Liens and Other Prior Interests

A financier will need to establish if any liens or other prior interests exist which may influence the financier's ability to enforce its security over the aircraft. The financier will need to consider whether any liens or other rights rank in priority to the financier's interest, establish if the aircraft will be subject to detention by the relevant airport authorities or EUROCONTROL and contact the relevant regulatory authorities to ensure all regulatory requirements in connection with the aircraft are satisfied.

It is worth noting that the Irish Aviation Authority ('IAA') has the authority to detain and sell an aircraft for unpaid navigational charges, including EUROCONTROL charges, on an Irish or non-Irish registered aircraft and an aircraft may be detained in Ireland due to substantial unpaid charges relating to the aircraft or any other aircraft in the relevant operator's fleet. Other common liens include those that arise in the context of storage, repair, maintenance or other services to aircraft, tax liens and judgement liens.

Sale of the Aircraft and Deregistration

The aircraft mortgage will usually provide the financier with an express power of sale. In addition, as a matter of Irish law, the financier will benefit from an implied power of sale where a legal (rather than equitable) mortgage exists.

Upon the occurrence of an event of default, the mortgagee may effect the sale of the aircraft by private sale. However, it is necessary to consider the likelihood of a potential challenge to such a private sale by other parties that possess security, interests or claims against the aircraft and/or borrower on the basis that such parties' rights may be infringed as a result of the private sale. A private sale may also be challenged in circumstances where the sale may not achieve what a challenger may consider to be the best price and/or the mortgagee may not have sufficient authority to pass good title to the aircraft. Therefore, as an alternative to such a private sale, the mortgagee may seek to effect the sale of the aircraft by pre-judgement court sale where the court is satisfied that an expedient sale is required, or, by enforcing a court issued judgement debt. In the event of a sale pursuant to a court order, the terms of the sale will be specified by the court. In most cases the court will order that the sale of the aircraft be carried out by public auction, unless the mortgagee can demonstrate that a better price can be obtained for the aircraft by a private sale.

The aircraft will need to be deregistered from the relevant aircraft registry in order to remarket and sell the aircraft. To deregister (and export) an aircraft, a request in writing from the registered owner(s) is required. Where the aircraft is registered in Ireland, the IAA may approve an application for deregistration when accompanied by an irrevocable deregistration and export request authorising the financier to effect deregistration upon behalf of the borrower.

Foreign Jurisdictions

A number of issues may arise where aircraft are based or operated in jurisdictions outside of Ireland. It is important that a financier obtain a legal opinion in respect of each relevant jurisdiction when entering into a loan agreement. A legal opinion should typically address the following:

- ▣ the choice of law and jurisdiction clauses, and whether such clauses would be recognised by the relevant foreign court;
- ▣ the steps necessary to perfect security over an aircraft in the relevant jurisdiction;
- ▣ any particular issues of local law that may impact the enforceability and validity of a security (e.g. aircraft mortgages are not recognised as valid security in Austria and Belgium);
- ▣ the effectiveness of the deregistration power of attorney provided by the borrower to the financier;
- ▣ the recognition or otherwise of self help remedies in the relevant jurisdiction;
- ▣ potential difficulties and procedures with respect to aircraft de-registration and export;
- ▣ the timeframe(s) involved in enforcement proceedings;
- ▣ any other risks, such as the likelihood of a local court allowing an aircraft owner to maintain possession and use of an aircraft subject to the owner meeting satisfying outstanding arrears; and
- ▣ all relevant documentation (and translations if relevant).

A financier should also consider the impact of any potential foreign insolvency procedures, international conventions (e.g. the Chicago Convention, the Geneva Convention, the Cape Town Convention) and any other jurisdictional requirements in order to successfully repossess the aircraft, engines and records.

The Cape Town Convention

The Convention on International Interests in Mobile Equipment and the Protocol on Matters Specific to Aircraft Finance (the 'Cape Town Convention') which entered into force on 1 March 2006, has been ratified by Ireland and has been given force of law in Ireland pursuant to the International Interests in Mobile Equipment (Cape Town Convention) Act 2005. The Cape Town Convention applies to 'international interests' in 'aircraft objects' which are created when either the borrower is located, or the aircraft is registered, in a Contracting State. 'International interests' include those interests under security agreements. 'Aircraft objects' include airframes which carry at least 8 persons (including crew) or at least 2750kgs of cargo; aircraft engines with at least 1750lbs thrust or at least 550 horsepower; and helicopters carrying 5 or more passengers.

Creditors may exercise standard default remedies under security agreements to take possession or control of the aircraft in order to: sell or grant a lease of the aircraft; receive income or profits that result from the management or use of the aircraft; and to procure the de-registration, export and physical transfer of the aircraft from the territory in which it is located. The Cape Town Convention provides that such remedies are exercisable without a court order unless the relevant Contracting State has declared otherwise. In Ireland, it has been declared that a creditor, who wishes to exercise a remedy that is available to the creditor under a provision of the Cape Town Convention, is not required to make an application to the High Court for leave to exercise that remedy unless the provision expressly requires the creditor to make such an application.

The Cape Town Convention provides for interim relief (provided that the borrower has agreed to same) and also outlines approaches to insolvency remedies which can be adopted by a Contracting State as an alternative to domestic insolvency law. Ireland has not opted for such an alternative and domestic insolvency laws apply.

The International Registry of Mobile Assets, which was established to record 'international interests', is located in Ireland. In addition, mediation cases for leasing disputes are to be heard in the High Court of Ireland – yet another landmark development in Ireland's role as a recognised international aircraft leasing centre of choice.

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