



Department
for Business
Innovation & Skills

**CONVENTION ON INTERNATIONAL
INTERESTS IN MOBILE EQUIPMENT
AND PROTOCOL THERETO ON
MATTERS SPECIFIC TO AIRCRAFT
EQUIPMENT**

**Government Response to the
Call for Evidence**

DECEMBER 2013

Contents

Contents	2
1.Executive Summary	3
2.Introduction	4
3.Government response	5
4.What happens next?	9
5.Further enquiries.....	9
6.List of Respondents	10

1. Executive Summary

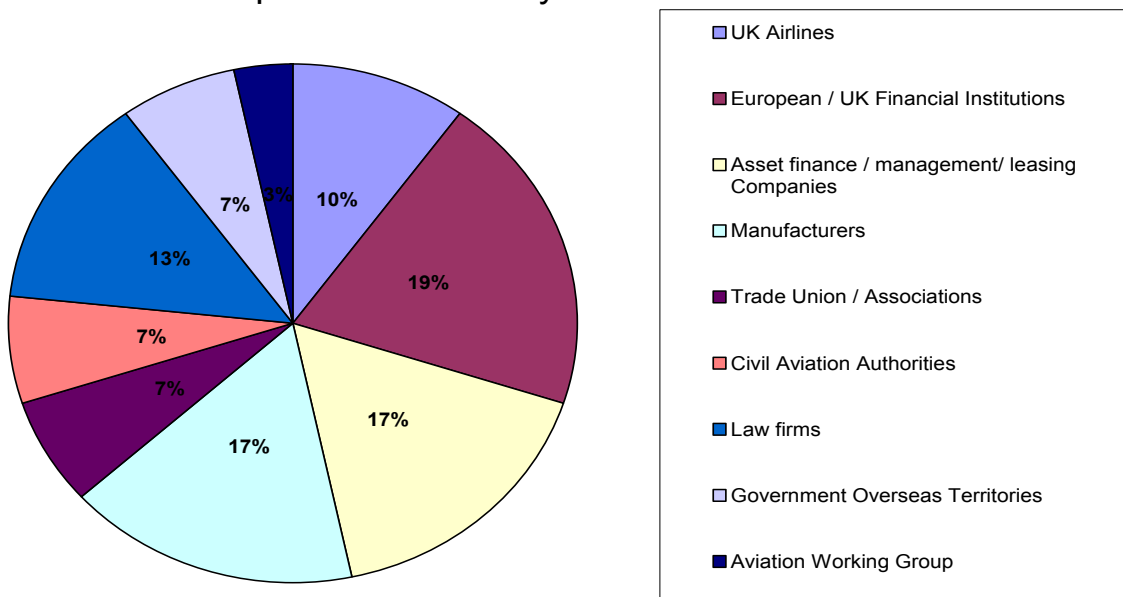
- 1.1. The Government published a call for evidence on 30 July 2010 (URN 10/1032) on the Convention on International Interests in Mobile Equipment (“the Convention”) and the Protocol thereto on Matters Specific to Aircraft Equipment (“the Protocol”). The Government would like to thank all those who responded to the call for evidence, we are grateful for all the contributions that were received and for the additional information provided by the Aviation Working Group (AWG). A summary of the responses was published by the Department for Business, Innovation and Skills (BIS) in February 2011 (URN 11/539).
- 1.2. The majority of respondents to the call for evidence were in favour of the UK ratifying the Convention and the Protocol as it relates to aircraft equipment (“the treaty”), and supported ratification as soon as possible. Those in favour of ratification said that it would reduce the risk for aircraft financiers and manufacturers in complex, cross-border, aircraft finance transactions, which would lower the cost to airlines of raising finance. Many respondents thought that ratification of the treaty, with certain optional provisions, would provide greater access to the US capital markets and may enable some airlines to diversify their sources of finance and would be in line with the OECD’s Aviation Sector Understanding.
- 1.3. Not all the respondents to the call for evidence were in favour of ratification. Some respondents thought that ratification would increase costs for UK airlines without any material benefit since UK law and the UK courts system are well respected. Some respondents commented that the UK Register of Aircraft Mortgages, run by the Civil Aviation Authority (CAA), works well and they did not think that the services provided by the International Registry would lead to any additional benefits, except the ability to register interests against aircraft engines separately.
- 1.4. The Government has carefully considered the views of the respondents to the call for evidence and has decided to proceed with ratification of the treaty. The Government agrees that ratification of the treaty may reduce costs for airlines who wish to raise finance through the capital markets. However, ratification is just one of many factors that financiers and ratings agencies consider when making their decisions and so the benefit of ratifying the treaty is difficult to quantify. The Government also recognises that the capital markets are just one funding option for airlines and many airlines will choose to raise finance in other ways; depending on an airline’s individual circumstances and how it chooses to raise finance, ratification of the treaty may not have a significant effect on financing costs. The Government agrees there is a benefit to UK business in being able to register interests against engines separately with the International Registry which would provide greater security for engine manufacturers and financiers since engines are routinely moved between aircraft. The Government also recognises that an International Registry open twenty-four hours a day, seven days a week could remove pressure from the closing logistics of aircraft finance transactions taking place in different jurisdictions and time zones, particularly when considered alongside the provisions to register prospective interests with the International Registry.

- 1.5. The treaty contains a number of options in terms of implementation. The Government will hold a consultation on these options.

2. Introduction

- 2.1. The Government published a call for evidence on 30 July 2010 (URN 10/1032) asking whether the UK should ratify the Convention on international interests in mobile equipment and the Protocol thereto on matters specific to aircraft equipment.
- 2.2. The call for evidence asked a number of questions seeking views on whether it would benefit the UK to ratify the treaty or whether the UK should take no further action at this time and retain the status quo.
- 2.3. The call for evidence closed on 8 October 2010. Thirty responses were received and a summary of the responses was published on 24 February 2011 (URN 11/539). A copy of this document can be obtained from the following link:
https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/31572/call-full-responses-mobile-aircraft-equipment.pdf
- 2.4. The Department agreed with the Aviation Working Group (AWG) that supplementary evidence to support the case for ratification would be considered after the official closing date. This was received on 23 September 2011.

Responses divided by source



- 2.5. The Government is grateful for all the views received as a result of the call for evidence and to those who provided supplementary information and discussed this matter with the Department for Business, Innovation and Skills.

3. Government response

- 3.1. The Convention on international interests in mobile equipment and the Protocol thereto on matters specific to aircraft equipment (“the treaty”) were agreed in 2001. The treaty aims to facilitate asset-based aircraft finance transactions by creating an international harmonised legal framework to govern the registration of international interests (such as mortgages and leases) in helicopters, aircraft frames and aircraft engines over a certain size and engine capacity. It also aims to provide a framework for how disputes under the treaty are managed. This includes the ability of asset owners to recover their aircraft equipment should an airline default on repayments. The Government has carefully considered all the views of respondents to the call for evidence, including the additional information presented by the AWG. As a result of the evidence submitted, the Government has decided to proceed with ratification of the treaty.
- 3.2. The aviation and aerospace industries make a significant contribution, both directly and indirectly to the UK economy. The air transport sector’s turnover is around £26 billion and the sector provides around 120,000 jobs in the UK, supporting many more jobs indirectly.¹ These figures exclude the aerospace industry which includes manufacturing. The aerospace sector contributes £24 billion to the economy every year and supports 230,000 jobs across the UK. UK aerospace has a 17% global market share, making it the number one aerospace industry in Europe and second globally behind the US and it exports circa 75% of what it produces².
- 3.3. UK airlines need to raise large amounts of finance in order to purchase or lease new aircraft and/or aircraft engines. These transactions often involve multiple parties located in more than one jurisdiction across multiple time zones. As set out in the summary of responses to the call for evidence, the majority of those who responded to the call for evidence said that cross-border aircraft financing and leasing affects and increases the complexity of aircraft finance transactions giving rise to conflict of laws issues. Many of those who responded to the consultation said that this often resulted in new legal documents being drafted to encompass the different jurisdictional legal rules and procedures, resulting in a multitude of legal documents being produced. The complexity of such transactions increases when repossession, deregistration and engine rights are considered.
- 3.4. However, a minority of respondents did not agree that cross-border financing and leasing increased the complexity of transactions. These respondents thought that, generally, parties involved in cross-border transactions agree at the outset which

¹ *Draft Aviation Policy Framework* – Department for Transport – July 2012

² *Lifting off – Implementing the Strategic Vision for UK Aerospace* – HM Government – March 2013

law will apply. In these circumstances, UK law is normally the applicable law which is seen to be reliable and robust.

- 3.5. The majority of respondents argued that where cross-border finance and leasing transactions are concerned, legal outcomes are less predictable, this is the case whenever there is a conflict of law. However, a minority of respondents disagreed and said that the predictability of legal outcomes is usually quite clear when UK law is applied to transactions.
- 3.6. The Government agrees with the majority of respondents that the cross-border nature of aircraft financing and leasing increases the complexity of these transactions and the unpredictable nature of legal outcomes. A single international harmonised framework could reduce these problems.
- 3.7. The majority of respondents to the call for evidence said that ratification of the treaty would lower the cost of raising financing since financiers would no longer need to charge higher rates to borrowers as the risk of lending capital would be reduced. A number of respondents mentioned the OECD's Aviation Sector Understanding (ASU) which allows Export Credit Agencies (ECAs) to give a discount to airlines applying from jurisdictions which have ratified the treaty. If the UK ratified the treaty with the necessary optional provisions, UK airlines applying for export credit support would be eligible to be considered for the OECD ASU discount. Traditionally, UK airlines have relied on commercial banks to finance new aircraft, however many respondents said that the financial crisis had led to less availability of private bank finance with borrowers increasingly seeking support from ECAs.
- 3.8. The majority of respondents thought that a reduction in the cost of finance would particularly apply to airlines seeking to raise finance in the capital markets through Enhanced Equipment Trust Certificates (EETCs), already an established source of finance for US airlines. EETCs are bonds which airlines issue to finance aircraft. Under such an arrangement the airline establishes a trust which issues certificates to investors and uses the raised funds to purchase the required aircraft which is leased back to the airline. The airline makes lease payments to the trust which passes these on to investors in the form of bond interest. EETCs are rated by credit agencies and one of the numerous factors they consider in reaching their decision is how quickly a creditor can recover the asset should the airline fail to keep up with repayments. To date, only one UK airline has chosen to raise finance in this way.
- 3.9. A minority of respondents did not think that the cost for cross-border transactions is a problem for UK airlines.
- 3.10. The Government agrees that ratification of the treaty may reduce costs for airlines who wish to raise finance through the capital markets. The Government also acknowledges that ratification of the treaty is just one of many factors financiers and ratings agencies consider when making their decisions and so the financial benefit of ratifying the treaty is difficult to quantify. The capital markets are just one funding option available to airlines and many airlines will decide to raise finance in other ways. Depending on an airline's individual circumstances and how they

choose to raise finance, ratification may not have a significant effect on financing costs.

- 3.11. The treaty sets out a number of options for Contracting States around how they implement the treaty. These options are set out in declarations contained within the treaty. The Government will consult further on these options.
- 3.12. The Government notes that the majority of respondents were in favour of adopting one of the declarations contained within the treaty in relation to insolvency remedies. The reason given was that this declaration, called alternative A, would provide financiers and manufacturers with greater predictability that an asset would be returned to the creditor or the default cured within a specified period. The majority of respondents said that this would reduce the cost of raising finance for UK airlines seeking funding through the capital markets and that it was one of the declarations which make up the ASU. The Government notes that the majority of countries which have ratified the treaty have opted for alternative A with a specified time period of 60 days. However, some respondents to the call for evidence stated they had not encountered any difficulty recovering assets in the UK and that the remedies under alternative A are not needed since UK law is well-respected and offers a good level of protection for creditors. The Government agrees that the provisions under insolvency law for creditors in the UK are strong and will consult further on the insolvency options contained in the treaty.
- 3.13. Aircraft engines are routinely moved from one aircraft to another for maintenance purposes and the majority of respondents thought that ratification would help to reduce the costs of engine financing because, under the treaty, security interests against aircraft engines can be registered separately. However a minority of respondents thought that the CAA which runs the UK national register could adapt its processes to offer such protection on the UK Register of National Mortgages. The Government agrees with the majority of respondents that there is an advantage in being able to register charges against aircraft engines separately which is not possible on the UK's national register. The provisions to register charges on engines separately with the International Registry would be an advantage for engine manufacturers and financiers, reducing the level of risk in any financial transaction and therefore potentially reducing the cost of financing aircraft engines.
- 3.14. However the Government also recognises that a critical mass of countries is needed to ratify the treaty in order for creditors to fully benefit from these provisions in the International Registry. The Government does not think that ratification of the treaty by the UK would resolve concerns raised by a number of respondents to the call for evidence that in some jurisdictions aircraft engines are indivisible from the aircraft frame. These concerns would not be resolved unless the jurisdiction in question had ratified the treaty.
- 3.15. The vast majority of respondents to the call for evidence said using the International Registry system would be advantageous because:
 - It is easy to use and available on-line and, unlike the UK's register, allows access twenty-four hours a day, seven days a week

- Many new aircraft finance transactions are already registered with the International Registry
- Prospective interests may be registered taking the pressure off expensive closing logistics
- Priority rules are clear and objective. This enables interested parties to search the system and determine exactly where they stand in terms of registered interests.

3.16. However, a minority of respondents did not think the International Registry would offer additional benefits above those provided by the CAA's register stating that:

- The general aviation market is currently well protected by the UK's CAA and the US Federal Aviation Administration (FAA) Register. However, some respondents did recognise that the International Registry could protect their interests if an aircraft was detained abroad.
- Ratification would introduce another level of unnecessary bureaucracy and duplicity, with additional costs and inefficient administration

3.17. The Government agrees with the majority of respondents to the call for evidence that there are benefits to using an International Registry which is open twenty-four hours a day, seven days a week. This would enable interests to be registered quickly and simply, an issue of particular importance for parties involved in aircraft finance transactions taking place across multiple jurisdictions and different time zones. A single International Registry would make it simpler and less burdensome for financiers to check whether any party already held an interest which would take precedence over their own interest. In these cases a financier would only be checking one register rather than multiple national registers. However the Government recognises that for these benefits to be fully realised, it is necessary for a critical mass of countries to ratify the treaty.

3.18. The Government notes that the majority of respondents commented that ratification of the treaty would resolve the uncertainty they feel exists around the application of the *lex situs* rule on aircraft mortgages. The Government does not agree with this view as application of the *lex situs* rule would depend on a number of factors, including whether the jurisdiction in which the aircraft was located at the time the mortgage was perfected had also ratified the treaty. However the Government does agree that ratification may resolve some of the concerns raised by respondents with regard to the *lex situs* rule.

3.19. Overall the Government agrees that ratification of the treaty would benefit the UK economy by creating a harmonised legal framework to register interests against helicopters, aircraft frames and aircraft engines. This could benefit UK airlines through lower financing costs, particularly for airlines choosing to raise finance through the capital markets. Financiers and manufacturers would also benefit from the ability to register interests against aircraft engines separately and from the service offered by the International Registry which allows interests to be registered twenty-four hours a day, seven days a week.

4. What happens next?

- 4.1. The Government is committed to ratifying the treaty for the reasons above. The treaty contains a number of options for implementation which are set out in the various declarations contained within the treaty. The Government will hold a consultation on these options to gather the views of stakeholders and decide how to proceed with implementation.
- 4.2. The UK Government retains responsibility for international relations and the regulation of aviation and air transport as set out in the Scotland Act 1998 and the Northern Ireland Act 1998. However, Northern Ireland Ministers may legislate on matters of civil aviation and navigation with the permission of the Secretary of State. Scottish Ministers and Northern Ireland Ministers have an interest in the implementation of this treaty and have been consulted on this response to the call for evidence. The subject matter of the treaty is not within the legislative competence of the Welsh Assembly under the Government of Wales Act 2006.
- 4.3 The Government will consult with the Crown Dependencies and Overseas Territories on whether ratification will be extended to any or to all of them at this time.

5. Further enquiries

- 5.1. If you have any queries about this response to the Call for Evidence, please contact:

Hayley Gowen

4th Floor – Abbey 1

Department for Business, Innovation and Skills

1 Victoria Street

London

SW1H 0ET

020 7215 6096

Hayley.gowen@bis.gsi.gov.uk

6. List of Respondents

Airbus S.A.S

Aircastle Advisor LLC

Aviation Capital Group

Aviation Working Group

Bermuda Department of Civil Aviation

Bombardier Inc

British Airways

British Exporters Association

Cayman Islands Government

Civil Aviation Authority

Clifford Chance LLP

David Baggot, Solicitor

Deutsche Bank AG London

Embrarer

Engine Lease Finance Corporation

GE Capital Aviation Services

Goldman Sachs

Helaba Landesbank Hessen-Thüringen

Maples and Calder

Natixis Transport Finance

Norton Rose LLP

Rolls-Royce PLC

Royal Bank of Scotland Aviation Capital

Singers Corporate Asset Finance

The Boeing Company

The Falkland Islands Government

TUI Travel PLC

Unite the Union

Virgin Atlantic Airlines

© Crown copyright 2013

You may re-use this information (not including logos) free of charge in any format or medium, under the terms of the Open Government Licence. Visit www.nationalarchives.gov.uk/doc/open-government-licence, write to the Information Policy Team, The National Archives, Kew, London TW9 4DU, or email: psi@nationalarchives.gsi.gov.uk.

This publication available from www.gov.uk/bis

Any enquiries regarding this publication should be sent to:

Department for Business, Innovation and Skills
1 Victoria Street
London SW1H 0ET
Tel: 020 7215 5000

If you require this publication in an alternative format, email enquiries@bis.gsi.gov.uk, or call 020 7215 5000.

BIS/13/1252