

The Cape Town Convention – one year on

On 1 March 2006 the Cape Town Convention on International Interests in Mobile Equipment 2001 came into force with respect to aircraft objects, with the eighth ratification of the Protocol on Matters Specific to Aircraft Equipment. This article comments on developments regarding the Convention over the last year and on how well the Convention has been received by the aviation industry.

Since the Protocol came into force, the following States have ratified the Protocol: Senegal, Angola, Afghanistan, Kenya, Mongolia, Columbia (effective 1 May, 2007) and South Africa (effective 1 June, 2007). There are now 15 ratifications.

In the first 10 months of operation, the International Registry certificated approximately 8,000 users/administrators, registered approximately 33,000 interests against approximately 15,000 aircraft objects and performed approximately 33,500 searches. About 90% of the activity originates from the US.

Reactions from the industry have, unsurprisingly, been mixed. On the negative side, it is said that implementation of the International Registry did not go as smoothly as some had hoped. When the website went online on 1 March 2006, various problems quickly emerged, many relating to the functioning and content of the website. There was a steep learning curve for those involved in registrations. The large number of people simultaneously seeking to become registered users put a strain on the system. Some credit card companies initially rejected payments on the basis that the International Registry was unknown to them.

In some initial cases, aircraft closings were delayed from a few days to a few weeks when buyers and sellers did not properly complete the necessary online registrations. Some users were unable to download the digital certificates issued by the International Registry due to strong internet firewalls maintained by their internet providers; others found that the International Registry's verification process was taking up to two weeks to complete; and some could not initially register against their aircraft because their particular aircraft was not listed on the website. An informal survey of US aircraft brokers, dealers, title companies, aircraft manufacturers and trade associations suggested that the initial glitches in the online registration system were in the process of being rectified and most users who had used the system a few times encountered less problems once they had initially registered. Aviareto has worked very hard to improve the system and much has been

done to solve the problems.

For US-registered aircraft transactions, there was previously only the need to register with the FAA and pay modest filing fees. The Convention is an additional layer of administration with substantially increased filing fees. One common criticism from users involved in the sale and purchase of US-registered aircraft is that the new procedures take time and registration costs are expensive. Given that Aviareto is a private company with no governmental financial support, it is not surprising that registration fees are higher than the FAA's standard fees.

Aircraft title insurance providers in the US are now offering title insurance policies covering Cape Town filings by way of a policy endorsement in addition to the traditional cover for FAA filings.

The International Registry's registered website is www.internationalregistry.com.

Someone registered another address, www.internationalaircraftregistry.com, and called itself the "International Aircraft Registry". This website caused some consternation in the industry as it directed those searching for details of the International Registry to this website. A series of misleading e-mails and postcards were sent to various aircraft owners enclosing official-looking notices from the "International Aircraft Registry" with ominous warnings to immediately contact that entity and enter into a registration agreement to register their aircraft. That website contained misleading and erroneous information including an indication that registrations must be renewed annually. The website further alleged that using their services avoided the need to contact a lawyer or title company. It appeared that this website was set up by fraudsters and has since been closed down.

The implementation of the Protocol has sparked off a potential battle at the World Trade Organisation (WTO). The WTO seeks to maintain a level playing field between countries that help subsidise the sale of aircraft in their country through export loan guarantees. New rules are currently being considered and these are expected to take into account the Convention. The Organisation for Economic Co-operation and Development (OECD) is currently involved in seeking to broker a compromise to resolve the current issue.

On the positive side, in general it appears that many aircraft financing banks and financial institutions view the Convention favourably. The Convention creates a "prospective international interest" which is a new concept. This enables a notice to be filed with the International Registry

prior to the actual closing of the aircraft transaction. Once the transaction closes, no additional registration is required and priority is given to the prospective interest. This is of particular interest to banks and financial institutions. In addition, aircraft financing banks and financial institutions can obtain from their borrower or lessee an Irrevocable De-Registration and Export Request Authorisation in the form annexed to the Protocol, which is an extremely useful document to protect their interests.

US Ex-Im Bank is offering a one-third reduction of its exposure fee on asset-backed financings of new US-manufactured large commercial aircraft for buyers in countries that ratify/accede to and implement the Convention and the Protocol (including certain optional provisions specified by US Ex-Im Bank). The current offer applies to approvals issued until 31 March 2007. It is anticipated that the discount policy will be extended in some form although details are not currently available. Various meetings at OECD are in progress, which may have an impact on US Ex-Im Bank's willingness to continue to offer the one-third reduction.

Prior to the Convention coming into force it was common for clauses to be inserted into aviation financing documents relating to compliance and registration under the Convention. Now that the Convention is in force, it has added focus regarding such further assurance clauses. It is now common for aviation financing documents to contain detailed further assurance clauses relating to actual and potential Convention registrations, especially aircraft sale and purchase agreements, aircraft lease agreements and aircraft mortgages.

Despite 15 ratifications, the overall impact of the Convention is still limited. It will have a far greater impact on the aviation industry as and when further states ratify the Protocol. A significant development will be when EU member countries ratify the Convention. At present, the European Commission and EU member states are still considering the ratification of the Convention by EU member states. In summary, those involved in the aviation industry are coming to terms with living with the new rules, new terminologies and new registration requirements.

Regarding the future development of the Convention itself, the rail industry is currently considering a Railway Rolling Stock Protocol in respect of rolling stock and Unidroit is working on the text of a Space Assets Protocol.

For further information please contact Austen Hall, Partner, Hogan & Hartson at aehall@hbhlaw.com