

# The Cape Town Convention – now coming into force

A significant milestone in the aviation industry is that the Cape Town Convention on International Interests in Mobile Equipment 2001 comes into force on 1 March 2006 regarding aircraft objects.

The Convention was designed to overcome the problem of obtaining secured and readily enforceable rights in mobile equipment and seeks to overcome one of the problems faced by the industry that national laws differ in their approach to security rights in mobile equipment. It focuses on aircraft objects, rolling stock and space assets and establishes a commercial, comprehensive international legal framework relating to the creation, recognition, priority and enforcement of security and leasing interests in such assets. Different Protocols can apply to different classes of mobile assets, the aim being to seek to ensure that the specific needs of the various industries are met. The Convention itself entered into force on 1 April 2004. To date, there is only one Protocol, the Protocol on Matters Specific to Aircraft Equipment (the "Protocol"). References to "the Convention" mean the Convention as supplemented by the Protocol and therefore as applying to aircraft objects.

## Key features

The Convention creates a new concept of "international interest" in "aircraft objects"; provides for the registration and priority of international interests and other interests at a newly established International Registry; provides creditors

with a range of basic default and insolvency remedies (and, in a default situation, seeks to grant creditors speedy interim relief pending a final decision of their claim); allows contracting parties a wide discretion as to whether or not the Convention will apply and preserves the importance of the national law of contracting states to make declarations on a wide variety of matters.

## What are aircraft objects?

Aircraft objects are defined to be: airframes that can carry at least eight persons (including crew) or goods over 2,750 kg; jet engines with at least 1,750lb of thrust and turbine or piston engines with at least 550 rated take-off shaft horsepower and helicopters that can carry at least five persons (including crew) or goods over 450kg. Aircraft used by military, customs or police services are excluded.

## Application of the Convention

The Convention applies to contracting states. At present there are only eight: Panama, Ethiopia, Nigeria, Pakistan, the USA, Oman, Ireland and Malaysia. Of considerable importance is the fact that the USA has ratified the Convention and the Protocol.

## What can be registered?

The International Registry is being established for the registration of: international interests; prospective international interests; registrable non-consensual rights and interests; assignments and prospective assignments of international interests; acqui-

sitions of international interests by legal or contractual subrogation under applicable laws; notices of national interests and subordinations of interests in any of the above.

An international interest is defined as an interest in a uniquely identifiable object (a) granted by a chargor under a security agreement, or (b) vested in a person who is a conditional seller under a title reservation agreement or (c) vested in a person who is a lessor under a leasing agreement. The Convention has specific definitions for these terms and others. An international interest in an object extends to its "proceeds".

## Application of the Convention

For the Convention to apply and for an interest to be an international interest, it must apply to an aircraft object and certain requirements must be met: (a) the debtor must be situated in a contracting state at the time of the conclusion of the agreement creating or providing for the international interest – the fact that the creditor is located in a non-contracting state does not affect the applicability of the Convention; (b) whether or not the debtor is situated in a contracting state, it also applies where an aircraft or a helicopter is registered in a contracting state or where the aircraft or helicopter is registered pursuant to an agreement envisaging such registration; (c) for an interest to be an "international interest", the underlying agreement must be in writing, relate to an object of which the chargor, conditional seller or lessee

has power to dispose, enable the object to be identified by reference to its manufacturer's serial number, the name of the manufacturer and its model designation and, in the case of a security agreement, enable the secured obligations to be determined (but without the need to state a sum or maximum sum secured).

## The International Registry

The International Registry is 100% electronic and goes live on March 1, 2006. Log onto [www.internationalregistry.aero](http://www.internationalregistry.aero) for registrations, amendments, extensions and discharges of registrable interests in aircraft objects. Registrations will be made by submitting the required information on the website. It will be possible for searches to be undertaken over the internet. Users will need to be registered and vetted. It will not be necessary for original or copy documents to be lodged. Registrations are completed by using various dropdown menus and inserting the required information in the relevant fields and paying the relevant fee. Registration and search certificates will be emailed to users.

## How does it affect the industry?

The Convention has already started to have an effect on aviation transactions. For some while, legal documentation has included "Cape Town clauses" – glorified further assurance clauses. These clauses will become far more common and, if financiers and lessors have not already updated their stand-

ard documents, they will certainly do so now.

The Convention applies to international transactions entered into after 1 March, 2006. Where an existing transaction is amended and/or restated, it will be possible to register an international interest which is created.

The Convention has benefits for all in the industry. For airlines, reduced cost of finance is one. US Ex-Im Bank has announced an extension of its one-third guarantee fee reduction for transactions involving countries that have ratified the Convention. Financiers benefit from enhanced security.

It is now common for Term Sheets to seek to identify potential registrations.

The Convention provides for the recording of de-registration documents in the form annexed to the Convention. Financiers and lessors will increasingly require their debtors to execute such documents, if required.

Lessees having a purchase option may wish to register their interests but will need agreement from the relevant parties to do so.

The Convention benefits engine financiers and lessors as engines are recognised as independent property.

In the US, there will be a significant effect on aviation transactions. The FAA is the central portal to be used in the USA. For US registered aircraft transaction, the parties will still make registrations with the FAA and, where relevant, a unique code will be given so that the applicable international registrations can then be made.

This is one small step for mankind but a huge leap for the aviation industry.

*Article contributed by Austen Hall, Partner, Hogan & Hartson, London*

# MKA to enter the Chinese market

MKA Capital, which was formed by the reverse merger of Financial Telecom Ltd (Fintel) and MK Aviation, plans to tap the fast-growing Chinese market.

Following the merger, which was complete in November, Fintel now has 75% of the issued and outstanding shares of MK Aviation. Mory Kraselnick owns more than 50% of the voting rights and is the chairman of the board.

MK Aviation was formed in 1978 and primarily has focused on the Central and South American markets. MKA Capital plans to expand the aircraft leasing and financing operations into Asia, particularly China, where airlines are ordering new aircraft. The company plans to place the older aircraft coming out of China into Latin America, in which the company has close ties.

"Latin American carriers want used aircraft and the big lessors don't want to be in the business of used aircraft. There is a lot of growth in this market and a lot of start-

ups," said Ariel Kraselnick, director of marketing at MKA Capital. "A lot of companies don't want to do business in Latin America because they believe it is too risky. If you look at Latin American carriers they have better pricing power than their European or US counterparts. Yes, there is a risk in Latin America but it is not risky."

MKA engaged Trenwith Securities to raise \$140m in debt financing that will be used to purchase additional aircraft and engines. Trenwith is an independent investment banking affiliate of BDO Seidman, which is a member of BDO International.

MKA recently purchased an ex-Delta Air Lines Boeing 737-300 (23596) for part out and a Boeing 737-200 on lease to Delta until October. The aircraft will then be released to a South American lessee. MKA also purchased a P&W JT8D-17A engine. The purchase of these assets increased the consolidated asset portfolio by approximately

\$2.5m. MKA says the leases will generate additional revenues of approximately \$900,000 annually over a five-year term.

The company currently has a portfolio of five aircraft and 14 engines. The five aircraft include an MD-80 on lease to Aerpostal, two 737-300s on lease to Sky Airlines, the 737-200 on lease to Delta, and a 737-300 that will be parted out by AAR. MKA is currently in negotiations for the purchase of a JT8D-200 engine.

"We are currently bidding for a number of aircraft to meet the demands of our airline customers. Our policy is to purchase aircraft and engines only when we have identified the leasing customers for such equipment, which allows us to manage our operating risks and cost of capital effectively," said Kraselnick.

MKA says it is also interested in the freighter market, particularly 737-300s and 737-500s.

MKA Capital has offices in Panama, China, and USA.

## ExpressJet repurchase programme

ExpressJet Holdings' board of directors has authorised the inclusion of the company's 4.25% convertible notes due 2023 in its \$30m securities repurchase programme, which includes the company's common stock. Since it announced the programme in July 2005, the

company has repurchased \$5.6m of common stock. The company expects any purchases of notes or stock to be made in the open market or in privately negotiated transactions. The timing of any repurchases under the programme will depend on a variety of factors, including

market conditions, and may be suspended or discontinued at any time. Common stock acquired through the repurchase programme will be available for general corporate purposes, and convertible notes repurchased under the programme will be cancelled.