

Convention on International Interests in Mobile Equipment, done at Cape Town on 16 November 2001

Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment, done at Cape Town on 16 November 2001

Introduction

- 3.1 On 1 November 2012, the *Convention on International Interests in Mobile Equipment, done at Cape Town on 16 November 2001*, and the *Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment, done at Cape Town on 16 November 2001*, were tabled in the Commonwealth Parliament.

Background

- 3.2 The Convention and Protocol are known as the ‘Cape Town Convention’. The Cape Town Convention entered into force generally on 1 March 2006,¹

¹ National Interest Analysis [2012] ATNIA 24 with an attachment on consultation *Convention on International Interests in Mobile Equipment (Cape Town, 16 November 2001)* [2001] ATNIF 35, and the *Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment (Cape Town, 16 November 2001)* [2001] ATNIF 36, (Hereafter referred to as ‘the NIA’), para 1.

introducing a uniform international legal framework to protect the financiers of aircraft.² A uniform framework should provide a mechanism for persons with a financial interest in aircraft (such as aircraft lessors, sellers or financiers) to recover their assets in the event that an airline defaults on its payments.³ The key objectives are to:

- provide financiers of aircraft with increased certainty around Australia's insolvency laws as they apply to highly mobile equipment; and
- allow for increased access by the Australian aviation industry to cheaper asset financing and sources of finance external to the domestic market.⁴

3.3 As at 3 July 2012, 45 States and one Regional Economic Integration Organisation (the European Union) had become party to both the Convention and the Protocol.⁵

Overview and national interest summary

3.4 The Cape Town Convention is intended to address the issue of inconsistent security and access to finance for mobile equipment creditors. The Convention will provide a homogenous securities system for such creditors.⁶

3.5 The Convention establishes an International Registry where creditors record security interests in mobile equipment. In the event of default, the International Registry gives a registered interest priority over other interests in the same equipment that are either registered later in time or are unregistered. The Convention also provides basic remedies in the event of default, increasing protection of creditors' interests and reducing their risks.⁷

3.6 The Protocol modifies and supplements the Convention in relation to aircraft. It enables security interests in the following types of aircraft to be registered on the International Registry:

- aeroplanes certified to transport at least eight persons including crew, or goods in excess of 2 750 kilograms;

2 NIA, para 5.

3 NIA, para 4.

4 NIA, para 7.

5 NIA, para 8.

6 NIA, para 8.

7 NIA, para 9.

- jet engines of at least 1 750 lb of thrust or its equivalent, and turbine or piston engines of at least 550 rated take-off shaft horsepower or its equivalent; and
 - helicopters certified to transport at least five persons including crew, or goods in excess of 450 kilograms.⁸
- 3.7 The Protocol offers two additional remedies to creditors in the event of default. The first is the removal of an aircraft from a State Party's civil aircraft register, and the second is the export of the aircraft to another State. It also establishes a special insolvency regime in relation to aircraft objects.⁹
- 3.8 Creditors who do not have access to the measures set out in the Convention and the Protocol remain subject solely to the domestic laws and processes of various jurisdictions at any given time, with varying levels of creditor protection. This instability has caused financiers to drive up their costs as a buffer against these risks, which are then passed on to the airline industry.¹⁰
- 3.9 It is worth noting that, under the Cape Town Convention, parties to financing agreements retain the right to determine what constitutes 'default' and what will give rise to default remedies.¹¹

Reasons for Australia to take the proposed treaty action

- 3.10 The NIA identifies two significant benefits arising from ratification of the Cape Town Convention: improved creditor security; and enhanced access to finance by Australian airlines.
- 3.11 According to the NIA, the collapse of Ansett in 2001 triggered a series of reforms of Australian law to deal with the problems that collapse highlighted in the domestic uniform securities framework.¹²
- 3.12 However, the aviation industry has expressed concern that this system does not provide for the unique financing requirements applicable to aviation, which have a significant international aspect, resulting from their mobility and the depreciative nature of aircraft.¹³

8 NIA, para 10.

9 NIA, para 11.

10 NIA, para 11.

11 NIA, para 18.

12 NIA, para 13.

13 NIA, para 13.

- 3.13 The NIA argues that accession to the Cape Town Convention will bridge this gap and reduce creditor risk exposure by providing a securities framework that applies across borders and allows for the prompt repossession of an aircraft asset or the taking of other action by a creditor upon insolvency.¹⁴ According to the NIA:
- By enhancing financier security and reducing their risks, the Cape Town Convention will assist Australian airlines in achieving significant savings on financing costs, at a time when industry participants are seeking to both recover from the impact of the global financial crisis and modernise their fleet.¹⁵
- 3.14 For airlines, accession to the Cape Town Convention may result in reduced financing costs, primarily achieved by lowering creditor risk which will, in turn, manifest itself in the form of cheaper finance for airlines for the purchase of aircraft.¹⁶
- 3.15 The NIA argues that the financial benefits will be best realised through the 2011 Sector Understanding on Export Credits for Civil Aircraft (ASU), developed by the Organisation for Economic Co-operation and Development.¹⁷
- 3.16 The ASU provides a common framework for export-credit agencies of Australia, the Republic of Korea, Norway, Switzerland, New Zealand, the European Union, the United States, Japan, Brazil and Canada to finance aircraft objects.¹⁸ A fee discount is offered for airlines of countries that are party to the Cape Town Convention provided they have made all specified 'qualifying declarations' upon becoming party to the Cape Town Convention. Should the Convention be ratified, Australia intends to make the requisite qualifying declarations upon accession.¹⁹

Obligations

- 3.17 Under Chapter III of the Convention and Chapter II of the Protocol, Australia will be required to observe and make available particular remedies to creditors in the event of debtor default, including rights of

14 NIA, para 14.

15 NIA, para 6.

16 NIA, para 15.

17 NIA, para 15.

18 "Aircraft objects" are airframes (aircraft bodies), aircraft engines and helicopters (Article 2(3)(a) of the Convention). NIA, p.1.

19 NIA, para 16. The relevant declarations can be found in para 1.17 of the Regulation Impact Statement.

repossession, sale and lease and rights to proceeds from objects subject to a security interest. All remedies are required to be carried out in a 'commercially reasonable manner'.²⁰ The ranking in priority of competing interests in Chapter VIII of the Convention will prevail over the *Personal Property Securities Act 2009* (PPS Act), to the extent of any inconsistency.²¹

- 3.18 Australia will have obligations arising from the declarations to the Cape Town Convention which Australia intends to make upon accession. For example, if a declaration is made in respect of Articles XI and XIII of the Protocol, the Civil Aviation Safety Authority would be required to record an irrevocable de-registration and export request (IDERA) form and make available certain remedies to the creditor within five working days. The IDERA form is the mechanism by which a creditor could procure the deregistration and export and physical transfer of the aircraft object from the territory in which it is situated.²²
- 3.19 Australian authorities would also be obliged to co-operate and assist in the exercise of those remedies. The remedies could include the right to procure the removal of the aircraft from the Australian Civil Aircraft Register in the event of default, where this has previously been agreed by the parties to the financing arrangement.²³
- 3.20 Australia is further obliged to permit a person to exercise those remedies and other remedies available under the Convention by recourse to Australian courts.²⁴

Unpaid employment entitlements in the event of insolvency

- 3.21 Under Australian law if a company is liquidated, the rights of secured creditors have priority over the right of unsecured creditors, including employee entitlements. The Committee heard that this situation would not alter with accession to the Cape Town Convention:

Whilst the Cape Town Convention does allow a Contracting State to declare under Article 39 certain categories of non-statutory liens that can have priority over a registered international interest, this provision cannot be used to alter priorities that are currently

20 "Remedies are exercised in a 'commercially reasonable manner' if the creditor takes proper steps to safeguard an object from loss or damage upon repossession and makes reasonable efforts to obtain the best price on sale of an object". Department of Infrastructure and Transport, *Submission 5.2*, p. 2.

21 NIA, para 19.

22 NIA, para 20.

23 NIA, para 20.

24 NIA, para 21.

applicable under national law. This means that a declaration cannot be made under Article 39(1) of the Cape Town Convention that would prioritise employee entitlements over the rights of secured creditors in the event of insolvency/liquidation.²⁵

Implementation

- 3.22 New legislation will be introduced to give the Convention the force of law in Australia. Minor amendments may also be required to existing legislation.²⁶
- 3.23 The *Personal Property Securities Act 2009* (PPS Act), introduced following the collapse of Ansett, may require minor amendments to reflect the prevalence of the Convention to the extent of any inconsistency. The *Corporations Act 2001* may require minor amendments to implement the Cape Town Convention. The *Civil Aviation Act 1988* may require amendment to confer upon the Civil Aviation Safety Authority (CASA) the powers to record IDERAs and create new regulations to this end, depending on how Australia decides to approach the administration of IDERAs.²⁷
- 3.24 The Civil Aviation Safety Regulations 1998 will require amendment to allow for Articles XIII (which requires the recording of an IDERA) and XI (remedies for insolvency) of the Protocol to be effectively carried out.²⁸

Costs

- 3.25 According to the NIA, accession to the Cape Town Convention will not result in significant financial implications for government stakeholders, business or industry. This is largely because registration under the Convention is voluntary and subject to commercial negotiations between creditor and debtor.²⁹
- 3.26 Airlines and creditors that choose to register interests in accordance with the Convention will be subject to a small administrative fee (one-off fee of US\$200 for first time users; registration and search fees ranging from US\$35 to US\$100). It is anticipated that these low costs will be offset by the
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25 'It is important to note that the secured creditors only have rights over the uniquely identifiable asset registered on the International Registry.' Department of Infrastructure and Transport, *Submission 5.2*, pp. 2-3.

26 NIA, para 22.

27 NIA, paras 23-24.

28 NIA, para 25.

29 NIA, para 27.

broad benefits – financial and otherwise – available under the Convention.³⁰

Conclusion

- 3.27 The Cape Town Convention introduces a uniform international legal framework to protect the financiers of aircraft by providing a mechanism for persons with a financial interest in aircraft to recover their assets in the event that an airline defaults on its payments. This is intended to address the issue of inconsistent security and access to finance for mobile equipment creditors.
- 3.28 The Committee agrees that current gaps in the Australian legislative framework do not provide for the unique financing requirements applicable to aviation, resulting from the mobility and depreciative nature of aircraft, and that the Cape Town Convention is a way to address this.
- 3.29 Together the Convention and Protocol should reduce creditor risk exposure by providing a securities framework that applies across borders and allows for the prompt repossession of an aircraft asset or the taking of other action by a creditor upon insolvency, and the Committee recommends that binding treaty action be taken.

Recommendation 7

The Committee supports the *Convention on International Interests in Mobile Equipment, done at Cape Town on 16 November 2001* and recommends that binding treaty action be taken.

Recommendation 8

The Committee supports the *Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment, done at Cape Town on 16 November 2001* and recommends that binding treaty action be taken.

30 NIA, para 28.

