

## **Aviation Newsletter – September 2015**

### **IMPROVING AIRCRAFT FINANCE IN BELGIUM\***

At the occasion of the last Ebace in Geneva, I spoke with various banks active in the business aviation sector. These banks are not only familiar with financing techniques in this sector, but they are trend-setters on how private aircraft may be financed.

They are active worldwide and they are familiar with the legal intricacies of many different jurisdictions.

But they are reluctant to finance private aircraft in Belgium.

And this purely based on reasons linked to how Belgian security and Belgian registration of aircraft work. Do these banks stop financing aircraft in Belgium? Certainly not. Do they feel uncomfortable and would they prefer a more lender-friendly system? Certainly yes.

#### **A Lender Friendly System**

Under Belgian law, an aircraft cannot be mortgaged.

The only form of security available on aircraft is a pledge. In order for a pledge to be valid and enforceable such pledge must meet the so called “dispossession requirement”.

This entails that the pledgor cannot be left in possession of the pledged asset. It is therefore impossible to finance aircraft or engines in Belgium under a loan structure coupled with a pledge on the asset.

Indeed, if the borrower is also the operator, it will not be able to pledge the relevant engine or aircraft if such goods are used by the operator itself.

As a consequence a Belgian law aircraft finance transactions contain always a lease or a hire purchase agreement which may not be attractive to lenders for accounting reasons.

If a loan is used and the borrower is the operator of the aircraft, the financing cannot be secured by using the aircraft as security (asset based finance). The consequence of this difficulty is therefore that the lenders may require other non asset-based types of security such as personal guarantees from the borrower or its shareholders.

The example I often use to explain the difference between asset based finance and other types of financing is the example of a loan granted to buy real estate. When borrowing money to buy a house, the bank will take a mortgage on the house which will be used as security therefore giving the possibility to the borrower to obtain funds to buy the house. If it is impossible to obtain a valid security on the house, the bank would ask the borrower to give other types of security such as a personal guarantee, security over the bank accounts of the borrower, etc. I believe that this example makes it clear how asset based finance mechanisms help borrowers having access to funds by allowing them to use the asset that they are willing to buy as security.

To add to the dismay of lenders (and Belgian borrowers alike), the Belgian aircraft registry is an ‘operator driven’ registry. This means that aircraft are registered in Belgium under the name of the operator and no publicity is given to security created on an aircraft. Lenders are more at ease with owner driven aircraft registries such as the French one. In France, an aircraft is registered under the name of the owner. This means that, under a classic lease agreement, the lessor will be indicated in

\* By Giulia Mauri, Head of the Aviation & Transport Department

the aircraft registry as owner of the aircraft. Moreover, if a lender has taken a mortgage on the aircraft, this will be clearly indicated on the registration certificate and in the French aircraft registry.

This is not how it works in Belgium. Even if a pledge has been created on a Belgian registered aircraft, this will not be published anywhere. There is therefore no possibility, for any third party or new lender to know if other security interests have been created on the aircraft that they intend to finance: they will have to rely on the representations and warranties of the borrower/lessee.

### **The law of 11 July 2013**

Belgium has recently adopted new legislation that will significantly reform how security interests may be taken on moveable goods.

The law of 11 July 2013 (the “Act”) is the final result of a long work of research that started in 2010 when the then Ministry of Justice commissioned a study aimed at preparing a bill for an in-depth reform of the Belgian regime of security interests over moveable goods.

The Act has several implications for aircraft finance transactions in Belgium as it allows to easily structure the financing of a Belgian registered aircraft through loan/pledge mechanisms instead of leasing arrangements.

The Act also has an important impact on engine financing as, once the Act will come into effect, engines could be pledged separately from the Aircraft.

The Act introduces several important innovations in particular in relation to perfection and enforcement of pledges over moveable assets.

#### *a) The national electronic registry*

The most important change introduced by the Act is undoubtedly the abolishment of the “dispossession requirement”. A pledge will now be created by the mere agreement of the parties and perfected through registration of the pledge in a national electronic registry of pledges.

The national registry of pledges will not be a purely public registry, but will only be accessible to pledgor and pledgee and to a list of parties to be determined by decree.

The abolishment of the dispossession requirement opens the Belgian market to new aircraft (and engines) financing structures as a loan coupled with a pledge will now be perfectly valid as the operator of the aircraft or engine will be able to remain in possession of the relevant assets and to grant a security interest over the same.

Unfortunately the national electronic registry has not been created yet and the entry into force of the Act has been postponed until 1<sup>st</sup> January 2017 unless the national electronic registry may be created before such date.

#### *b) Enforcement of a pledge*

Enforcement rules have also been significantly changed by the Act. If an event of default occurs, the pledgee will have the right to enforce the pledge without prior court authorisation. Enforcement may be carried out through a public or private sale of the asset, a lease or, if so agreed, the appropriation of the asset.

However, at least ten days before enforcing its pledge, the pledgee must inform the debtor or the pledgor of its intention to enforce the pledge.

If the pledgor intends to object to the enforcement, it will have to raise its objections within the ten days period before the competent judge of the attachments.

If the relevant agreement provides that the pledgee may repossess the asset, the value of the pledged asset must be determined by an expert or based on the fair market value of the asset at the time of the repossession.

### **Recent developments**

The Belgian Civil Aviation Authority seems to be aware that a change in the rules applicable to aircraft financing is needed. Some months ago, all Belgian airlines and operators were convened by the Belgian CAA in order to open a debate about the creation of an aircraft mortgage.

This initiative of the Belgian CAA is extremely positive as it shows interest in relation to a vital element for the development of a sound aviation sector in Belgium: easy access to financing.

I would however venture to suggest to the Belgian CAA that it might be simpler to link in the aviation related aspects to the already adopted reform of security interests in mobile goods. Indeed a pledge registered in the national electronic registry would have the same effect of a mortgage on an aircraft or an engine and it would not be necessary to start legislative proceedings again: it would be sufficient to encourage the creation of the electronic registry in a reasonable period of time.

Moreover, Belgium has ratified the Geneva Convention on security in aircraft, but it has never fully implemented such convention which provides that, for a Belgian security interest to be recognised in another contracting state, the Belgian security interest must be registered in a specific registry. Indeed, such registry has never been created. The national electronic registry to be created following the coming into effect of the Act could also be considered as an implementing measure of the Geneva Convention and finally bring Belgium to comply with such implementation.

In addition to the above, it would be useful for the Belgian CAA to monitor how such registry will be functioning so as to assure, for example, that the name of the owner of the aircraft or the engine and the name of the possible pledgee is clearly identified and that prospective lenders may have access to such registry and search, for example, on the basis of the serial numbers of the airframe and/or the engines.

### **Concluding remarks**

I consider that the Act is an important step towards modernisation of Belgian law on security interests and its provisions appear to be quite close to the system introduced by the Cape Town Convention on International Interests in Moveable Goods.

However, an important difference from the Cape Town system is that the national registry of pledges will not be freely accessible. A decree will indicate the persons authorised to access the registry.

This choice of the Belgian legislator is regrettable as it creates a group of preferred creditors which will have access to the registry and will therefore be able to better assess the situation of the relevant debtor as opposed to the other creditors which will not benefit of such right.

I believe that this reform of Belgian security interests over moveable goods, coupled with a renewed interest of the Belgian Civil Aviation Authority for financing and security related issues, create a unique opportunity to find a much needed solution to the issues raised by several banks in relation to Belgian financing of aircraft and engines and finally attract more liquidity to the country.