MASON HAYES & CURRAN

Alternative A of the Aircraft Protocol to the Cape Town Convention in Irish Restructuring Proceedings

Ireland is a global centre for aircraft leasing and financing. It is therefore important for those involved in leasing and financing of commercial aircraft and engines and for insolvency practitioners to have clarity as to how the insolvency provisions of the aircraft protocol to the Cape Town Convention are interpreted by the Irish courts.

The High Court has now provided that clarity in the Norwegian Air Shuttle case.

Background

Examinership

Examinership is an Irish restructuring process, akin to Chapter 11, albeit quicker and less expensive. It is a court supervised process which provides a general moratorium on enforcement for up to 100 days[1] to enable a scheme of arrangement to be put forward by the examiner to restructure the company.

There are two key features of examinership for those involved in aircraft leasing as aircraft owner, lessor or financiers;

- first, debts can be written down (but generally only to the value of the security) and,
- second, contracts can be repudiated, but not modified absent consensual agreement.

Related companies

Five companies in the Norwegian Group, each of which had its registered office and centre of main interests in Ireland petitioned the High Court for the appointment of an examiner to them and to their ultimate parent Norwegian Air Shuttle ASA ("NAS") as a related company. NAS is registered in Norway.

As Norway is not a Member State of the EU, the Recast Insolvency Regulation did not apply to NAS. However, the Court was content, to appoint an examiner to NAS on the basis that it was a related company, which is permissible under the Companies Act 2014 (Ireland). A related company includes a holding company or a subsidiary.

To appoint an examiner to a related company which is incorporated and carrying on business outside of Ireland, the Court had to be satisfied that such company:

1. had a real prospect of survival,
2. had a substantial connection to Ireland, and
3. the judgment of the Court would bind the parties to relevant agreements i.e. creditors whose debts had been

[1] *Up to 150 days during the COVID-19 pandemic.*

[2] *Section 517.*

crammed down in examinership could not ignore the scheme and sue for the full debt in another relevant jurisdiction.

This was technically the most difficult. Most of the relevant agreements to which NAS was a party were subject to English governing law and jurisdiction. Norwegian counsel opined that the courts of Norway would respect those clauses. English Queen's Counsel provided an opinion to the effect that the Irish Examinership was capable of recognition in the courts of England and Wales. Separately, NAS proposed to run parallel proceedings in Norway, if necessary.

Accordingly, the Court was willing to and made an order to appoint an examiner to NAS.[3]

In our view, there is a relatively small number of groups of companies with a non-Irish parent where the Irish Courts would likely be willing to make similar orders. This is because this order was made in light of the particular facts of the NAS group structure; its connection and relationship to the Irish airline operator group and supportive legal opinions from counsel in the relevant jurisdictions.

The Cape Town Convention

The Cape Town Convention (the "Convention") incorporating the protocol to the Convention on matters specific to aircraft equipment (the "Protocol") has the force of law in Ireland pursuant to the International Interests in Mobile Equipment (Cape Town Convention) Act 2005.

Article XI of the Protocol provides for alternate remedies on insolvency. As permitted under the Protocol, Ireland adopted Alternative A remedies.

Issues clarified

In the judgment approving the proposed scheme of arrangement,[4] the High Court set out, in very clear terms, a number of the rights and obligations of lessors, lessees and secured parties in relation to aircraft, when an airline operator/lessee in an examinership.

In particular, the judgement has clarified four matters of Irish law on the interpretation of the Convention.

1. Insolvency administrator

The Convention imposes certain obligations on the insolvency administrator. The term "insolvency administrator" is defined in the Convention[5] to include "a debtor in possession if permitted by the applicable insolvency law".

The Court held that, in examinership, the company is clearly "a debtor in possession".

Accordingly, for the purposes of the Convention (including the Protocol) both the company and the examiner are insolvency administrators.

2. Repudiation of leases

Article XI (10) Alternative A of the Protocol prohibits the modification of an agreement without the consent of the creditor counterparty, and Article XI(11) Alternative A states that paragraph 10 shall not be construed to affect the authority, if any, of the insolvency administrator under the applicable law to terminate the agreement

The Court held that, as a matter of Irish law being the applicable law to the insolvency administrator, the repudiation of a contract is an act of termination and not modification. Repudiation is therefore not prohibited by the Protocol. Moreover, as the company in examinership is included in the scope of the definition of insolvency administrator, the company can bring an application to repudiate leases in examinership.

[3] *In the Matter of Arctic Aviation Assets DAC & Ors [2020] IEHC 664.*
[4] *In the Matter of Arctic Aviation Assets DAC & Ors [2021] IEHC 268.*
[5] *Article 1(k).*

3. The obligation to redeliver the aircraft

Article XI (2) Alternative A of the Protocol provides:

"*Upon the occurrence of an insolvency-related event, the insolvency administrator or the debtor, as applicable, shall, subject to paragraph 7, give possession of the aircraft object to the creditor no later than the earlier of:*

(a) the end of the waiting period [60 days in Ireland]; and

(b) the date on which the creditor would be entitled to possession of the aircraft object if this Article did not apply."

Paragraph 7, which was not considered in the case provides:

"*The insolvency administrator or the debtor, as applicable, may retain possession of the aircraft object where, by the time specified in paragraph 2, it has cured all defaults other than a default constituted by the opening of insolvency proceedings and has agreed to perform all future obligations under the agreement. A second waiting period shall not apply in respect of a default in the performance of such future obligations.*"

The Court held that: "*there is nothing in the Cape Town Convention or Protocol to preclude a lessor or holder of security from exercising the self-help remedy of taking possession of the asset.*"

We are of the view that it is reasonably clear that where Article 11(2) Alternative A of the Protocol applies, it overrides the automatic stay in Irish law, however the Court was not called on to determine this issue, noting:

"*If any of the companies sought to rely against lessors on the protection of the court conferred by s. 520, the automatic stay, different questions would arise by reference to the Convention and the Protocol.*"

Accordingly, a creditor may rely on Article XI (2) Alternative A, to seek redelivery of aircraft after minimum period of 60 days, notwithstanding that the domestic moratorium period is longer under the examinership regime.

4. The cost of discharging third party liens

The Court, drawing on Australian and Malaysian jurisprudence, held that it would not be appropriate to require the company in examinership to discharge the claims of third party lienholders, or to effect physical delivery to a specific location, for the benefit of the contract counterparty in priority to all other claims against the company as a condition for permitting the company to repudiate a lease.

Accordingly, the company as lessee may be required to redeliver possession of aircraft. However, that redelivery will take place where the aircraft are located and where there are third party liens or detention orders over the aircraft, such as possessory liens of maintenance, repair and overhaul companies ("MROs"), airport authorities or otherwise, the lessor or secured party may have no alternative other than to discharge such liens. The cost of discharging such liens would give rise to a subrogated claim against the company. This would likely be treated as unsecured debt and, if the examinership is successful, crammed down in examinership.

Comment

The clarity provided by the judgments in the Norwegian Case is to be welcomed.

In particular, it is clear that Irish examinership can, in certain circumstances, be used to restructure an airline group provided that one or more group companies is registered in and has its centre of main interests in Ireland. Examinership may be possible on application and interrogation of the particular facts even where the ultimate parent of the group does not have its centre of main interests in Ireland.

However, it is important to note that any third party liens and detention orders, whether arising due to lessee's non-payment of repairer or mechanics fees; MRO fees or otherwise, are unlikely to be discharged by the company in examinership before the aircraft is redelivered to the lessor or secured party. Indeed, where they are pre-petition debts there are restrictions on the company's ability to discharge them.[6]

This emphasises that a lessor or secured party should closely monitor amounts owed by the lessee to third party MROs and agencies such as airport authorities and Eurocontrol who have statutory detention rights.[7]

With careful planning and advice, there may be some scope for lessors and secured parties to negotiate payment of certain pre-petition debts and certification of debts incurred during the examinership, which can mitigate risks in this regard.

The content of this article is provided for information purposes only and does not constitute legal or other advice.

Key contacts

Christine O'Donovan
Partner, Head of Aviation & International Asset Finance
+353 1 614 5082
codonovan@mhc.ie

Maurice Phelan
Head of Dispute Resolution
+353 1 614 5083
mphelan@mhc.ie

Frank Flangan
Partner, Restructuring & Insolvency
+353 1 614 5250
fflanagan@mhc.ie

Judith Riordan
Partner, Restructuring & Insolvency
+353 1 614 5201
jriordan@mhc.ie

[6] *Without leave of the Court or a recommendation in the independent expert's report presented with the petition for the appointment of the examiner.*
[7] *In the case of Eurocontrol this is possible via CEFA with the consent of the airline.*