

2023

## The Cape Town Convention Offers Registered International Interests Providing Maximal Security to American Lessees of Aircraft

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### Recommended Citation

B. Patrick Honnebier, *The Cape Town Convention Offers Registered International Interests Providing Maximal Security to American Lessees of Aircraft*, 88 J. AIR L. & COM. 817 (2023)

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**THE CAPE TOWN CONVENTION OFFERS  
REGISTERED INTERNATIONAL INTERESTS  
PROVIDING MAXIMAL SECURITY TO  
AMERICAN LESSEES OF AIRCRAFT**

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ABSTRACT

This paper focuses on the *acquisition* of aircraft by United States-based airlines. At present in the U.S., airlines are faced with a fierce competition, and to commercially survive, they keep advertising that they operate modern and safe aircraft. Since the beginning of aviation, there does not exist a fully state-owned “flag carrier” in the U.S. On the contrary, the commercial airlines market has always been in the hands of private undertakings. Traditionally, the airlines themselves have arranged the acquisition of their fleets of aircraft. For this purpose, they have to obtain loans from private banks and other non-governmental financial institutions. A substantial amount of credit is annually extended

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DOI: <https://doi.org/10.25172/jalc.88.4.4>

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to realize the acquisition of the costly aircraft. The credit is generally supplied through a "purchase-money loan" that is secured on the aircraft. This practice is called asset-based financing. In the U.S., the aircraft which are operated by the local airlines have generally been acquired by means of international finance and lease transactions.

As the acquisition of aircraft is extremely capital-intensive, the financier or lessor must be able to successfully enforce its proprietary interests in the specific aircraft. This requirement is of particular significance in the event that an airline defaults or becomes insolvent.

While the aforementioned need to safeguard the financiers and lessors is undisputed, this article firmly puts forward that also the lessees of aircraft must be adequately protected. The arguments contained in this contribution are substantiated by the *local laws* and *international aviation finance and lease conventions* which apply in the United States.

With respect to the local situation currently existing in the U.S., this contribution focuses on the relevant articles of the Uniform Commercial Code (UCC). Moreover, it refers to the manner in which these provisions have been implemented in the substantive property law of the State of New York. It is noted that in several other countries, the local airlines may obtain similar proprietary rights from the lessors. These foreign legal regimes aim, *inter alia*, to facilitate the creation, validity, and enforcement of the secured rights of the lessees of aircraft. Nevertheless, not all of these instruments are successful in providing the aircraft lessees with adequate security.

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I. INTRODUCTION

AT PRESENT GLOBALLY, the grave consequences of the COVID pandemic have decreased.<sup>1</sup> Consequently, one may label the international aviation financing and leasing practice as an aircraft operators’ market. At present, there is an increasing need<sup>2</sup> of modern and safe commercially and privately operated *aircraft objects*.<sup>3</sup> In this article, the term aircraft object means an *airframe*, *helicopter*, and *aircraft engine*. Besides, airframes and aircraft engines are jointly called *aircraft*.<sup>4</sup>

This contribution focuses on the issues relating to the *acquisition* of aircraft by U.S.-based airlines. It is noted that, to a large extent, similar problems arise in regard to acquiring helicopters and aircraft engines.

Moreover, at present there exists a very strong competition in the international aviation practice.<sup>5</sup> Consequently, to commercially survive in both economically-developed and developing

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<sup>1</sup> See Nigel Chiwaya, *Covid Deaths: Track the Latest Trends and Current Fatality Count*, NBC News (Dec. 23, 2022, 9:17 AM), <https://www.nbcnews.com/data-graphics/covid-deaths-track-latest-trends-fatality-count-rcna61052> [<https://perma.cc/3NZL-LYU2>].

<sup>2</sup> See *Boeing Market Outlook 2022-2031*, BOEING, <https://www.boeing.com/market/index.page> [<https://perma.cc/6XR8-8ZPZ>]; *Commercial Market Outlook 2023-2041*, BOEING, <https://www.boeing.com/commercial/market/commercial-market-outlook/index.page> [<https://perma.cc/UJW9-VLPM>]; see also *Global Market Forecast 2023-2042*, AIRBUS, <https://www.airbus.com/en/products-services/commercial-aircraft/market/global-market-forecast> [<https://perma.cc/CJ2D-5CK9>].

<sup>3</sup> For a definition of “aircraft objects,” see Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment, art. I(2)(c), Nov. 16, 2001, 2367 U.N.T.S. 615 (hereinafter Aircraft Protocol). However, the present contribution concentrates on aircraft (airframes and engines).

<sup>4</sup> See *id.* at art. 1(2)(a) for a definition of “aircraft.”

<sup>5</sup> *Airline Competition*, ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, <https://www.oecd.org/competition/airlinecompetition.htm> [<https://perma.cc/9HPE-FRWZ>].

countries,<sup>6</sup> the airlines continuously promote that they exclusively fly *new* aircraft.<sup>7</sup>

Historically, the operated aircraft were *owned* by the national *flag-carriers*.<sup>8</sup> These local airlines were fully financed by the governments of the states in which they were based.<sup>9</sup> The acquisition of their fleets was realized by imposition of compulsory levies on individuals and companies. Thus, ultimately the taxpayers funded the purchase of the aircraft of the flag-carriers.

Nevertheless, the situation in the United States was an *exception*, as in this country, only privately-financed airlines existed.<sup>10</sup> Presently, in the European Union (EU) and most other jurisdictions,

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<sup>6</sup> Not only in economically-developed areas such as the Middle East, Asia, Europe, and the U.S do the airlines operate modern aircraft. A prime example is Ethiopian Airlines, which keeps ordering new aircraft, including in 2022. Joanna Plucinska, *Ethiopian Airlines Expects to Order 130 Airbus, Boeing Jets Soon*, ZAWYA (June 20, 2023), <https://www.zawya.com/en/economy/africa/ethiopian-airlines-expects-to-order-130-airbus-boeing-jets-soon-cnfdm145> [<https://perma.cc/6WBX-GMPT>]. Ethiopia was the second state to adopt the Cape Town Convention in 2003. *Convention On International Interest In Mobile Equipment (Cape Town, 2001) - States Parties*, UNIDROIT, <https://www.unidroit.org/instruments/security-interests/cape-town-convention/states-parties/> [<https://perma.cc/WVV9-W32V>]. Since that year, it has substantially benefited from the financial advantages of the treaty. For Ethiopia's Cape Town Convention status and declarations, see *Declarations Lodged by the Federal Democratic Republic of Ethiopia Under the Airport Protocol at the Time of the Deposit of its Instrument of Ratification*, UNIDROIT, <https://www.unidroit.org/instruments/security-interests/cape-town-convention/states-parties/d-ethiopia-ct/> [<https://perma.cc/B7GC-F8GW>].

<sup>7</sup> See, e.g., Michael Jonga, *How Airlines Buy New Aircraft: A Mix of Price, Strategy and In-Flight Innovation*, AEROTIME HUB (Feb. 27, 2023), <https://www.aerotime.aero/articles/how-airlines-buy-new-aircraft-a-mix-of-price-strategy-and-in-flight-innovation> [<https://perma.cc/8H3B-ZJA6>].

<sup>8</sup> *Flag carrier*, WIKIPEDIA, [https://en.wikipedia.org/wiki/Flag\\_carrier](https://en.wikipedia.org/wiki/Flag_carrier) [<https://perma.cc/5JWN-7WDP>].

<sup>9</sup> See Joanna Bailey, *What Are the Pros and Cons of State-Owned Airlines?*, SIMPLE FLYING (June 24, 2020), <https://simpleflying.com/pros-cons-state-owned-airlines/> [<https://perma.cc/C4B8-LNG4>].

<sup>10</sup> See Jay Singh & Gauarav Joshi, *Why Doesn't the United States Have a Flag Carrier?*, SIMPLE FLYING (updated Sept. 19, 2022) <https://simpleflying.com/us-no-flag-carrier/#:~:text=Growing%20in%20prominence%20during%20World,international%20airline%20representing%20the%20US> [<https://perma.cc/Z2NC-DX3V>].

the *legacy carriers*<sup>11</sup> have been *privatized*.<sup>12</sup> This means that funding from *the private financial sector* is required to acquire their fleets of aircraft.<sup>13</sup>

As modern aircraft became technically more developed, larger, and extremely expensive, the airlines started looking for alternative modes of financing. Over the years, as *lessees*, an increasing number of carriers decided to *lease* aircraft from specialized leasing companies.<sup>14</sup> At the same time, the lessors have to purchase the costly aircraft from the manufacturers, which implies that they need financing from the private financial sector.<sup>15</sup> The catalogue price of a *wide-body* aircraft may run up to about \$450 million and of an aircraft engine to \$45 million.<sup>16</sup>

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<sup>11</sup> For example, Air France-KLM, British Airways, Lufthansa, Air India, Qantas have been privatized. See *List of Government-Owned Airlines*, WIKIPEDIA, [https://en.wikipedia.org/wiki/List\\_of\\_government-owned\\_airlines](https://en.wikipedia.org/wiki/List_of_government-owned_airlines) [<https://perma.cc/Y9X6-U62Y>]. However, until today, China, Egypt, Pakistan, Dubai, Abu Dhabi, Kuwait, Saudi Arabia, Tanzania, Russia, Kazakhstan, and several other countries still have flag-carriers that are, to a more or less extent, owned by local governments. *Id.* Surprisingly, rather recently the Mexican Federal Government has purchased the *insolvent* carrier Mexicana de Aviación. Héctor Soto, *Government Finalizes Purchase of Mexicana de Aviación*, MEXICO BUSINESS NEWS (Aug. 10, 2023, 10:18 AM), <https://mexicobusiness.news/aerospace/news/government-finalizes-purchase-mexicana-de-aviacion> [<https://perma.cc/VT6Z-PFWR>]. The Ministry of Defense (SEDENA), which has no relevant experience whatsoever, will operate its own commercial airline. Kim Lim Park, *Mexican Airline: The Planned Military-Owned National Carrier of Mexico*, AVIATIONNEPAL (Dec. 7, 2022), <https://www.aviationnepal.com/mexicana-airline-the-planned-military-owned-national-carrier-of-mexico/> [<https://perma.cc/R6HK-SW2L>].

<sup>12</sup> For instance, under EU competition law, the Portuguese state-owned airline TAP had to be (partially/majority) privatized in 2015. John McDermott, *Portuguese Government Takes Majority Stake in TAP Air Portugal*, AIRLINEGEEKS (July 6, 2020, 2:54 PM), <https://airlinegeeks.com/2020/07/06/portuguese-government-takes-majority-stake-in-tap-air-portugal/> [<https://perma.cc/QPW5-ESH4>]. It was the only commercial carrier in the Member States of the European Union which was still fully controlled by a national government. See WIKIPEDIA, *supra* note 11.

<sup>13</sup> See Marshall Hargrave, *Privatization: What it is, How it Works, Examples*, INVESTOPEDIA (last updated July 27, 2022) <https://www.investopedia.com/terms/p/privatization.asp> [<https://perma.cc/CUY8-5WMK>].

<sup>14</sup> Specialized aircraft leasing companies started their businesses, while in the beginning at a small scale, in the early 1970s. See Robert F. Agnew, *The Birth and Growth of the Aircraft Leasing Business*, WORLD LEARNING YEARBOOK, <https://www.world-leasing-yearbook.com/feature/the-birth-and-growth-of-the-aircraft-leasing-business/> [<https://perma.cc/VYV6-ABUW>].

<sup>15</sup> See Vesna Palevska, *Introduction to Aircraft Financing, Special focus on secured lending*, A presentation addressing the relationship between lessors and their financiers to University of Mississippi, School of Law, October 31, 2022.

<sup>16</sup> See *Wide-Body Aircraft*, THE BREAKTHROUGH INST., <https://thebreakthrough.org/issues/energy/wide-body-aircraft> (May 3, 2017) [<https://perma.cc/NHU5-3TAD>]; Oman Memon, *How Much Do Jet Engines Cost?*, SIMPLE FLYING (Nov. 16,

Therefore, the acquisition and operation of these objects is extremely capital-intensive. In the United States and abroad, the principal forms of financing are (1) a *loan* which is guaranteed by a *secured interest*<sup>17</sup> in the aircraft, and (2) a *lease agreement*. For example, Article 9 of the UCC provides for *security interests* created by *security agreements*.<sup>18</sup> This provision has been implemented in every state in the United States.<sup>19</sup> However, the implementation of Article 9 has *not* occurred identically in all these jurisdictions. Although the substantive content is largely similar, some states have made structural modifications. Consequently, due to the existing different local legal regimes in the U.S., the global aviation finance and lease practice frequently prefers the security interest regime of New York.<sup>20</sup> Accordingly, in international finance and lease agreements, the parties routinely include a *choice of law clause* selecting New York law.

The abovementioned finance and lease transactions require that a financier (secured creditor) or lessor (owner) can adequately uphold its proprietary interest<sup>21</sup> in the aircraft. For example, a leasing company will only agree to lease the aircraft to an airline when the former party can successfully enforce its *remedies* when the latter party defaults or becomes insolvent.<sup>22</sup>

This article firmly submits that also the *lessees* of aircraft require adequate protection. For this purpose, it discusses the existing

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2022), <https://simpleflying.com/how-much-do-jet-engines-cost/> [<https://perma.cc/EK6R-72LS>].

<sup>17</sup> See the *extremely* detailed U.C.C. § 9 (AM. L. INST. & UNIF. L. COMM'N), which is addressed in more detail, *infra* Part II.

<sup>18</sup> See U.C.C. § 9-102(a) (74) (AM. L. INST. & UNIF. L. COMM'N) (defining “security interest”).

<sup>19</sup> See B. Patrick Honnebier, *The Dutch Real Rights of Airlines Can Be the Basis of International Interests Under the Cape Town Convention, Just Like Their Equivalent American Security Interests*, 12 EUR. REV. OF PRIV. L. 46, 55 (2004).

<sup>20</sup> See Dominic E. Pearson, *Aircraft Repossession: Hoping for the Best, Planning for the Worst*, A presentation to University of Mississippi School of Law, Nov. 2, 2022. Slide 10: Transfer of possession (and ownership on sale), Priority of property rights.

<sup>21</sup> In this publication the term ‘proprietary interest’ includes *all* the secured interests and the right of ownership.

<sup>22</sup> See, e.g., GUIDANCE MATERIAL AND BEST PRACTICES FOR AIRCRAFT LEASES 48 (Int'l. Air Transp. Ass'n ed., 4th ed. 2017); *Financial Security Of An Aircraft Lease – Managing Assets*, IALTA (June 14, 2023), <https://ialta.aero/financial-security-of-an-aircraft-lease-managing-assets> [<https://perma.cc/DZJ9-EPWW>].

local and international<sup>23</sup> secured rights of the lessees of aircraft.<sup>24</sup> In the United States,<sup>25</sup> Canada,<sup>26</sup> Australia,<sup>27</sup> New Zealand,<sup>28</sup> the Kingdom of the Netherlands,<sup>29</sup> China,<sup>30</sup> Serbia,<sup>31</sup> Suriname,<sup>32</sup> and other countries, the local airlines and other operators of

<sup>23</sup> Other detailed materials regarding the goal, intent, and sphere of application of the Cape Town Convention are available. See B. Patrick Honnebier, *The Fully-Computerized International Registry for Security Interests in Aircraft and Aircraft Protocol That Will Become Effective Toward the Beginning of 2006*, 70 J. AIR L. & COM. 63, 73-74 (2005); B. Patrick Honnebier, *The Convention on International Interests in Mobile Equipment and Aircraft Equipment Protocol Encourages European Property Law Reform*, 8 EDINBURGH L. REV. 118, 125 (2004); see also B. Patrick Honnebier, *Analysing the Effects of the Cape Town Convention on Four Selected Issues That Hinder the International Financing and Leasing of Aircraft Engines*, 22 IUS COMPARATUM – GLOB. STUD. IN COMPAR. L. 337, 342 (2017).

<sup>24</sup> See discussion *infra* Parts II, III.

<sup>25</sup> See discussion *infra* Part II.

<sup>26</sup> Article 9 UCC inspired the introduction of the Personal Property in all Canadian provinces and territory, except in Quebec, which is a civil law jurisdiction, in 1990. *U.S.'s Article 9 of the Uniform Commercial Code (UCC) and Canada's Personal Property Security Act (PPSA)*, NCS CREDIT (July 27, 2023), <https://www.ncs-credit.com/education-center/blog/us-article-9-of-the-ucc-and-canadas-ppsa/>. [https://perma.cc/7XUK-YGMW]; see Michel Deschamps, *Les Régles de Propriété de la Convention et du Protocole du Cap*, Unif. L. Rev. 17 (2002), for aviation finance matters.

<sup>27</sup> For Australia, see *Personal Property Securities Act 2009*, BAKER MCKENZIE 1 (2018), [https://www.bakermckenzie.com/en/-/media/files/insight/publications/2018/10/flyer\\_aus\\_ppsa\\_oct2018.pdf](https://www.bakermckenzie.com/en/-/media/files/insight/publications/2018/10/flyer_aus_ppsa_oct2018.pdf) [https://perma.cc/9Q2A-PPGP].

<sup>28</sup> For New Zealand, see the *Personal Property Securities Act, 1999 No. 126* (199) (N.Z.).

<sup>29</sup> For example, under the special aviation finance-related regulations of all the territorial units of the Kingdom of the Netherlands, such a secured right (*zakelijk recht*) can be established. See B. Patrick Honnebier, *The New Legal and Fiscal Regimes That Facilitate the Financing and Leasing of Aircraft in the Netherlands and Dutch Caribbean*, 6 Tax Plan. Int'l. Rev., 1, 4 (2012). Provided, however, that the aircraft is recorded in the local *Aircraft Title Registry*. *Id.* The secured right to possess the aircraft finds its origin in what is in practice called an *operational lease agreement* which must include a term of at least six months. DUTCH CIVIL CODE art. 8.1309 para. 1 (Neth.). The secured right of the lessee to *acquire and possess* (to purchase) the aircraft is in practice known as a *financial lease agreement*. DUTCH CIVIL CODE art. 8:1308 (Neth.). See B.P. Honnebier, *De komende UNIDROIT goederenrechtelijke regeling waarborgt de Nederlandse volwaardige zakelijke rechten die aan de houder van een luchtvaartuig kunnen worden toegekend*, Weekblad Privaatrecht en Notariaat, WPNR, June 2001.

<sup>30</sup> See Ma Feng, Wang Ning, & Chen Jie, *Aviation Finance in China: Overview*, THOMSON REUTERS, <https://uk.practicallaw.thomsonreuters.com/w-038-0761?transitionType=Default&contextData=/> [https://perma.cc/8YME-Y6RF].

<sup>31</sup> See Uroš Popović & Stefan Golubović, *Aviation Finance & Leasing 2023*, CHAMBERS AND PARTNERS (July 25, 2023), <https://practiceguides.chambers.com/practice-guides/aviation-finance-leasing-2023/serbia> [https://perma.cc/C7UM-VTMX].

<sup>32</sup> See *Landsverordening houdende vaststelling van regelen nopens teboekgestelde luchtvaartuigen*, (1973) art. 8, 9 (Surin.). See also B. Patrick Honnebier, *De nieuwe ontwikkelingen in de internationale financieringspraktijk zijn de laatste strohalm*



aircraft (lessees) may obtain these significant proprietary rights from the lessors.

#### A. THE AMERICAN AIRLINES NEED ADEQUATE LOCAL PROTECTION

As is briefly mentioned *supra*, this contribution's center of concentration concerns the secured interests of the lessees of aircraft in the United States. Besides, as far as U.S. domestic law is concerned, it primarily refers to the substantive property laws of New York.

For example, *locally*, the airlines in the United States need adequate protection in the event that the lessor of the aircraft changes, defaults, or goes bankrupt.<sup>33</sup> This means that the lessee requires appropriate secured rights which can be upheld against the third-party creditors of the lessor.

#### B. THE AMERICAN AIRLINES NEED ADEQUATE INTERNATIONAL PROTECTION

It is argued that also at the *international level* an American operator that leases an aircraft needs sufficient security when the *initial* lessor intends to *sell* this object to *another* lessor abroad.<sup>34</sup> The trading of (portfolios of) aircraft on the aviation market is essential to the global aircraft financing and leasing practice.<sup>35</sup> Otherwise, the aircraft would be substantially less valuable for lessors (owners), financiers, and other investors. When these stakeholders start negotiating aircraft international transactions, they will generally condition that these objects can be sold in the *secondary market*.<sup>36</sup> Arguably, the international trading of aircraft increases their value.<sup>37</sup> It has been asserted that selling these aircraft also provides the lessees stronger leverage *vis-a-vis* their lessors as the former parties may obtain lower lease rates. As aircraft are regularly traded during their economic lifespan, even when the agreed lease terms have not yet ended,<sup>38</sup> their title transfers

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*voor de Surinaamse Luchtvaart Maatschappij*, Surinaams Juristen Blad (SJB), August 2004.

<sup>33</sup> For more details, see *infra* Part II.

<sup>34</sup> For more details, see *infra* Part II.

<sup>35</sup> See Zack Cronin, *The Aircraft Trading Market: Considerations for Aircraft Leasing and Transfer Provisions*. A presentation to the University of Mississippi, School of Law, Wednesday, Oct. 30, 2023. . Slide 2: *Market Background*.

<sup>36</sup> See *id.* at slide 2.

<sup>37</sup> See *id.* at slide 2.

<sup>38</sup> See *id.* at slide 15.

have a major impact on the international aviation finance and lease practice at large.

Therefore, the airlines frequently consider aircraft trading as a problematic undertaking. For instance, in the airlines' opinion, the subsequent lessors, having purchased the aircraft, may have ulterior motives.<sup>39</sup> More specifically, the new lessor may trump up a reason to *cancel* the existing lease agreement. Its actual goal is to lease the aircraft to another (foreign) airline, as the new lessee has agreed, *inter alia*, to pay more rent pursuant to a subsequently established lease agreement.<sup>40</sup>

Evidently, in all the above-described situations, it is assumed that the lessee is in *good standing*. This means that the airline is *not* defaulting in regard to its financial and other obligations which are contained in the continuing lease agreement!

### C. THE AMERICAN AIRLINES OBTAIN ADEQUATE PROTECTION UNDER THE CAPE TOWN CONVENTION

This article asserts that the national secured interests of operator-lessees may<sup>41</sup> form the basis of *registered international interests*<sup>42</sup> pursuant to the *Convention on International Interest in Mobile Equipment* (Convention)<sup>43</sup> and the *Protocol thereto on Matters Specific to Aircraft Equipment* (Protocol).<sup>44</sup> The two instruments were finalized at a Diplomatic Conference in Cape Town, South Africa on November 16, 2001.<sup>45</sup> In practice, together the Convention and Protocol are called the *Cape Town Convention*, and they must be interpreted *jointly*. The intent of the Cape Town Convention is to facilitate the international financing and leasing of aircraft objects.<sup>46</sup>

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<sup>39</sup> See *id.* at slide 9.

<sup>40</sup> See *id.* at slide 9.

<sup>41</sup> Evidently, whether a specific local secured interest of a lessee that is created in an aircraft *can* legally form the basis of a registered international interest under the regime of the Cape Town Convention, entirely depends on the facts and circumstances of the certain related transaction.

<sup>42</sup> See Roy M. Goode, *The International Interest as an Autonomous Property Interest*, 12 EUR. REV. OF PRIV. L. 18, 22 (2004).

<sup>43</sup> Convention on International Interests in Mobile Equipment, Nov. 16, 20021, (hereinafter Convention).

<sup>44</sup> Aircraft Protocol, *supra* note 3.

<sup>45</sup> The author of this paper attended the Diplomatic Conference for the finalization of the Cape Town Convention in 2001.

<sup>46</sup> See ROY GOODE, CONVENTION ON INTERNATIONAL INTERESTS IN MOBILE EQUIPMENT AND PROTOCOL THERETO ON MATTERS SPECIFIC TO AIRCRAFT OBJECTS: OFFICIAL COMMENTARY 13 (UNIDROIT, 5th ed. 2022).

This article solely refers to the specific provisions of the Cape Town Convention that relate to the registered international interests of the lessees. It only considers these topics, as space restraints make it impossible to analyze the entire regime of this treaty.

The major importance<sup>47</sup> of the Cape Town Convention is apparent, as presently already eighty-six states have adopted the Convention and eighty-one of these jurisdictions the Protocol.<sup>48</sup> The Contracting States represent economically-developed and developing jurisdictions.<sup>49</sup> Moreover, they include aircraft manufacturing and purchasing states.<sup>50</sup>

As a Regional Economic Integration Organisation (REIO),<sup>51</sup> the European Union (EU) has, to some extent, ratified the Cape Town Convention (CTC). The Cape Town Convention makes it possible that a REIO accepts it as far as it has *competence* over certain matters that are addressed in it.<sup>52</sup> In ratifying the CTC, the EU has asserted competence in respect of those provisions regarding *choice of law, jurisdiction, and insolvency*.<sup>53</sup> That assertion leaves the Member States of the EU unable to make declarations<sup>54</sup> in respect of those matters.<sup>55</sup>

#### D. THE STRUCTURE OF THIS ARTICLE

This article is structured as follows. Part II discusses the local American laws that aim to protect the interests of the aircraft lessees. Subsequently, the two international conventions which

<sup>47</sup> See Martin J. Stanford, *The New Regimen: Its History And Future After South Africa*, 12 EUR. REV. OF PRIV. L. 9, 17 (2004).

<sup>48</sup> The authentic languages and some translations of the Cape Town Convention instruments are available at the UNIDROIT Secretariat. See *Cape Town Convention – Authentic Texts*, UNIDROIT, <https://www.unidroit.org/instruments/security-interests/cape-town-convention/cape-town-convention-authentic-texts/> [https://perma.cc/57VT-RMPF]. For the status of the number of contracting states, see *Convention On International Interest In Mobile Equipment (Cape Town, 2001) – States Parties*, UNIDROIT, <https://www.unidroit.org/instruments/security-interests/cape-town-convention/states-parties/> [https://perma.cc/YE3T-QUX6].

<sup>49</sup> See *Convention On International Interest In Mobile Equipment (Cape Town, 2001) – States Parties*, UNIDROIT, <https://www.unidroit.org/instruments/security-interests/cape-town-convention/states-parties/> [https://perma.cc/YE3T-QUX6].

<sup>50</sup> *Id.*

<sup>51</sup> See Aircraft Protocol, *supra* note 3, at art. XXVII.

<sup>52</sup> *Id.*

<sup>53</sup> See *id.* at art. VIII, XI, XXI.

<sup>54</sup> The Cape Town Convention requires or permits declarations to be made by the Contracting States which can be opt-in or opt-out in kind. See GOODE, *supra* note 46, at 515 for more detail.

<sup>55</sup> See Kenneth Gray, *CTC in Europe: Assessment of Ratifications to Date and Implications of Brexit on the Ratification by the UK*, 5 CAPE TOWN CONVENTION J. 1,1 (2016).

intend, to more or less extent, to protect the secured rights of the airlines are reviewed in Part III. Both treaties have been ratified by the United States. Finally, Part IV provides some concluding remarks.

## II. THE LOCAL AMERICAN LAWS PROTECTING THE RIGHTS OF THE AIRCRAFT LESSEES

This Part reviews the local proprietary laws that apply to the aircraft finance and lease transactions which have a direct connection with the United States. More specifically, the addressed legal regimes intend to protect the secured rights of the American operators of aircraft.

### A. THE RIGHT OF QUIET POSSESSION OF THE AMERICAN AIRLINES

Since 1931,<sup>56</sup> the international aviation practice agrees that the huge financial interests of the owners, mortgagees, and other financiers must be adequately protected. However, as is noted *supra*, this contribution submits that also the lessees of aircraft need proper protection in the event that the lessor legally changes,<sup>57</sup> defaults, or is insolvent.<sup>58</sup> Therefore, as has been stated *supra*, in several jurisdictions the lessor may provide the lessee of an aircraft with a secured right.

Regrettably, as to date it is *not* standard practice in the United States that a lessor agrees to give the airline a *separate* and *distinct* security interest in the aircraft. This view is substantiated by the fact that the need, or even the possibility, to provide the lessee of an aircraft with a local (New York) security interest is rarely

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<sup>56</sup> The international aviation organisation Comité International Technique d'Experts Juridiques Aériens (CITEJA), the predecessor of ICAO's Legal Bureau, had prepared two draft Conventions covering the substantive proprietary aspects of the international financing of aircraft between 1927 and 1931. See G. Nathan Calkins Jr., *Creation and International Recognition of Title and Security Rights in Aircraft*, 15 J. AIR L. & COM. 156, 162 (1948). One draft Convention related to the *registration* and the other to *mortgages* and other *secured rights* in aircraft. See CITEJA Doc. No. 162. Unfortunately, the time was *not* ripe for conventions regulating the *property law* aspects of international aircraft financing. It took until 2001 when the Cape Town Convention was finalized and provided for such a *mandatory* legal regime! See *Cape Town Convention and Protocol*, ICAO, <https://www.icao.int/sustainability/Pages/Capetown-Convention.aspx> [<https://perma.cc/LR3T-4MFJ>].

<sup>57</sup> See NCS CREDIT, *supra* note 26.

<sup>58</sup> See B. Patrick Honnebier, *The New International Regimen Proposed by UNIDROIT As a Means Of Safeguarding Rights In Rem Of the Holder Of an Aircraft Under Netherlands Law*, 1 UNIF. L. REV. 5, 21 (2001).

discussed in American aviation law reviews and other aviation industry journals.<sup>59</sup>

Presently, pursuant to Article 2A of the Uniform Commercial Code,<sup>60</sup> which is *differently* implemented<sup>61</sup> in all the constituent states of the United States, the lessor and lessee of an aircraft can enter into a *true* lease agreement.<sup>62</sup> The lessor is the *owner*, and the lessee has *possession* of the aircraft.

To give the airline *to a limited extent* protection, it is standard that the lease agreement contains a provision covering the *right of quiet enjoyment*. In practice, this right is also called the *right of quiet possession* of the aircraft.<sup>63</sup> It is important for the lessee that it can operate the aircraft during the entire term of the lease agreement.<sup>64</sup> Therefore, while structuring the aircraft lease agreement in the United States, the lessee will *negotiate* with the lessor that the former party has the right to possess and operate the aircraft *without any interference* from the latter party *and* its third-party creditors.<sup>65</sup> Clearly, under the condition that the lessee has not defaulted on its obligations as included in the lease agreement.

The lessee's quiet possession right against third-party creditors is strongly negotiated, as such a *covenant* is *not mandatory* under the applicable New York<sup>66</sup> or other local law. However, practice shows that the lessor's lender prefers that the lessee does *not* obtain a covenant of quiet enjoyment.<sup>67</sup> This is because in the event that the lessor defaults, the *lender* can repossess the aircraft and sell it without any legal encumbrance.<sup>68</sup> Alternatively, in this case, the aircraft can be *leased* to a new lessee *free and clear*.<sup>69</sup>

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<sup>59</sup> Only a very limited number of writings covering this important legal subject is available. See John I. Karesh, *Repossession of Collateral and Foreclosure of Security Interests in Leverage Lease Aircraft Finance Transactions*, AIR & SPACE LAW. 9 (1995).

<sup>60</sup> See generally IAN SHRANK & ARNOLD G. GOUGH, JR., EQUIPMENT LEASING-LEVERAGED LEASING (Ian Shrank & Arnold G. Gough, Jr. eds., 4th ed., 2004).

<sup>61</sup> See *supra* Part I.

<sup>62</sup> See U.C.C. § 2A-103 (Am. L. Inst. & Nat'l Conf. of Comm'rs on Unif. State L. 2023) for the definition of a (true) *lease agreement*. See *UCC Article 2A, Leases*, UNIF. L. COMM'N., <https://www.uniformlaws.org/committees/community-home?CommunityKey=16b9e44b-f2c5-4210-99c3-78e7d3fe985f> [<https://perma.cc/YD2F-FTCU>] for more details.

<sup>63</sup> See Raymond G. Wells & John T. Curry, *Protecting the Aircraft Lessee's Quiet Possession Right Under the Cape Town Convention*, 2 BLOOMBERG L. REPS.—BANKING & FIN. n. 6, 1 (2009).

<sup>64</sup> *Id.*

<sup>65</sup> *Id.*

<sup>66</sup> See Cronin, *supra* note 35, at slide 2; see Wells & Curry, *supra* note 63, at 1.

<sup>67</sup> *Id.*

<sup>68</sup> See Wells & Curry, *supra* note 63, at 1.

<sup>69</sup> *Id.*

In the United States, under the UCC, the lessee is to *a certain extent* provided with a right to quiet enjoyment.<sup>70</sup> However, in American aviation practice, the local airlines will most likely *negotiate* their covenant of quiet possession provisions, which *explicitly* give them a certain protection.<sup>71</sup> Historically in the United States, the aircraft lessees had the perception that the *filing* of the New York-based lease agreements at the Federal Aviation Administration (FAA) would boost their quiet enjoyment rights.<sup>72</sup> Basically, the lessees assumed that filing the lease agreement at the FAA would effectively give *notice* to the third-party creditors of the lessor regarding their rights of quiet possession of the aircraft.<sup>73</sup> In their views, this notice-filing would enhance their legal rights.<sup>74</sup> For example, it might bolster an airline's *possessory right* vis-a-vis the lessor's judgment creditors or its lenders, which had provided loans *after* the certain lease agreement had been entered into.

However, it must be kept in mind at all times that the right of quiet enjoyment of a lessee under a lease agreement is legally *not* characterized as a *secured right*! Consequently, it does *not* adequately protect the lessee against the third-party creditors of the lessor! This paper emphasizes that such a right is merely a *personal right*. Accordingly, it has a *limited effect*, as it can *only* be enforced against the aircraft lessor, which is the *contracting party* (inter parties).<sup>75</sup>

#### B. THE SECURITY INTERESTS OF THE AMERICAN AIRLINES

As has been addressed *infra*, in essence, the right of quiet possession of the lessee of an aircraft solely has effect against the lessor. Therefore, it is of major interest to an American-based airline that it negotiates and obtains a security interest. This is made possible by Article 9 of the UCC,<sup>76</sup> which has been implemented

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<sup>70</sup> *Id.*

<sup>71</sup> *Id.*

<sup>72</sup> See Wells & Curry, *supra* note 63, at 2.

<sup>73</sup> *Id.*

<sup>74</sup> *Id.*

<sup>75</sup> *Inter partes* is the Latin term for *between the parties*. See *inter partes*, BLACK'S LAW DICTIONARY (11th ed. 2019). In legal practice, it is a term that can be distinguished from *in rem*, which refers to a legal action which is based on the control of property and it has *erga omnes*, against third parties, effect. See *In rem*, BLACK'S LAW DICTIONARY (11th ed. 2019); *Erga Omnes*, BLACK'S LAW DICTIONARY (11th ed. 2019).

<sup>76</sup> Article 9 UCC governs security interests in personal property as security to secure a debt. U.C.C. § 9-109 (AM. L. INST. & NAT'L CONF. OF COMM'RS ON UNIF. STATE L. 2023). A creditor with a security interest is called a *secured party*. *Id.* § 9-102(a) (73). Fundamental concepts under Article 9 include how a security interest is created (called *attachment*); how to give notice of a security interest to the public,

in the State of New York.<sup>77</sup> Pursuant to Article 9, the lessor *may* provide the lessee with a security interest<sup>78</sup> that legally secures that the lessee has the possession of the aircraft. In other words, it guarantees that the lessee can operate the aircraft. This secured right is formally established by entering into a separate and distinct *security agreement*.<sup>79</sup> It is emphasized that pursuant to the security agreement, the lessor is the *chargor* (debtor) and the lessee is the *chargee* (creditor).

Pursuant to Article 9 UCC, a transaction will regularly secure the payment of U.S. dollars or another form of *monetary obligation*. Nevertheless, this provision does not dictate that the secured obligation has to relate to a sum of money that has to be paid by the chargor to the chargee.

The following example intends to clarify how the various instruments that form a specific transaction are structured. It is assumed that a specific agreement is *characterized* as a true lease as defined in Article 2A of the UCC.<sup>80</sup> This provision has been implemented in the substantive property law of the State of New York. Pursuant to this article, the aircraft lessor may provide the lessee with a *separately created* security interest.<sup>81</sup> The interest secures the obligation of the former party under the lease agreement to provide the possession of the aircraft. For instance, the lessee may want to seek protection against the lessor, which is insolvent. More specifically, the lessee intends to avoid an unsecured third-party claim for damages. By taking a security interest, it obtains itself a secured claim. It has been contended that one of the most significant features of Article 9 of the UCC is the practically *uncontrolled freedom* it gives the parties to arrange

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which makes the security interest enforceable against others who may claim an interest in the collateral (called *perfection*); when multiple claims to the same collateral exist, determining which interests prevail over others (called *priority*); and what remedies a secured party has if the debtor defaults in payment or performance of the secured obligation. *Id.* §§ 9-203(a), 9-308(a), § 9-322(a), § 9-601(a).

<sup>77</sup> *Uniform Commercial Code: Overview*, NEW YORK DEPARTMENT OF STATES, <https://dos.ny.gov/uniform-commercial-code> [<https://perma.cc/R6RA-3PH9>].

<sup>78</sup> See B. Patrick Honnebier, *The Dutch Real Rights of Airlines can be the Basis of International Interests Under the Convention of Cape Town, Just Like Their Equivalent American Security Interests*, 12 EUR. REV. OF PRIV. L. 46, 55 (2004).

<sup>79</sup> U.C.C. § 9-102(a)(74) (AM. L. INST. & UNIF. L. COMM'N. 2023) (explaining that “‘security agreement’ means an agreement that creates or provides for a *security interest*”).

<sup>80</sup> See U.C.C. § 2A-103(1)(j) for the definition. See also J.B. Vegter, *The distinction between true leases and secured transactions under the Uniform Commercial Code*, Molengrafica, 1994.

<sup>81</sup> See U.C.C. § 9-110.

their transaction. Under the UCC, the parties *can provide each other* with security interests.<sup>82</sup> Moreover, the secured interest of the airline can be recorded separately from the lease agreement at the FAA.<sup>83</sup> In fact, every party may acquire a security interest, provided that it complies with the requirements of Article 9 UCC. It applies to any transaction that is intended to create a security for payment of money *or* the performance of any other obligation in personal property. Therefore, the obligation secured does *not* need be a monetary obligation. For example, the lessee can obtain a security for the lessor's *contractual obligation* to provide the lessee with title to or possession of the object. Under the UCC, this party can secure the lessor's obligation. Upon the creation and perfection of the security interest, by filing it at the FAA, the lessee is a secured party. When the lessor becomes insolvent, the lessee's secured claim is effective against third party claims and the lessor's bankruptcy trustee.

In sum, so long as the lessee has complied with the formal requirements of Article 9 UCC this provision affords it adequate protection. Finally, under the Code the holder of a perfected security interest can also claim its *priority status*, *enforce* its special remedies, and recover the object. Evidently, whether a lessor will in fact provide an American airline with a security interest depends, among other things, upon the economic and financial leverage of the parties in a specific situation.<sup>84</sup>

It is reiterated that regrettably the above-described possibility to provide the airlines with New York law-based security interests is *not* (yet) customary in the local aviation finance and lease practice of the United States.<sup>85</sup>

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<sup>82</sup> See generally GRANT GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY (1965); Grant Gilmore, *Security Law, Formalism and Article 9*, 47 Neb. L. Rev. 659 (1968); GRANT GILMORE, THE AGES OF AMERICAN LAW (2d ed. 2014). Professor Gilmore was an American lecturer at Yale Law School, University of Chicago Law School, and several other academic institutions. See Law School Record Editors, *Grant Gilmore*, 28 UNIV. OF CHI. L. SCH. REC., 43, 43 (1982). He was a leading scholar of commercial law and one of the principal drafters of the Uniform Commercial Code, including, importantly, Article 9. *Id.*

<sup>83</sup> See B. Patrick Honnebier, *The Cape Town Convention and the Aircraft Equipment Protocol: Protecting the Registered Secured Interests of Airline Lessees*, 30 AIR & SPACE L. 27, 31 (2005).

<sup>84</sup> *Id.* at 31–32.

<sup>85</sup> *Id.* It is noted that in several other jurisdictions it is general practice that the lessees of aircraft will negotiate to obtain secured rights. *Id.* at 28. For example, in the European Netherlands the aircraft lessors will provide the major commercial airlines secured interests. *Id.* On the other hand, the legal systems of the Kingdom of the Netherlands do not include special operational or financial lease laws. See B.P. Honnebier, *De (internationale) leasing transactie als financieringsmethode*



### III. THE INTERNATIONAL CONVENTIONS PROTECTING THE SECURED RIGHTS OF THE AMERICAN AIRLINES

This Part reviews the treaties which, in general, aim to facilitate the financing and leasing of aircraft. More importantly, to a more or less extent, they provide protection to the American airlines by either recognizing their validly-created (New York) local security interests or providing them with registrable international interests.

#### A. THE GENEVA CONVENTION REQUIRING THE INTERNATIONAL RECOGNITION OF THE SECURED RIGHTS OF THE LESSEES

At the international level, originally the legal topic covering the existing secured rights of the lessees is based on the regime of the *Convention on the International Recognition of Rights in Aircraft* (Geneva, 1948).<sup>86</sup> This treaty has been adopted by the United States and more than eighty other jurisdictions.<sup>87</sup> However, as the name of the treaty indicates, it solely requires that the New York-based security interests of the airlines are *recognized* in all the other Contracting States.

Immediately after World War II, an aviation treaty that would provide for a uniform substantive property law regime was politically and practically not possible. As the Geneva Convention only covers the recognition of foreign secured interests in aircraft, by its very nature it is not as effective as is desired.<sup>88</sup>

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*van roerende kapitaalgoederen*, 50 ONDERNEMING EN FINANCIERING 59 (2007) (Neth.); *Een internationale uniforme materiële regeling voor het eigendomsvoorbehoud is tot stand gekomen: De conventie van Kaapstad*, 6 NEDERLANDS TIJDSCHRIFT BURGERLIJK RECHT [N.T.B.R.] 233 (2003) (Neth.); *De internationale financieringspraktijk heeft wederom behoefte aan de uitbreiding van het bestaande pakket van Nederlandse zakelijke rechten*, Weekblad voor Privaatrecht, Notariaat Registratie (WPNR), 2000, 914.

<sup>86</sup> See B. Patrick Honnebier, *Analysing the Conflict of Laws Rule of the Convention on the International Recognition of Rights in Aircraft: A Topical Issue*, 59 ZLW 23, 25 (2010); *Analyzing the effects of the Cape Town Convention on four selected issues that hinder the international financing and leasing of aircraft and engines*, Implementing the Cape Town Convention and Domestic Laws on Secured Transactions, ISBN 2214-6881, *The matter of the secured interests of the operator lessees*, 337, at 342, para 21.3.

<sup>87</sup> See *Convention on the International Recognition of Rights in Aircraft*, ICAO, [https://icao.int/secretariat/legal/list%20of%20parties/geneva\\_en.pdf](https://icao.int/secretariat/legal/list%20of%20parties/geneva_en.pdf) [<https://perma.cc/L3J5-P9NP>].

<sup>88</sup> This view has been expressed by several authors who were the delegates the Diplomatic Conference for the realization of the Geneva Convention in 1948. See, e.g., R.O. Wilberforce, *The International Recognition of Rights in Aircraft*, 2 INT'L L. Q. 421, 435 (1948). See also Anda Djojonegoro, *The UNIDROIT Proposal for a Uniform Air Law: A New Aircraft Mortgage Convention*, 22 ANNALS OF AIR & SPACE L. 53, 62 (1997);

The Geneva Convention includes the following provision: “The Contracting States undertake to recognize . . . (b) rights to *acquire* aircraft by purchase *coupled with possession* of the aircraft; (c) rights to *possession* of aircraft *under leases of six months or more*.”<sup>89</sup>

However, the Contracting States were not required to implement the above-cited article into their local laws. For example, the Netherlands was one of the few jurisdictions in Europe to incorporate it in its national mandatory property laws.<sup>90</sup>

These Geneva Convention possessory rights are, in turn, derived from the local proprietary legal regimes, which existed in the constituent states of the United States before Article 9 UCC entered into force.<sup>91</sup> More specifically, the aforementioned property laws were valid in New York and Pennsylvania, and they protected the *conditional buyer* and *lessee* respectively. As is indicated *supra*, at present, they fall under the application of Article 9 UCC,<sup>92</sup> which has been (differently) implemented in all the constituent states of the United States. Similar laws exist in other jurisdictions.<sup>93</sup>

However, a major issue that arises is that the local proprietary legal regimes of many other countries are hostile to the secured interests of the airlines. These secured rights are totally unfamiliar to them. Accordingly, they do *not* fit in their *closed system* (*numerus clausus*) of property rights. For instance, the security interest of a lessee that is validly created and recorded (perfected)

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Jan A. Krupski, *Conflict of Laws in Aircraft Securitization*, 24 ANNALS OF AIR & SPACE L. 91, 129 (1999).

<sup>89</sup> The Geneva Convention provides four classes of rights that if they have been validly constituted in aircraft in one Contracting State, they must be recognized in all the other Contracting States. See *International*, 16 J. AIR L. & COM. 65, 70–71 (1949) (listing Article I (1) (b-c) Geneva Convention).

<sup>90</sup> Contrarily, in Germany, for instance, the airlines can only obtain personal rights, as opposed to secured interests, in order to lease an aircraft. See Hans-Georg Bollweg & Christoph Henrichs, *Das Übereinkommen von Kapstadt: Diplomatische Konferenz beschließt Übereinkünfte über Sicherungsrechte an Luftfahrtäusrüstung*, 51 ZLW 186, 192 (2002).

<sup>91</sup> See, e.g., Aircraft Protocol, *supra* note 3, art. XXVII; Karesh, *supra* note 59, at 9; Shrank, *supra* note 59; Wells & Curry, *supra* note 63, at 1; see also Gilmore, *supra* note 82.

<sup>92</sup> See JOHN HONNOLD, CASES AND MATERIALS ON THE LAW OF SALES AND SALES FINANCING 30 (4th ed. 1976); Richard E. Speidel, *Advance Payments in Contracts for Sale of Manufactured Goods: A Look at the Uniform Commercial Code*, 52 CAL. L. REV. 281, 303 (1964) (discussing the situation in the United States); Frank R. Kennedy, *The Trustee in Bankruptcy Under the Uniform Commercial Code: Some Problems Suggested by Articles 2 and 9*, 37 RUTGERS L. REV. 518, 558–59, 561 (1960); William E. Hogan, *The Marriage of Sales to Chattel Security in the UCC*, 38 B.U. L. REV. 571, 595–96 (1958).

<sup>93</sup> For example, the Netherlands, Canada, Australia, New Zealand, China, Serbia, and Suriname make it possible that the lessor may provide the lessee secured rights. See *supra* notes 26–32.

in New York will *not* be recognized in various jurisdictions that have *not* adopted the Geneva Convention. Moreover, they *cannot* be validly created and enforced pursuant to the local mandatory *substantive property law* of many other jurisdictions.<sup>94</sup>

In conclusion, an international *uniform substantive aviation finance and lease treaty* is needed to solve the above addressed major problem. As far as lessees are concerned, only this kind of convention will facilitate the global finance and lease of aircraft.

#### B. THE CAPE TOWN CONVENTION ADEQUATELY PROTECTS THE SECURED RIGHTS OF THE LESSEES

The Cape Town Convention (Convention) is the one and only instrument providing for the desired international uniform substantive aviation finance and lease laws. While this treaty does *not* explicitly state that the secured rights of the lessees *may* be covered by its sphere of application, it follows from its goal and intent that this is the case. For example, the Preamble to the Cape Town Convention explicitly states that it “desir[es] to provide broad and mutual economic benefits for all interested parties.”<sup>95</sup> In addition, the Aircraft Protocol adds that it is “necessary to implement the Convention . . . as it relates to aircraft equipment, in the light of the purposes set out in the preamble to the Convention.”<sup>96</sup>

Provided, however, that these proprietary interests fall within the definition of an international interest. Article 2(2) of the Convention contains the following broadly formulated definition: “[A]n international interest in mobile equipment is an interest . . . (a) *granted by the chargor under a security agreement*;<sup>97</sup> (b) vested in a person who is the *conditional seller* under a title reservation

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<sup>94</sup> See, e.g., *Blue Sky One Ltd. v. Mahan Air* [2010] EWHC 631 (Comm) (Eng.). The case concerned the validity of an English mortgage that had been created in a United Kingdom registered aircraft while it was temporarily located in the Netherlands. *Id.* The English rulings had a disastrous outcome for the international aviation finance and lease practice at large. See Cameron A. Gee, *Vedder Thinking | Articles Choice of Law After England’s Blue Sky One Case*, VEDDERPRICE (June 2011), <https://www.vedderprice.com/choice-of-law-after-englands-blue-sky-one-case-06-30-2011> [<https://perma.cc/WVP2-JKAG>]. For the validity and enforcement of proprietary rights in aircraft, see B. Patrick Honnebier, *The English ‘Blue Sky’ Case About the Enforcement of Aircraft Mortgages and Its Impact on the Global Financial Market*, 60 ZLW 47, 48 (2011); *The English ‘Blue Sky’ Case Shows That the Aircraft Finance Practice Needs Uniform International Substantive Mortgage Laws as the Existing Conflict Rules Fail*, 2 TIJDSCHRIFT VERVOER & RECHT 70, 71–72 (2011).

<sup>95</sup> See Convention, *supra* note 43, at pmb. (emphasis added).

<sup>96</sup> See Aircraft Protocol, *supra* note 3, at pmb. (emphasis added).

<sup>97</sup> See Convention, *supra* note 43, at art. II(2) (b) (emphasis added).

agreement; or (c) vested in a person who is the *lessor* under a leasing agreement.”

Under the Cape Town Convention, the interests of the lessees are *not* legally characterized as interests falling under the definitions in paragraphs (b) and (c), as they do *not* provide protection to the conditional seller or lessor. However, they *do* fall within the definition of security agreement contained in category (a). This means that they are Convention interests. Besides, a New York or other secured interest of the lessee is characterized by the applicable local special aviation finance law (*lex specialis*) or general (*lex generalis*) substantive property law as a *security interest*.<sup>98</sup> Thus, New York law decides whether a certain interest falls under Article 2(2)(a) of the Cape Town Convention. If affirmative, this implies that the airline is entitled to the remedies of this treaty.<sup>99</sup>

The extensive Cape Town Convention remedies can be internationally enforced against third parties.<sup>100</sup> However, they must have been registered (perfected)<sup>101</sup> at the International Registry.<sup>102</sup> In the event that the lessor defaults, the registered international interest of the lessee has *priority over any other interests subsequently registered* and over an *unregistered* interest.<sup>103</sup> Furthermore, it can be upheld against third-party creditors if the lessor becomes insolvent. For this purpose, it must have been registered at the International Registry before the bankruptcy proceeding formally starts.<sup>104</sup>

It is stressed that the Cape Town Convention does *not* characterize the secured interest of the lessee as a right of quiet enjoyment.<sup>105</sup> As is more addressed in more detail, *supra*, under the UCC, New York, and foreign laws, this type of right does not have

<sup>98</sup> See Convention, *supra* note 43, at ch.1, art. I(jj) (emphasis added) (defining security interest).

<sup>99</sup> See Convention, *supra* note 43, at ch. 3, art. VIII; see also Aircraft Protocol, *supra* note 3, at ch. II, art. IX.

<sup>100</sup> For example, the creditor may, “to the extent that the debtor has at any time so agreed . . . (a) procure the de-registration of the aircraft; and (b) procure the export and physical transfer of the aircraft object from the territory in which it is situated.” Aircraft Protocol, *supra* note 3, at ch. II, art. IX(1).

<sup>101</sup> See Erin van Laanen, *Cape Town, The International Registry and The FAA – Putting all the Pieces Together*, A presentation to the University of Mississippi, School of Law, Wednesday, Oct. 24, 2022. Slide 7: *Effects of Cape Town on the FAA Registry*.

<sup>102</sup> See Convention, *supra* note 43, at ch. 8, art. XXVIII.

<sup>103</sup> See *International*, *supra* note 89, at 79.

<sup>104</sup> An international interest is effective if, prior to the commencement of the insolvency proceedings, it was registered in conformity with the Convention. See Convention, *supra* note 43, at ch. 8, art. XXX.

<sup>105</sup> See GOODE, *supra* note 46, at 141–42; Convention, *supra* note 43, arts. XXVIII(1), (4), (5), XXX; see also Aircraft Protocol, *supra* note 3, at Article XVI(1).

a proprietary character. The same is valid under the Cape Town Convention, as the right of quiet possession is just a personal right.<sup>106</sup>

This implies that this kind of right *cannot* be registered as a separate international interest. The lessee has to rely on the lessor to register the latter's international interest in the International Registry. Practically, the registration implies that third parties are merely *notified* that the lessee has a personal right of quiet enjoyment in the certain aircraft. Consequently, the right to quiet possession does *not* provide the lessee with the significant Cape Town Convention remedies.<sup>107</sup> Contrarily, these remedies *are* provided to an airline that has obtained a registered international interest. It is concluded that it is of major significance for an American or other lessee, which has obtained a security interest under the applicable New York law, to negotiate and obtain a registered international interest pursuant to the Cape Town Convention. Only such an interest can be enforced against third parties in more than eighty contracting states of the Cape Town Convention.

Evidently, whether in practice a lessor will provide a lessee with a registered international interest depends, *inter alia*, upon the negotiation skills and financial leverage of the parties to a specific lease transaction. In this respect, there may exist major cultural differences between the various jurisdictions.

For instance, assume that a prominent airline is located in the European Netherlands. For this Dutch lessee, it will be an essential condition that it obtains a local secured interest.<sup>108</sup>

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<sup>106</sup> See *supra* note 75 and accompanying text.

<sup>107</sup> See GOODE, *supra* note 46, at 103.

<sup>108</sup> The author has contacted the National Title Registry (Kadaster) of the European Netherlands to enquire whether it is still possible to register the secured right of the lessee of a recorded (teboekgesteld) aircraft on 5 September 2023. The answer was affirmative. Due to confidentiality requirements, while not explicitly prohibited, it is not advisable to refer to the recent recordings of such interests. However, in the view of the author of this article, the information concerning older recordings may be circulated publicly. They are just as informative for the readers and relevant for the topic that is addressed in the current article. See for example the recording of KLM (Royal Dutch Airlines), as lessee, in Amsterdam International Lease Finance Corporation, Los Angeles, USA, regarding a Boeing 777, as lessor, dated 25 April 2006, at 9.00 a.m.; KLM, as lessee and STARLING LTD, in Tokyo, Japan, as lessor, regarding an Airbus 330, dated 30 August 2006, at 9.19 a.m.; KLM as lessee and Salaria Leasing Limited, as lessor, in Caymen Islands, regarding an Airbus 330, dated 28 April, 2006 at 9.00 a.m.; KLM, as lessee and CIT Aerospace International, in Ireland, as lessor, regarding a Boeing 737, dated 18 May, 2006 at 9.00 a.m.; KLM, as lessee and Wells Fargo Bank Northwest, S.A, in Salt Lake City, Utah, U.S.A., regarding a Boeing 737, dated 9 July, 2002, at 1,50 p.m. Other lessors include Wilmington Trust Company, in Delaware, USA (recorded in

As indicated in more detail, *supra*, this is because, presently, lessors may trade (portfolios) of aircraft, they may default, or they may even become insolvent. In these scenarios, the lessees need adequate protection against the creditors of the lessors and other third-party stakeholders. Practice shows that the aircraft lessors that are based in the United States and elsewhere<sup>109</sup> are generally willing to provide the lessees that are based in the European Netherlands with Dutch secured interests to *acquire* or *possess* the aircraft.<sup>110</sup> When the lease agreement and secured right of the airline are structured appropriately,<sup>111</sup> the local proprietary interest of the lessee may form the basis of a registered international interest under the Cape Town Convention.

This positive situation may be difficult to realize when the lessor, lessee, and other financial stakeholders are located in the United States. *Anecdotal evidence* has shown that in this scenario, the US-based lessor, or its financier, generally will be fearful to grant a New York law-covered security interest to the local

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1996 and 1995); IAI XII LLP, Las Vegas, Nevada, USA (recorded in 2001); NBB Leiden Lease Co., LTD, Tokyo Japan, (recorded in 2001), etc. Copies of the Deeds and other documents relating the recordings of the secured rights of the lessees are in the possession of the author.

<sup>109</sup> See *supra* note 108 for several examples of aircraft lessors that are located in USA, Ireland, Cayman Islands, and Japan.

<sup>110</sup> In the European Netherlands, the Title Registry of the city Rotterdam has a special section for the registration of secured rights that have been created in a recorded (teboekgesteld) aircraft. See *supra* note 108. These interests include the secured rights that protect the lessee of recorded aircraft. The Title Registry shows that the local airlines insist on the recording of their secured rights. *Id.*

<sup>111</sup> The Kingdom of the Netherlands has acceded to the Cape Town Convention. *Declarations Lodged by the Kingdom of the Netherlands Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Accession*, UNIDROIT, <https://www.unidroit.org/instruments/security-interests/cape-town-convention/states-parties/d-netherlands-ct/> [<https://perma.cc/Z7PD-BXVM>]. It has entered into force on September 1, 2010. *The Kingdom of the Netherlands, the European Union and the Cape Town Convention*, EBARY.NET, [https://ebruary.net/32364/law/kingdom\\_netherlands\\_european\\_union\\_cape\\_town\\_convention#aftercont](https://ebruary.net/32364/law/kingdom_netherlands_european_union_cape_town_convention#aftercont) [<https://perma.cc/LX7Z-DPC6>]. The treaty applies in the *Caribbean Netherlands*, and when a lease and finance transaction is *properly* structured, this convention also has direct effects in the *European Netherlands*. *Id.* Jointly, the Caribbean Netherlands and European Netherlands form *the Netherlands*. *What Are the Different Parts of the Kingdom of the Netherlands?*, GOVERNMENT OF THE NETHERLANDS, <https://www.government.nl/topics/caribbean-parts-of-the-kingdom/question-and-answer/what-are-the-different-parts-of-the-kingdom-of-the-netherlands> [<https://perma.cc/V946-K8FS>]. When an aircraft is leased by a (sub)lessee (*debtor*) in the Caribbean Netherlands or it is *registered* there, the Cape Town Convention applies. The aircraft obtains the 'PH-flag' of the Netherlands *and* can be operated without any problems in the European Union and worldwide!

airline.<sup>112</sup> A reason for this hostile approach may be that most United States-trained aviation finance and lease lawyers have neither learned in their law school, nor during professional training, that security interests of lessees may be established pursuant to Article 9 of the UCC. This implies that they will have no clue that this kind of secured right can, in turn, be the basis of a registrable international interest under article 2(2)(a) of the Cape Town Convention.<sup>113</sup> Consequently, they will *not* advise their clients to negotiate and obtain these interests. This is even the case when these lawyers are representing American-based airlines and other operators of aircraft. This is amazing, as the local secured rights of the lessees originated in the United States. More specifically, they find their origin in the old pre-UCC substantive property laws of New York and Pennsylvania. See more details, *supra*.

In addition, anecdotal evidence affirms that, generally, aviation lawyers in the United States are rather uncomfortable having their clients provide security interests to lessees.<sup>114</sup> In the event that their clients are financiers and lessors, in their unsubstantiated view, this will obstruct the priority and hinder the enforcement of the registered international interests of these stakeholders. In practice, however, there exists no cause for alarm. To satisfactorily establish the desired priority, the international interest of the financier will be first-in-time registered at the International Registry. Subsequently, the interest of the lessor will be registered. The international interest of the airline will be recorded last-in-time. This registration procedure establishes that the ranking of the international interests of the financier and lessor will be satisfactorily guaranteed.<sup>115</sup> However, the Cape Town Convention declares

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<sup>112</sup> This particular information is based on the personal knowledge and practical expertise of the author himself. The author has discussed the matter at hand, *inter alia*, with the Secretary of the Aviation Working Group during meetings of the American Bar Association, its Aircraft Finance Subcommittee, a prominent Article 9 UCC security interest expert who was also a Member of the US Delegation to the Diplomatic Conference for the finalization of the Cape Town Convention in South Africa (2001), the Ministry of Justice of the Netherlands and several academics and practitioners in the US, UK and EU.

<sup>113</sup> *See id.*

<sup>114</sup> *See id.*

<sup>115</sup> *See* B. Patrick Honnebier, *The Cape Town Convention and the Aircraft Equipment Protocol: Protecting the Registered Secured Interests of Airline Lessees*, 30 AIR & SPACE L. 27, 34 (2005); *see also* Convention, *supra* note 43, ch. VIII, arts. 29(1) (covering priorities of registered international interests), 29(5) (explaining that the priority of competing international interests may be varied by an agreement between the holders of these interests).

that the priority of these international interests may be varied by an agreement which has been entered into by their holders.<sup>116</sup>

It is emphasized that the possibility of providing local New York law-based security interests to the lessees of aircraft, which rights may be the basis of registered international interests as provided for by the Cape Town Convention, is of major significance to any US-based airline or other operator. Depending on the location of the airline, in the United States or abroad, this opportunity may decide whether it will enter into an aircraft lease agreement. This is because the regime of the Cape Town Convention establishes extensive remedies, which can be enforced by the lessee in all its contracting states. This adds to the existing remedies of the secured rights obtained under New York or other local laws.

#### IV. CONCLUSION

The serious problem is that the lessee's secured interests in aircraft which have been validly established in one jurisdiction, may not be valid and enforceable in other countries.

Presently, in the United States, particularly pursuant to Article 9 UCC as implemented in New York, the lessors and lessees are heavily negotiating the legal and practical aspects of quiet enjoyment covenants in their lease agreements. However, they know, or should know, that the right of quiet possession of a lessee is legally not a secured right! To the contrary, the former is merely a personal right, and consequently, it has a limited effect. The right of quiet enjoyment can only be enforced against the lessor. Accordingly, it does not satisfactorily protect the lessee against the local and foreign creditors of the lessor! This issue is of major concern to the airline in the event that the initial lessor sells the aircraft to a new lessor which has grave intentions. In addition, it provides no security to the airline *vis-a-vis* third-party creditors when the lessor is defaulting or becomes insolvent.

Therefore, it is of utmost importance that the mandatory uniform substantive aviation related regime of the Cape Town Convention applies. Only this treaty does adequately guaranty the financial interests of the financier, lessor *and* lessee at the global level as it applies in the United States and more than eighty other Contracting States! More specifically, the Cape Town Convention appropriately protects the secured interests of the airlines, as, in turn, these rights can form the basis of registered international interests. Consequently, all the stakeholders are well-advised to

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<sup>116</sup> See Convention, *supra* note 43, ch. VIII, art. 29(5).



structure their financial and lease transactions via the Contracting States of the Cape Town Convention. However, it is pertinent that the relevant Contracting State strictly abides to the goal, intent, and sphere of application of this treaty.<sup>117</sup> It is concluded that the Cape Town Convention provides for a modern and solid uniform substantive aviation finance and lease regime which adequately protects the registered international interests of the lessees and all the other stakeholders.

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<sup>117</sup> In the international aviation finance and lease practice, certain jurisdictions are known as *high-risk* states. See Sidanth Rajagopal & Kevin J. Pearson, *The Accession of the State of Qatar to the Cape Town Convention*, K&L GATES (Nov. 5, 2020), <https://klgates.com/The-Accession-of-the-State-of-Qatar-to-the-Cape-Town-Convention-11-5-2020> [<https://perma.cc/R8A4-GYA5>]. This is due to the fact they do *not* abide to the mandatory regime of the Cape Town Convention. *Id.*