

THE AVIATION LAW
REVIEW

SIXTH EDITION

Editor
Sean Gates

THE LAWREVIEWS

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REVIEW

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PREFACE

The sixth edition of *The Aviation Law Review* marks the continuation of one of The Law Reviews' most successful publications; the readership of which has been vastly enhanced by making it accessible online since the fifth edition to over 12,000 in-house counsel as well as subscribers to Bloomberg Law and LexisNexis. This year I welcome new contributors from Egypt, Israel, Lebanon and Romania, as well as extending my thanks and gratitude to our seasoned contributors for their continued support. Readers will appreciate that contributors voluntarily donate the considerable time and effort needed to make these contributions as useful as possible to readers.

As this is written, news has come in of an aviation disaster in Cuba where an ageing 737 operated by Mexican carrier Global Air, on behalf of Cubana crashed during a domestic flight, killing 110 of the occupants. The Mexican carrier had assumed responsibility for the liabilities under its agreement with Cubana and reportedly insured the hull and liabilities in Russia. The accident will throw up familiar issues as to the extent to which Cubana audited the operation of Global Air, the latter having apparently been barred for safety reasons from operating in Guyana. Doubtless plaintiff lawyers from Florida will be gathering to secure instructions and seek routes out of Cuba's jurisdiction to maximise compensation, and questions will be asked about the adequacy of oversight of the operator given reports as to its operating history.

In the year since the last review was published, there have been some significant developments with regard to international air carrier liability, with both Russia and Thailand acceding to the Montreal Convention on air carrier liability of 1999 alongside Chad, Indonesia, Mauritius, Sudan and Uganda. Russia, which seems to have had a disproportionate share of recent aviation accidents (Socchi in 2016 and Saratov in 2018), will now face the challenge of persuading its domestic courts to apply the treaty, as they have, historically, awarded moral damages in the absence of bodily injury in Warsaw Convention cases. Thailand's accession brings one of the jurisdictions that has been most resistant to international regulation of carrier legal liability to passengers (ever since the Warsaw Convention of 1929) within the international family. International practitioners will also be aware of the historic resistance of Brazilian courts to the internationally accepted exclusivity of the Warsaw/Montreal system, with many Brazilian courts preferring to apply conflicting provisions of national law. The recent decision of the Brazilian Supreme Court upholding the supremacy of the Montreal Convention may mark a turning point in what has historically been a difficult country within which to defend aviation liability claims.

Inevitably, the European aviation legal scene continues to be dominated by Brexit where reassuring words, at least by regulators in the UK, have yet to be capped by any positive developments in terms of final agreements. This has led major carriers to focus on developing

European air operator certificates and some are also now ensuring they satisfy the European tests for majority ownership, which may cause interesting issues in the future for some of the low-cost carriers that heretofore have been able to operate from the UK – assuming always that the UK continues to apply majority ownership and control rules and that outmoded rule does not fall away.

The other seemingly inevitable development of note within Europe concerns the infamous EU Regulation 261, which from its humble beginnings as a modest attempt to ensure fair treatment of passengers has become, by virtue of the legislative inclinations of the Court of Justice of the European Union (CJEU), a monster devouring the assets of European airlines. Practitioners will be aware that one of the principal focuses of attack of the CJEU has been to decree that although airlines are entitled to a defence based on exceptional measures, nowadays in Europe there are no exceptions.

The latest decision defining extraordinary as ordinary is that of *Krusemann v. TUI Fly* where the CJEU held that a wildcat strike by flight staff following a surprise announcement of a restructuring does not constitute an extraordinary circumstance releasing the airline from its obligation to pay compensation in the event of cancellation or long delay of flight. The court reasons that the risks arising from the social consequences that go with such measures are inherent in the normal exercise of the airline's activity. The decision is another in a long line of aviation decisions by the CJEU that underscore the proposition that in European jurisprudence, Orwellian doublethink is alive and well! As was made clear at a recent conference of the European Regions Airlines Association, the uninformed extrajudicial legislative impulses of the CJEU in this area threatens regional connectivity and the operation of routes that are only marginally profitable. It can hardly be appropriate to inhibit operations in the regions so as to provide passengers with compensation from events that in any right-thinking person's view would be regarded as outwith the reasonable control of the operator. The European Regions Airline Association continues with other industry groups to lobby for change, which, once Brexit takes effect and the Spanish veto on progress pending resolution to its satisfaction of the Gibraltar dispute falls away, may at last happen.

CJEU 261 decisions are not uniformly in favour of consumers. In May 2017, the Court held in *Marcela Pešková v Travel Service* that a collision between an aircraft and a bird may constitute extraordinary circumstances. The decision is contrary to the EU advocate general's 2016 opinion in the case, which stated that bird strikes do not constitute extraordinary circumstances. The ruling is inconsistent as it appears to contradict the consolidated consumer-friendly court's orientation regarding the interpretation of extraordinary circumstances, and though welcome to carriers and comporting with common sense, underlines that the CJEU does little to ensure the predictability of the court; which of course is in conflict with its own principle of legal certainty, in its supposedly mandatory General Principles of Law.

The year 2017 also posed a number of new old problems for aviation legal practitioners in the context of aviation liquidations; not least of Air Berlin, Alitalia and Monarch Airlines. The collapse of Monarch and the consequent costs incurred by the UK Department for Transport (DFT) posed another challenge to the funds held by the DFT to support passengers stranded in the event of airline collapse. The DFT has announced an independent airline insolvency review to determine whether its system is fit for purpose and adequate to protect passengers after having to repatriate 110,000 passengers following the collapse. The risk for operators is, of course, that the assets of the many will be used to repatriate the passengers

of the few at further and greater cost to the many, which has inevitably resulted in resistance from trade bodies including the International Air Transport Association.

In the regulatory world, the General Data Protection Regulation has been an immense boon to regulatory lawyers while burdening all industries including aviation. Numerous developments have also taken place with regard to unmanned aerial devices following a series of near misses around the world. At the same time, Amazon and Google are collaborating on package delivery by drone and Boeing is actively pursuing the goal of pilotless aircraft. Each of these developments has and will continue to produce new regulations, and developments in this area will continue to be followed closely in this Review.

Once again I would like to extend my thanks to the many contributors to this volume and welcome those who have joined the group. Their studied, careful and insightful contributions are much appreciated by all those who now refer to *The Aviation Law Review* as one of their frontline resources.

Sean Gates

Gates Aviation Limited

London

July 2018

CAYMAN ISLANDS

*Dale Crowley, Wanda Ebanks, Shari McField and Barnabas Finnigan*¹

I LOCAL REGISTRATION

i The regulator

The Civil Aviation Authority of the Cayman Islands (CAACI) is responsible for the regulation of the aviation industry within the Cayman Islands. A body corporate originally established under the Civil Aviation Authority of the Cayman Islands Law 1987 (the current law is the Civil Aviation Authority Law (2015 Revision)), this self-funding statutory authority has actually proven to be a revenue-generating operation for the Cayman Islands government.²

The CAACI's functions include those conferred on the Governor of the Cayman Islands by the Air Navigation (Overseas Territory) Order 2013 (ANOTO) and other similar regulations.³ The CAACI's authority covers all aspects of regulation and supervision of the aviation sector within the jurisdiction, including aircraft registration through the Cayman Islands Aircraft Registry operated by the CAACI (the Registry), safety of air navigation and aircraft (including airworthiness), regulation of air traffic, certification of operators of aircraft, licensing of air crews, licensing of air transportation services and certification and licensing of airports.⁴ The CAACI is also responsible for ensuring that civil aviation in the Islands conforms to the standards of the International Civil Aviation Organization, established by the Convention on International Civil Aviation, signed in Chicago on 7 December 1944 (ICAO).

The CAACI is headed by a director general and a statutorily appointed board of directors. The board is responsible for the effective implementation and performance of the CAACI in accordance with applicable law.⁵

1 Dale Crowley and Wanda Ebanks are partners, and Shari McField and Barnabas Finnigan are associates, at Maples and Calder.

2 CAACI revenues are generated from regulatory activities and the registration of aircraft (private and corporate) on the Cayman Islands Aircraft Registry. The CAACI's latest annual report indicates that 2015–2016 was another successful year for the CAACI.

3 Civil Aviation Authority Law (2015 Revision), Section 5(1)(a).

4 *Ibid.*, Section 5(1)(a).

5 Civil Aviation Authority Law (2015 Revision), Section 7(1).

The register maintained by the Registry (the Aircraft Register) is primarily a 'private-use category' register and aircraft registered thereon must not be used for commercial operations (i.e., for 'hire or reward') unless a separate air operator's certificate (AOC) is granted.⁶ Despite its relatively small size,⁷ the Registry has evolved as a highly regarded private aircraft registry.

ii Registration of aircraft

Requirements relating to the registration of aircraft are fully set out in the ANOTO.

Eligibility for registration

To register an aircraft with the Registry, the owner, or, if the aircraft is chartered, the charterer by demise, must be a 'qualified person' as defined in the ANOTO.

A qualified person includes:

- a the Crown in right of Her Majesty's government in the United Kingdom or in right of the government of the territory;
- b United Kingdom nationals;
- c Commonwealth citizens;
- d nationals of any European Economic Area state;
- e bodies incorporated in any part of the Commonwealth and that have their registered office or principal place of business in any part of the Commonwealth; or
- f undertakings formed in accordance with the law of a European Economic Area state and that have their registered office, central administration or principal place of business within the European Economic Area.⁸

An unqualified person holding a legal or beneficial interest in an aircraft or a share therein may still register an aircraft if he or she resides or has a place of business in the Cayman Islands and the CAACI is satisfied that the aircraft may properly be registered. Similarly, if the aircraft is chartered by demise (whether by dry or wet lease) to a qualified person the CAACI may permit registration, irrespective of whether an unqualified person is entitled as owner to a legal or beneficial interest in an aircraft or a share in the aircraft. Both of the foregoing exceptions are subject to the discretion of the CAACI and the full facts and circumstances must be presented to the CAACI before any such registration will be considered.

The ANOTO also provides that an aircraft shall not be registered or continue to be registered in the Cayman Islands if it appears to the Registry that:

- a the aircraft is registered outside the Cayman Islands and that registration does not cease by operation of law upon the aircraft being registered in the Cayman Islands;
- b an unqualified person holds any legal or beneficial interest in the aircraft;
- c the aircraft could more suitably be registered in some other state (including the United Kingdom and its territories and dependencies) that is a party to the ICAO; or
- d it would be inexpedient in the public interest for the aircraft to be or to continue to be registered in the Cayman Islands.

6 Only six approved AOC holders are reported in the 2015–2016 CAACI Annual Report.

7 As at 19 May 2017, the CAACI records indicated a total of 241 aircraft were registered on the Cayman Islands Aircraft Registry (Active Aircraft Register on CAACI website at www.caacayman.com).

8 Air Navigation (Overseas Territories) Order 2013, Article 16(1).

Requirements for registration of aircraft for private use

Applications for registration are made to the CAACI and applicants can typically take advantage of the CAACI's online portal, VP-C Online, to submit much of the documentation supporting the application.

The application process is as follows:

- a* submission of an aircraft registration application to the Registry and payment of deposit;
- b* satisfactory completion of financial and legal due diligence with respect to the applicant;
- c* issuance by the Registry of (1) notice of acceptance of the applicant, and (2) a reserved Cayman Islands registration mark;
- d* completion of airworthiness survey of aircraft by a CAACI surveyor;
- e* completion and submission of supporting documentation (including various technical forms); and
- f* effecting deregistration from existing state of registry (if applicable).

A Cayman Islands certificate of registration, certificate of airworthiness and all associated certification documents will be issued by the Registry on registration.

Requirements for registration of aircraft for commercial operations

An application for a Cayman Islands AOC permitting the holder to undertake commercial operations requires provision of certain information, including the following:

- a* the official name, address and telephone number of the applicant;
- b* the types, serial numbers and registration marks of each aircraft for which a certificate is required;
- c* the purpose for which the aircraft will be operated;
- d* the specific location of the principal operating base and any other places at which the aircraft will be operated or based;
- e* the names and addresses of organisations responsible for all maintenance of each type of aircraft;
- f* the names, qualifications and experience of the accountable manager and nominated post holders and details of the duties for which each individual is responsible (with résumés); and
- g* the names, qualifications and experience of persons nominated to be responsible for conducting on behalf of the operator, the training and assessments specified in the relevant legislation.⁹

In addition, the CAACI requires that the holder of a Cayman AOC operate a Cayman Islands office. An applicant for an AOC is encouraged to seek Cayman Islands legal advice on setting up a physical presence in the Cayman Islands to meet this requirement.

Fees payable on registration of aircraft

The fees payable on registration of aircraft are set out in the Air Navigation (Fees) Regulations 2010. A summary of these may be found on the CAACI's website at: www.caacayman.com.

⁹ More detailed information is available from the CAACI directly.

Effect of registration

The registration of title to the aircraft constitutes *prima facie* evidence of ownership of the aircraft. However, such evidence is not conclusive. The ANOTO provides that, to the extent its provisions apply to Cayman Islands aircraft, such provisions have extraterritorial effect.¹⁰

No registration of leases

Leases are not required to be registered with the Registry in relation to Cayman registered aircraft and the law of the Cayman Islands does not otherwise provide for their registration by filing or recording in the Cayman Islands.

Deregistration of aircraft registered with the Registry

When it becomes necessary to deregister an aircraft from the Registry (following a sale or otherwise):

- a the registered owner¹¹ or the person responsible for the aircraft, must provide the CAACI with instructions to deregister the aircraft;
- b the registered owner's financial account with the CAACI must be fully settled;
- c if a certificate of airworthiness for export is required by the importing state, a CAACI surveyor must inspect the aircraft prior to issuance. To initiate this process a certificate of airworthiness request form must be submitted to the CAACI;
- d the original certificate of registration must be submitted to the CAACI, with Section III on the reverse side signed by the registered owner of the aircraft or the person responsible for the aircraft (accompanied by the related certified power of attorney in the latter case);
- e if an aircraft has a mortgage registered against it on the aircraft mortgage register maintained by the Registry (the Mortgage Register), the mortgagee must confirm in writing to the Registry how the mortgage is to be addressed following deregistration. If the mortgage is to be discharged, this must be effected prior to or simultaneously with deregistration. If not, the CAACI will require a certified or notarised confirmation letter from the mortgagee that:
 - the mortgage will not be discharged;
 - the mortgage remains in force; and
 - a notation will remain on the Mortgage Register; and
- f if necessary, the CAACI will confirm to the new state of registry that the aircraft is being or has been deregistered from the Register.

In a default enforcement scenario, the above deregistration procedure applies save that the following will also be required:

- a a notarised or original deregistration power of attorney (in favour of the person seeking to instruct the CAACI);
- b proof of default under the agreement giving rise to the right to deregister the aircraft and the details thereof;
- c proof of right to deregister the aircraft in an event of default (i.e., reference to the relevant section of the agreement);

¹⁰ Air Navigation (Overseas Territories) Order 2013, Article 188 (1).

¹¹ References to 'registered owner' mean either the owner or the charterer by demise (as relevant).

- d* confirmation that the adversely affected party is seeking to enforce its rights under the agreement; and
- e* if the enforcement is contentious and the original certificate of registration cannot be obtained from the owner, an affidavit by the adversely affected party confirming that to be the case and requesting deregistration of the aircraft indicating the new state of registry.

iii Security and aircraft mortgages

Aircraft mortgages may be governed by the law chosen by the parties. If the parties agree that it will be governed by foreign law, the Cayman Islands courts will uphold contractual terms to that effect unless the selection of the governing law was (1) made in bad faith, (2) illegal or contrary to the public policy of the Cayman Islands, or (3) would not be regarded as a valid and binding selection or be upheld by the courts of the foreign jurisdiction selected.

A mortgage in relation to an aircraft registered in the Cayman Islands may be registered in the Mortgage Register to secure the benefit of priority.

The Cape Town Convention (referenced below) came into force in the Cayman Islands on 1 November 2015 pursuant to the International Interests in Mobile Equipment (Cape Town Convention) Law 2015 (the Cape Town Law). At present under Cayman Islands law, there exists a dual system for perfection and priority of security over Cayman registered aircraft for entities that qualify as follows:

- a* where there is a registerable ‘international interest’ under the Cape Town Convention (as defined in the Cape Town Law), any such international interest in respect of an aircraft may be recorded on the international registration facilities established under the Cape Town Convention (the IR). Registration on the IR is permitted for aircraft that qualify under the Cape Town Convention. Cape Town registrations and filings on the IR are made in the usual way. Where an international interest has been registered against an aircraft that is registered with the CAACI in accordance with the Cape Town Convention, priority of a mortgage over that aircraft will be determined solely by the filings on the IR. No additional registrations are required with the CAACI in relation to a mortgage over such aircraft; or
- b* if the Cape Town Convention does not apply, then the priority of a registered mortgage against Cayman Islands registered aircraft will be determined in accordance with registration on the Mortgage Register pursuant to the Mortgaging of Aircraft Regulations 2015 (the Regulations). The Regulations, among other things, offer a system for obtaining priority for a security interest, perfecting the security interest and protection from deregistration of an aircraft without the registered mortgagee’s consent. Registration on the Mortgage Register constitutes express notice to all persons of all facts appearing thereon.

Requirements to register a mortgage with the CAACI

To register a mortgage on the Mortgage Register:

- a* a completed or executed application form must be submitted on behalf of the mortgagee;

- b the application must be accompanied by a copy of the mortgage (a PDF copy is sufficient and advisable since Cayman Islands stamp duty becomes payable if the original mortgage is brought to or executed in the Cayman Islands);¹² and
- c payment of the applicable mortgage registration fee must be made.

It is also possible to file a priority notice with the Registry by filing the applicable documentation and payment of the relevant fee. Provided the relevant mortgage is filed within 14 days of the date of such a priority notice it shall be deemed to have priority from the time when the priority notice was registered.

Under the current legislation, an international interest (as defined in the Cape Town Law) registered on the IR has priority over any other interest subsequently registered on the IR and over an interest that is not registered on the IR, subject to certain exceptions.¹³

Discharge of mortgage registered with the CAACI

The following is the procedure to effect deregistration of a mortgage with the CAACI:

- a submission of a mortgage discharge form signed by the mortgagor and mortgagee (together with copies of signing authorities);
- b provision of a copy of a fully executed deed of release of mortgage. Alternatively, a letter addressed to the CAACI signed by an authorised signatory of the mortgagee instructing the CAACI to deregister the mortgage will suffice; and
- c payment of the applicable mortgage discharge fee.

Creditor rights

The courts of the Cayman Islands will enforce a foreign money judgment made against the owner or charterer by demise of a Cayman Islands registered aircraft without a retrial of the merits provided the judgment: (1) is made by a foreign court of competent jurisdiction; (2) imposes on the judgment debtor a liability to pay a liquidated sum for which the judgment has been given; (3) is final; (4) is not in respect of taxes, a fine or a penalty; (5) is not impeachable on the grounds of fraud; and (6) does not offend natural justice or the public policy of the Cayman Islands.¹⁴

The judgment creditor holding an enforceable foreign judgment has a wide range of options to enforce the judgment against the debtor. These include: (1) writs of *fi. fa.* (i.e., seizure and sale of goods); (2) charging orders in respect of land and securities; (3) garnishee orders (i.e., attachment of debts including bank deposits); (4) appointment of a receiver (who might collect receivables or even run a business); or (5) an attachment of earnings order.

Recent English authorities (which are persuasive, although not binding on the Cayman Islands courts) suggest that foreign judgments that are integral to bankruptcy proceedings may be enforceable without satisfying the usual requirements set out at the first paragraph above and without the need to embark on fresh proceedings in the Cayman Islands. However, these authorities have yet to be fully considered by the Cayman Islands courts.

12 *Ad valorem* duty at the rate of 1.5 per cent of the sum secured is payable if the original mortgage is executed in or brought to the Cayman Islands following execution.

13 See Sections 3 and 4 of the International Interests in Mobile Equipment (Cape Town Convention) Law 2015.

14 In any application to exercise enforcement options under Cayman Islands law, the judgment creditor will need to establish the factors outlined above, to the satisfaction of the Cayman Islands court.

Assignment of security rights

Security interests may be assigned under Cayman Islands law. If an assignment is to be governed by Cayman Islands law, it should be in writing and notice of the assignment must be given to the debtor to perfect the assignment. If the document creating the security interest is brought to, or executed in, the Cayman Islands, it must be stamped with applicable Cayman Islands stamp duty.

A Cayman Islands company must make an entry in its register of mortgages and charges in respect of all mortgages and charges created by it under any transaction documents to comply with local law; failure by the company to comply with this requirement does not operate to invalidate any mortgage or charge though it may be in the interests of the secured parties that the company should comply with the statutory requirements. The register of mortgages and charges is not a public document and is maintained by the company's registered office in the Cayman Islands on the company's minute book.

Enforcement of security over aircraft registered in Cayman¹⁵

Enforcement will be determined by the provisions of the relevant agreement.

Taking physical possession of the aircraft is permitted under Cayman Islands law. Self-help remedies are permitted without the need to obtain a court order; however, it is open to the relevant enforcing party to seek a court order.

Permission of the CAACI is not required prior to pursuing remedies on enforcement. However, possession via either a transfer of title or change of details of the entity registered with the CAACI will require the cooperation of the CAACI (and thus compliance with CAACI's transfer formalities for Cayman-registered aircraft).

Liens and rights of detention

Liens are not registrable in the Cayman Islands.

It is believed¹⁶ that the following aircraft liens exist under Cayman Islands law:

- a* seller's lien – pursuant to the Sale of Goods Law (1997 Revision), an unpaid seller may have a lien over an aircraft to the extent that the buyer fails to pay the purchase price;
- b* salvage lien – based on the principle that a person providing voluntary assistance should recover their costs prior to the other parties with an interest in vessels;¹⁷
- c* possessory lien – a common law legal lien relating to specific aircraft. Applicable where a person bestowed labour upon authorisation from its owner, enhancing the aircraft's value. That person will have a lien on the aircraft to the extent that it remains unpaid for its labour; and
- d* contractual lien (including pledge) – parties may create a lien by contract that is 'certain', regardless of whether a possessory lien exists at common law. The owner of an aircraft may pledge it to the creditor as security for a debt, or a lien may arise as a result of a person expending labour on an aircraft, which improves its value in some way in accordance with a contractual agreement, or a contractual salvage lien may also arise.

15 Enforcement by a Cayman court requires originals of the relevant documents (with Cayman stamp duty paid thereon), and applicable court fees to be paid.

16 It is not possible to be definitive since no legislation and, to the best of our knowledge, no Cayman Islands case law has analysed aircraft liens in detail.

17 The absence of relevant cases makes it uncertain whether an aircraft salvage lien can be asserted in the Cayman Islands.

The Cayman Islands are not a signatory to international conventions that relate to aircraft liens.¹⁸ However, the Cayman court will recognise a foreign aircraft lien provided it is valid under its appropriate governing law, subject to qualifications relating to enforceability being met.

In addition to aircraft liens, under the Cayman Islands legislation persons can be granted a right to detention. In the event that more than one detention right exists over an aircraft at the same time, their priority will likely be determined according to the time each contravention occurred. In addition to the statutory rights to detain aircraft, detention may also arise as result of a breach of contract or in a case where an attachment of an aircraft is sought (e.g., for the non-payment of a debt or on the liquidation or insolvency of the owning company). Statutory detention rights are generally not based on possession and do not seek to prevent other parties with an interest in the aircraft from having access to it.

- Under Cayman Islands law, persons are granted a right to sell (or detain) an aircraft for:
- a* Airport charges: aircraft can be detained and sold for non-payment of airport charges; default of payment creates a statutory lien.¹⁹
 - b* Customs: where anything becomes liable to forfeiture under the Customs Law (2017 Revision), any aircraft used for the carriage, handling, deposit or concealment of that thing shall also be liable to forfeiture. Forfeiture of an aircraft may also occur where it has been adapted to be used for or is used for the purposes of smuggling or concealing goods.²⁰
 - c* Crimes: where a person is convicted of an offence, any vessel in his or her possession or under his or her control that was used in connection with such an offence or intended to be used for that purpose may be forfeited to the Crown by order of the court.²¹
 - d* War or national emergency: regulations made under the Emergency Powers Law (2006 Revision) can give powers to the governor of the Cayman Islands to authorise the taking possession or acquisition of any property.²²
 - e* Terrorism: the court can make a forfeiture order in accordance with Section 28 of the Terrorism Law (2018 Revision).

The priority of domestic aircraft liens and detention rights will be in the following order:

- a* statutory detention rights;
- b* contractual lien;
- c* salvage lien;
- d* possessory lien;
- e* registered mortgages; and
- f* unregistered mortgages.

18 The 1948 Geneva Convention on the International Recognition of Rights in aircraft or the 1933 Rome Convention on Precautionary Arrest.

19 Airports Authority Law (2005 Revision) Section 34.

20 Customs Law (2017 revision) Section 61.

21 Misuse of Drugs Law (2017 Revision) Section 25(2). Note also that the court has broad powers under the Proceeds of Crime Law (2017 Revision) to order the confiscation of property derived from the proceeds of criminal conduct. (Applications for compensation in these situations are dealt with thereunder.)

22 Emergency Powers Law (2006 Revision) Section 5(2)(b).

The priority of foreign aircraft liens before a Cayman court will be determined by Cayman Islands law, as the law of the forum deciding the matter (the *lex fori*), since the question of priority is a procedural rather than a substantive matter under Cayman Islands law.

iv Strict liability under Cayman Islands law

The owner of an aircraft registered with the CAACI is subject to Section 40(2) of the Civil Aviation Act 1949 (as extended to the Cayman Islands by the Civil Aviation Act 1949 (Overseas Territories) Order 1969), which states that:

Where material loss or damage is caused to any person or property on land or water by, or by a person in, or an article or person falling from, an aircraft while in flight, taking off or landing, then unless the loss or damage was caused or contributed to by the negligence of the person by whom it was suffered, damages in respect of the loss or damage shall be recoverable without proof of negligence or intention or other cause of action, as if the loss or damage had been caused by the wilful act, neglect, or default of the owner of the aircraft:

Provided that where material loss or damage is caused as aforesaid in circumstances in which:

- a damages are recoverable in respect of the said loss or damage by virtue only of the foregoing provisions of this subsection; and*
- b a legal liability is created in some person other than the owner to pay damages in respect of the said loss or damage;*

the owner shall be entitled to be indemnified by that other person against any claim in respect of the said loss or damage.

The normal exemption on which a passive owner relies is contained in Section 76(4) of the Civil Aviation Act 1982 as extended to the Cayman Islands by the Civil Aviation Act 1982 (Overseas Territories) (No. 2) Order 2001, which states that:

Where an aircraft has been bona fide demised, let or hired out for any period exceeding fourteen days to any other person by the owner thereof, and no pilot, commander, navigator or operative member of the crew of the aircraft is in the employment of the owner, Section 40(2) of the Civil Aviation Act 1949 (as extended by the Civil Aviation Act 1949 (Overseas Territories) Order 1969 to any of the Territories specified in Schedule 2 to this Order) shall have effect as if for references to the owner of the aircraft there were substituted references to the person to whom the aircraft has been so demised, let or hired out.

v Emerging trends

Registration of 'green aircraft'

The CAACI is able to accommodate registration of aircraft on the Aircraft Register for short periods; for example, during the fit-out stage following a 'green delivery'. The applicant must qualify to register an aircraft on the Aircraft Register as discussed above. In lieu of a certificate of airworthiness, the CAACI will issue special flight authorisations as may be required to transport the aircraft. One attractive feature of this offering is that the aircraft may be subject to the financiers' registered security interest. Once the period specified for the registration is

concluded, the aircraft can be deregistered and re-registered on an alternative register as may be required; for example, for commercial operations. The deregistration process is simple and low cost and can be completed on a same-day basis.

Article 83 bis arrangements

Notwithstanding that the Registry is primarily for private use aircraft, the CAACI have been open to putting in place arrangements under Article 83 *bis* of ICAO, which permits the Registry to transfer all or part of its functions relating to oversight and operation to the state of operation of the aircraft. The Cayman Islands currently has an Article 83 *bis* arrangement with Saudi Arabia.

II INTERNATIONAL FINANCE TRANSACTIONS

Although commercial aircraft are not commonly registered in, or operated out of the Cayman Islands, the jurisdiction plays an important role in the structuring of some of the more complex cross-border transactions used in the acquisition, financing and leasing of aircraft.

The Cayman Islands' long-established reputation for being politically stable, tax neutral and having a well-established legal system based on English common law principles has led to the jurisdiction's preferred status as a place to establish special purpose vehicles (SPVs) for owning or leasing aircraft.

The SPV will typically hold title to the aircraft. SPVs are flexible corporate structures that can be utilised either as a single-aircraft owning company or to hold multiple aircraft in a single entity. The acquisition of the aircraft by the SPV will most commonly be financed by way of a loan from a third-party lender, who will in turn take security over the aircraft in the form of an aircraft mortgage. Other typical features include the granting of security over lease payments in the structure and a charge or mortgage over the issued share capital of the SPV itself.

Although these traditional debt financing arrangements remain the norm, other alternative forms of financing are becoming increasingly common and in recent years there has been a marked increase in the number of aircraft financing transactions accessing the capital markets (e.g., through bond issuances; use of the Enhanced Equipment Trust Certificates (EETC) regime; or through direct equity injection from private equity firms).

There are two basic structures that are commonly used for the financing and leasing of aircraft through a Cayman Islands SPV: (1) an off-balance sheet, bankruptcy remote or 'orphan trust' structure; or (2) an on-balance sheet direct ownership structure.

A common advantage of both structures is the choice of the Cayman Islands as the jurisdiction of incorporation of the SPV. In both scenarios, the assets are held by a company incorporated in a first-class jurisdiction with a high degree of political and economic stability and a familiar and trusted legal system. Financiers find this particularly attractive as they are comfortable that if an enforcement event arises, the financing documents will be capable of enforcement in a jurisdiction where the legal system is based on English common law.

Another key advantage for both structures is taxation. The Cayman Islands does not currently have any form of direct taxation and therefore payments made into or out of the Islands will not be subject to taxation, under Cayman Islands law. To give additional comfort on this point, the Cayman Islands government will on request provide an undertaking confirming that the SPV is exempt from direct taxation in the Cayman Islands for a period of 20 years from the date of the issuance of the undertaking.

i Off-balance sheet structures

In a typical Cayman Islands orphan trust structure: (1) the issued share capital of the SPV will be held by an offshore trust company as share trustee on charitable or purpose trusts; and (2) the directors of the SPV will be provided by a third-party corporate administrator (which is often the same entity as the share trustee) pursuant to the terms of an administration agreement entered into between the SPV, the administrator and the airline or leasing company.

The SPV will enter into the financing and leasing documents necessary to enable it to acquire the aircraft, and lease it to an end user (which is typically an airline).

To avoid either a breach of duty or the payment of significant transaction fees to the SPV to balance the commercial risk of the assumption of open-ended loan repayment obligations, the SPV limits its obligations both in amount and recourse to the value of the security granted by the SPV. As the SPV will grant security over all its material assets (namely, the aircraft and its rights under the lease) the lender is not being deprived of recourse against any significant asset.

Following termination of the transaction, the trust will terminate and the trust property (namely, the issued share capital and any transaction fees earned by the SPV net its expenses, (i.e., the net asset value of the SPV)) will be distributed by the trustees to one or more charities as the trust document provides.

A key attraction of this structure is that ownership of the aircraft does not vest with the airline but with the SPV owned and controlled by the trust company, which holds title in an off-balance sheet capacity. This ensures that the SPV will not be consolidated on the balance sheet of the lender, airline or the trustee.

From the lender's perspective, the fact that the bankruptcy of the airline will not have an impact on the assets provides lenders a greater degree of control and certainty over the underlying assets that constitute the basis of their security. Additionally, as the SPV is entirely independent from both the lender and the airline, in a default scenario the lender is likely to experience a greater degree of cooperation from and (through the covenants in the financing documents) control over the SPV.

ii On-balance sheet structures

In a typical on-balance sheet structure, either the airline or operator, or the financier, will establish the SPV directly and will hold the shares in the SPV themselves (rather than these being held on the terms of a charitable or purpose trust). The directors are also commonly employees or nominees of the shareholder (although it is not uncommon for one or more of the directors to be provided by a third-party corporate administrator to act as an 'independent director').

The choice of structure will depend on a number of factors including the jurisdiction where the airline is incorporated, the jurisdiction in which the aircraft will be operated, the desired tax treatment of the overall structure and the needs of the financiers.

The on-balance sheet structure lacks bankruptcy-remote characteristics and there will be implications up and down the chain upon a default or winding up of one or other of the parties. There is also not the same protection from consolidation as that offered in an orphan structure as the assets of the SPV are likely to be treated as being consolidated onto the balance sheet of the parent shareholder.

III EMERGING TRENDS

There continues to be a strong interest in alternative sources of funding for aviation financing transactions, and the trend for using transaction structures that allow airlines and lessors to access the capital markets looks set to continue through 2018 and 2019.

Asset-backed securitisation platforms structured using Cayman-incorporated Irish tax resident issuers to issue notes, the proceeds of which are used to acquire an underlying portfolio of aircraft, remain popular. Even where the issuer vehicles are not incorporated in the Cayman Islands, many of the issuer vehicles are taking advantage of the flexible and user-friendly listing regime of the Cayman Islands stock exchange to list the notes and other securities.

There also continues to be interest in using EETC structures to finance the acquisition of new aircraft.

IV THE YEAR IN REVIEW

i Financing transactions

The securitisation of aircraft portfolios through Cayman Islands SPVs continues to show strong demand in the market, and it is expected that these will continue to be used to provide access to funding for portfolio acquisitions or financing, or both.

ii Ratification of Cape Town Convention

The ratification and implementation of the Cape Town Convention by the United Kingdom is of great significance to the Cayman Islands as it allows Cayman Islands incorporated SPVs to take full advantage of the registration regime implemented by the Convention. This is of particular importance for financing transactions as it means that financiers now have the ability to obtain a Cape Town registration for any security interests created in respect of an aircraft owned by a Cayman Islands incorporated SPV. In particular, the early adoption by the Cayman Islands of the creditor-friendly 'Alternative A' insolvency regime under the Cape Town Convention gives the Cayman Islands an advantage over other jurisdictions that have not adopted Alternative A.

iii Cayman Maritime & Aviation City

The Cayman Islands has recently approved the addition of the Cayman Maritime & Aviation City to the special economic zone, provided by Cayman Enterprise City, which is designed to make it easier for aviation services providers, including commercial air transport operators, aerospace developers and manufacturers to set up a physical presence in the Cayman Islands.

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