

Title: Ratification of the Convention on International Interests in Mobile Equipment and the Protocol thereto on matters specific to Aircraft Equipment IA No: BIS0362 Lead department or agency: Department for Business, Innovation and Skills Other departments or agencies: Department for Transport, Civil Aviation Authority, Insolvency Service	Impact Assessment (IA)		
	Date: 11th December 2014		
	Stage: Final		
	Source of intervention: International		
	Type of measure: Secondary legislation		
Contact for enquiries: Hayley Gowen - 020 7215 6096			

Summary: Intervention and Options	RPC Opinion: Green
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Cost of Preferred (or more likely) Option			
Total Net Present Value	Business Net Present Value	Net cost to business per year (EANCB on 2009 prices)	In scope of One-In, Two-Out? Measure qualifies as
£-0.98 m	£-0.48 m	£	Yes Zero net cost

What is the problem under consideration? Why is government intervention necessary?

UK airlines require large amounts of finance to hire or purchase helicopters, airframes and/or engines (“aircraft objects”). Following the economic downturn, the availability of traditional sources of finance for UK airlines, such as bank debt, has reduced and a number of airlines have looked to diversify their sources of finance. The Convention on international interests in mobile equipment and the Protocol thereto on matters specific to aircraft equipment (“the treaty”) is a private international law instrument which aims to facilitate asset-based, cross-border aircraft finance transactions by providing creditors with greater legal certainty that they can recover their assets in cases of default, which may lead to lower financing costs for purchasers and lessees.

What are the policy objectives and the intended effects?

The policy objective is to reduce the cost of raising aircraft finance to UK businesses. The treaty aims to reduce the risk to creditors of lending to airlines and leasing companies by creating a harmonised international legal framework for the creation and registration of *international interests* (such as mortgages and leases) and to deal with related disputes, including insolvency. A reduction in the risk to financiers in aircraft finance transactions should lead to a reduction in the cost of raising finance for airlines and others looking to purchase and/or lease aircraft and may result in increased sales by UK manufacturers. The policy therefore aims to overcome an information asymmetry issue, where foreign entities may give UK businesses higher risk ratings than they would if the UK adopted a harmonised international legislative system. Ratification of the treaty would enable interests created under the treaty and registered with the International Registry to be enforced through the UK courts.

What policy options have been considered, including any alternatives to regulation? Please justify preferred option (further details in Evidence Base)

Option 0 – Do nothing. This option was rejected as UK businesses would not benefit from the potential lower cost of raising finance and a potential related increase in sales for UK aircraft and engine manufacturers.

Option 1 – Ratify the treaty. This is the government’s preferred option as the provisions of the treaty could be enforced in the UK courts. UK businesses could benefit from a reduction in the cost of raising aircraft finance with potential benefits for UK manufacturers through increased sales.

Alternatives to regulation are unlikely to be suitable as they would not provide financiers with legal certainty that they can recover their asset if a purchaser or lessee defaults on repayments. The treaty contains a number of optional provisions. The Government’s approach to these optional provisions is set out in this impact assessment.

Will the policy be reviewed? It will be reviewed. If applicable, set review date: 12/2019					
Does implementation go beyond minimum EU requirements?				No	
Are any of these organisations in scope? If Micros not exempted set out reason in Evidence Base.		Micro Yes	< 20 Yes	Small Yes	Medium Yes
What is the CO ₂ equivalent change in greenhouse gas emissions? (Million tonnes CO ₂ equivalent)				Traded:	
				Non-traded:	

I have read the Impact Assessment and I am satisfied that, given the available evidence, it represents a reasonable view of the likely costs, benefits and impact of the leading options.

Signed by the responsible: _____ **Matthew Hancock** Date: _____ **23/03/2015**

Summary: Analysis & Evidence

Policy Option 1

Description: Option One

FULL ECONOMIC ASSESSMENT

Price Base Year 2014	PV Base Year 2014	Time Period Years 10 years	Net Benefit (Present Value (PV)) (£m)		
			Low: -1.92	High: -0.58	Best Estimate: -0.98

COSTS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Cost (Present Value)
Low	0.4	0.0	0.6
High	0.7	0.2	1.9
Best Estimate	0.5	0.1	1.0

Description and scale of key monetised costs by 'main affected groups'

Businesses involved in aircraft financing and UK airlines will incur one-off familiarisation costs to understand the changes to UK legislation. Total costs are estimated at £375,000 - £650,000. Businesses registering interests with the International Registry are likely to incur additional familiarisation costs to understand how to use the International Registry. Total business costs are estimated at £75,000 - £150,000. These costs will not be incurred by UK businesses already familiar with the International Registry such as legal firms advising non-UK airlines and UK financiers lending to airlines whose home state has already ratified the treaty. As registration with the International Registry is not mandatory, it would be up to business to decide whether the benefits of using the International Registry would outweigh the costs. If businesses choose to register with the International Registry rather than the UK National Register of Aircraft Mortgages run by the Civil Aviation Authority (CAA), the CAA may experience a reduction in annual income of £18,700 - £140,250.

Other key non-monetised costs by 'main affected groups'

Some businesses may face additional fees to register on the International Registry instead of, or in addition to, registering interests on the UK's National Register of Aircraft Mortgages, however registration of interests on the International Registry will not be mandatory allowing business to decide how best to protect its interests. Therefore we expect businesses will only choose to incur additional costs to the extent that they believe these costs are outweighed by the benefits.

BENEFITS (£m)	Total Transition (Constant Price) Years	Average Annual (excl. Transition) (Constant Price)	Total Benefit (Present Value)
Low			
High			
Best Estimate			

Description and scale of key monetised benefits by 'main affected groups'

Although there may be considerable benefits to UK businesses from reduced financing costs, it is not possible to monetise these benefits. However the benefits are very likely to outweigh the very small familiarisation costs, as even a slight reduction in financing costs for one airline would easily cover familiarisation costs for all airlines given the size of some aircraft financial deals (in the order of \$60-400m for a single aircraft).

Other key non-monetised benefits by 'main affected groups'

UK businesses may benefit from a reduction in the cost of raising finance to purchase and/or lease aircraft objects. This is difficult to quantify as airlines can raise finance in a number of ways and the circumstances of individual airlines differ. Lower financing costs may result in increased investment in aircraft and therefore increased sales by UK manufacturers. Depending on the maximum take-off weight of the aircraft, businesses could benefit from a reduction in the fee to register their interest on the International Registry compared with the UK's National Register of Aircraft Mortgages. Secondary benefits may include a reduction in administrative burdens as interests can be registered with the International Registry 24 hours a day, 7 days a week.

Key assumptions/sensitivities/risks	Discount rate (%)	3.5
The costs and benefits are based on an assumption that the amount of aircraft finance needed globally will continue to grow and that a number of UK businesses are already familiar with the International Registry. The benefits to individual airlines will depend on how the airline intends to raise finance and its individual circumstances. In some cases, individual airlines may not benefit from any reduction in the cost of raising finance due to factors outside the scope of this treaty.		

BUSINESS ASSESSMENT (Option 1)

Direct impact on business (Equivalent Annual) £m:	In scope of OITO?	Measure qualifies as
Costs: 0.04 Benefits: Net:	Yes	Zero net cost

Evidence Base (for summary sheets)

Background to the treaty

1. The Convention on international interests in mobile equipment and the Protocol thereto on matters specific to aircraft equipment (commonly called the “*Cape Town Convention*”) is a private international law treaty conducted under the auspices of the International Organisation for Civil Aviation (ICAO) and the International Institute for the Unification of Private Law (UNIDROIT). The aim of the treaty is to reduce the cost of raising finance for large, high value aircraft, helicopters and aircraft engines which routinely cross borders by reducing the risk to creditors of lending the finance to purchase or lease aircraft equipment.
2. The Convention provides an over-arching framework for the financing of large, high value assets that cross borders and the accompanying protocols address issues raised by financing a specific type of asset. There are three protocols currently in existence – aircraft equipment; rolling railway stock and space objects. The UK is only ratifying the Protocol on matters specific to aircraft equipment. Therefore this impact assessment does not consider ratification of either the rail or the space protocols.
3. The Convention and the Protocol, although separate instruments, should be seen as one treaty as the Convention is only effective alongside a protocol and has no effect on its own.
4. The treaty aims to reduce the cost of raising finance for aircraft, helicopters and aircraft engines above a certain size and engine capacity. It only applies to the aircraft objects meeting the following criteria:
 - aircraft which can carry at least eight people or 2750 kilograms of cargo or
 - aircraft engines with thrust exceeding 1,750 pounds-force (7,800 N) or 550 horsepower (410 kW) or
 - helicopters carrying 5 or more passengers

Light aircraft, such as those used by the general aviation community, are not covered by this treaty. It does not include military, customs or police equipment.

5. The treaty has two main provisions:
 - (i) Providing for the creation, registration and prioritisation of an “*international interest*” (such as a mortgage or a lease)
 - (ii) Remedies available to creditors in the event of a default on repayments where an international interest exists
6. The treaty provides a uniform set of criteria for the creation of an international interest, recognised across any country which has ratified the treaty. This interest can be registered with the International Registry, based in Dublin. The International Registry is a notification and prioritisation system for international interests on a first to file basis. The creation, registration and prioritisation of international interests is a core part of the treaty and therefore falls outside the scope of One In, Two Out. UK companies can already register interests with the International Registry, however they are not recognised under UK law as the UK has not ratified the treaty. Following ratification of the treaty, it will not be mandatory to register interests with the International Registry and will be up to business to decide how best to protect their interests. The table below sets out the core provisions of the treaty compared to the current position under UK law.

	Current position under UK law (baseline case)	Position following ratification of the treaty
Recognition of interests under UK law	Interests registered with the UK's National Register of Aircraft Mortgages against a specific aircraft object are recognised under UK law. UK businesses may register interests with the International Registry. However any interests registered with the International Registry are not recognised under UK law.	Interests registered with the International Registry against a specific aircraft object are recognised under UK law. Interests registered on the UK's National Register of Aircraft Mortgages against a specific aircraft object are also recognised under UK law but are subordinate to interests registered on the International Registry.
Type of interest that can be registered and recognised under UK law	Aircraft mortgages and any other agreement where the aircraft is used as security for the loan, with no restriction on the size of the aircraft can be registered on the National Register of Aircraft Mortgages and are recognised under UK law. Interests against engines cannot be registered separately – they must be included as part of an aircraft mortgage. Leases, prospective interests, assignments and contracts of sale cannot be registered	Interests can still be registered as outlined in the baseline case on the National Register of Aircraft Mortgages. Interests can also be registered on the International Registry – interests can be registered separately against airframes, helicopters and aircraft engines above a certain size and engine capacity (this excludes military, customs and police aircraft equipment). Additional interests such as leases, assignments and prospective leases can also be registered.
Can prospective interests be registered?	No – only in the form of a priority notice	Yes
When can interests recognised under UK law be registered?	10-4, Mondays to Fridays. Certain transactions (such as registration and de-registration of aircraft) can be carried out 24 hours a day, 7 days a week by prior arrangement.	24 hours a day, 7 days a week on the International Registry. Registration on the UK's National Register of Aircraft Mortgages remains the same as the baseline case.
Electronic or paper filing system to register interests recognised under UK law?	Mixture of electronic and paper filing system	Electronic for the International Registry Filing on the UK's National Register of Aircraft Mortgages will remain the same as the baseline case.

7. The treaty also contains a number of remedies available to creditors. The extent to which these remedies are applied is a decision for the Contracting State. These are therefore optional provisions which a Contracting State can decide whether or not to adopt through a series of declarations made at the time of ratification. There is one mandatory declaration concerning the extent to which extra-judicial remedies (i.e. remedies without leave of the court are permitted

under the treaty). Contracting States must declare whether they are fully available, partially available or not available.

8. This treaty is a shared competency treaty with some of the optional provisions falling within the competence of the EU and some within the competence of Member States. In 2009, the EU issued a Decision¹ on the areas within the competence of the EU. There is no EU Directive for implementation of the treaty and it was agreed that Member States would be free to decide whether or not to ratify the treaty. Nevertheless, those Member States that decide to ratify the treaty should follow the EU Decision on matters within the EU's competence. Member States are free to decide how to implement the provisions within their own competence. As a result, the optional provisions within the competence of the EU are outside the scope of One In, Two Out as the UK will be applying the decision of the EU. Therefore, only the optional provisions within the competence of the UK fall within scope of One In, Two Out.
9. The table below sets out the optional provisions of the treaty, whether these fall within EU or UK competence and consequently whether they fall within scope of One In, Two Out. In addition, the table sets out the UK's approach to the optional provisions and whether there is an expected overall cost or benefit. Further detail can be found in paragraph 90. A number of the optional provisions maintain the current position under UK law and therefore there are no expected costs or benefits to a number of the optional provisions. Where the UK intends to maintain the current position under UK law where this is not required by the treaty, the table explains why the UK believes that maintaining the UK position is important and will lead to a benefit to business or will not impose additional costs.
10. The greatest economic benefits from ratifying the treaty are gained by adopting some of these optional provisions. The optional provisions are the part of the treaty that provide creditors with greater confidence that they can recover an aircraft in cases of default. If the UK does not adopt any of these provisions, it is unlikely that the risk to creditors in lending finance to airlines and leasing companies will be reduced and therefore it is unlikely that those airlines and leasing companies will benefit from a reduction in the cost of raising finance. The treaty allows parties to an aircraft finance transaction to exclude the majority of provisions in the treaty in their contractual negotiations, therefore we would expect businesses to exclude any provisions of the treaty which they did not believe are of benefit. The majority of stakeholders responding to the consultation strongly supported ratification of the UK, including adoption of some of the optional provisions.
11. In addition to the individual optional provisions, if the UK adopts a certain combination of declarations, UK airlines may be eligible to receive a discount of up to 10% from Export Credit Agencies (ECAs) (this is at the discretion of ECAs). Further detail on the relevant declarations is given under paragraph 91-98. The UK intends to make the relevant declarations. Therefore, although the individual optional provisions may lead to no additional costs or benefits in and of themselves, cumulatively they may lead to a financial benefit for those UK airlines eligible for ECA support. However, since not all airlines are eligible for or will be granted export credit support, not all airlines will benefit from this reduction in the premium of export credit support.
12. The Government does not intend to make registration with the International Registry mandatory and it will be up to business to decide whether it is in its interests to use the provisions of the treaty or continue to use the provisions available under current UK law. The treaty itself sets out a range of provisions for creditors under the optional provisions. In many cases parties to an aircraft finance transaction can choose to disapply the optional provisions, for example in their contractual negotiations. Therefore business is only expected to use the treaty if there is a clear benefit to do so.
13. The table does not include familiarisation costs as these are set out in paragraph 42-56; however in summary there are two levels of familiarisation costs:

¹ <http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=OJ:L:2009:121:0003:0007:EN:PDF>

- (i) **Stage one familiarisation costs (incurred by all businesses the treaty affects)** – airlines and businesses involved in aircraft financing will incur familiarisation costs to understand the core provisions of the treaty and how the UK has implemented the optional provisions. Businesses need to understand how the UK has implemented the treaty as a whole, including the optional provisions, in order to decide whether or not to make use of the provisions of the treaty.

- (ii) **Stage two familiarisation costs (only incurred by those that wish to use the treaty)** – if as a result of stage one, businesses choose to make use of the provisions of the treaty, they will incur stage two familiarisation costs. These costs are to understand how the International Registry works and how to register international interests with the International Registry.

Optional Provision	Within scope of One In, Two Out?	UK approach	Summary of costs and benefits	Can parties to an aircraft finance transaction disapply the provision?
Area under EU competence				
(a) - Interim relief available pending final determination of a creditor's claim by the courts	EU competence, covered by the EU Decision – out of scope	Implement EU Decision Interim relief is available to creditors pending final determination of a claim under existing EU Regulations 44/2001 – Jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (Brussels I)	Maintains current position under EU and UK law – no additional costs or benefits	Yes
(b) - Parties may choose which law will govern their contractual obligations	EU competence, covered by the EU Decision – out of scope	Implement EU Decision The EU has competence and the UK has adopted the relevant EU Regulations regarding choice of law - 593/2008 – law applicable to contractual obligations (Rome I). These Regulations allow parties to choose the law that will govern their contractual obligations	Maintains current position under EU and UK law – no additional costs or benefits	Yes – parties may choose not to nominate which law will govern their contractual obligations
(c) - Co-operation with courts in another Contracting State in insolvency proceedings under the treaty	EU competence, covered by the EU Decision – out of scope	Implement EU Decision The EU has competence and the UK has adopted the relevant EU Regulations regarding provision of assistance in insolvency proceedings – Regulations 1346/2000 on insolvency proceedings	Maintains current position under EU and UK law – no additional costs and benefits	N/A – Requirement for co-operation between courts

Area under UK competence				
(d) - Non-consensual rights	UK competence – in scope of One In, Two Out	<p>Declare that all current and future rights to detain aircraft with priority over an interest equivalent to an international interest are retained. This includes the right to arrest or detain aircraft for payments of amounts owed for the provision of public services.</p> <p>Whilst the treaty does not require Contracting States to make a declaration regarding non-consensual rights, it is important the priority given to detention rights to recover unpaid charges relating to the provision of public services is maintained to ensure these public services are funded. For example, the right to detain aircraft for non-payment of Eurocontrol charges. Eurocontrol is the body responsible for the provision of and collection of charges for air navigation services across the EU, a safety critical service.</p> <p>This ensures the air navigation system is able to carry out its functions and that good operators are not penalised through higher air navigation fees and put at a commercial disadvantage compared with operators that try to avoid paying their air navigation charges.</p>	Maintains priority for non-consensual rights under UK law, therefore there are no additional costs or benefits to business.	N/A – maintains rights for other parties

<p>(e) – Whether other categories of non-consensual rights (such as liens for unpaid charges or court judgments) which can be registered with the International Registry and treated as international interests</p>	<p>UK competence – in scope of One In, Two Out</p>	<p>Other categories of non-consensual rights cannot be registered with the International Registry.</p>	<p>Maintains current position under UK law, therefore there are no additional costs to business</p>	<p>N/A</p>
<p>(f) - Whether interests arising out of internal transactions (i.e. transactions where the asset and all parties to the transaction are located in the same state when the transaction is concluded) can be registered with the International Registry</p>	<p>UK competence – in scope of One In, Two Out</p>	<p>Allow interests arising out of internal transactions to be registered with the International Registry.</p> <p>Whilst the treaty does not require Contracting States to allow internal interests to be registered on the International Registry, the UK position allows business to use one system to register all their interests rather than having two parallel systems which may increase confusion and costs.</p> <p>All the stakeholders who responded to the question on this provision in the consultation supported allowing internal transactions to be registered on the International Registry.</p> <p>The majority of respondents to the consultation stated that it would be confusing if the treaty did not apply to internal transactions as two registration systems would need to operate in parallel.</p>	<p>Overall this will reduce costs for business as businesses can register all their interests on one system rather than using different systems for different types of interests.</p>	<p>Yes – it is not mandatory to register interests arising out of internal transactions with the International Registry. Business is only expected to make use of this provision if there is a clear benefit.</p>
<p>(g) - The courts</p>	<p>UK</p>	<p>Declare the relevant</p>	<p>Confirms relevant</p>	<p>N/A – Sets out</p>

<p>that will have jurisdiction over matters covered by the treaty (other than in insolvency)</p>	<p>competence – in scope of One in, Two Out</p>	<p>courts are the High Court in England and Wales, the Court of Session in Scotland and the High Court in Northern Ireland.</p> <p>This declaration clarifies the relevant courts in the UK.</p> <p>Due to the high value of aircraft objects, claims regarding aircraft finance disputes are currently likely to be made through the High Court in England and Wales, the Court of Session in Scotland and the High Court in Northern Ireland.</p>	<p>courts are those currently most likely to hear claims concerning aircraft equipment – no additional costs or benefits to business.</p>	<p>relevant courts in the UK.</p> <p>Parties can choose the law which will govern their contractual agreements as set out under (b).</p>
<p>(h) - Whether creditors can grant a lease of an aircraft object when the aircraft object is situated in the Contracting State</p>	<p>UK competence – in scope of One In, Two Out</p>	<p>Allow a lease of an aircraft object situated in the UK to be granted. This maintains the current position under UK law and therefore there are no additional costs to business.</p> <p>Whilst the treaty does not require Contracting States to allow creditors to grant a lease of an aircraft object situated in the Contracting State, the granting of a lease of an aircraft object situated in the UK is already permitted under UK law.</p> <p>If the Government were to change existing law and not allow creditors to grant a lease of an aircraft object within the UK, airlines, leasing companies and creditors would need to adjust current practice which would increase</p>	<p>Maintains current position under UK law, therefore there are no additional costs or benefits to business</p>	<p>Yes</p>

		<p>costs. It would also create a confusing distinction between remedies available to creditors with regard to aircraft objects and remedies available to creditors with regard to other assets where the granting of a lease would still be permissible.</p> <p>If the Government were not to allow creditors to grant a lease of an aircraft object situated in the UK, the UK would not meet the criteria for the Organisation for Economic Co-operation and Development (OECD) Aviation Sector Understanding discount and UK airlines would not be eligible for a potential discount of up to 10% on the premium rate of export credit support.</p> <p>All stakeholders responding to the consultation question on the granting of leases supported allowing creditors to grant a lease of an aircraft object situated in the UK.</p>		
(i) - Extra-judicial remedies (remedies available to creditors without leave of the court) that are available to creditors	<p>UK competence – in scope of One In, Two Out</p> <p>The extent to which extra-judicial remedies apply is a mandatory declaration.</p>	<p>Allow the use of extra-judicial remedies under the treaty. Extra-judicial remedies are already permitted under UK law.</p> <p>Whilst the treaty does not require Contracting States to permit the use of extra-judicial remedies, if the Government were to change existing law and not allow the use of extra-judicial remedies,</p>	Maintains current position under UK law, therefore there are no additional costs or benefits to business	Yes – the parties can opt out of the individual remedies that can be exercised through extra-judicial remedies

		<p>leasing companies and creditors would need to adjust current practice which would increase costs. It would also create a confusing distinction as extra-judicial remedies would still be available for other types of assets or aircraft objects falling outside the treaty. This would also increase costs to business who would have to pay court fees and could face delays in being granted the remedies available under the treaty.</p> <p>If the Government were not to allow the use of extra-judicial remedies, the UK would not meet the criteria for the OECD Aviation Sector Understanding discount and UK airlines would not be eligible for a potential discount of up to 10% on the premium rate of export credit support.</p> <p>All stakeholders responding to the consultation question on extra-judicial remedies supported maintaining their use within the UK.</p>		
(j) - Whether interests registered on the UK's national register must be re-registered with the International Registry in order for them to maintain their priority following ratification of the treaty by the UK	UK competence – in scope of One In, Two Out	Interests registered with the UK's Register of Aircraft Mortgages prior to ratification of the treaty do not need to be re-registered with the International Registry in order to maintain priority	No additional costs or benefits. Overall this will reduce costs to business as they will not need to pay to re-register interest with the International Registry nor incur costs of an estimated £400 per transaction to identify relevant	N/A

			international interests	
(k) - Whether the term <i>speedy</i> relief available to creditors whilst their claim is being determined by the court should be defined and, if so, how	UK competence – in scope of One In, Two Out	<i>Speedy</i> relief will not be defined. There is no evidence that UK courts are slow in making decisions.	No additional expected costs to business as there is no evidence that the UK courts are slow in making decisions	N/A
(l) – Remedies on insolvency – Contracting States can adopt “Alternative A”, “Alternative B” or maintain national law	UK competence – in scope of One In, Two Out Under the EU Decision, Member States cannot make a declaration in favour of adopting “Alternative A” or “Alternative B” but can amend national insolvency law to align with the provisions of either Alternative under the treaty.	Insolvency law will be amended to adopt the provisions of Alternative A with a waiting period of 60 days. Alternative A states that after a waiting period (60 days), creditors may repossess an aircraft (without a requirement to obtain leave of the court) if the aircraft object has not been returned by the insolvency practitioner or the defaults have not been cured and a commitment made to keep up to date with all future repayments. Whilst the treaty does not require the adoption of Alternative A, if the Government were not to adopt Alternative A, the UK would not meet the criteria for the OECD Aviation Sector Understanding discount and UK airlines would not be eligible for the potential discount of up to 10% on the premium rate of export credit support. The majority of stakeholders supported adoption of Alternative A. A number of stakeholders said that this is the provision that will lead to the greatest economic benefit to UK airlines in terms of a	Adoption of Alternative A will lead to familiarisation costs for business. These are included within the familiarisation costs in paragraph 42-48. However these are expected to be outweighed by the potential benefits for airlines in reduced financing costs, particularly in capital markets transactions. Respondents to the consultation estimated these benefits to be in the region of 25-75bps based on an uplift of 1-3 notches on the ratings given to these transactions.	Yes

		reduction in the cost of raising finance, particularly for finance raised through the capital markets.		
(m) - To allow the expeditious de-registration and export of an aircraft object	UK competence – in scope of One In, Two Out	<p>Allow the expeditious de-registration and export of an aircraft object through the IDERA (Irrevocable De-registration and Export Request Authorisation) route.</p> <p>Creditors can already obtain a court order under UK law to request that the CAA de-register an aircraft from the UK's register for nationality purposes.</p> <p>Creditors can already obtain de-registration of an aircraft under UK law without a court order by providing documentary evidence of their right to de-register an aircraft such as a de-registration power of attorney – this is a similar concept to the IDERA.</p> <p>Although the treaty does not require Contracting States to adopt the IDERA route, if the Government were not to adopt the IDERA route, the UK would not meet the criteria for the OECD Aviation Sector Understanding discount and UK airlines would not be eligible for the potential discount of up to 10% on the premium rate of export credit support.</p> <p>The majority of</p>	<p>As this is similar to the current power of attorney process in the UK, the familiarisation costs to business are expected to be minimal. These familiarisation costs are included within the costs outlined in paragraph 42-48.</p> <p>Use of the IDERA will lead to a reduction in costs for some businesses because it is a standard form which is recognised across several jurisdictions whereas the power of attorney is only recognised in the UK.</p>	Yes – a debtor is not required to grant an irrevocable de-registration and export request authorisation to a creditor

		stakeholders responding to the question on the IDERA route supported its use.		
(n) - Designating any entry points to pass information and/or registrations to the International Registry	UK competence – in scope of One In, Two Out	No designated entry points will be created. UK business can already register information with the International Registry without using a designated entry point.	UK businesses can register information directly with the International Registry - there are no additional costs or benefits to business. Creation of a designated entry point would increase costs to business as administrative costs would be passed on to business through additional fees.	N/A

14. Due to the low familiarisation costs, the ability for business to decide whether or not to register interests with the International Registry and the ability of business to disapply a number of the remedies in their contractual provisions and the potential benefits in terms of a reduction in the cost of raising finance, this Impact Assessment is presented as zero net cost.

Background to aircraft financing

15. The aviation and aerospace industries make a significant contribution, both directly and indirectly, to the UK economy. The air transport sector's turnover is around £26 billion and the sector provides around 120,000 jobs in the UK, supporting many more jobs indirectly². These figures exclude the aerospace industry which includes manufacturing. The aerospace sector supports 230,000 jobs across the UK, including 109,000 directly. UK aerospace has a 17% global market share, making it the number one aerospace industry in Europe and second globally behind the US and it exports around 90% of production with a value of £25 billion per year³. In 2012, the UK's aerospace export balance was positive totalling £5.2 billion. In 2014, the turnover of the UK aerospace industry was £28 billion⁴.
16. The purchase and/or leasing of new aircraft objects is expensive. Prices for different models of large commercial aircraft can range from around \$60m-\$400m with prices varying according to factors such as engine choice, performance capability, fuel capacity and other design requirements specified by the customer. The cost of leasing a spare engine for a month can vary from between \$25,000 and \$120,000 per month. UK airlines and leasing companies therefore need to raise large amounts of finance in order to purchase or lease new aircraft objects. These

² Draft Aviation Policy Framework – Department for Transport – July 2012

³ Flying High – One year on from lifting off – Aerospace Growth Partnership – July 2014

⁴ Flying High – One year on from lifting off – Aerospace Growth Partnership – July 2014

transactions often involve multiple parties located in more than one jurisdiction across multiple time zones which can increase the legal and administrative complexity of the transactions.

17. The purchase and/or leasing of new helicopters, airframes and aircraft engines therefore requires high levels of financing. Boeing estimates that the global aircraft finance requirements in 2014 will be \$112 billion⁵. Airlines and leasing companies have access to a wide range of different sources of finance. Most airlines purchasing aircraft objects use asset-backed financing, usually over 10-12 years for airframes. Spare engines can be leased on timescales ranging from a single day to several years. Airlines and leasing companies can finance aircraft in a number of ways as set out in Morrell (2007)⁶. Each company will finance aircraft in different ways and may use more than one type of financing in any transaction. Funding options include:

Company financing

Airline companies finance the purchase and/or leasing of new aircraft themselves either through cash reserves or income. They may also raise the necessary funds from equity capital raised from their shareholders.

Commercial bank lending

Banks may provide airlines with the necessary finance usually in the form of asset-secured loans. In the same way as a home mortgage, with asset-secured loans the bank would repossess the aircraft if the airline defaults on its loan repayments.

Export Credit Agencies (ECAs)

ECAs are government or government supported organisations which promote exports by offering guarantees or insurance on loans. In aircraft financing, the ECA would usually step in and cover the bank's financial losses in the event that the airline defaulted on its loan or went into insolvency, seeking to repossess and remarket the asset to make recoveries. ECA guarantees or insurance may be used in cases where banks are reluctant to lend the full amount owing to the large risks associated with the loan and the airlines⁷.

Operating leases

Operating leases cover arrangements where one entity purchases an aircraft and then leases it on a temporary basis to an airline. Where an airline uses this to provide finance on delivery, the arrangement is referred to as sale/leaseback. The lessor would still need to find its own source of funds/finance to make the purchase. Aircraft leases come in a variety of forms, and an operating lease refers to an arrangement where ownership does not transfer to the lessee at the end of the term. Leases can be either dry or wet leases. Dry leases involve just the leasing of the aircraft while wet leases include the leasing of the crew and the pilots as well.

Financing Leases

Under financing leases, a financier purchases the asset and leases it to the airline or leasing company. At the end of the lease, the airline or leasing company has the option to purchase the helicopter, airframe or aircraft engine. Financing leases are similar to hire-purchase agreements.

Enhanced Equipment Trust Certificates (EETCs)

⁵ Boeing Capital Corporation, *Current Aircraft Finance Market Outlook 2014-2018*, <http://www.boeingcapital.com/cafmo/2013/brochure.pdf>

⁶ Morrell, P.S. (2007) *Airline Finance* 3rd Edition

⁷ National ECAs include Ex-Im Bank (USA), UK Export Finance (formerly the Exports Credits Guarantee Department – ECGD), COFACE (France), Euler Hermes (Germany), NEXI (Japan), Export Development Corporations (EDC) (Canada), BNDES (Brazil) and SACE (Italy). All these institutions generally only provide guarantees, with actual finance being provided by banks, but BNDES, Ex-Im, UKEF and EDC can lend money directly.

EETCs are bonds which airlines issue to finance aircraft. Under an EETC, the airline establishes a trust which issues certificates to investors and uses the raised funds to purchase the required aircraft which is then leased back to the airline. The airline makes lease payments to the trust which passes these on to the investors in the form of bond interest. These bonds are rated by credit agencies. EETCs involve financing leases and therefore ownership will transfer to the airline at the end of the lease.

Manufacturer support

On occasion, manufacturers may provide airlines with the necessary finance. This may take the form of an operating lease or a residual value guarantee arrangement whereby the manufacturer guarantees the aircraft's value at the end of the lease or loan.

18. The terms and conditions attached to many forms of aircraft finance will depend on the level of perceived risk. The risk may be specific to the individual transaction, the airline itself or the wider industry. Golbeck and Linetsky (2010)⁸ identify three types of risk that will influence the price of aircraft financing and leasing:
 - (a) Credit risk – the likelihood the borrower or the lessee will default
 - (b) Collateral asset price risk – second hand market value of aircraft declines, the collateral is worth less than the expected value due to market volatility
 - (c) Repossession risk – difficulties reclaiming owned assets such as a delay in repossession, fixed costs and distressed sale discount
19. In 1999, the International Institute for the Unification of Private Law (UNIDROIT), the International Civil Aerospace Organisation (ICAO) and UNIDROIT's members recognised that there are particular challenges in raising finance for large, high-value, mobile assets which cross borders, particularly aircraft objects, due to the large sums involved and the different laws in different countries relating to taking security, leasing and insolvency. These challenges result from the risk of bankruptcy and uncertainty for creditors regarding the location of the asset should the creditor need to take possession of it⁹. As a result, work began under the auspices of UNIDROIT and ICAO to create a private international law treaty consisting of an over-arching Convention which would create a harmonised international legal framework to try to reduce some of the difficulties identified in financing large, high-value mobile assets. The aim of the work was to address the problems which Golbeck and Linetsky highlighted in their study some years later, and provide creditors with greater certainty that they could enforce interests such as mortgages and leases and, if needed, repossess their asset from any jurisdiction, thereby reducing the cost of raising finance for companies seeking to purchase or lease high-value mobile assets.
20. The Convention was designed to provide an over-arching framework which would only be effective when accompanied by a Protocol addressing the particular difficulties faced in financing a specific class of asset. The first of the Protocols to be signed was the Protocol on matters specific to aircraft equipment. Aircraft equipment is defined as helicopters, airframes and aircraft engines above a certain size and engine capacity¹⁰.
21. The Convention and aircraft Protocol ("the treaty") were signed in Cape Town on 16th November 2001 and they fully came into force on 1st March 2006. Since the treaty was signed in Cape Town it is commonly known as the "Cape Town Convention". Currently the Convention is in force in 59 countries and the Protocol is in force in 53 countries. Brazil, Canada, China, the European

⁸ Golbeck, St. and Linetsky, V. (2010) *Asset financing with credit risk*

⁹ *Introduction to the Cape Town Convention and the Aircraft Protocol (Module for Law School Courses on Public International Law)* Brian F. Havel <http://www.law.ox.ac.uk/conferences/ctc/papers/HavelBrianB.pdf>

¹⁰ It does not include military, customs or police equipment

Union, Ireland, New Zealand, Norway, Singapore, the United Arab Emirates and the United States have already ratified the treaty. Australia is in the process of ratifying the treaty¹¹.

Problem under consideration

22. UK airlines need to raise large amounts of finance in order to purchase or lease helicopters, airframes and aircraft engines (“aircraft objects”). Boeing estimates that the global aircraft finance requirements in 2014 will be \$112 billion rising to \$139 billion in 2018¹². Airbus’ Global Market Forecast 2013-2032 estimates that global air traffic will grow by 4.7% per year during that time which will require approximately 29,000 new aircraft with a total value of approximately \$4.4 trillion¹³. The Aerospace Growth Partnership estimates that 40,000 helicopters will be needed over the same timeframe worth \$165 billion. The Aerospace Growth Partnership also estimates that the global civil aerospace market is in excess of \$5 trillion¹⁴. When businesses are looking to add to their fleet, they have the option to purchase or lease helicopters, airframes and/or engines. Whichever option they choose, it is likely that they will need to raise finance through third parties. Boeing estimates that of the \$112 billion of aircraft finance requirements in 2014, 23% would be funded through cash, 22% through the capital markets, 9% through lessors self-funding, 25% through bank debt and 18% through export credit with the remainder of financing needs met through a variety of means including finance provided by manufacturers¹⁵.
23. For the third parties, providing finance for aircraft transactions is risky as airlines generally have low credit ratings. The risk for financiers is magnified by the high value of these assets and the large sums of finance airlines and leasing companies seek to raise. Secondly, aircraft objects are a moveable asset and should a creditor need to take possession of the aircraft object, they cannot be sure in which jurisdiction the aircraft object will be located and therefore how easy or difficult this will be. It is important that creditors can repossess their assets quickly so that they can be put to use and generate an income as the depreciation rate is very high on an idle aircraft. Repossession of an aircraft object prevents the helicopter, airframe or aircraft engine deteriorating through non-use as these assets have a limited lifespan. In order to protect themselves, creditors factor this level of risk into aircraft finance transactions.
24. Pricing the level of risk for creditors is complicated not only by the fact that a creditor does not know where an aircraft object will be located at a particular time, but also by the differences in how various jurisdictions treat claims against aircraft objects by creditors and by the differences between insolvency laws in different jurisdictions. The treaty aims to reduce some of this risk by creating a single harmonised international framework for the creation and registration of international interests (such as mortgages and leases) and a framework to deal with disputes arising under the treaty, including insolvency related matters. This should provide greater certainty to creditors that they will be able to recover their aircraft object from any jurisdiction which has ratified the treaty. Since creditors should no longer need to price as high a level of risk into aircraft finance transactions for airlines based in these jurisdictions, the overall cost of raising finance should reduce.
25. There is evidence to suggest that the traditional sources of finance for airlines and leasing companies in the UK is changing with new investors, such as investors in the capital markets who have traditionally invested in US airlines, providing a greater proportion of aircraft finance for airlines outside of the US. Following the economic downturn, the availability of commercial bank financing decreased as many banks sought to build up their capital reserves. Boeing expects the total share of aviation financing to be met by commercial banks to fall from 28% in 2013 to 25% in 2014¹⁶. In addition, the Basel III rules began to take effect in 2013 which impose stricter requirements on banks’ capital reserves and the holdings of risky assets. This could lead to reduced lending to markets which are perceived to be too risky and higher lending costs in order

¹¹ http://www.infrastructure.gov.au/aviation/international/consultation_cape_town.aspx

¹² Boeing Capital Corporation, *Current Aircraft Finance Market Outlook 2014-2018*, <http://www.boeingcapital.com/cafmo/2013/brochure.pdf>

¹³ Airbus *Global Market Forecast 2013-2032 “Future Journeys”*, <http://www.airbus.com/company/market/forecast/>

¹⁴ *Flying High – One year on from Lifting Off – Aerospace Growth Partnership – July 2014*

¹⁵ Boeing Capital Corporation, *Current Aircraft Finance Market Outlook 2014-2018*, <http://www.boeingcapital.com/cafmo/2013/brochure.pdf>

¹⁶ Boeing Capital Corporation, *Current Aircraft Finance Market Outlook 2014-2018*, <http://www.boeingcapital.com/cafmo/2013/brochure.pdf>

to cover the cost to banks of holding increased levels of capital. As a response to this, a number of airlines have looked at alternative sources of finance¹⁷.

- 26 In the wake of the economic downturn, ECAs increased the amount of support they provided to the sector through providing guarantees to bank loans. However, a new Aviation Sector Understanding (ASU), governed by the Organisation for Economic Co-operation and Development (OECD), came fully into effect in 2013 which increased the cost of export credit support to airlines. Under the 2007 agreement, airlines expected to pay upfront fees of 4-7.5%, however this range rose to 7.72-14.74%. Rates move to reflect market sentiment and the latest table of premiums is set out below. In addition, the limit on loan-to-value arrangements which airlines will be able to secure will fall from 85% to 80%¹⁸. The European Export Credit Agencies, including UK Export Finance (UKEF) covered aircraft with a value of over \$10bn in 2012. However, the amount of support they will provide to the sector in 2014 is expected to fall.

**Table 1: 2011 ASU Table 5 - Minimum Premium Rates as of 15 July 2014
(12-year repayment term, asset backed transactions)**

Risk Category	Risk Classification	Minimum Premium Rates	
		Per annum spreads (bps)	Up front (%)
1	AAA to BBB-	89	4.98
2	BB+ and BB	125	7.03
3	BB-	144	8.12
4	B+	168	9.51
5	B	183	10.38
6	B-	196	11.14
7	CCC	217	12.38
8	CC to C	223	12.73

27. In contrast to the expected fall in the total share of global aviation finance from commercial banks and ECAs, Boeing expects the share of finance provided by the capital markets to increase from 14% in 2013 to 22% in 2014¹⁹.

Rationale for intervention

28. UK and other European airlines have historically been more dependent on commercial bank financing than American airlines which have traditionally raised finance through the capital

¹⁷ Airline Fleet Management: *the next credit crunch*, published Mar-Apr 2012 <http://www.afm.aero/magazine/trading-legal-and-finance/item/283-the-next-credit-crunch>

¹⁸ OECD *Arrangement on officially supported export credits*, October 2013 [http://search.oecd.org/officialdocuments/displaydocumentpdf/?doclanguage=en&cote=tad/pg\(2013\)11](http://search.oecd.org/officialdocuments/displaydocumentpdf/?doclanguage=en&cote=tad/pg(2013)11)

¹⁹ Boeing Capital Corporation, *Current Aircraft Finance Market Outlook 2014-2018*, <http://www.boeingcapital.com/cafmo/2013/brochure.pdf>

markets. So far, only one UK airline, British Airways, has chosen to raise finance through the capital markets in a deal in 2013²⁰.

29. As the balance of sources of aircraft financing is expected to shift and as UK, European and other non-US airlines explore other sources of financing (such as the capital markets), creditors and investors who are new to the aviation financing industry or to UK airlines and the UK legal regime in particular are likely to require security that they will be able to recover the aircraft object should an airline or leasing company default on repayments or enter insolvency. These investors may base decisions on incomplete information about the UK legal system. This could result in an increased risk for creditors, reflected in the cost of finance. Therefore there is potentially an asymmetric information problem which adopting an international framework, already in force in a number of other jurisdictions, would reduce. This may provide non-traditional investors in aircraft finance, or investors new to the UK legal system, with greater confidence that they can recover their assets under a system they already know and use.

Policy objective

30. The treaty aims to address some of the difficulties faced by cross-border asset-based aircraft finance transactions. The treaty created an international legal framework to govern the creation and registration of international interests (such as mortgages and leases) in helicopters, airframes and aircraft engines over a certain size and engine capacity²¹. This is a core part of the treaty. The treaty outlines remedies available to creditors should there be a default on repayments, including in cases of insolvency. The extent to which these remedies apply is determined by the Contracting State. In the case of EU Member States, the application of some of the remedies falls within the competence of the EU. Parties to an aircraft finance transaction can also decide to what extent many of the remedies adopted by a Contracting State will apply to their agreement.
31. UK airlines which choose to continue to utilise traditional forms of finance and do not wish to explore alternative sources of finance may not see a benefit in reduced financing costs from ratifying the treaty, as they will be working with financiers who are already familiar with the circumstances of the particular airline and the UK legal structure, which already affords a good level of protection to creditors. Therefore, the greatest benefits are likely to be realised if investors who are unfamiliar with the UK's legal system reduce the cost of lending to UK airlines or leasing companies because the UK has adopted an international framework whose protections are widely understood. However, ratification of the treaty is only one factor considered by investors, financiers and the ratings agencies involved in rating capital markets transactions. Parties to these transactions consider a number of other factors outside the scope of this treaty such as an airline's own credit rating and repayment history. Therefore, depending on an airline's individual circumstances, airlines may not see any reduction in the cost of raising finance.
32. UK businesses can already register interests with the International Registry and use its search facilities to ascertain whether any interest has already been registered against a particular aircraft object. However, interests registered on the International Registry are not recognised under UK law and therefore creditors are unable to enforce these interests through the UK courts. Ratifying the treaty would enable creditors to enforce interests created under the treaty through the UK courts and may provide greater certainty to creditors that they can recover their asset and redeploy it quickly in the event that an airline defaults on repayments, reducing the level of risk to investors. If this reduction in risk is factored in to asset-backed aircraft finance transactions, this may lead to a reduction in the cost of raising financing for airlines. A reduction in the cost of raising finance may lead to increased investment by airlines and leasing companies in their fleets and therefore increased sales of helicopters, airframes and aircraft engines from UK manufacturers.

²⁰ Financial Times, *Airlines tap capital markets for financing*, 10th December 2013 <http://www.ft.com/cms/s/0/42f1d9be-6197-11e3-916e-00144feabdc0.html#axzz2qYZYYXWK>

²¹ The treaty excludes aircraft used in military, customs and police services

33. Ratification of the treaty would provide additional benefits to parties involved in financing arrangements for aircraft engines. The provisions of the treaty extend to aircraft engines over a certain size. It is not possible to register interests against aircraft engines separately on the UK's Register of Aircraft Mortgages; they have to be included as part of an aircraft mortgage. Under the treaty, interests in respect of aircraft engines can be created and registered separately with the International Registry. This may provide greater security for financiers and manufacturers of aircraft engines that their interests are protected. This provision is particularly important for creditors in transactions involving aircraft engines since engines, which are valuable assets in their own right, are routinely moved between airframes for maintenance reasons. It is common practice for airlines to lease spare engines on a short or long-term basis. As such, creditors to aircraft engine transactions not only face uncertainty as to which jurisdiction the aircraft engine will be in at any one time but they also face uncertainty as to which airframe the engine will be attached to.
34. The Department for Business, Innovation and Skills held a call for evidence in 2010 asking for views on whether the UK should ratify the treaty. The majority of respondents were in favour of the UK ratifying the treaty stating that they expected ratification to lower the cost of raising finance as financiers "*would no longer need to charge higher rates to borrowers as the risk of lending capital would be reduced*"²². The Department for Business, Innovation and Skills published a response to the call for evidence on 6th December 2010 stating its intention to proceed with ratification²³.
35. There are a number of secondary benefits to ratifying the treaty which may be available to UK businesses. The majority of these benefits are administrative benefits as a result of using the International Registry. Unlike the UK Register of Aircraft Mortgages maintained by the Civil Aviation Authority (the CAA), the International Registry allows interests to be registered electronically 24 hours a day, seven days a week. This will make it more convenient for creditors to register interests, taking the pressure off closing complex finance transactions which may be taking place across multiple jurisdictions and time zones. Under the treaty, prospective interests can be registered on the International Registry, something that is not possible on the UK Register of Aircraft Mortgages other than in the form of a "priority notice". Ratifying the treaty would make it more convenient for business to register prospective interests on the International Registry compared with the current system of priority notices in the UK.
36. The International Registry enables companies and individuals to search for interests registered against a specific aircraft object and the order of priority for any existing registered interests. This allows interested parties to see whether any other party has an interest which would take priority over its own. The intention of the treaty is that any interests registered with the International Registry would take priority over an interest registered on the relevant national register, in the case of the UK, the National Register of Aircraft Mortgages. There may be an administrative benefit to companies and individuals of searching a single International Registry rather than searching for relevant interests on multiple national registers alongside the International Registry as well as a reduction in costs to search multiple registers. However, the full benefits of searching on the International Registry will only be realised if a critical mass of countries ratify the treaty and if businesses choose to register their interests with the International Registry. It will not be mandatory to register charges on the International Registry and businesses will be able to decide how best to protect their interests.

Description of options considered (including do nothing)

37. Two options have been considered

²² *Convention on International Interests in Mobile Equipment and Protocol thereto on matters specific to aircraft equipment – Government Response to the Call for Evidence* <https://www.gov.uk/government/consultations/call-for-evidence-convention-on-international-interests-in-mobile-equipment-and-protocol-thereto-on-matters-specific-to-aircraft-equipment>

²³ <https://www.gov.uk/government/consultations/call-for-evidence-convention-on-international-interests-in-mobile-equipment-and-protocol-thereto-on-matters-specific-to-aircraft-equipment>

Option 0 - Do nothing. This would involve maintaining the current national system of registration. This option was rejected on the basis that UK businesses would not be able to benefit from the potential lower cost of finance to be gained through ratification of the treaty.

Option 1 - Ratify the treaty. This is the government's preferred option and would introduce the provisions of the treaty into UK law. This means that international interests created under the treaty and registered on the International Registry would be enforceable through the UK courts.

Monetised and non-monetised costs and benefits of each option (including administrative burden)

38. Option 0 maintains the status quo and there are therefore no additional costs or benefits associated with this option.
39. Option 1 is that the UK ratifies the treaty and this is the preferred option. The treaty aims to reduce the risk for financiers in aviation finance transactions and this may lead to lower financing costs for airlines and leasing companies. This may enable airlines to access new sources of funding and diversify their sources of finance. A reduction in the cost of raising finance may also lead to increased investment by airlines and leasing companies and therefore increased sales of helicopters, airframes and aircraft engines by UK manufacturers. There may be a number of secondary administrative benefits to ratifying the treaty through using the International Registry.
40. Ratification of the treaty will affect the UK aviation industry, helicopter, airframe and aircraft engine manufacturers, aircraft financiers such as banks and investors in the capital markets, legal firms specialising in aircraft finance transactions, insolvency practitioners and the CAA, the public body which operates the UK's National Register of Aircraft Mortgages.

Costs

Familiarisation costs

41. There are two stages of familiarisation costs for business as a result of ratifying this treaty. The first set of implementation costs would be incurred by all businesses involved in aircraft financing including airlines, asset finance lawyers and financiers. The second stage of familiarisation costs would only be incurred by those deciding to make use of the provisions of the treaty:
 - (i) **Stage one familiarisation costs** (incurred by all businesses with an interest in aircraft financing) – businesses need to understand the provisions of the treaty, this includes the core provisions and the UK's approach to the optional provisions. Only once businesses have understood how the UK has ratified the treaty as a whole can they decide whether to make use of the treaty.
 - (ii) **Stage two familiarisation costs** (non-mandatory costs only incurred by businesses wanting to use the treaty) – if businesses decide to make use of the provisions of the treaty, they will incur familiarisation costs to understand how to make registrations with the International Registry. Businesses are only expected to choose to use the International Registry, and therefore incur familiarisation costs, if they see a clear benefit in doing so.

Stage one familiarisation costs – to understand the provisions of the treaty and the UK's approach to the optional provisions

42. There are approximately 30 national, regional and local airlines offering passenger or freight services or both in the UK²⁴ which are expected to incur familiarisation costs as a result of ratification of the treaty. These costs relate to the need for airlines to familiarise themselves with the regulatory changes as a result of ratifying the treaty. In addition there are a number of UK legal firms, banks and other financial institutions involved in the aircraft finance industry that will be directly affected by ratification of the treaty and may incur familiarisation costs.

²⁴ <http://www.caa.co.uk/default.aspx?catid=80&pagetype=88&pageid=1&sqlid=1>

43. There are approximately 250 entities with interests registered on the UK's National Register of Aircraft Mortgages, over half of these entities are international banks or international legal firms. This indicates that there is a small group of financiers and legal firms with expertise in the global aircraft finance market. Approximately 100 of the entities or individuals with interests registered on the UK's National Register of Aircraft Mortgages are UK entities. Businesses which have registered interests on the National Register of Aircraft Mortgages tend to be financial institutions, manufacturers, leasing companies or legal firms acting on behalf of clients rather than airlines since airlines are unlikely to be the holders of mortgages or leases.
44. The number of UK entities with a current interest registered on the UK's National Register of Aircraft Mortgages provides an estimate of the number of UK businesses involved in the aircraft finance industry and therefore an estimate of the number of businesses that will need to familiarise themselves with the provisions of the treaty.
45. Based on the number of airlines in the UK (approximately 30) and current usage of the UK's National Register of Aircraft Mortgages by British companies (approximately 100), it is assumed that a maximum of 130 UK businesses will incur familiarisation costs as a result of ratifying the treaty. However, the treaty has been in place for several years and has been ratified by a number of countries including Brazil, Canada, China, Ireland, New Zealand, Norway, Singapore, the United Arab Emirates and the United States. It is expected that the majority of UK legal firms and financial institutions are already familiar with the main provisions of the treaty as they advise clients or provide funding for airlines in jurisdictions which have already ratified the treaty. However, they will still incur some familiarisation costs to understand how the UK has implemented the treaty.
46. Any businesses and individuals using the UK National Register of Aircraft Mortgages that only have interests in aircraft that fall outside the scope of the treaty will not incur these familiarisation costs.
47. We are unable to provide an estimate of how many of the registrations made on the UK National Register of Aircraft Mortgages would be covered by the treaty. However, the figures below estimate the familiarisation costs for UK financiers and legal firms based on a maximum of 130 UK entities. The best estimate is based on 100 businesses needing to familiarise themselves with the International Registry and assumes that around 30 businesses and individuals only have interests in aircraft objects which do not meet the minimum requirements of the treaty with regard to size of helicopter or airframe or engine capacity. The low estimate is based on 75 businesses incurring the familiarisation costs which assumes that some UK banks and legal firms will not need to familiarise themselves with how the UK has implemented the treaty as they will already be familiar with the provisions of the treaty through advising clients or providing finance for businesses in jurisdictions which have already ratified the treaty. It also assumes that a number of aircraft registered on the UK's National Register of Aircraft Mortgages will not meet the treaty's requirements regarding aircraft and helicopter size and engine capacity.
48. As part of a consultation on the optional provisions, BIS asked stakeholders whether an estimated familiarisation cost of £5,000 per business was reasonable. Respondents included airlines, aerospace manufacturers, leasing companies and asset finance lawyers. 72% of those consulted agree with the Government's estimation of the familiarisation cost being a one off cost of £5,000 or less. Many respondents to the consultation expected the familiarisation costs to be lower than estimated as there is a range of free resources available to help businesses in jurisdictions that have ratified the treaty such as the practitioners' guide produced by the Aviation Working Group²⁵.

Table 2: Estimated familiarisation costs – understanding the provisions of the treaty

Low estimate	Best estimate	High estimate
(based on 75 UK businesses incurring familiarisation)	(based on 100 UK businesses incurring familiarisation costs)	(based on 130 UK businesses incurring familiarisation costs)

²⁵ <http://www.awg.aero/assets/docs/Practitioner-Guide-November-2012.pdf>

costs)		
£375,000	£500,000	£650,000

Stage two familiarisation costs – to understand how to use the International Registry

49. Once a business is familiar with the provisions of the treaty and how the UK has ratified the treaty, it will need to decide whether it wishes to make use of the treaty's provisions, including registration of international interests on the International Registry. Those businesses that wish to register with the International Registry will incur additional familiarisation costs. For the reasons set out below, we expect that only UK airlines, previously unfamiliar with the International Registry will incur the familiarisation costs. Since it would not be mandatory to register interests with the International Registry, only those businesses choosing to make use of the provisions of the treaty would incur these costs. In practice we expect the majority of UK businesses to use the International Registry as the intention of the treaty is that interests registered with the International Registry take priority over interests registered with the relevant national register.
50. A number of UK businesses are already familiar with the International Registry, particularly UK financiers, legal firms and leasing companies providing finance for businesses or advising clients in jurisdictions which have already ratified the treaty. These businesses would not incur the stage two familiarisation costs. Data from the International Registry shows the number of UK entities which have already registered with the International Registry. This figure has increased from 99 in 2007 to 156 in 2012, down from a peak of 197 in 2009, suggesting that the International Registry is widely used by UK businesses. The difference in the number of UK entities which have registered with the International Registry compared to the number of UK entities which have an interest registered on with the UK's National Register of Mortgages may be due to one company registering separate parts of its business with the International Registry or the UK based arm of international banks or legal firms registering separately with the International Registry.

Table 3: UK entities registered with the International Registry

Year ended	Number of UK entities registered with the International Registry
2007	99
2008	199
2009	197
2010	155
2011	155
2012	156

Source – International Registry

51. Data from the International Registry indicates that a number of registrations have been made on the International Registry relating to aircraft frames or helicopters which have the UK as their State of Registry²⁶.

Table 4: Registrations relating to aircraft frames and helicopters on the International Register, by year

²⁶ Under the Chicago Convention on International Civil Aviation, aircraft must be registered with a national aviation authority for nationality purposes and can only be registered with one national aviation authority at any one time.

Year	Number of Airframe registrations	Number of helicopter registrations
2006	25	1
2007	86	N/A
2008	23	2
2009	74	4
2010	134	2
2011	66	9
2012	105	43
2013	74	82

Source – International Registry

52. Since aircraft engines cannot be registered with a national aviation authority for nationality purposes, comparable figures for aircraft engines are not available. However, data from the International Registry on the number of transactions where one of the named parties is based in the UK includes information on registrations against aircraft engines. The data shows that a number of UK businesses are already using the International Registry to register interests against aircraft objects. This is likely to be for transactions where one party is located in a jurisdiction which has already ratified the treaty since interests on the International Registry are not currently enforceable through the UK courts. This suggests that UK financiers and legal firms rather than airlines are currently the predominant users of the International Registry. The high number of engine registrations compared to airframes is expected since every airframe carries a number of engines and interests can be registered against each engine separately.

Table 5: Registrations relating to aircraft objects on the International Register

Aircraft Object	Number of Registrations
Engine	9018
Airframe	3553
Helicopter	389

Source – International Registry

53. Therefore, it is likely that the only UK businesses that will incur costs in familiarising themselves with the International Registry will be UK airlines. These familiarisation costs are likely to be in the form of increased legal fees to set up the documentation required by the International Registry. A study for the Aviation Working Group (AWG), a group of airframe and aircraft engine manufacturers, leasing companies and financiers, conducted by Professor Vadim Linetsky of Northwestern University, Illinois, estimates that there will be an additional one-off legal cost of £5,000 per transaction in the first year to set up the necessary documentation to register interests with the International Registry²⁷. Discussions with businesses have indicated that this would be a small fraction of the total legal costs an airline would pay during an aircraft finance transaction. Legal fees for an operating lease are estimated to be in the range of £20,000-£25,000. Legal fees for an aircraft financing are estimated to be in the range of £100,000-£120,000. Both of these estimates are for a straightforward transaction. Costs could increase significantly for a complex transaction.

²⁷ Linetsky, Vadim *Accession to the Cape Town Convention by the UK: An Economic Impact Assessment Study*, December 2010, <http://www.awg.aero/assets/docs/UKCTC%20Econ%20Impact%20Final%20Version.pdf>

54. Since registration with the International Registry is not mandatory, it is possible that not every aircraft finance transaction will involve registration on the International Registry and therefore that not every airline will incur these costs. However in practice it is likely that the vast majority of financiers will register their interests with the International Registry to give them the greatest possible protection. In addition, creditors from outside the UK who may not be familiar with the protection provided by the UK's National Register of Aircraft Mortgages are likely to require their interests to be registered on the International Registry, a system of registration they may already be familiar with.
55. The table below gives a low, high and best estimate of the one-off legal costs for airlines, based on different numbers of airlines making use of the International Registry. Discussions with businesses involved in the aircraft finance industry have indicated that the majority would require their interests to be registered on the International Registry as this would give them greater priority over other creditors. Therefore, it is expected that the majority of airlines will need to familiarise themselves with the International Registry so that their creditors' interests can be registered. Consequently the best estimate assumes that the majority of airlines will face these familiarisation costs.
56. As airlines do not purchase helicopters, airframes or aircraft engines every year, any familiarisation costs related to the International Registry may be spread across several years, depending on when airlines renew their fleet. Since airframe mortgages last on average 10-12 years, it is assumed that these familiarisation costs are spread evenly across ten years, starting the year after implementation.

Table 6: Estimated costs of setting up set up the necessary documentation to register interests with the International Registry

Year	Low Estimate (based on 15 airlines using the International Registry)	Best Estimate (based on 25 airlines using the International Registry)	High Estimates (based on 30 airlines using the International Registry)
2015	£7,500	£12,500	£15,000
2016	£7,500	£12,500	£15,000
2017	£7,500	£12,500	£15,000
2018	£7,500	£12,500	£15,000
2019	£7,500	£12,500	£15,000
2020	£7,500	£12,500	£15,000
2021	£7,500	£12,500	£15,000
2022	£7,500	£12,500	£15,000
2023	£7,500	£12,500	£15,000
2024	£7,500	£12,500	£15,000
2025	£7,500	£12,500	£15,000
	Total - £75,000	Total - £125,000	Total - £150,000

Other non-mandatory costs to business

Fees to register interests with the International Registry

57. Should businesses decide to register international interests with the International Registry, they will be required to pay fees as set out by the International Registry. Depending on the maximum

take-off weight of the aircraft, for some businesses registering interests with the International Registry may be a benefit and for some it may be a cost as the International Registry charges a flat fee whilst the Civil Aviation Authority's fee increases as the maximum take-off weight of the aircraft increases.

58. However, businesses registering interests against aircraft engines will face additional fees as it is not possible to register interests against aircraft engines separately on the UK's National Register of Aircraft Mortgages, they must be included in an aircraft mortgage. The information below outlines the fees charged by the International Registry and the UK's National Register of Aircraft Mortgages to register interests and to search the register.

Charges depend on the maximum take-off weight of the aircraft that is the subject of the mortgage.

Table 7: Charge for entry of Aircraft Mortgage on National Register of Aircraft Mortgages²⁸

Maximum take-off weight	CAA Charge
<= 5700 kg	£174
5701 kg - 15000 kg	£346
15001 kg - 50000 kg	£577
> 50000 kg	£1038

Source - CAA

If one mortgage covers several aircraft, the fee payable is as shown above for the heaviest aircraft, plus £174 for each additional aircraft. This is based on all the aircraft mortgages being submitted at the same time.

The charge to search the register is £29.

Table 8: Charge for entry on International Registry and for searches²⁹

Service	Fee
Controlled entity set-up fee (1 year)	\$180/£108
User set-up fee (1 year)	\$200/£120
Registration fee	\$100/£60
Spare engine fee	\$50/£30
Priority search fee	\$22/£13

Source – International Registry

The conversion rate for pounds to US dollars is taken as the average for 2014 of 1.67. This has been used as the conversion rate throughout this Impact Assessment.

59. The table below compares the total estimated cost to register an interest against an airframe and four engines with the International Registry and with the National Register of Aircraft Mortgages to highlight the difference in fees between registering with the two different registers. The table includes data on the number of aircraft mortgage registrations with the CAA by maximum take-off weight in 2012-13 as a guide as to how many airframes are likely to fall into each category. Not all of the aircraft mortgage registrations with the CAA last year will fall in scope of the treaty since the treaty only covers airframes above a certain weight whereas the CAA allows registrations to be made against a wider range of aircraft. Therefore these figures are only indicative. For the purposes of the comparison, it has been assumed that the controlled entity set-up fee and the user set-up fee are payable, however since both of these fees only have to be paid once a year, they may not apply to every transaction.

²⁸ <https://www.caa.co.uk/default.aspx?catid=121&pagetype=90&pageid=112>

²⁹ <https://www.internationalregistry.aero/ir-web/faq>

Table 9: Comparison of fees - total estimated cost to register an interest against an airframe and four engines with the International Registry and with the National Register of Aircraft Mortgages

	International Registry	UK National Register of Mortgages	Aircraft Mortgage registrations with the CAA in 2012-13
Cost to register an airframe with a maximum take-off weight of 5,700kg	Controlled entity set-up fee (\$180) + User set-up fee (\$200) + Registration fee (\$100) = \$480/£287	£174	124
Cost to register an airframe with a maximum take-off of 5,701 – 15,000 kg	Controlled entity set-up fee (\$180) + User set-up fee (\$200) + Registration fee (\$100) = \$480/£287	£346	28
Cost to register an airframe with a take-off weight of 15,001 – 50,000kg	Controlled entity set-up fee (\$180) + User set-up fee (\$200) + Registration fee (\$100) = \$480/£287	£571	27
Cost to register an airframe with a take-off weight greater than 50,000kg	Controlled entity set-up fee (\$180) + User set-up fee (\$200) + Registration fee (\$100) = \$480/£287	£1038	111
Cost to register four engines on either aircraft	User set up fee (already paid) + Registration fee (\$100 x 4) = \$400/£240	N/A	N/A

60. Since it will not be mandatory to register interests with the International Registry, some businesses may decide not to use the provisions of the International Registry and may not incur these costs. However, discussions with businesses specialising in aviation finance have indicated that most financiers register interests on the International Registry and the relevant national register to give them the greatest possible protection. For example, if one party to an aircraft finance transaction is based in a jurisdiction which has not ratified the treaty, that party may request that the interest is registered on the relevant national register as interests registered on the International Registry may not be recognised in their home country. In this case, there may be some duplication as the National Register of Aircraft Mortgages and International Registry would provide similar protection to creditors and two sets of registration fees would be payable. It is unclear how many businesses would choose to register their interests on both registers. This is a business decision and it is expected that businesses would only register with the International Registry and the UK's National Register of Aircraft Mortgages if they saw clear benefits.

Public costs – Loss of income to the CAA through a reduction in number of registrations on the UK's national register

61. There are some potential costs to the Civil Aviation Authority, a public body, in lost income from registration fees if businesses register their interests with the International Registry rather than the National Register of Aircraft Mortgages. It is unclear how many businesses will stop registering with the CAA and discussions with businesses have indicated that the vast majority of businesses register their interests with the International Registry and the relevant national register to give them the greatest level of protection, at least to begin with.
62. In 2012-13, the CAA's total income from aircraft mortgages was £210,000 of which an estimated £187,000 came from transactions which would fall within scope of the treaty. This was an

increase from a total income from aircraft mortgages of £176,000 in 2011-12 of which an estimated £149,000 came from transactions likely to fall within scope of the treaty.

63. The table below shows the number of aircraft mortgage transactions handled by the CAA over the last three years, inclusive and exclusive of requests to search whether a mortgage already exists against a particular aircraft object. It is estimated that approximately two thirds of the transactions would fall within scope of the treaty:

Table 10: Aircraft mortgage transactions handled by the CAA over the last three years

Year	No. of transactions (including searches)	No. of transactions (excluding searches)
2010-11	1573	746
2011-12	1930	827
2012-13	1477	679

64. As mentioned in paragraph 60, discussions with experts and businesses involved in aircraft finance have indicated that creditors like to have their interests registered on both the International Registry and the relevant national register to afford them the greatest possible protection. The table below provides a low, high and best estimate of the income to the CAA based on 25%, 75% and 90% of eligible businesses registering their interests with both the National Register of Aircraft Mortgages and the International Registry and based on an estimated income of £187,000 for 2012-13 for transactions within scope of the treaty. The best estimate has been set at 75% based on discussion with business which suggests that the majority of creditors would register their interests on both the International Registry and the UK's National Register of Aircraft Mortgages. The second table shows the estimated loss to the CAA based on 25%, 75% and 90% of businesses continuing to register their interests with the National Register of Aircraft Mortgages based on an estimated income of £187,000 for 2012-13. Since businesses register interests with the CAA every year, the cost to the CAA is expected to be incurred every year.

Table 11: Estimated income to the CAA – based on a baseline income of £187,000 (this is an annual expected costs)

Low Estimate – 25% of businesses register with CAA and International Registry	Best Estimate – 75% of businesses register with CAA and International Registry	High Estimate – 90% of businesses register with CAA and International Registry
£46,750	£140,250	£168,300

Table 12: Estimated reduction in income to the CAA - based on a baseline income of £187,000 per year (this is an expected annual cost)

Low Estimate – 90% of businesses continue to register with the CAA	Best Estimate – 75% of businesses continue to register with the CAA	High Estimate – 25% of businesses continue to register with the CAA
£18,700	£46,750	£140,250

Public costs – Costs to the courts of enforcing interests under the treaty

65. By ratifying the treaty, international interests created under the treaty and registered with the International Registry will be enforceable through the UK court system. However, creditors with interests registered on the UK's National Register of Aircraft Mortgages can already enforce their interests in cases of default through the UK courts and therefore this is not a new provision for creditors. Therefore ratification of the treaty is not expected to lead to additional cases coming before the UK courts. Therefore there are no expected increased costs to UK courts as a result of ratifying this treaty.

Summary of costs

66. Businesses are likely to incur two stages of familiarisation costs. The first stage of costs will be incurred by businesses interested in aircraft financing. These costs relate to understanding the provisions of the treaty, including how the UK will approach the optional provisions. The majority of UK businesses involved in aircraft financing (an estimated 30 airlines and approximately 100 businesses with interests registered on the UK's National Register of Aircraft Mortgages) are likely to incur familiarisation costs following ratification of the treaty. However, a number of UK legal firms, leasing companies and financiers which provide advice to or are parties to transactions with airlines in jurisdictions which have already ratified the treaty will not incur the full familiarisation costs. Since the treaty only covers helicopters, airframes and aircraft engines above a certain weight and engine capacity, some of the current users of the UK's National Register of Aircraft Mortgages may have interests relating to aircraft that would fall outside the scope of this treaty and would not need to familiarise themselves with the provisions of the treaty. The best estimate for the total familiarisation costs to business relating to the changes in regulations is £500,000.
67. Having understood the provisions of the treaty, those businesses that choose to make use of the provisions of the treaty are expected to incur additional familiarisation costs (stage two costs) to understand how to use the treaty. These costs are expected to be incurred by UK airlines. UK legal firms and financiers are not expected to incur these costs as they already use the International Registry as a result of advising clients in jurisdictions that have already ratified the treaty. Since it will not be mandatory to register interests with the International Registry it would be a business decision whether to register interests with the International Registry, the UK's National Register of Aircraft Mortgages, on both registers or on neither. Businesses are only expected to incur these costs if they see a clear benefit in registering interests with the International Registry. Businesses that choose not to use the International Registry will not incur these familiarisation costs, nor will businesses with interests relating to aircraft objects outside the scope of this treaty. These costs are likely to be incurred over several years as airlines do not purchase airframes or engines every year. In practice, we expect the majority of financiers to require their interests to be registered with the International Registry and therefore the best estimate of familiarisation costs relating to use of the International Registry is £12,500 per year for ten years.
68. Businesses may face additional costs in terms of increased fees to register with the International Registry. However, since it would be a business decision whether or not to register interests with the International Registry, some businesses may not incur these costs. Depending on the maximum take-off weight of the airframe, there may be a benefit to businesses in registering with the International Registry compared to the fee to register interests on the UK's National Register of Aircraft Mortgages.
69. There are likely to be some public costs to the CAA as a result of ratifying the treaty through a loss of fee income if businesses choose to register interests with the International Registry instead of the UK's National Register of Aircraft Mortgages run by the CAA. Discussions with business have indicated that the majority of businesses will register their interests on both registers, therefore the cost to the CAA is estimated to be a small annual cost. The best estimate of a loss of income to the CAA per year is £46,750. Ratification of the treaty is unlikely to result in an increased number of cases coming before the UK courts and therefore there are no expected costs to the UK court service.

Benefits

70. Ratification of the treaty is expected to lead to a reduction in the cost of raising aircraft finance for UK airlines and leasing companies. However, the expected benefit to UK airlines is difficult to quantify for a number of reasons. Airlines and leasing companies have a number of different funding options available to them and ratification of the treaty is only one of the factors financiers consider. Other relevant factors include the credit rating of the airline, the type of asset and the duration of the loan; factors which fall outside the scope of this treaty.

71. A study by Professor Linetsky, commissioned by the Aviation Working Group, estimated that UK airlines could benefit from a reduction in funding costs of between £538 million and £2.075 billion (with a best estimate of £1.2 billion) for aircraft deliveries over the next 20 years on an estimated £98 billion of aircraft finance based on certain assumptions of how the UK would implement the Cape Town treaty (CTC). If only a small percentage of these benefits are realised, the benefits are expected to far outweigh the costs of ratifying the treaty to UK businesses.
72. Several respondents to the consultation thought that ratification of the Cape Town treaty, including the adoption of Alternative A, would lead to a possible reduction in the cost of raising aircraft finance for capital markets transactions of 25-75bps based on an uplift of 1-3 notches to the rating given to these transactions. However, this should be seen as the high end of the potential benefits of ratifying the treaty.
73. Further detail on the estimated benefits is set out below and it is for these reasons this policy is presented as a zero net cost.
74. In 2010, the Aviation Working Group commissioned a study by Professor Linetsky of Northwestern University, Illinois, to estimate the benefits of ratifying the treaty to the UK³⁰. This study concluded that the UK based airlines could benefit from a reduction in funding costs of between £538 million and £2.705 billion (with a best estimate of £1.2 billion) for aircraft deliveries over the next 20 years on an estimated £98 billion of aircraft finance. This study made a number of assumptions with regard to how UK airlines would meet their future financing needs, the delays faced by creditors in repossessing aircraft objects on insolvency under current UK law and which optional provisions the UK would adopt. As a result of these assumptions, this study should be seen as a high estimate of the possible benefits to the UK.
75. Professor Linetsky's study assumes that UK airlines will meet their future aircraft financing needs as follows:

Export Credit Agencies	20%
Capital Markets	20%
Commercial finance (including banks)	40%
Equity	20%

Although the majority of aviation finance experts expect capital markets to make up a greater share of aircraft financing in the future and Boeing expects 22% of the global share of aircraft finance to come from the capital markets this year³¹, only one UK airline has so far raised finance through the capital markets and it is unclear how many other UK airlines intend to raise part or all of their financing needs through the capital markets in the short and long term. The percentage of support provided by European ECAs is expected to fall in 2014 and so the proportion of aircraft financing needs to be met by ECAs in future years is unclear.

76. Secondly, all of the benefits from Professor Linetsky's study come from the assumption that the UK will adopt one of the optional provisions in the treaty called "Alternative A" which provides for additional benefits for a creditor on insolvency. Professor Linetsky assumed a worst case scenario of 4-8 months for a creditor to recover an aircraft object in the UK without the provisions of Alternative A. However, in many cases creditors can gain possession of an aircraft object in a shorter timescale, particularly in cases of liquidation. The majority of respondents to the consultation on the optional provisions were supportive of the adoption of Alternative A. Alternative A requires that on insolvency, the insolvency practitioner must either (i) give up possession of the aircraft object to the creditor or (ii) cure all defaults and agree to perform all

³⁰ Linetsky, Vadim *Accession to the Cape Town Convention by the UK: An Economic Impact Assessment Study*, December 2010, <http://www.awg.aero/assets/docs/UKCTC%20Econ%20Impact%20Final%20Version.pdf>

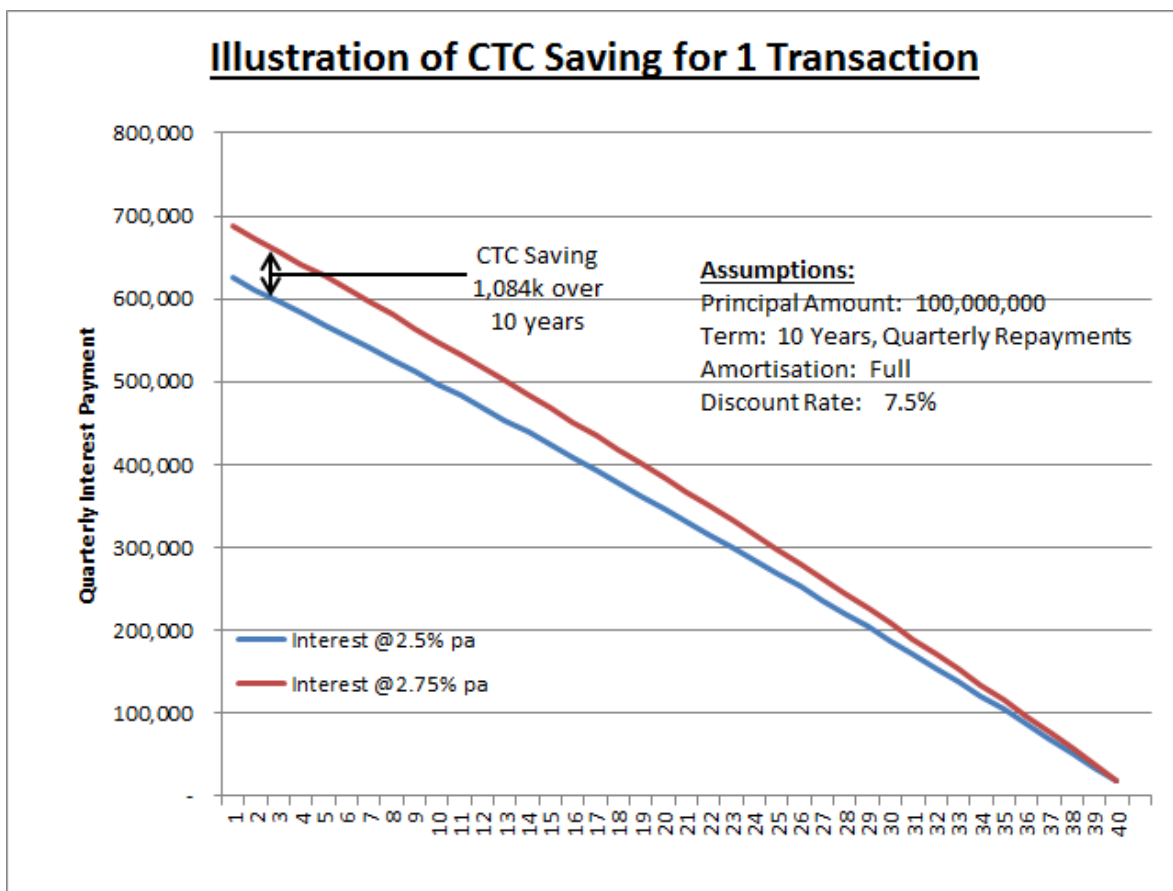
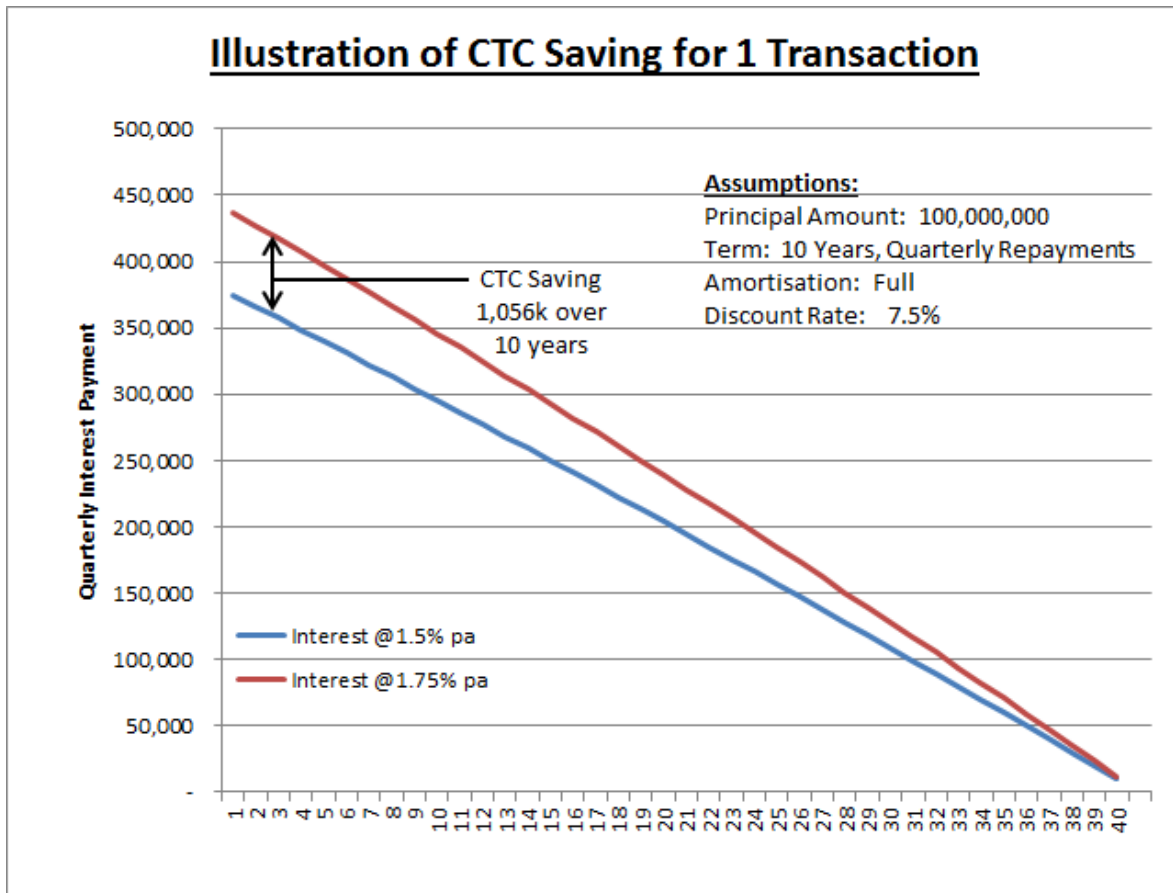
³¹ Boeing Capital Corporation, *Current Aircraft Finance Market Outlook 2014-2018*, <http://www.boeingcapital.com/cafmo/2013/brochure.pdf>

future obligations under the relevant transaction documents by the end of the specified waiting period. If under national insolvency law a creditor is entitled to possession prior to the end of the waiting period, that entitlement takes precedence to the waiting period. Alternative A requires the insolvency practitioner or the debtor to preserve the aircraft object and maintain it and its value in accordance with the transaction documents until possession of the aircraft object is given to the creditor. Alternative A does not require a creditor to obtain permission from the court before taking possession of the aircraft object at the end of the waiting period. The majority of countries that have ratified the treaty have adopted Alternative A with a waiting period of 60 days.

77. Alternative A would not affect the right of a secured creditor to take possession of an aircraft on winding up or bankruptcy. However it would displace UK insolvency law on administration and on company voluntary arrangements (CVAs) for this type of asset. Current UK insolvency law on administration and CVAs creates a moratorium so a creditor will need to obtain leave of the court in order to repossess an aircraft object as there is no requirement to handover the aircraft object to a secured creditor without a court order.
78. The Government has decided to adopt Alternative A and a summary of the costs and benefits is set out in paragraph 89(l).
79. For these reasons it is difficult to quantify the benefits of ratifying the treaty in the UK as a number of factors are involved in pricing aircraft finance transactions and many of these factors are outside the scope of this treaty (such as the underlying credit rating of the airline or the duration of the finance agreement). However, given the high value of aircraft objects, if only a small percentage of the benefits estimated in the AWG commissioned study materialise, or if only a small number of businesses benefit from a reduction in the cost of finance, the benefits are expected to far outweigh the small additional costs to business. As businesses can choose whether or not to register interests on the International Registry, we would only expect businesses to choose to incur these costs if they are outweighed by the benefits of using the provisions of the treaty.
80. The majority of the respondents to the consultation estimated that the potential benefits to UK airlines of ratifying the treaty for capital markets transactions in particular were a reduction of 25-75bps based on an uplift in the rating of EETC transactions of 1-3 notches. Due to the high value nature of these assets, even a small bps reduction could have a significant impact on the overall cost of financing. The impact for other types of financing arrangements, such as bank finance is unclear.
81. The charts below are an illustration of the potential benefits, based on the benefits estimated by stakeholders in response to the consultation. The illustration looks at the potential reduction in the cost of raising finance based on one aircraft finance transaction where an airline has raised finance through the capital markets only. There are illustrations are for two transactions, one priced between 1.5% and 1.75% and one at 2.5% to 2.75%. The estimates assume the following:
 - (i) The cost of the underlying aircraft is \$100m – this is in the range of the average price of aircraft of \$60-400m.
 - (ii) The term of the loan is 10 years and is to be repaid quarterly – the average duration of aircraft finance agreements is 10-12 years.
 - (iii) Full amortisation of the loan.
 - (iv) Discount rate of 7.5% has been applied – IATA's (International Air Transport Association) forecast average working weight of capital for airlines in 2014 is between 7% and 8% as per its June 2014 Airline Industry Economic Performance report (<http://www.iata.org/publications/economics/Pages/industry-performance.aspx>)
 - (v) Ratifying the Cape Town treaty will result in a reduction of 25bps to the cost of raising finance through capital markets transactions – this is the lower bound of the estimate given by

the majority of stakeholders responding to the consultation and should not be taken as an illustration of the benefits to airlines used other methods of funding

A change in the above estimates would produce a different expected benefit.



82. The estimated savings based on these two illustrative examples range between \$1,056,000 and \$1,084,000 - and the higher the interest rate, the larger the savings. Therefore, these illustrations (which are based on the reduction in bps estimated by the majority of stakeholders responding to the consultation) suggest that the possible savings on one aircraft finance transaction through the capital markets transactions would outweigh the costs to business. As explained in paragraph 25, global finance experts expect the role of the capital markets in aircraft financing to increase. So far one UK airline has raised finance through the capital markets in a transaction in 2013.
83. If UK airlines and leasing companies benefit from a reduction in the cost of raising finance, this may lead to increased investment in the aircraft objects covered by the treaty. This may result in a benefit for UK manufacturers through increased sales of helicopters, airframes and aircraft engines. Increased sales of newer aircraft objects may lead to knock-on benefits for customers in terms of improved comfort and environmental benefits through reductions in carbon dioxide and nitrogen oxide emissions and a reduction in noise levels.
84. Although not the primary reason to ratify the treaty, UK businesses may see some secondary benefits from using the International Registry, such as a reduction in administrative burdens. UK engine leasing companies and financiers will benefit from the provisions in the International Registry to register interests against aircraft engines separately. This is important as engines are routinely moved between aircraft for maintenance reasons. Aircraft engines are high value assets in their own right and airlines routinely lease spare engines (both in the long-term and the short-term) which they can move between aircraft frames as required to match their needs. As such a creditor cannot be certain which airframe an engine will be attached to or in which jurisdiction that engine will be located at any one time. Comparatively, aircraft engines retain their value well over time and therefore these provisions are particularly important for engine manufacturers and engine leasing companies. Ratifying the treaty will recognise rights created and registered against aircraft engines separately under UK law and this may lower the cost of raising finance for engines as creditors will have greater confidence they can recover an aircraft engine if necessary.
85. If the UK ratifies the treaty with a certain set of declarations (see paragraph 91-98 for further detail), airlines may be eligible for a discount of up to 10% on the premium of export credit support. This discount is discretionary and export credit agencies can decide how much of a discount to apply. The latest table of premiums is set out at paragraph 26. The discount will not apply to all airlines since not all airlines are eligible for or apply for export credit support. The Government intends to make the declarations necessary for the Aviation Sector Understanding discount.
86. As noted in paragraph 57, some UK businesses may benefit from a reduction in the fee to register an interest with the International Registry compared with registering an interest with the UK's National Register of Aircraft Mortgages. However, this would only relate to registrations made against airframes and helicopters since it is not possible to register interests against engines separately on the UK's National Register of Aircraft Mortgages. As stated in paragraph 60, discussions with businesses have indicated that creditors are likely to register their interests on the International Registry and the relevant national register, therefore it is unclear whether and to what degree these benefits will materialise.
87. UK businesses choosing to use the International Registry may benefit from a reduction in administrative costs as the International Registry, unlike the UK's National Register of Aircraft Mortgages, is open twenty-four hours a day, seven days a week. It may therefore be more convenient to register interests with the International Registry, particularly as the parties to an aircraft finance transaction may be located in several different jurisdictions and time zones. UK businesses may benefit from provisions to register prospective interests with the International Registry for the same reasons. A single International Registry would make it more convenient for financiers to check whether any party held an interest which would take precedence over its own as they may not need to check multiple national registers. However, these benefits will only be fully realised if a critical mass of countries ratifies the treaty.

Summary of costs and benefits of optional provisions

88. The Government has consulted on the optional provisions contained within the treaty. The government's approach to the optional provisions is set out below along with an estimate of the costs and benefits. The Government's best understanding of the costs and benefits of the options within the competence of the EU is also set out below. This does not include familiarisation costs which are set out in paragraph 41-56.
89. Under the terms of the treaty, the parties to an aircraft finance transaction can agree to exclude the majority of the provisions of the treaty in their contractual negotiations, including optional declarations made by the UK. Therefore, businesses would be expected to only include these provisions in their financial agreements if the benefits outweigh the costs.

Declarations within the competence of the EU – out of scope of 'One In, Two Out'

(a) The courts having jurisdiction to grant creditors relief pending final determination of their claim

The EU has made a declaration stating that where a debtor is domiciled in an EU Member State, that Member State should only apply this provision in accordance with the existing EU Regulations as interpreted by the European Court of Justice. This declaration does not change the current position under UK law and is not expected to have any impact on business. The EU regulations are broadly equivalent to the provisions under the treaty.

(b) Allowing parties to choose which law will govern their contractual obligations, either wholly or in part

The EU has not made a declaration allowing parties to choose which law will govern their contractual obligations, therefore current EU Regulations will continue to apply within the UK. This does not change the current position under UK law and so is not expected to have any impact on business. The EU regulations are broadly equivalent to the provisions under the treaty.

(c) Courts in one Contracting State are obliged to co-operate with courts in another Contracting State in respect of insolvency proceedings

The EU has not made a declaration with regard to the provision of Insolvency Assistance under the treaty and therefore current EU Regulations will continue to apply within the UK. This does not change the position under UK law and so is not expected to have any impact on business. The EU regulations are broadly equivalent to the position under the treaty.

Declarations within the competence of the UK – In scope of 'One In, Two Out'

(d) Non-consensual rights– *maintains current priority for this class of rights under UK law and therefore there are no additional costs or benefits*

The UK has decided to make a declaration under Article 39 of the Convention that all current and future rights with priority under UK law without registration will retain their priority. In addition nothing in the Convention will affect the right of a State or a State entity, intergovernmental organisation or other private provider of public services to arrest or detain an aircraft object for payments of amounts owed directly related to the provision of public services in respect of that object or another object.

Since some non-consensual rights already have priority in the UK, there are no additional costs or benefits of the UK making a declaration under Article 39(1)(a). However, some respondents to the consultation commented that:

- (a) existence of non-consensual rights or interests result in increased risks for financiers and lessors and so may increase finance costs. It is difficult to quantify such costs; and

- (b) a declaration that any category of non-consensual right or interest has priority over a registered interest requires UK business to regularly monitor legal developments to ensure that they fully understand the scope of such interests.

However, since this is consistent with the current position under UK law, no additional costs are expected to be incurred by business. In addition there is no additional risk for financiers involved in aviation finance transactions since these provisions already exist in the UK and are already taken into account by financiers. As the scope of non-consensual rights and interests under current UK law is narrow, any such costs are unlikely to significantly affect costs of financing or leasing of aircraft objects.

Whilst the treaty allows the UK to remove the priority given to non-consensual rights, it is important the priority given to detention rights to recover unpaid charges relating to the provision of public services is maintained. For example, the ability to collect outstanding debts for the payment of public services such as Eurocontrol charges which fund the provision of air navigation services across Europe, a safety critical service. The average yearly billing of route charges is €7 billion and due to the UK's geographical location and in particular the use of London as a hub and the high number of carriers that fly through London, the ability to detain aircraft in order to recover outstanding debts is important to the collection of these outstanding charges. This includes retention of the fleet lien which allows the CAA to detain one aircraft to recover charges across an airline's entire fleet. This minimises disruption to passengers and airlines.

If outstanding Eurocontrol charges are not collected, this will lead to an increase in route charges to ensure the air navigation system is well-funded and will impact on airlines that pay on time, who will end up subsidising airlines that do not pay these charges.

The preservation of all current and future rights has the benefits of consistency of priority of non-consensual rights and interests against international interests registered before and after the date of ratification of the Convention by the UK, thereby reducing familiarisation costs for UK businesses in ratification of the treaty by the UK.

- (e) **Other categories of non-consensual rights which can be registered with the International Registry and treated as international interests) – maintains current position under UK law and therefore there are no additional costs or benefits**

The UK will not make a declaration under Article 40 of the Convention and allow for the registration of other interests, such as judgment debts, with the International Registry.

Since judgment debts granted through the UK courts cannot be enforced against a specific asset, allowing the registration of these judgments on the International Registry would change the priority of debts and potentially grant unsecured creditors rights against secured creditors. A new class of creditor would also incur familiarisation costs with the International Registry and fees to register their interest.

Holders of judgment debts will still be able to pursue their claim through the UK courts, this is in line with the current position and therefore there are no expected additional costs for business.

- (f) **Whether interests arising out of internal transactions (i.e. transactions where the asset and all parties to the transaction are located in the same state when the transaction is concluded) can be registered with the International Registry**

The UK will not make a declaration under Article 50 of the Convention. The effect is that all remedies under the Convention will apply to internal transactions (i.e. a transaction where all parties and the asset are located in the UK at the time the transaction is completed). Registration with the International Registry is not mandatory and it would be up to business to decide whether or not to make use of this provision.

Whilst the treaty does not require Contracting States to allow internal interests to be registered on the International Registry, allowing businesses to register internal transactions with the International Registry if they wish, is important to ensure consistency of legal remedies, thereby reducing familiarisation costs for UK businesses. Without this declaration, UK businesses would need to use two systems – one for internal transactions and one for international transactions. This would increase costs and the complexity of the system for business.

All the stakeholders who responded to the question on this provision in the consultation expressed support for allowing internal transactions to be registered on the International Registry.

The majority of respondents to the consultation stated that it would be confusing if the treaty did not apply to internal transactions, as two registration systems would need to operate in parallel.

(g) The courts that will have jurisdiction over matters covered by the treaty (other than in insolvency) – maintains current position under UK law and therefore there are no additional costs or benefits

The UK will make a declaration under Article 53 of the Convention to specify the court in respect of proceedings under the Convention. The relevant courts are the High Court in England and Wales, the Court of Session in Scotland and the High Court in Northern Ireland, due to the high value nature of the asset.

The benefits of a declaration under Article 53 of the Convention are greater clarity and certainty for creditors and debtors. This will save business time and money in trying to determine the relevant court should they need to make a claim.

There are no costs for a declaration under Article 53 of the Convention as this declaration offers clarification that the courts with jurisdiction under the treaty are those courts that have jurisdiction over similar claims outside the treaty.

(h) Whether creditors can grant a lease of an aircraft object when the aircraft object is situated in the Contracting State – maintains current position under UK law and therefore there are no additional costs or benefits for the individual option, however this is one of the criteria for the OECD Aviation Sector Understanding discount and therefore there is a benefit when taken with other relevant declarations as a whole

The UK will not make a declaration under Article 54(1) of the Convention to exclude the remedy of a grant of a lease of an aircraft object when the aircraft object is situated in the UK. Parties to a finance transaction can agree to disapply this remedy.

The benefits of the UK not making a declaration under Article 54(1) of the Convention are as follows:

- (a) creditors may already grant a lease of an aircraft object situated in the UK and a declaration would weaken the current protections available to creditors;
- (b) a declaration under Article 54(1) of the Convention restricts remedies for creditors, which may result in higher costs for business in aircraft finance transactions. These additional costs are difficult to quantify; and
- (c) a declaration under Article 54(1) would prevent inclusion of the UK on the OECD's Cape Town List – and therefore prevent a reduction in the ASU's premiums, resulting in possible higher aircraft finance costs for UK airlines and lessors using export credit support. The reduction available is up to 10% of the risk premium and is at the discretion of export credit agencies. Under the ASU, for a B rated airline (considered to be the average credit rating for airlines), this would result in a lower risk premium of up to US\$1,038,000 for each \$100m of financing, based on prevailing minimum rates.

Whilst the treaty does not require Contracting States to allow the creditors to grant a lease of an aircraft object situated in the Contracting State, the granting of a lease of an aircraft object situated in the UK is already permitted under UK law.

If the Government were to change existing law and not allow creditors to grant a lease of an aircraft object within the UK, airlines, leasing companies and creditors would need to adjust current practice which would increase costs. It would also create a confusing distinction between remedies available to creditors with regard to aircraft objects and remedies available to creditors with regard to other assets where the granting of a lease would still be permissible.

If the Government were not to allow creditors to grant a lease of an aircraft object situated in the UK, the UK would not meet the criteria for the OECD Aviation Sector Understanding discount and UK airlines would not be eligible for the potential discount of up to 10% on the premium rate of export credit support.

All stakeholders responding to the consultation question on the granting of leases supported allowing creditors to grant a lease of an aircraft object situated in the UK.

- (i) **Extra-judicial remedies (remedies available to creditors without leave of the court) that are available to creditors**— *maintains current position under UK law and therefore there are no additional costs or benefits for the individual option, however this is one of the criteria for the OECD Aviation Sector Understanding discount and therefore there is a benefit when taken with other relevant declarations as a whole*

The UK has decided to make a declaration under Article 54(2) of the Convention that leave of the court is not required for remedies available under the Convention which are not expressed to require application to the court. Parties to a finance transaction can agree to opt-out of the individual remedies concerned.

The benefits of this declaration are:

- (a) consistency with existing UK law that already allows the use of extra-judicial remedies or self-help remedies that do not require leave of the court, thereby reducing costs for UK business in familiarisation with ratification of the treaty by the UK and ensuring there is no reduction in the benefits already available to creditors under UK law;
- (b) certainty for creditors regarding the availability of remedies, thereby reducing risks and costs of aircraft finance;
- (c) reduced costs and time for UK businesses in exercising remedies under the Convention as they do not need to apply to a court and pay the relevant court fee;
- (d) no additional costs for the UK Government in providing access to the courts for exercise of remedies; and
- (e) it will allow the UK airlines to benefit from a potential discount of up to 10% on the premium rate of export credit support. To qualify, a Contracting State on the OECD's Cape Town List must either make a declaration under Article 54(2) that leave of the court is not required for remedies available under the Convention which are not expressed to require application to the court, or a declaration to apply the provisions of Article X of the Protocol by defining 'speedy' as no more than ten days for the remedies set out in Article 13(1) (a)-(c) and no more than thirty days for the remedies set out in Article 13(1) (d) and (e). This may result in lower aircraft financing costs for UK airlines and lessors using export credit support. The reduction available is at the discretion of export credit agencies. Under the ASU, for a B rated airline (considered to be the average credit rating for airlines), this would result in a lower risk premium of up to US\$1,038,000 for each \$100m of financing based on prevailing minimum rates.

Whilst the treaty does not require Contracting States to allow the use of extra-judicial remedies, if the Government were to change existing law and not allow the use of extra-judicial remedies, leasing companies and creditors would need to adjust current practice which would increase costs. It would also create a confusing distinction as extra-judicial remedies would still be available for other types of assets or aircraft objects falling outside the treaty. This would also increase costs to business, who would have to pay court fees and could face delays in being granted the remedies available under the treaty.

As stated above, if the Government were not to allow the use of extra-judicial remedies, the UK would not meet the criteria for the OECD Aviation Sector Understanding discount and UK airlines would not be eligible for the potential discount of up to 10% on the premium rate of export credit support.

All stakeholders responding to the consultation question on extra-judicial remedies supported maintaining their use within the UK.

(j) A requirement for creditors to re-register interests on the UK's national register with the International Registry in order for them to maintain their priority following ratification of the treaty by the UK

The UK has decided not to make a declaration under Article 60 of the Convention. This means that pre-existing rights or interests registered with the CAA before the treaty was ratified would have priority over subsequently registered international interests.

The benefits of the UK not making a declaration under Article 60 are that parties will not incur any additional costs to re-register pre-existing rights or interests. These costs would be a combination of the fee charged by the International Registry to record the interest and time to review all previous transactions. The fees to register interests with the International Registry are set out in paragraph 48. It is estimated that the costs of reviewing transactions, determining whether or not to register interests and if necessary filing interests with the International Registry would be £400 for each historical transaction. This is based on a time estimate of 2 hours to check each historical transaction, determine whether any filings need to be made and making the necessary filings, and internal costs of £200 per hour. These costs would be high for UK businesses with a large portfolio of transactions which may be covered by UK ratification of the CTC.

As the UK has decided not to require pre-existing interests to be re-registered, businesses will not have to pay these additional costs.

There are no additional costs associated with not making a declaration under Article 60. However in order to fully identify registered interests in aircraft objects, businesses are likely to need to search the CAA's UK Register of Aircraft Mortgages, which incurs a charge of £29 per search, in addition to searches with the International Registry. These are costs businesses are likely to incur irrespective of this decision as they routinely check the CAA's National Register of Aircraft Mortgages to understand who else may have an interest over an asset and so are not additional costs. Therefore there are no expected additional costs or benefits. In addition, businesses are not required to search the CAA register and it would be a decision for the business whether or not it needed to do so.

(k) Whether the term *speedy relief* available to creditors whilst their claim is being determined by the court should be defined and, if so, how– *The UK will not define "speedy" relief and therefore there are no additional costs or benefits to business*

The UK has decided not to change its national law and define the term *speedy* under the treaty as there is no evidence that the UK courts are slow in determining claims.

(l) Remedies on insolvency – Provisions in line with Alternative A adopted

The UK has decided to amend its national laws to be consistent with a declaration under Article XXX(3) of the Protocol to apply the entirety of Alternative A to all types of insolvency related

events with a waiting period of 60 days. The effect of this declaration is that upon occurrence of an insolvency related event, the insolvency practitioner or the debtor must, within 60 days, either give up possession of the aircraft object to the creditor, or cure all defaults and agree to perform all future obligations under the relevant transaction documents.

The parties to an aircraft finance transaction can agree to opt-out of Alternative A in their contractual agreements.

The benefits of the UK amending its national laws to apply the entirety of Alternative A to all types of insolvency related events with a waiting period of 60 days are as follows:

- (a) Alternative A provides certainty to creditors that upon the occurrence of an insolvency related event they can recover their aircraft within 60 days or that the defaults will be cured. This certainty reduces risks for the financiers and lessors of aircraft objects, and is particularly important for capital markets investors, and therefore is likely to reduce aircraft financing costs. Respondents to the consultation estimated these benefits could be between 25-75 bps based on an uplift of 1-3 notches on the rating of these types of transactions. If only a small reduction in bps is realised, this could have a significant impact on the cost of raising finance due to the high value nature of these assets. In addition, the certainty provided by Alternative A reduces transactional risk for financiers and airlines; and
- (b) a declaration to apply Alternative A with a waiting period no longer than 60 days is a qualifying declaration for the purposes of inclusion of a Contracting State on the OECD's Cape Town List in order to benefit from a discount of up to 10% on the premium rate of export credit support. This may result in lower aircraft financing costs for UK airlines and lessors using export credit support. The reduction available is at the discretion of export credit agencies. Under the ASU, for a B rated airline (considered to be the average credit rating for airlines), this would result in a lower risk premium of up to US\$1,038,000 for each \$100m of financing based on prevailing minimum rates.

The costs of the UK amending UK insolvency law to adopt the provisions of Alternative A are:

- (a) familiarisation costs for businesses as a result of the change from existing insolvency law to a new regime. Familiarisation costs relating to ratification of the treaty are set out in paragraph 42-48 of this Impact Assessment; and
- (b) impact on the ability of an insolvency practitioner to restructure an airline in administration due to the 60 day waiting period. This would shorten the period within which an insolvency practitioner would need to make a decision on the future of the business. In addition there is no evidence that the administration regime is widely used by UK businesses in financial difficulty.

Whilst the treaty does not require Contracting States to adopt Alternative A, if the Government were not to adopt Alternative A, the UK would not meet the criteria for the OECD Aviation Sector Understanding discount and UK airlines would not be eligible for the potential discount of up to 10% on the premium rate of export credit support.

The majority of stakeholders supported adoption of Alternative A. A number of stakeholders said that this is the provision that will lead to the greatest economic benefit to UK airlines in terms of a reduction in the cost of raising finance, particularly for finance raised through the capital markets.

(m) To allow the expeditious de-registration and export of an aircraft object

The UK has decided to make a declaration under Article XXX(1) of the Protocol to apply the provisions of Article XIII. This means that where a debtor has issued and submitted to the registry authority (in the case of the UK, the Civil Aviation Authority or CAA) an irrevocable de-registration and export request authorisation ("IDERA"), the IDERA will be recorded with the CAA. As a result, the creditor can request the expeditious de-registration and export of an aircraft object, allowing the creditor to quickly gain possession should an airline default on repayments.

A debtor is not required to grant an IDERA to a creditor.

The benefits of the UK making a declaration to allow the use of an IDERA is

- (a) registration of an IDERA allows creditors to gain possession of the aircraft object quickly in cases of default so that it can be re-sold or leased to generate income. This may reduce the cost of raising finance for airlines;
- (b) creditors can already request de-registration of an aircraft object where a power of attorney is in place – the adoption of the IDERA will minimise negotiation as to the form of the IDERA as it is a standard form used by many jurisdictions. This will reduce time and legal costs for airlines and aircraft financiers; and
- (c) a declaration under Article XXX(1) of the Protocol to apply the provisions of Article XIII is a qualifying declaration for the purposes of inclusion of a Contracting State on the OECD's Cape Town List in order to benefit from a discount of up to 10% on the premium rate of export credit support. This may result in lower aircraft financing costs for UK airlines and lessors using export credit support. The reduction available is at the discretion of export credit agencies. Under the ASU, for a B rated airline (considered to be the average credit rating for airlines), this would result in a lower risk premium of up to US\$1,038,000 for each \$100m of financing based on prevailing minimum rates.

The costs of the UK making a declaration under Article XXX(1) of the Protocol are as follows:

- (a) there may be additional administrative and/or internal costs for the CAA in recording IDERAs;
- (b) additional costs for businesses in preparing and registering IDERAs, although such costs are likely to be low in light of the fact that airlines currently provide deregistration powers of attorney to creditors; and
- (c) familiarisation costs for businesses as a result of the change from the existing regime of rights to detain or arrest aircraft to a new regime. However familiarisation costs are likely to be low, given that airlines currently provide deregistration powers of attorney to creditors (although deregistration powers of attorney cannot be registered with the CAA). These familiarisation costs are included in the stage one familiarisation costs in paragraphs 42-48.

Whilst the treaty does not require Contracting States to allow the use of IDERAs, if the Government were not to adopt the IDERA route, the UK would not meet the criteria for the OECD Aviation Sector Understanding discount and UK airlines would not be eligible for the potential discount of up to 10% on the premium rate of export credit support.

The majority of stakeholders responding to the question on the IDERA route supported its use.

- (n) **Designating any entry points to pass information and/or registrations to the International Registry (not adopted)** – *maintains current position under UK law and therefore there are no additional costs or benefits to business*

The UK has decided not to make a declaration under Article XIX of the Protocol and will not designate any entry points through which information may or is required to pass through before being sent to the International Registry.

The benefits of the UK not making a declaration under Article XIX of the Protocol are as follows:

- (a) no additional costs for the UK Government or for end users in establishing and maintaining an entry point;
- (b) no additional costs and time for UK business in travelling to the entry point to make filings;

- (c) reduced familiarisation costs and transaction costs through having one regime for both aircraft and helicopters and aircraft engines; and
- (d) consistency with the current position under UK law. UK businesses may already register interests with the International Registry without sending the information through a designated entry point

There are no costs associated with this approach.

OECD Aviation Sector Understanding Discount

- 91. If the UK adopts a specific set of provisions, airlines that apply for and are granted export credit support may be eligible for a discount of up to 10% on the premium rate of export credit support. The Sector Understanding on Export Credits for Civil Aircraft is an annex to the OECD Arrangement on Officially Supported Export Credit, commonly referred to as the Aviation Sector Understanding (ASU). It sets out the internationally agreed rules for officially supported export credits in the aviation sector. The ASU provides a framework for export credit agencies (ECAs) to set the price and levels of cover for export credit support so that all participating states use the same principles, creating a level playing field. The current participants in the ASU are Australia, Brazil, Canada, the EU, Japan, Korea, New Zealand, Norway, Switzerland and the US. The ECA in the UK is UK Export Finance (UKEF).
- 92. Under the ASU, a buyer/lessor in a Contracting State which has ratified the Cape Town Convention and Protocol, incorporating certain declarations, is eligible for a discount of up to 10% on the premium rate of their export credit support. The level of the discount is at the discretion of the ECA. The UK is adopting the relevant declarations to meet the ASU criteria. However, since not all airlines are eligible for or will be granted export credit support, not all airlines will benefit from this reduction in the premium of export credit support. The potential benefits of the ASU discount are outlined above.
- 93. The ASU states which declarations under the treaty must be made and which must not be made in order for a Contracting State to meet the requirements to qualify for the discount. The declarations that Contracting States must make are:
 - (i) Adoption of Alternative A on insolvency proceedings with a maximum waiting period of 60 days
 - (ii) Ability to de-register and export an aircraft object
 - (iii) Allowing parties to agree which law should govern their contractual rights and obligations
- 94. The Contracting State must also make one of the following two declarations:
 - (iv) Declare that the remedies available to creditors on default, which are available in the treaty without leave of the court, are indeed available without leave of the court
 - (v) Declare that the additional remedies available to creditors pending final determination of their claim are available, with the exception of the requirement to allow parties to an agreement to disapply the ability of the court to protect debtors as set out in Article 13(2). The term *speedy* should be defined as no more than a certain number of days, depending on the type of relief to be granted.
- 95. In addition, Contracting States should *not* make the following declarations:
 - (i) A declaration to exclude the remedies available to creditors pending final determination of their claim, unless the Contracting State has made declaration (iv) above.

(ii) A declaration opting-out of provisions which state that the treaty supersedes the Convention for the Unification of Certain Rules Relating to the Precautionary Attachment of Aircraft – as the UK has not ratified the Convention for the Unification of Certain Rules Relating to the Precautionary Attachment of Aircraft, the UK will not make this declaration.

(iii) A declaration preventing the granting of a lease in the Contracting State's territory

96. The EU has not made a declaration regarding insolvency, however Member States can amend national law to reflect Alternative A or B under Article XI. In light of this, the ASU states that a Member State shall be deemed to have made the qualifying declaration regarding insolvency provisions provided that its national law has been amended to reflect the terms of Alternative A with a maximum waiting period of 60 days. The Government intends to amend national law to reflect the provisions of Alternative A.
97. The EU has made a declaration disapplying Article VIII regarding the choice of law and under Article 55 in respect of the availability of interim remedies pending final determination of a claim. The ASU also states that the requirements regarding choice of law and remedies will be considered to be satisfied if the laws of the EU or the relevant Member State are substantially similar to those set out in the treaty. The OECD has confirmed that the laws of the EU with regard to choice of law are substantially similar.
98. Although each airline's premium rate of their export credit support is different, if we assume that a B rated airline (the average airline credit rating) were to receive the 10% discount, this would lead to a lower risk premium of \$1,038,000 for each £100m of financing.

Summary of benefits

99. Ratification of the treaty is expected to lead to a reduction in the cost of raising aircraft finance for UK airlines and leasing companies. However, the expected benefit to UK airlines is difficult to quantify for a number of reasons. Airlines and leasing companies have a number of different funding options available to them and ratification of the treaty is only one of the factors financiers consider. Other relevant factors include the credit rating of the airline, the type of asset and the duration of the loan; factors which fall outside the scope of this treaty.
100. A study by Professor Linetsky, commissioned by the Aviation Working Group (AWG), estimated that UK airlines could benefit from a reduction in funding costs of between £538 million and £2.075 billion (with a best estimate of £1.2 billion) for aircraft deliveries over the next twenty years on an estimated £98 billion of aircraft finance, based on certain assumptions regarding how the UK would implement the Cape Town treaty. Even if only a small percentage of these benefits are realised, the benefits are expected to far outweigh the costs of ratifying the treaty to UK businesses. Therefore this policy is presented as a zero net cost.
101. Several respondents to the consultation thought that ratification of the Cape Town treaty, including the adoption of Alternative A, would lead to a possible reduction in the cost of raising aircraft finance for capital markets transactions. It was suggested it could be a reduction of 25-75bps based on an uplift of 1-3 notches to the rating given to these transactions. However, this should be seen as the high end of the potential benefits of ratifying the treaty.
102. A reduction in the cost of raising finance may lead to increased investment by UK airlines and leasing companies in aircraft objects. This in turn may lead to increased sales for UK manufacturers. There may also be knock-on comfort and environmental benefits for customers through reduced carbon dioxide and nitrogen oxide emission and reduced noise pollution.
103. UK businesses may benefit from a reduction in administrative burdens as a result of using the International Registry which is open 24 hours a day, seven days a week. This will make registering interests where the parties are located in multiple jurisdictions across different time zones more convenient.

104. The provisions in the treaty which allow interests to be created and registered separately against aircraft engines are expected to benefit UK aircraft engine manufacturers, creditors and airlines through a reduction in the cost of raising finance. Since the treaty allows the parties to an aircraft transaction to exclude by agreement many of the provisions of the treaty, businesses would only be expected to choose to bear any additional costs if they believed the benefits outweighed the costs.

Summary: Preferred option and implementation plan

105. Overall the Government believes that ratifying the treaty will benefit UK businesses by reducing the cost of raising finance to UK airlines and leasing companies. This reduction in the cost of raising finance is likely to be as a result of a reduced risk to creditors associated with lending to UK airlines. In turn, this may lead to increased investment in helicopters, airframes and aircraft engines and increased sales by UK manufacturers. There may be additional benefits for airlines and leasing companies seeking to purchase or lease aircraft engines since interests against aircraft engines can be registered separately on the International Registry. Interests against aircraft engines cannot be registered separately on the UK Register of Aircraft Mortgages.
106. UK businesses may see some secondary, administrative benefits through using the International Registry which is open 24 hours a day, seven days a week. This is likely to take some of the pressure off the aircraft finance transactions involving parties located in multiple jurisdictions. Some businesses may pay less in fees to register an equivalent interest with the International Registry compared with the UK National Register of Aircraft Mortgages. However, this will depend on the maximum take-off weight of the aircraft and will depend on whether the business decides to register their interest with the International Registry and with the UK's National Register of Aircraft Mortgages, with just one of the registers or with neither.
107. UK businesses involved in aircraft financing will incur some costs to familiarise themselves with the new regulations. This is estimated to apply to a maximum of 130 UK businesses, based on the number of UK airlines and the number of UK companies with a current interest registered with the UK's National Register of Aircraft Mortgages. Some businesses, mainly the 30 or so UK airlines, are likely to face some costs in the form of additional legal costs to familiarise themselves with the International Registry. However, not all UK businesses will incur these costs since a number of UK businesses already use or are familiar with the International Registry. Therefore a very small number of UK airlines are likely to be affected by these familiarisation costs.
108. Some airlines may pay increased fees to register their interest if they choose to register with both the International Registry and the National Register of Aircraft Mortgages. However, since the Government is not proposing to make registration on the International Registry mandatory, it will be up to business to decide how best to protect its interests. Businesses can decide whether to register interests on the UK National Register of Aircraft Mortgages, the International Registry, on both registers or on neither. Therefore businesses would only be expected to pay two sets of fees if they believe the benefits outweigh the costs.
109. The benefits individual airlines will receive will depend on a number of factors, some of which are outside the subject matter of this treaty and are therefore difficult to quantify. However, if only a small proportion of the benefits estimated in the study commissioned by the AWG materialise, the benefits are expected to far outweigh the costs and lead to a net benefit to the UK. The majority of respondents to the consultation expected this to result in a reduction in the cost of finance for capital markets transactions, suggesting a reduction of 25-75bps or a 1-3 notches uplift on the rating given to these transactions. However, depending on how airlines finance aircraft and their underlying financial situation, some airlines may not see a reduction in their costs of financing. This is due to the very small costs to business as a result of ratifying the treaty and the high value of helicopters, airframes and aircraft engines and large amounts of financing required by UK airlines and leasing companies. If ratification of the treaty results in a small number of additional sales by UK manufacturers of helicopters, airframes or aircraft engines, the benefits of ratifying the treaty would again outweigh the costs of ratification.

110. The Government intends to implement the treaty through secondary legislation using Section 2(2) of the European Communities Act. The Government intends to implement the treaty during 2015 and for the regulations to come in to force in 2015.

Small and micro business assessment

111. Small and micro businesses are not exempted from regulations to ratify the treaty. Since the aim of the treaty is to reduce the cost to business of raising aircraft finance, excluding small and micro businesses from regulations to ratify the treaty would prevent them from benefitting from a reduction in the cost of finance. If small and micro businesses were excluded from the provisions of the treaty, they would therefore pay a proportionately higher cost for aircraft finance compared with medium and large businesses. This would disadvantage small and micro businesses, including start-ups, in this sector. The majority of airlines, aircraft manufacturers, financiers and legal firms involved in the aircraft finance industry are medium and large firms and therefore the number of small and micro businesses who would be affected by the treaty is expected to be small.