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BRIEFING

AIRCRAFT REPOSSESSION IN THAILAND:
CHANGE IS IN THE AIR?

MARCH 2017

- THE THAI CIVIL AVIATION AUTHORITY (“CAAT”) HAS DECIDED TO ADDRESS THE ISSUE OF THAI AIRCRAFT LESSEES IN DEFAULT
- THE CAAT MAY EXERCISE ITS DEREGISTRATION POWERS MORE ACTIVELY
- WILL THIS PROVIDE LESSORS AND FINANCIERS WITH MORE SECURITY AND COMFORT?



The Civil Aviation Authority of Thailand (“CAAT”) is focusing on Thai aircraft lessees in default and, on 1 March 2017, it announced that it would take steps to address the problem of lessees.

Why is the CAAT doing this?

It is important to bear in mind that the CAAT was created to replace its predecessor, the Department of Civil Aviation (“DCA”), following the International Civil Aviation Organization (“ICAO”) ‘red flag’ and Federal Aviation Administration (“FAA”) downgrade in 2015. A key focus of the CAAT is to remove the ICAO ‘red flag’ and for Thailand to be upgraded to Category 1 by the FAA. ICAO and the FAA will need to be satisfied that the deficiencies identified in regulatory supervision and oversight by the DCA have been addressed. A critical component is an independent regulator that will properly supervise airlines and enforce laws and regulations, even if this results in the loss of air operators’ licences of delinquent airlines.

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Since 2016, the CAAT has inspected the annual audited financial records of all Thai airlines and operators. This is a positive step as it will ensure that airlines focus on financial management and ensuring that their financial position is sound and stable. In addition to access to annual audited financial statements, the audits should also make it easier for lessors and financiers to more effectively assess the creditworthiness of Thai airline lessees.

The ability to meet lease payment obligations is a significant indication of the financial health of an airline. A lessee unable to meet these obligations may also have difficulties in paying for maintenance, landing and navigation charges and crew salaries. These issues should raise concerns for the regulator and ensuring that the regulator is focused on these issues is likely to be part of the next ICAO audit.

Prior to the ICAO 'red flag', a number of Thai operators experienced financial difficulties, including failing to pay airport landing, navigation and related charges. Steps taken by airports to address this left the passengers of these airlines stranded in foreign airports with no assistance from the financially troubled airlines. A closer scrutiny of the financial position of Thai airlines and operators should reduce the risk of further such incidents.

It is in this context, that the CAAT made its announcement on 1 March.

What does the announcement change?

The CAAT announcement does not suggest that the CAAT is seeking additional or expanded powers in relation to deregistration. The announcement suggests that the CAAT may more actively exercise its existing powers in relation to deregistration.

Although the DCA, and now the CAAT, have the power to deregister aircraft, deregistration of aircraft typically proceeded only with the consent of the lessee. This made deregistration where the lessee is in default difficult and infrequent.

"THAI LAW DOES NOT RECOGNISE AIRCRAFT MORTGAGES AND JUDGMENTS OF FOREIGN COURTS IN FAVOUR OF LESSORS."

Thai law does not recognise aircraft mortgages and judgments of foreign courts in favour of lessors and financiers against defaulting Thai lessees are not recognised by Thai courts. Lessors and financiers had little alternative but to commence proceedings in the Thai courts for breach of contract or of a Thai pledge. It is not unusual in such circumstances for Thai lessees to defend such claims. Contested litigation in the Thai courts can take years to resolve and Thai courts are reluctant to make interim orders, particularly to deregister the aircraft in question. If the aircraft remains in the possession of the Thai lessee, the lengthy litigation can allow time for the lessee to restructure its operations and to delay making lease payments. There have been cases where the lessee refused to make any payments until the litigation was completed and judgment handed down.

Some lessees may also have used their continued possession of aircraft to prevent the CAAT from cancelling their Air Operator Certificate and/or Aircraft Operating Licence for failing to have a minimum of two operational aircrafts.

While these tactics and litigation may have assisted some lessees in financial difficulties, the practical effect was to increase the risk profile for Thai lessees, regardless of their financial position. Many financiers and lessors were unable or unwilling to accommodate this risk. This reduced the number of options and may have increased leasing costs for Thai lessees.

As Thailand appears unlikely to ratify and accede to Cape Town Convention on International Interests in Mobile Equipment ("the Cape Town Convention"), any steps that provide more certainty and comfort to lessors and financiers should be seen as a positive development.

“IF THE CAAT IS SEEN TO ACT SWIFTLY AND FIRMLY... THE DETERRENT EFFECT MAY BENEFIT LESSORS AND FINANCIERS.”

How will it work?

The CAAT is proposing to hold a meeting with the lessee and lessor to assess the situation and the position of both parties. Where the lessor indicates that it will terminate the lease and the CAAT accepts that it can validly do so, the CAAT has indicated that it would proceed with immediate deregistration of the aircraft from the Thai register. This should enable lessors to re-register the aircraft in another jurisdiction and assist with the removal of the aircraft from Thailand.

The initial deregistration applications made after the 1 March announcement are likely to provide a structure for future applications. Critical to the effectiveness of these powers and the ability of the CAAT to properly supervise airlines and operators will be the extent to which it can act to deregister aircraft where the lessee is in default. If the CAAT is seen to act swiftly and firmly in such situations, the deterrent effect may benefit lessors and financiers as Thai lessees will be less confident about their ability to prevent the deregistration and return of aircraft where they are in default on their lease payments.

What this means in practice

For meetings between the CAAT, lessee and lessor to be an effective means of determining whether an aircraft should be deregistered, there should be guidelines and procedures setting out the level of detail required and the focus of the meetings. If the lessor is alleging that the lessee is in default and that it seeks the deregistration of the aircraft because of an event of default, the CAAT should ensure that the submissions of both parties focus on these issues and that the meeting does not become an opportunity for a lessee to present arguments and submissions to further delay making lease payments.

The CAAT will also need to exercise care to ensure that it is not drawn into adjudicating disputes between lessee and lessor or to becoming involved in issues that may become the subject of subsequent proceedings between lessee and lessor.

If the CAAT becomes involved in proposals or arrangements to restructure outstanding and/or future lease payments, it should also exercise care to avoid becoming involved in enforcing such agreements.

The CAAT announcement does not address the role of other organisations, notably the Airports of Thailand (“AoT”), Aero Thai and maintenance and other service providers. The assistance and co-operation of the AoT and Aero Thai will be necessary to allow for the removal of aircraft from Thailand.

Where an aircraft remains in Thailand and cannot be removed by the lessor, issues in relation to its registration, insurance and ongoing and routine maintenance should also be considered. It is not clear if and how the CAAT would be involved in dealing with these issues, particularly the risk that an aircraft becomes uninsured while being operated by a lessee in default or while being stored at a Thai airport pursuant to a court order. For the latter, the issue of aircraft parking and related charges should also be considered and addressed.

It is also not clear how the CAAT proposes to address attempts by lessees to obtain injunctions and other court orders to prevent the removal of the aircraft from Thailand. These can be in breach of Thailand’s obligations under the Chicago Convention. The application of foreign law and international conventions by Thai

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courts remains limited and judgments and court orders in breach of international treaty obligations should be viewed in this context. It is not clear how the CAAT proposes to address this.

The CAAT and AoT appear reluctant to take steps contrary to court orders preventing the removal of aircraft from Thailand. While this may be based on concerns about the consequences of being found in contempt of court, if Thai lessees can continue to prevent the removal of aircraft through injunctions and other orders, the practical effect of the 1 March announcement may be limited and narrow.

FOR MORE INFORMATION

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