

What a Lessor and Secured Lender Should Expect From an Opinion Letter of Local Counsel in a Cross-Border Lease

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Overview

The leasing of a commercial aircraft to an airline in a foreign jurisdiction presents risks to the lessor and its secured lender, including whether an aircraft may readily be repossessed if a lease event of default occurs. Local counsel in that jurisdiction is typically engaged not simply to explain legal risks in its home country but also to help the lessor take reasonable precautions before the lessor delivers the aircraft to the lessee. In addition to protecting against default risk, the documents and collateral package prepared with the advice of local counsel help (1) satisfy the standard of care that a servicer must exercise in an aircraft secured financing and (2) make the aircraft with lease attached marketable to prospective purchasers. The opinion letter local counsel can deliver at closing should satisfy the expectations of finance parties and potential buyers, as well as create a roadmap that corresponds to the due diligence and precautions a lessor should take.

Who Gives the Opinion, Lessor's Counsel or Lessee's Counsel?

In most cases, the lessor will retain local counsel of its choosing and at its expense. The lessee will normally use its internal counsel or external counsel. Internal counsel to the lessee could provide the lessor an opinion letter, but such an opinion letter generally would provide only cursory opinions as to internal matters such as due authorization, execution and delivery of the lease and related documents, and potentially no violation of any other agreement to which the lessee is a party. As to the matters on which it will opine, internal counsel is the most qualified to give such opinions because it is deeply involved with the lessee's organizational matters. External counsel to the lessee in the lessee's jurisdiction is more likely to give a fuller opinion on the other legal issues that arise from the lease and may sometimes rely on the opinion of the lessee's internal counsel as to the matters on which internal counsel is most competent. However, in some jurisdictions, the lessee's external counsel may take the position that it is customary for counsel to issue an opinion only to its own client, not to a counterparty. Moreover, even if the lessor relies on an opinion or opinions of the lessee's internal and/or external counsel, the lessor may not be entirely comfortable that all issues about which the lessor and its lender should be concerned are being brought to light. Therefore, at the end of the day, the customary course of action is for the lessor to have its own counsel provide an opinion letter, with perhaps the opinions as to due authorization, execution and delivery being provided in a separate opinion letter issued by lessee's internal counsel. If the lessee's counsel does provide the full opinion letter, the lessor's counsel should at least have the opportunity to review and comment on it and the documents the lessee's counsel examines to give the opinions.

To Whom Is the Opinion Letter Addressed?

Counsel should address the opinion letter not only to the lessor, but also to the lessor's lease servicer or aircraft manager and any equity or debt finance parties and trustees identified to such counsel. The opinion letter will later state that it may be relied on by its addressees only. So, addressees who have an interest in the aircraft and lease, in addition to the lessor, should be included in order for such parties to receive the full benefit of the opinion.

To Whom May the Opinion Be Disclosed?

A question, related to that of permitted addressees, is to whom may the opinion letter be disclosed by the addressees. The opinion will likely state that it is confidential and may be relied on only by its named addressees. Counsel will normally resist including as addressees "the Lenders from time to time" or other general terms meant to pick up transferees of the addressees. So, the opinion should also state that it may be disclosed to (but not relied on by) actual and potential transferees of the addressees and their finance parties, and to counsel and other advisers of the addressees and such other parties. Only the addressees may potentially have a claim against counsel for professional negligence, if the advice in the opinion violates professional standards. But transactional counsel and other advisers to the addressees will need to see the opinion to properly advise their clients. Similarly, actual and potential transferees and their finance parties, and the counsel and other advisers to each of them, will wish to see the opinion as part of their due diligence on whether adequate steps have been taken to protect the interests of the lessor in the aircraft and the lease.

Documents Examined and Searches Made

The opinion letter should recite that counsel has examined every document (including results of searches of public registries) that is relevant to the giving of the opinion letter, including the following (originals or copies of which – other than the "such other documents" described below – would also be provided to the lessor):

- Lease. The lease (or, in the case of a purchase of an aircraft subject to a lease, the lease novation).
- Acceptance Certificate. The delivery acceptance certificate or lease supplement by which the lessee accepts delivery of the aircraft (or, in the case of a purchase of an aircraft subject to a lease, the effective time certificate that memorializes the date and time the existing lessor transfers the lease to the new lessor).
- Guarantee. Any guarantee of the obligations of the lessee under the lease and other transaction documents issued by the lessee's parent company (together with the lessee, the Opinion Parties). It is assumed that the lessee and the guarantor are organized under the laws of the same jurisdiction. If that is not the case, the guarantor will have to be the subject of a separate opinion issued by counsel in the guarantor's jurisdiction.
- Other Transaction Documents. Each other "Transaction Document" or "Operative Document" (as such terms are defined in the lease), listed by name, to be signed by an Opinion Party. (Typically, the Opinion Parties are the lessee and any parent entity providing a guarantee of the lessee's obligations under the lease and related documents.)
- Organizational Documents. The certificate of organization, by-laws, memorandum and articles of association, or similar organizational documents, as amended, of each Opinion Party.
- Board Resolutions. The resolutions of the board of directors, supervisory board, or similar body, of each Opinion Party directing such Opinion Party to enter into and perform the Transaction Documents to which it is a party.
- Consents. Any consent, authorization or approval required to be issued by a government authority, other creditor or other third party for an Opinion Party to execute, deliver and perform its obligations under the Transaction Documents.

- International Registry Priority Search Certificates. Recent priority search certificates issued by the International Registry (established under the Convention on International Interests in Mobile Equipment and the Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment (Cape Town Convention)) for the airframe and each of its engines. Sometimes, however, registrations at the International Registry will be handled by separate counsel, who may not necessarily be in the same jurisdiction as counsel giving the opinion discussed herein. In such an event, the priority search certificates will be examined and opined on only by such other counsel.
- Civil Aircraft Registry Search Results. Results of a recent search conducted by counsel with respect to the aircraft at the civil aircraft registry and any other applicable companies or charges (i.e., security interest) registry in the lessee's home country, including the current certificate of registration for the aircraft.
- Certificate of Airworthiness. The existing certificate of airworthiness for the aircraft.
- Proof of Valid Importation. If the aircraft has already been imported into the lessee's home jurisdiction, the documents showing the valid importation, including payment of or exemption from import value-added tax (VAT).
- Authorizations to Operate as Air Carrier. The lessee's air operator certificate, air transport license, or any similar documents evidencing the authority of the lessee to operate as an airline.
- Other Documents. Such other documents (that do not have to be listed), if any, that counsel has determined are necessary to give its opinions.

Opinions Given

A complete opinion letter (or opinion letters in combination) should include the following:

- Organization. Each Opinion Party is duly organized, validly existing and (if the concept exists in the Opinion Party's jurisdiction) in good standing.
- Air Carrier. The lessee is a licensed air carrier.
- No Bankruptcy. According to the search by counsel of the companies registry, each Opinion Party has not initiated a bankruptcy, insolvency or related proceeding.
- Power and Authority. Each Opinion Party has the power and authority, and has taken all necessary organizational action, to execute, deliver and perform the Transaction Documents to which it is a party.
- Transactional Documents Do Not Violate Law, Organizational Documents or Other Agreements. The execution, delivery and performance of the Transaction Documents to which it is a party will not violate the Opinion Party's organizational documents or any law or contract (to counsel's knowledge) to which such Opinion Party is bound. The last opinion carries more weight if issued by internal counsel to the Opinion Party, who is closer to the contracts of the Opinion Party.
- Enforceability. The Transaction Documents, to which each Opinion Party is a party, constitute its legal, valid and binding obligations, insofar as the law of the jurisdiction of the Opinion Party is concerned. What this means is that the Transaction Documents do not violate the public policy of that jurisdiction.
- Registrations Necessary. It is not necessary in order to ensure the priority, legality, validity, enforceability or admissibility into evidence of the Transaction Documents that any Transaction Document or a memorandum or other evidence, thereof, be filed, registered or recorded in any public office in the jurisdiction or on the International Registry, except for filings specified in the opinion. Such registrations often include applying to record the interest of the lessor as such on the aircraft certificate of registration, registering a deregistration power of attorney with the civil aircraft registry, and (if applicable) registering an Irrevocable Deregistration and Export Request Authorization (IDERA) (as discussed below) with the civil aircraft registry and having the civil aircraft registry countersign it.

- Deregistration Power of Attorney. The deregistration power of attorney signed by the lessee (and drafted under the lessee's local law) is effective to authorize the person granted the authority therein (usually the lessor but may be a security trustee on behalf of a lender or lenders) to perform the functions granted to the attorney therein (such as to cause the aircraft to be deregistered if a lease event of default occurs), is not revocable by the lessee (if that is the case under local law), and will not be revoked or otherwise rendered ineffective by the filing of a bankruptcy petition by or against the lessee (if that is the case).
- IDERA. If the lessee's jurisdiction is a signatory to the Cape Town Convention, the IDERA to be provided in favor of the lessor or security trustee under the Cape Town Convention is effective in the lessee's jurisdiction.
- Enforcement by Security Trustee. For a financed aircraft, the financing agreements often require that the opinion state whether the security trustee under such agreements may, as security assignee of the lessor, exercise remedies under the lease against the lessee and, if so, whether that requires that the security trust agreement or a local law mortgage or another instrument be filed in any office. Often, the ability of the security trustee to take enforcement action will require that the security trustee be named as the attorney in the deregistration power of attorney and IDERA. The recording of a mortgage in the lessee's home jurisdiction often is not commercially practical because doing so would require payment of a large stamp duty (as discussed below).
- Choice of Law. The choice of law set forth in the Transaction Documents (typically New York or English) will be upheld by the courts of the Opinion Party's jurisdiction. Each Transaction Document is in proper legal form for enforcement in that jurisdiction.
- Choice of Jurisdiction. The consent of each Opinion Party to the jurisdiction of New York or English courts, set forth in the Transaction Documents, is valid.
- Enforcement of Judgment. Any final judgment of a competent court obtained by the Lessor against an Opinion Party in a New York or English court (assuming minimum due process, such as notice to the Opinion Party and opportunity to be heard) will be enforced in the courts of the Opinion Party's jurisdiction.
- No Sovereign Immunity. No Opinion Party (or its assets) is subject to sovereign immunity – i.e., immunity as a government entity – in any action to enforce the Transaction Documents.
- Ranking of Obligations. The obligations of each Opinion Party under the Transaction Documents rank at least *pari passu* with (i.e., would not be subordinated to) all other unsecured unsubordinated obligations of such Opinion Party.
- Recording Taxes. No stamp duties, transfer taxes or other documentary taxes are payable with respect to the signature, performance, registration or enforcement of the Transaction Documents, or if there are any, they are nominal. In the case of a finance lease, or a leveraged operating lease, the finance lessor or lender may be permitted under the rules of the civil aircraft registry to file a mortgage on the aircraft with that registry. However, in many jurisdictions, this would be commercially impractical because filing a mortgage requires payment of a stamp tax that is a non-nominal percentage of the amount secured (either the principal portion of the present value of the finance lease payments or the principal of the secured loan).
- Other Tax Opinions. Counsel may be able to opine that payments of rent and other amounts by the Opinion Parties under the lease and other Transaction Documents may be made free of withholding tax imposed by the Opinion Party's jurisdiction, particularly if, as a matter of local law (rather than bilateral tax treaty), cross-border rent payments are not subject to withholding. Counsel may also be able to opine whether lease rent and other payments are subject to VAT or similar tax. In a sale-leaseback, counsel may be asked to opine that the transfer of title to the aircraft at closing, while the aircraft is on the ground in the jurisdiction or while it is registered in the jurisdiction, will not attract VAT or other transfer tax. Finally, if the transaction involves the contribution of the shares of the lessor to another entity, counsel may be asked to opine that such contribution does not attract VAT or similar transfer tax. However, frequently the tax advice comes from lessor's separate tax advisor, often the local office of a Big Four accounting firm.

- No Place of Business. Neither the lessor nor any other addressee of the opinion is required to establish a place of business in the Opinion Party's jurisdiction or be licensed or qualified to do business in such jurisdiction in order to exercise or enforce any rights under the Transaction Documents.
- No Trade or Business. The lessor will not be deemed to be carrying on a trade or business in the Opinion Party's jurisdiction solely by virtue of entering into the Transaction Documents (meaning that the leasing of the aircraft will not subject the lessor to income taxation in the jurisdiction).
- Usury. The payment provisions of the Transaction Documents, including the provisions on overdue or default interest, do not violate laws of the Opinion Party's jurisdiction on the maximum amount of interest that may be charged.
- Execution Formalities. No Transaction Document need be notarized, legalized, apostilled or consularized, or signed in original counterparts, as a condition of its legality, validity, filing, enforceability, or admissibility in evidence in the Opinion Party's jurisdiction, except as stated here in the opinion.
- No Violation of Law. No addressee of the opinion will violate any law of the Opinion Party's jurisdiction by reason of entering into and performing its obligations under the Transaction Documents.
- No Strict Liability to Third Parties. No addressee of the opinion will have strict liability for any damage or injury arising out of a defect in the aircraft or the registration, ownership, operation, leasing, possession, use or maintenance of the aircraft by reason of entering into and performing its obligations under the Transaction Documents.
- No Detention of Aircraft. The aircraft may not be detained or forfeited except for circumstances listed here in the opinion, such as nonpayment of VAT or navigational charges, requisition, or use of the aircraft for an illicit purpose.
- Exchange Control Authority. Each Opinion Party has obtained permission from the exchange control authority, if applicable, to allow such Opinion Party to make payments under the Transaction Documents in US dollars (or any other currency specified in the Transaction Documents).
- Insolvency/Bankruptcy. Counsel should describe the statute under which an Opinion Party may become a voluntary or involuntary debtor in a bankruptcy, insolvency or related proceeding and, if so, whether an automatic stay would generally apply to prevent enforcement action against the Opinion Party as debtor under such law.
- No Recorded Liens. Confirm that counsel's search has determined that there are no liens recorded against the aircraft on the civil aircraft registry or any other public registry in the jurisdiction at which such a lien may properly be registered.
- Cape Town Jurisdiction. State whether the lessee's jurisdiction is a signatory to the Cape Town Convention. If it is, confirm that such jurisdiction has enacted legislation to implement the Cape Town Convention.
- Cape Town Declarations. State which declarations the jurisdiction has made under, and as contemplated by, the Cape Town Convention. For example, the jurisdiction may have elected to apply Alternative A of Article XI of the Protocol and specifying a waiting period of 30 days. In such event, the lessor could repossess an aircraft from a lessee 30 days after the lessee had filed for bankruptcy or insolvency protection, notwithstanding the automatic stay that may apply in such proceeding.
- Lessee Cape Town Status. If the lessee's jurisdiction is a signatory to the Cape Town Convention, confirm that the lessee has registered as a Transacting User Entity on the International Registry and that such registration has not lapsed or otherwise terminated.
- Cape Town Registrations. Unless there is separate International Registry counsel to effect the registrations, counsel should opine that it has made such registrations and attach the new Priority Search Certificates showing such registrations. This may present a timing issue. The Cape Town registrations are normally done

immediately following closing. If the opinion must be issued upon closing, the Cape Town registrations can be covered in a supplemental opinion or confirmation letter.

- Civil Aircraft Registry Registrations. Counsel should opine that it has filed or confirmed filing by the lessee of the applicable documents, which may include the lease or a memorandum thereof, the deregistration power of attorney and the IDERA. If these filings are not to occur until after the opinion is issued at closing, the confirmation may come by a supplemental opinion or confirmation letter.

CONTACTS

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