

CLIENT UPDATE

AIRCRAFT REPOSSESSION IN RUSSIA

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Until the emergence of the global financial crisis in 2008, the Russian airline industry was growing at a fast pace, with several new regional and low-cost airlines entering the market and expanding their fleets, primarily through operating leasing. Until that time, aircraft repossession remained largely a theoretical topic hardly tested in courts and the rare cases of repossession typically involved a substantial amount of lessee cooperation. The global financial crisis dealt a significant blow to the Russian airline industry, with only the strongest and most efficient airlines surviving. More than a dozen regional and low-cost airlines went bankrupt or were taken over by larger airlines. This process was accompanied by numerous cases of aircraft repossessions, including through court proceedings. Today, the Russian airline industry is stronger and repossession procedures are better defined.

GENERAL LEGAL FRAMEWORK

The current Russian legislation generally allows for aircraft repossession and re-export from Russia. Although the legal position of the lessor is very strong following valid termination of the lease, significant obstacles still remain in the course of retaking possession of the aircraft. As a practical matter, cooperation of the Russian lessee may still be required.

The repossession of an aircraft from a Russian lessee generally involves physical repossession of the aircraft, its de-registration and customs clearance and obtaining a flight permission for a ferry flight outside Russia.

REPOSSESSION WITHOUT RECOURSE TO COURTS OR ARBITRATION

If the lessor can gain unrestricted access to the aircraft, it may repossess the aircraft without recourse to courts or arbitration. As an example, a lessor was able to repossess an aircraft from a Russian airline when the aircraft was undergoing scheduled maintenance outside of Russia. If the aircraft is located in Russia, then the lessor may face difficulties getting access to the aircraft, unless the airline, its employees or airport authorities are willing to provide cooperation. Any self-help remedies that involve use of force, violence or other extraordinary measures may expose the lessor to the risk of being accused of abuse of its rights, which could result in administrative or even criminal liability.

REPOSSESSION VIA COURTS OR ARBITRATION

If the lessee is unwilling to surrender the possession of the aircraft and is not willing to cooperate, the lessor will have to apply to a relevant court or international arbitration. The strategy for repossession should also take into account the dispute resolution clause of the aircraft lease.

If the lease contains a valid arbitration clause, the lessor may seek an arbitral award for the aircraft's return. If an arbitral award is rendered by a foreign tribunal, it should generally be recognized and enforced by Russian courts since Russia is a party to the 1958 New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards.

A foreign court judgment, on the other hand, will not be enforceable in Russia unless the relevant court decision is adopted by a court in a country that has an agreement on the mutual recognition of court decisions with Russia (and Russia has no such agreements with US, UK and most Western European countries).

If the aircraft is registered in the Russian State Registry of Civil Aircraft (the "Aircraft Registry"), a Russian court may refuse to recognize a dispute resolution clause providing for recourse to foreign courts or foreign arbitration as aircraft are considered immovable property and all disputes regarding the rights to Russian immovables are subject to exclusive jurisdiction of the Russian commercial (arbitrazh) courts.

If the lease contains no valid arbitration clause, or a Russian court assumes jurisdiction over the lease as set out above, the enforcement of the lessor's rights under the lease will be

within the jurisdiction of Russian courts. The lessor may also consider applying to the Russian courts if it does not want to wait for a final arbitration award. Before filing a claim on the merits of the case with a Russian court, the lessor may seek protective interim measures (for example, grounding of the aircraft), which can be granted fairly quickly. But the court may demand counter-security from the claimant. Protective measures may also be sought after the commencement of a court action or during the enforcement of a court judgment.

A final Russian court judgment or a decision on the recognition and enforcement of an arbitral award on the repossession will be enforced by a special service of Russian court marshals. The marshals are authorized to take a variety of actions, including arrest, removal and repossession of an aircraft. Individuals refusing to comply with a court judgment or preventing its enforcement by the marshals run the risk of criminal liability. Yet, there is a very limited practice of enforcement of court judgments on aircraft repossession by the marshals in Russia.

AIRCRAFT DE-REGISTRATION AND IDERA

Civil commercial aircraft operated by Russian airlines must be registered in the Aircraft Registry or in an aircraft register of another jurisdiction with which Russia has entered into an agreement on maintenance of airworthiness. In the latter case, de-registration will be governed by the laws of such foreign jurisdiction.

Russia maintains a dual registry system, and since September 17, 2009, change of title to and encumbrances over a civil aircraft registered in the Aircraft Registry must be registered in the Russian Unified State Registry of Interests in Aircraft and Transactions Therewith (the "Title Registry"). The Federal Agency on Air Transport ("Rosaviatsiya") keeps the Aircraft Registry and the Title Registry.

Normally, only mortgages and finance leases are entered as encumbrances in the Title Registry and require discharge upon termination of the lease. Upon termination of the lease, the lessor as a titleholder may apply to Rosaviatsiya for removal of the aircraft from the Aircraft Registry and the discharge of the encumbrances over the aircraft, if any, from the Title Registry.

The good news for foreign lessors and creditors is that Russia has recently acceded to the provisions of the Protocol to the 2001 Cape Town Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment relating to the Irrevocable De-Registration and Export Request Authorization (IDERA). This new commitment is expected to enter into force on August 1, 2013.

IDERA should support the lessors and creditors in the de-registration, export and physical transfer of aircraft from Russia. Rosaviatsiya and other relevant governmental authorities will have to co-operate with IDERA holders. But implementation procedures for IDERA have not yet been issued.

In addition, starting from September 1, 2013, Russian legislation will permit irrevocable powers of attorney which may be issued for an unlimited period of time. But such powers of attorney may not provide delegation and will require notarization.

CUSTOMS CLEARANCE

Removal of an aircraft from Russia requires its customs clearance. As a general rule, a lessor may not apply for the customs clearance of the aircraft in its own name and will need the lessee to cooperate. If the lessee refuses to cooperate, the lessor may be unable to complete customs clearance without a court order.

If at re-export of the aircraft there appear to be outstanding customs payments with respect to the aircraft, the lessor may be required to settle them. It may become even more difficult if it turns out that the lessee has committed any customs offences, including failure to comply with the declared customs procedure, or otherwise breached the customs legislation. Such offences may result in grounding and confiscation of the aircraft. The lessor therefore should monitor the lessee's compliance with Russian customs regulations, including due payment of any applicable customs duties, fees and import VAT.

The lessee's unwillingness to assist in customs clearance may be cured by obtaining a court order for specific performance. A power of attorney given by the lessee at the start of the lease may also be helpful, although there is no assurance that customs authorities will fully recognize such delegation of rights by lessee to lessor.

FLIGHT PERMISSIONS

Ferrying the aircraft from Russia requires a flight permission from Rosaviatsiya to be obtained by the aircraft operator. Such permission is subject to discretion of Rosaviatsiya and may lead to additional delays.

CONCLUSION

Although the Russian airline industry is financially stronger following consolidation during the last five years and the legislature framework is more developed, lessors may still face a number of challenges in the course of repossession: regardless of the dispute

clause in the lease agreement, the lessor may have to apply to the Russian courts to get access to the aircraft; repossession without recourse to courts or arbitration may be unsuccessful and self-help may result in liability if not exercised cautiously; the lessor may be unable to clear the aircraft through customs without the cooperation of the lessee and may be required to discharge any outstanding customs payments; and repossessions are still uncommon and may pose unexpected practical difficulties.

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Please do not hesitate to contact us with any questions.

July 10, 2013