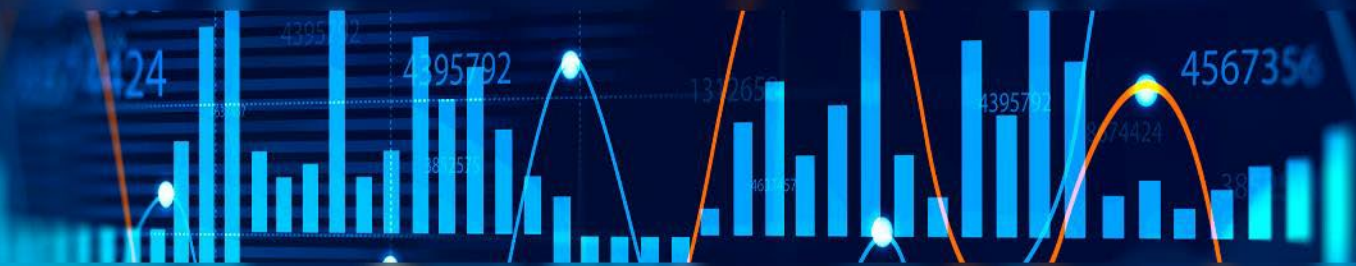


C L I F F O R D
C H A N C E



FUNDAMENTALS OF FINANCIAL MARKETS
SINGAPORE | TUESDAY, 3 SEPTEMBER 2024

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INTRODUCTION TO ASSET FINANCE

NATTAWAT VILASDECHANON

SINGAPORE | TUESDAY, 3 SEPTEMBER 2024

INTRODUCTION

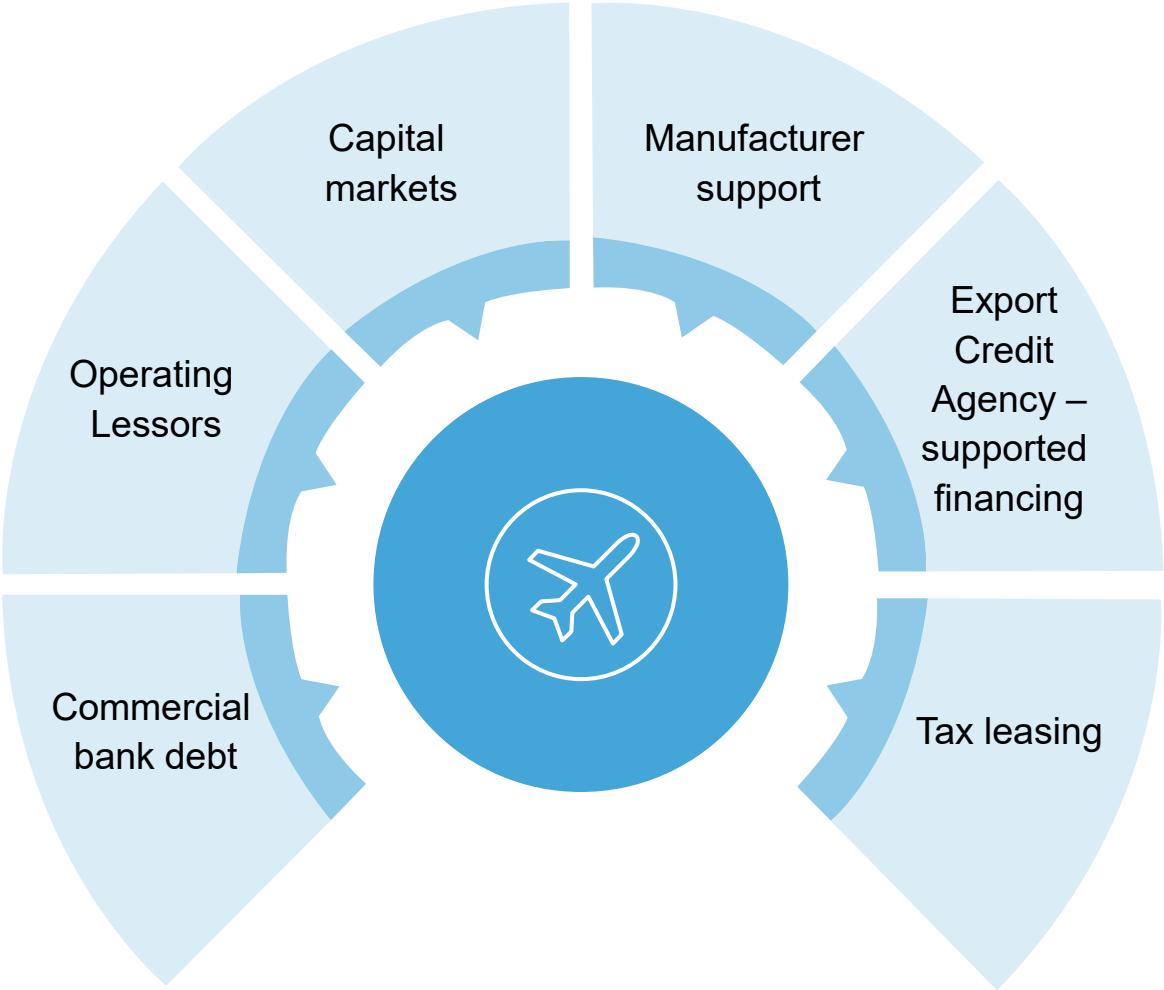
General Features

- Specialised market.
- “Big ticket” leasing (>US\$30-50m asset value).
- Capital intensive (high value, long order times, long life assets).
- Real economy, market sensitivities.
- Complicated structures.
- Asset as security, movables.
- Income-generating assets, cash flows.
- Cross-border, multi-jurisdictional.

Typical work

- New orders.
- Acquisitions.
- Sale & leasebacks.
- Secondary market trading (transfers and portfolios).
- Related M&A activity.
- Restructurings and work-outs.
- Dispute resolution.
- Securitisations, capital markets financings, receivables financing, structured finance, project/PFI financing, infrastructure financing.

PRINCIPAL SOURCES OF AIRCRAFT FINANCE



AIRCRAFT

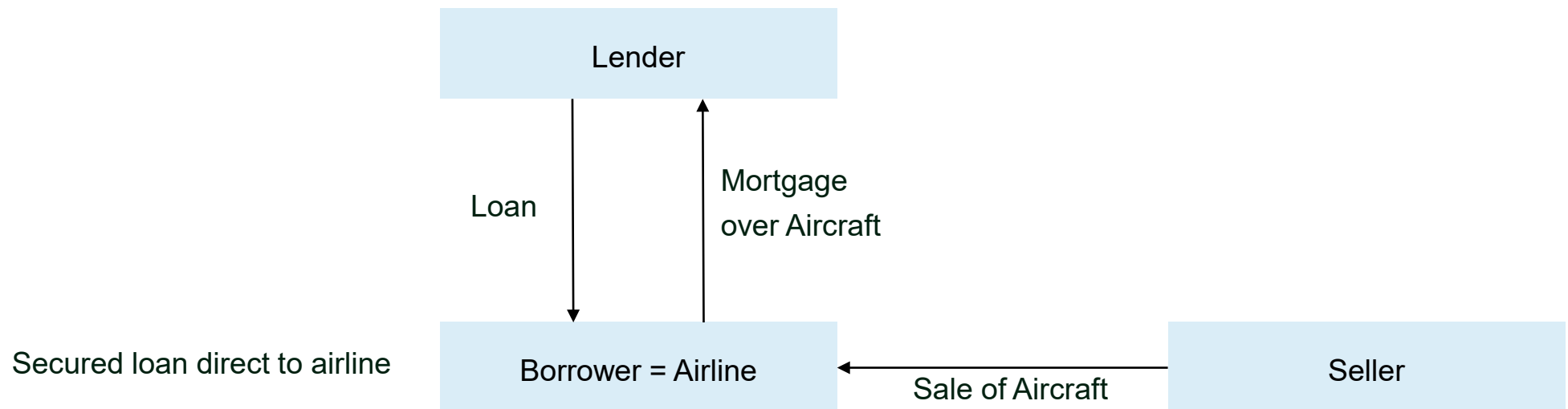


- Commercial passenger aircraft
 - “Large Aircraft”, regional, narrow bodies, wide bodies, corporate/business jets
 - Helicopters.
- Cargo/freighter aircraft (conversions)
- Engines (in particular for wide bodies)
- Military aircraft
 - e.g. FSTA, Eurocopter, MFTS (training).
- Manufacturers
 - e.g. Boeing, Airbus, Bombardier, Embraer, ATR.

COMMERCIAL DEBT FINANCING OF AIRCRAFT

“Base case” – assume an airline is seeking financing for purchase of an aircraft from (bank) lender

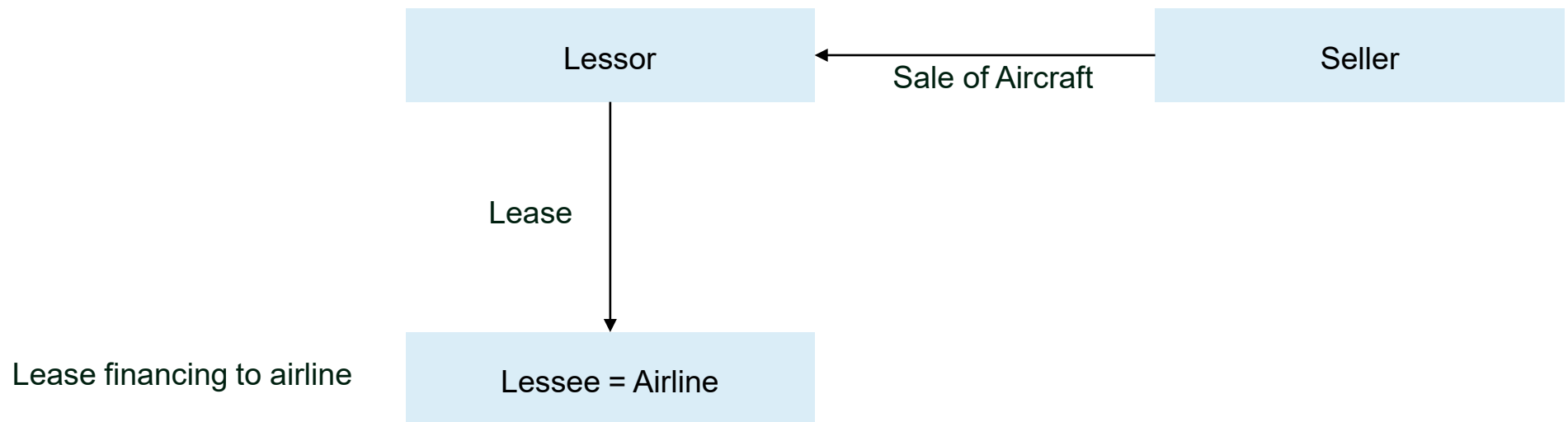
Lender requires security for repayment of loan



LEASE AS SECURED FINANCING DEVICE

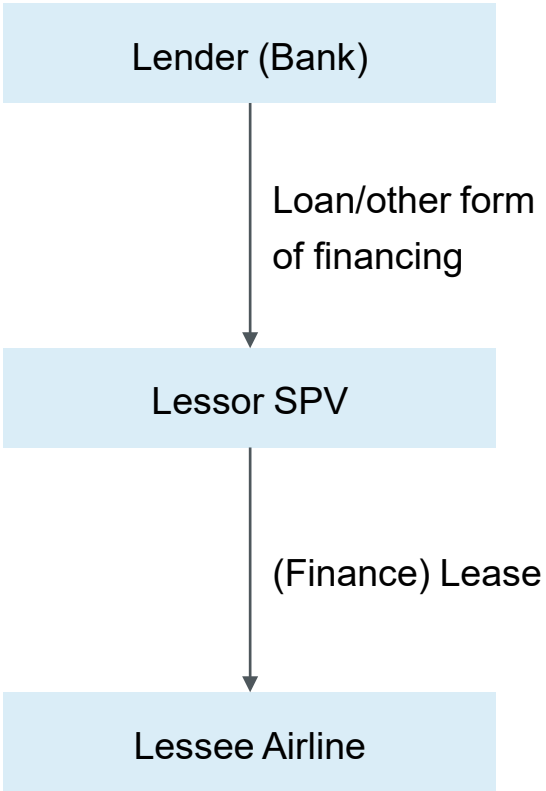
Bankruptcy-remoteness and “ring-fencing” of asset

“Ownership as security” concept

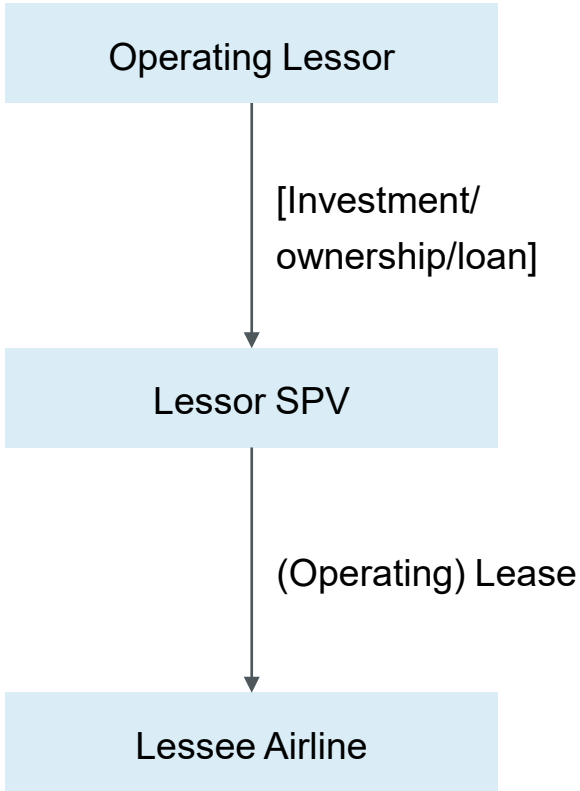


USE OF LESSOR SPVS IN AIRCRAFT LEASE FINANCING STRUCTURES

Example – commercial debt financing



Example – Operating Lease



In both examples, Lessor SPV is owner of aircraft, borrower under financing and provides aircraft to airline operator under lease

SPCS – REASONS FOR USE

Bankruptcy Risk

SPC is owner of asset, lender lends into SPC as borrower under the loan and not direct to the operator

Security

SPC grants security over asset, lease rentals, insurances and rights to lender; lender also has security over SPC itself = control

Tax

exclusion or mitigation of any withholding taxes on lease rentals, loan payments, deposit payments or other amounts

Asset registration

e.g. aircraft nationality registers

Cash Flows

e.g. separation of loan cash flows

Accounting

e.g. non-consolidation requirements

Liability re. Ownership

separates financiers from owner and operator of asset

Enforcement and Transferability

Enforcement through SPC as owner. Possible to transfer/trade aircraft by selling SPC Shares.

SPCS – KEY FEATURES

Special purpose, bankruptcy-remote:

Newly set-up, no other business (“clean”) (so no other creditors likely), separate legal entity

Limited recourse borrowing – also links to solvency of SPC

SPC can give security e.g. aircraft mortgage – “ring-fencing” of asset

May be backed by leasing company or another transaction party, depending on deal

May be special purpose trust (e.g. statutory trust) or another special purpose vehicle

Tax neutral jurisdiction, favourable jurisdiction for creation, registration and enforcement of security and possibly for asset registration (e.g. owner registers)

N.B. a transaction may be structured with multiple SPCs – e.g. one SPC per aircraft financed/leased; e.g. head-lease and sub-lease structures/chains

SPCS – SECURITY

Security over SPC and other control rights

Share charge

SPC covenants in documentation

No other business

No prejudice to asset and other collateral

No liens over asset

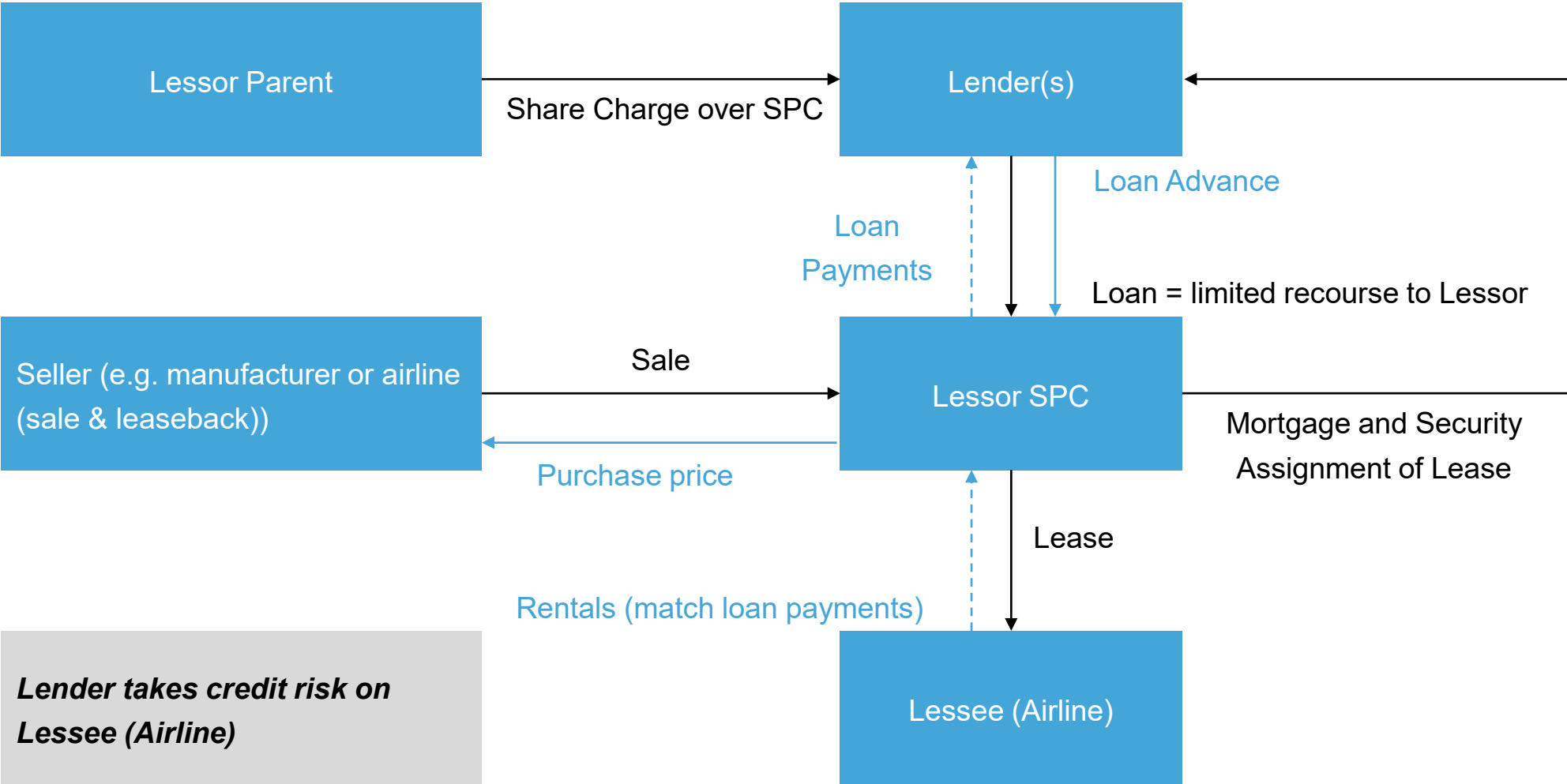
No change to constitution

Independent directors or professional trustees; constitutional documents/trust terms; resignation letters

Direct cash flows or charges over SPC accounts

Legal opinion

EXAMPLE COMMERCIAL DEBT FINANCING



FINANCE LEASE VS. OPERATING LEASE

Accounting term

Finance lease = substantially all risks and rewards of asset ownership transferred from lessor to lessee, whether or not legal title transfers (on balance sheet of Lessee)

Operating lease = any lease other than a finance lease (historically off balance sheet but IFRS 16 has changed that)

Economic/commercial term:

Finance lease = full payout of lessor's investment (plus interest) – no equipment risk

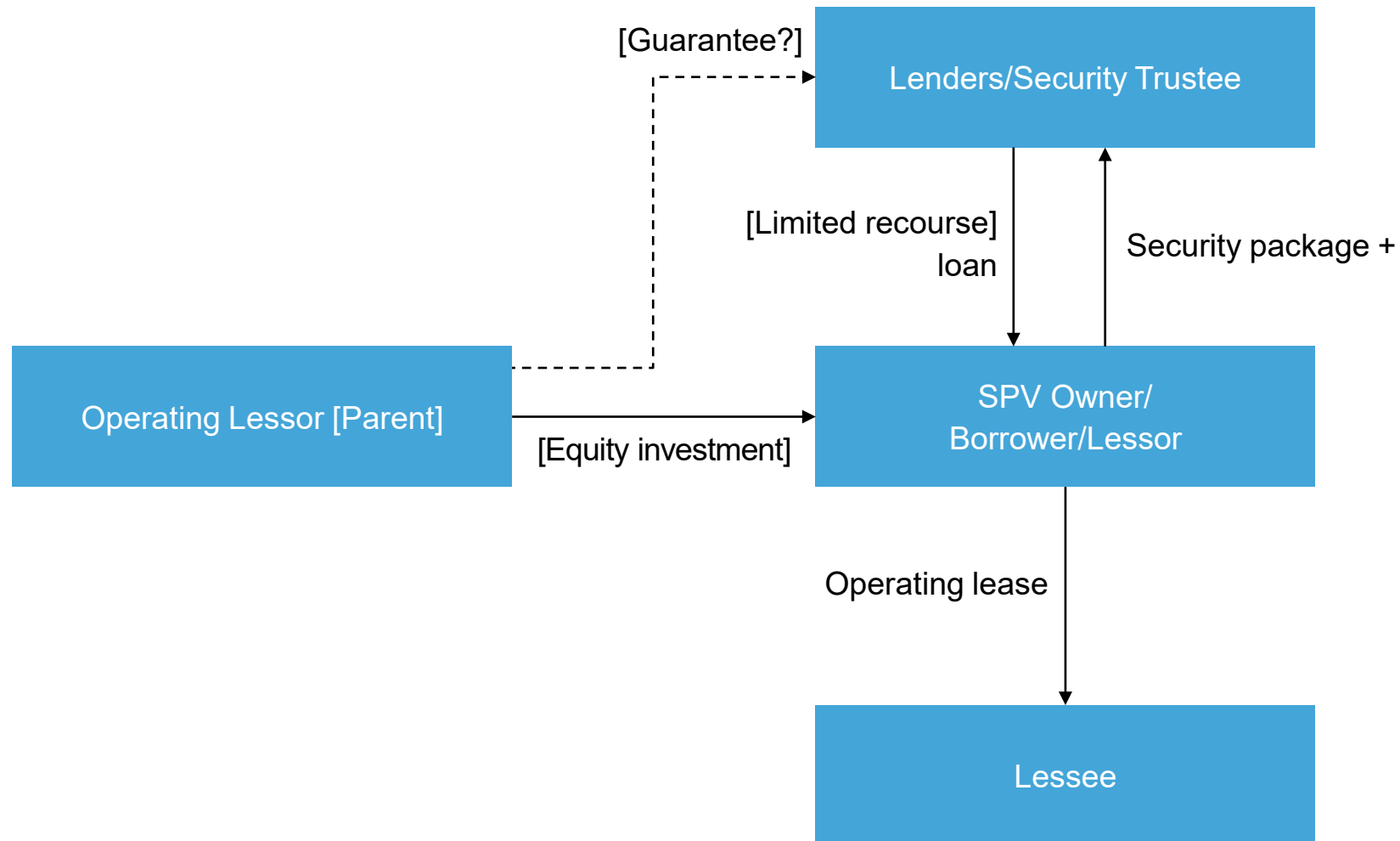
Operating lease = rentals will pay portion of lessor's investment – remainder will come from residual value

FINANCE LEASE VS. OPERATING LEASE

(CONTINUED)

Operating Lease Indicators	Finance Lease Indicators
Shorter term (use agreement), may have several lessees during useful life of asset	Longer term (useful life of asset)
Rentals plus residual (lessee may terminate w/o full payout liability), payment for usage, rentals usually fixed	Full payout rentals (loan amortisation) – not linked to usage, termination value payments , rentals may be adjustable
Lessor’s focus on maintenance, insurance & operational provisions, sometimes lessor shares responsibility for maintenance, insurance & property taxes – security deposits, maintenance reserves, cost sharing	Triple net lease (maintenance, insurance & property taxes), less restrictions on operational provisions, operational and tax indemnities
Risks of ownership with lessor	Lessee takes risk of loss, destruction & obsolescence
Return usually – with specific return conditions Lessor takes upside (residual position)	May include fixed/nominal purchase option or sales rebate procedure (remarketing) or even automatic title transfer (full pay-out concept). Plus less restrictive/detailed return conditions.

SINGLE AIRCRAFT OPERATING LEASE FINANCING



COLLATERAL PACKAGE

Start with the (bankruptcy-remote) SPV
borrower/owner/lessor

English law – types of “true” security interest (possessory
and non-possessory)

- Asset (i.e. aircraft) → mortgage or other security interest (incl. local law security).
- Lease → Assignment (by way of security) of rentals, rights and interests, requisition proceeds.
- Cash → Account Charge/Assignment/Control Agreement.
- Servicing Agreement.
- SPC → Share Charge (or Pledge); or trust documents, if special purpose trust.
- Warranties (and proceeds) – manufacturer’s – e.g. airframe and engines.
 - Security Assignment; or.
 - Manufacturer Agreement (more common).

Aviation Insurances

- AVN67B – Contracts and Contract Parties endorsement.
- Insurable interest.
- Loss Payee concept.
- Hull and liability insurances.
- Security interest pursuant to assignment of insurances/reinsurances (depending on airline).
- Reinsurance cut-through clause.

PLEASE GET IN TOUCH AND CONTINUE THE CONVERSATION



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