

GUIDELINES ON REMEDIES IN STRUCTURED FINANCINGS WITH SHARED SECURITY

REVISION DATE: 14 October 2022

A. This document comprises a set of guidelines (the **guidelines**, and, each, a **guideline**) which the Aviation Working Group (**AWG**) recommends in order to provide greater predictability for financiers and investors in situations where multiple classes of debt share in a single security interest over aircraft equipment and related collateral (**aircraft collateral**) and remedies are being exercised. This statement of guidelines has been prepared by AWG as an elective guidance tool.¹

B. Where this document is referred to, including in correspondence or legal documentation, such reference should be to the **AWG guidelines on remedies in structured financings with shared security, revised 14 October 2022**, or, in short the **AWG remedies guidelines, rev. 14.10.22**. If this document is amended, an updated reference will be included.

C. In this document, references to an **intercreditor agreement** refer to an agreement among all classes (or representatives of all classes) of debt that share in a single security interest over aircraft collateral, references to **junior creditors** refer to all creditors that are not in control of the exercise of remedies, and references to the **UCC** refer to the Uniform Commercial Code as in effect in the State of New York. While aspects of these guidelines have broader application, the underlying legal analysis for purposes of the development of these guidelines is on the UCC.

D. The guidelines are as follows:

Guidelines relating to commercially reasonable remedies

Guideline 1: expressly require that all remedial action, including, without limitation, foreclosure sales and the compromise or sale of any deficiency claims or other derivative rights, must be commercially reasonable

The intercreditor agreement should expressly provide that any foreclosure sales of aircraft collateral and other remedial action must be commercially reasonable under applicable law, including under the UCC, and, to the extent applicable, under the Cape Town Convention.

Purpose and rationale: The UCC requires that all aspects of a foreclosure sale be commercially reasonable, however, the UCC does not provide specific relief for junior creditors that share in a single security interest if a sale does not comply with these requirements. Many intercreditor agreements have included express provisions requiring re-leases of aircraft as part of the exercise of remedies to be commercially reasonable, but have been silent on foreclosure sales. Including an express agreement to such effect in a contract provides junior creditors with rights to enforce such an obligation on the party controlling the exercise of remedies through the contract even if junior creditors may not have express rights under applicable law.

Once aircraft collateral is sold, any deficiency claim is for the benefit of the creditors of all classes remaining unpaid. The party in control of remedies should not be permitted to compromise, sell or dispose of such claims – or take any other remedial action binding on all classes – except in a commercially reasonable manner. As the UCC does not directly address this point, it should be a contractual undertaking

Guideline 2: expressly provide that any or all of the aircraft collateral may be sold

The intercreditor agreement should expressly state that any or all aircraft may be sold in the exercise of remedies.

Purpose and rationale: The UCC does not require or preclude that all aircraft collateral be sold as a group. Many intercreditor agreements include ambiguous requirements to sell "all" of certain types of collateral, but the intention is that "all" means "all or part". That should be made express. Therefore, it should be made clear that any or all aircraft may be sold in one or more sales and that all aspects of such sales must be commercially reasonable. This would provide junior creditors with contractual rights which mirror the UCC and would provide them with a basis for enforcing such rights contractually even if they may not have express rights under applicable law.

¹ This document is not intended to, and should not be construed as, representing the policies, positions or views of, nor an agreement among or binding upon, the Aviation Working Group's members, or any of them, either as a general matter or with regard to any specific circumstance.

Guideline 3: require certification that all remedial action complies with applicable law and the transaction documents

The intercreditor agreement should require the controlling party to certify for the benefit of representatives of all classes that any remedial action complies with applicable law and the transaction documents. The controlling party is the group (normally majority of the most senior class of debt) that directs the trustee after a default.

Purpose and rationale: Such a certification would require the party controlling the remedies process to make a determination that a proposed action is commercially reasonable, thus increasing the likelihood that it would not be the subject of a dispute. Many transactions have requirements that a trustee makes a determination that any requested action complies with applicable law, but require no certification. A certification undertaking would enhance transparency and strengthen the underlying remedial provisions.

Guidelines relating to enforcement of rights

Guideline 4: expressly provide junior creditors with a contractual right to challenge

The intercreditor agreement should expressly provide the representatives of junior creditors with the right to challenge any actions of a controlling party that do not comply with the requirements of applicable law.

Purpose and rationale: As the UCC does not provide relief for, or the right of challenge by, junior creditors that share in a single security interest if a sale does not comply with commercial reasonable requirements, such relief and right of challenge should be added by contract.

Guideline 5: expressly provide for an agreement on irreparable harm

The intercreditor agreement should expressly state that the parties agree that the junior creditors will suffer irreparable harm if a foreclosure sale is not conducted in a commercially reasonable manner.

Purpose and rationale: This would give junior creditors the right to seek an injunction without having to prove whether they are irreparably harmed by virtue of the sale proceeding. If coupled with an express right in favor of junior creditors to enforce commercial reasonableness standards prior to a proposed sale, this clause could help junior creditors to obtain a temporary restraining order if there were to be an unreasonable sale proposed.

Guidelines relating to specific aspects of foreclosure sales

The intercreditor agreement should specify features which constitute a commercially reasonable foreclosure sale and in so doing, decrease the likelihood of disputes arising over foreclosure sales.

Guideline 6: prohibit breakup fees as a feature of a commercially reasonable foreclosure sale

No fees should be payable to a party that merely provides a minimum bid in a foreclosure sale (**breakup fee**). All amounts paid by any bidder in a foreclosure sale should go through the application of proceeds "waterfall" in the intercreditor agreement.

Purpose and rationale: The presence of a breakup fee payable to a minimum bidder is prejudicial to a commercially reasonable sale (and a commercially reasonable bidding process), and, consequently, is likely to result in lower bids for aircraft collateral thus harming junior creditors (and potentially the debtor). All proceeds of any foreclosure sale should be applied in accordance with the terms of the intercreditor agreement and should not go directly to third parties, which should be an express requirement of a commercially reasonable sale. Requiring funds to be so applied will maximize proceeds of aircraft collateral for the benefit of all creditors and reduce the chances of disputes arising over commercial reasonableness.

Guideline 7: prohibit fees to, or other financial benefits in favor of, a controlling party as part of a commercially reasonable foreclosure sale

The payment of any fees to, or other financial benefits in favor of, the party controlling remedies or its affiliates is prejudicial to a commercially reasonable foreclosure sale, and, consequently, is likely to result in lower bids for aircraft collateral, thus harming junior creditors. Junior creditors should not have to prove unjust enrichment in order to stop such a foreclosure sale, which might be the case absent such a provision.

Purpose and rationale: The presence of any fees or other financial benefits in favor of a party that is, or is affiliated with, the party controlling remedies is likely to have an adverse effect on bidding and may result in lower bids for aircraft collateral, which has a disproportionate effect on junior creditors (and potentially the debtor). The party controlling remedies should not be entitled to an economic benefit at the expense of the other parties to the transaction.

Guideline 8: prohibit minimum bids as part of a commercially reasonable foreclosure sale

In any foreclosure sale, a specific minimum bid should not be part of a commercially reasonable bidding process. In a properly conducted public sale under the UCC there should be minimal, if any, barriers to potential competitive bidders. Sophisticated parties will know that senior ranking parties can "credit bid" the amount of their debt and adjust their bids accordingly, without any minimum being set by the party controlling the sale.

Purpose and rationale: The presence of a minimum bid amount is prejudicial to a commercially reasonable sale and, consequently, is likely to result in lower bids for aircraft collateral, thus disproportionately harming junior creditors (and potentially the debtor).

Guideline 9: provide the objectives of, and prevent impediments to, a commercially reasonable foreclosure sale process

The parties should agree on the objectives of a commercially reasonable foreclosure sale process: maximizing the number of bidders and generating the highest bid. As a necessary corollary, the parties should contractually prevent impediments to these objectives, such as requiring potential bidders to post cash deposits prior to an auction or closing in a timeframe that is not customary in the industry.

Purpose and rationale: The UCC takes into account the concept that process impacts results and provides the parties with latitude in defining what constitutes a commercially reasonable foreclosure sale process. Stating the objectives and contractually preventing impediments to such objectives will maximize value for creditors (and for the debtor) and decrease the likelihood of disputes arising over foreclosure sales.

E. AWG may issue revisions to these guidelines and/or supplemental materials to aid in or facilitate its use, interpretation, or application.

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