

**Come Fly with me,
we'll fly,
we'll fly away.....**

AIRCRAFT FINANCING IN NIGERIA CHALLENGES AND PROSPECTS IN A GROWING ECONOMY

INTRODUCTION

One of the major impediments to Nigeria becoming a regional hub for air transportation, is the lack of funding necessary to finance the acquisition or leasing of aircraft fleets. As the country seeks to revive its national carrier, it will no doubt need to acquire a fleet of aircrafts to meet its objective. These acquisitions will be facilitated by various financial institutions both local and international, and they will require guidance on the governing laws and procedures applicable to the Nigerian aviation sector for such transactions.

FORMS OF AIRCRAFT FINANCING

Financing the purchase, or leasing of an aircraft and related assets can take several forms including but not limited to the following:

1. A loan from a bank or other financial institutions secured by a mortgage over the aircraft purchased;
2. The lease of the aircraft involving either an operating lease or a finance lease; and
3. A capital markets transaction through the issuance of bonds or notes secured by a mortgage on the aircraft.

Loans

The most common forms of financing peculiar to the Nigerian aviation sector are secured loans and leases. The secured loan structure involves a lender granting a loan to an airline or leasing company to purchase an aircraft with the loan secured by way of a mortgage or other security interest over the aircraft. With this structure, the ownership of the aircraft resides with the airline (owner) or leasing company and the aircraft is operated either by the airline or it is leased to another party.

Leases

Leasing on the other hand, can take different forms including but not limited to Operating leases; Finance leases; Leveraged leases; and Sale and leaseback arrangements. While differences exist among these various leasing structures, they nevertheless share common characteristics such as, ownership of the aircraft not residing with the airline or leasing company, and upon the expiration of the lease term, the airline or leasing company returns the aircraft to the lessor (though in some circumstances an option and or right to purchase the aircraft is granted). The two most common forms of leases in the Nigerian aviation sector is the operating and finance leases.

Operating Leases

Under an operating lease arrangement, the owner or lessor acquires or owns the aircraft leased to an airline or other lessees and retains substantially all the risks and rewards incident to the ownership of the aircraft. Upon the expiration of the lease term, possession of the aircraft reverts to the owner or lessor and they can either re-lease it or sell it. Operating leases usually comes in two forms namely, "dry lease" or "wet lease". Under a dry Lease, only the aircraft is provided by the owner or lessor with the lessee responsible for operating, maintaining, insuring, and providing the crew for the aircraft. In contrast, with a wet lease, the owner or lessor retains operational control of the aircraft, operates the flights, provides the crew, maintains the aircraft and ensures that it is adequately insured. The cost of providing these services is borne by the lessee under the lease. The wet lease option is typically adopted when the owner or lessor is an airline or a leasing company that has some expertise in operating aircrafts.

The Nigerian Civil Aviation Regulations 2015 ("NCAR") makes ample provisions for dry and wet lease operations. Under the regulations, the borrowing or lending of aircraft between air operation certificate holders requires the prior approval of the Nigerian Civil Aviation Authority ("NCAA") . Further, an air operation certificate holder or applicant cannot dry lease an aircraft only from another air operation certificate holder, without the approval of the NCAA. An applicant may take out a wet lease only where it indisputably proves to the NCAA that a dry lease is not feasible at the time (recourse to the use of a wet lease can only be as a last resort) and such use of a wet lease aircraft shall not exceed six months within a 12-month period.

In a finance or capital lease arrangement, the owner or lessor purchases the aircraft from a manufacturer which it in turn leases to an airline or other lessees. The rental payments from the lease ensures the payment of all or substantially all of the purchase price; with the lessee expected or required to purchase the aircraft at the end of the lease.

Similar to the finance lease is a leveraged lease save that in a leveraged lease, lenders provide the owner or lessor with loans to cover a portion (typically 70% to 85%) of the acquisition cost of the aircraft with the balance provided by the owner. The owner uses the lease payments it receives to repay the loans and its obligations under the loan agreement and the loan is secured by a first priority lien on the aircraft and related assets and receivables from the lease rentals

Sale leaseback transactions involve, an airline selling either a used aircraft or its right to purchase a new aircraft from a manufacturer to either a leasing company or an SPV lessor. The airline then leases the aircraft back from the SPV. Sale leasebacks are often used when an airline desires flexibility to manage its fleet (which shorter-term leases can provide, unlike ownership of the aircraft) or it needs to raise capital.

SECURITY AND REGISTRATION

The legal framework for the aviation sector in Nigeria allows for the creation of a mortgage over an aircraft/engine that is registered in Nigeria. Thus for the creation of a mortgage over an aircraft or its engine, such aircraft and engine must first have been registered in Nigeria. This process is regulated by the Civil Aviation Act, 2006 ("the Act") and the NCAR made pursuant to the Act. The Act established the NCAA as the regulator for the aviation industry, with powers to regulate and monitor the conduct of air navigation, grant licences and air permits, issue safety certificates and register aircrafts. The Act also domesticates other international conventions on aviation which have been ratified by Nigeria and these include but are not limited to: **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, 2001)**; the **Protocol relating to an amendment to the Convention on International Civil Aviation (article 83-bis (Montreal, 1980))**; **Convention on the International Recognition of Rights in Aircraft (Geneva, 1948)**, and **Convention on International Civil Aviation (Chicago, 1944)**.

The Act requires the NCAA to maintain an aircraft registry to record proprietary rights, interests, liens and other dealings restricting the ability to register an aircraft to the "owner" who must be a Nigerian. The NCAR defines an 'owner' for the purpose of aircraft registration as follows:

1. *a citizen of Nigeria;*
2. *an individual citizen of another state who is lawfully admitted for permanent residence in Nigeria;*
3. *a corporation lawfully organized and doing business under the laws of Nigeria, where the aircraft is based and primarily used in Nigeria;*
4. *a government entity of Nigeria or political subdivision thereof; or*

5. *a foreign person who has leased the aircraft to one of the persons described in the points above, provided that:*
- a. *the aircraft may remain on the Nigerian registry only for as long as the lease remains in effect; and*
 - b. *the certificate of registration includes the names and addresses of the lessee and, if different, the operator of the aircraft.*

Once the aircraft has been registered, the mortgagee who wishes to register a mortgage interest, must apply in writing to the Director General of the NCAA and submit the deed of mortgage duly endorsed by the parties with stamp duty paid. The deed of mortgage must specify the aircraft type, registration marks, and serial number amongst others. It is pertinent to note, that where the Mortgagor is a company, then the mortgage must be registered with Corporate Affairs Commission (“CAC”) within 90 days pursuant to **Section 197 of the Companies and Allied Matters Act**. If under the mortgage deed the mortgagee is empowered to deregister and export the mortgaged asset, a deregistration power of attorney (DPoA) or an irrevocable deregistration and export request authorisation (IDERA) is also required to be filed with the NCAA.

For Leases, the lease agreement must be in writing with the requisite stamp duties paid to the Federal Inland Revenue Service (FIRS) and same submitted to the NCAA for the purposes of registration.

The Cape Town Convention offers another method of registering an aircraft mortgage, that is, as an international interest with the International Registry established under Article XVII of the Cape Town Convention's Aircraft Protocol. As a signatory to the Cape Town Convention, Nigeria is obligated to comply with Article 30(1), which is to the effect that an international interest (i.e. a lease or mortgage) remains effective, provided it was registered prior to the commencement of insolvency proceedings and in accordance with the provisions of the Convention. Thus, if the lessee operator (as the party in possession) is put into liquidation, administration or similar process, the liquidator of the lessee operator can impose the rights of any other creditors in priority to the lease or delay the ability of the lessor to repossess the aircraft on the termination of the lease in Nigeria.

CHALLENGES TO AIRCRAFT FINANCING IN NIGERIA

There are a number of challenges to aircraft financing in Nigeria including but not limited to multiple charges by the regulator, high operation costs including bank interest rates, multiple taxation and a lack of understanding of the sector by local financial institutions. These factors have led to the extinction of various local airlines such as First Nation and IRS airlines and the reduction of operating aircrafts in the country from 90 in 2015 to 53 in 2019. To address some of these challenges, the Federal Government through the NCAA is mulling the granting of incentives to operators such as tax waivers and other concessions as a means of attracting investment to the sector. The Government is also seeking to establish an aircraft leasing company to help domestic and African carriers procure new planes. It must be said that despite the challenges in accessing financing for the acquisition of aircrafts, 2019 saw the acquisition of some additional aircrafts by local airlines with Dana acquiring two boeing 737-300, Air Peace acquiring two ERJ 145 and leasing a boeing 737-800 while Arik wet leased two bombardier CRJ 900.

CONCLUSION

As Nigeria's infrastructure continues to be expanded and upgraded, the demand for air transportation will increase and to satisfy this demand, there will be need for significant investment in aircraft fleets. We expect the financing of these fleets to be through a hybrid of financing solutions which will be subject to the extant laws and regulations governing the sector. In addition, the government's plan to encourage the growth of the aviation sector through the provision of waivers and incentives should be actualized.

¹ This is known as the notice of charge and it is necessary for the purpose of ranking of priority and to validate the transaction in the event of default

² There is an International Registry, under the Convention on International Interests in Mobile Equipment and its Protocol on Matters Specific to Aircraft Equipment (Aircraft Protocol) where trans-border transaction and interest are registered.

³ Bank interest rates can be circa 26% from Nigerian Banks

⁴ Air Peace 26, Arik Air 11, Dana Air 6, Overland 6, Azman Air 2, and Ma Air 3

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