



Global Transportation Finance Newsletter

March 2023

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Insolvency Claims Trading

Airlines throughout the world were unable to fully trade during the pandemic-related lockdowns and their subsequent travel restrictions, creating significant liquidity constraints during 2020–22. As a result, a number of major international airlines—including Aeroméxico, Avianca, LATAM, Norwegian Air Shuttle, SAS and Virgin Australia—were forced to file for bankruptcy protection or insolvency administration, and many airline lessors were forced to agree to defer lease rental payments from their airline customers.

For some lessors, their airline customers entered bankruptcy protection regimes, resulting in the return of aircraft that were deemed “excess” to the airlines’ needs, and leaving those lessors with unsecured claims for financial losses that are most likely to be settled by the insolvent estate of the relevant airline at a significant discount to par value.

Rather than wait for a distribution, following the bankrupt debtor’s claims administration process, creditors with unsecured claims against an insolvency estate have the option to trade their claims, which can avoid the uncertainty and delay of being an expectant creditor.

So how does a claim trade work, and what are the key issues for a “selling” creditor?

A (Very) Brief Guide to Claims Trading

A creditor with claims against a debtor in an insolvency estate is able to trade such claims by way of an assignment of its rights to a third party “buyer.” In the airline context, the rights to be assigned under the trade include all of the creditor’s rights arising under the lease or other deal-related documents, including, its rights to receive the distribution from the insolvency estate afforded to the creditor’s claim.

Creditors can sell both proven “allowed” claims and those claims that have yet to be allowed or fixed against the insolvent debtor. In either case, the creditor, as seller, would enter into an agreement with the buyer to sell the principal amount of the filed or proven claim for an agreed price. Claims are traded below par, so the sale price will represent an agreed discount to the principal amount of the claim.

Upon completion of the trade, the buyer would become the creditor of record and be entitled to all applicable claim distributions from the insolvent estate.

There is a well-established market in claims trading.

Key Issues

- 1. Documentation.** There are two main documents that form part of a claims trade: the trade confirmation and the assignment of claim. The trade confirmation is a relatively short document setting out the key commercial terms, such as the principal amount of the filed claim, the purchase price and any conditions to completion of the assignment. Although it is similar to a term sheet or letter of intent, the trade confirmation is a legally binding document and constitutes an agreement to trade the relevant claims subject to completion of any agreed conditions and the signing of the assignment of claim. The seller and the buyer would typically be unable to avoid completing the intended sale and purchase once the trade confirmation is signed and dated.
- 2. Prior Transfers/Assignability.** To establish title to the claim, the buyer will take an assignment of rights under any prior assignment of the traded claim and will seek disclosure of any other assignment document. Accordingly, if the seller has assigned the claim within its group, for example, that intra-group assignment will need to be assignable or a consent to assignment (and to disclosure of its terms) will need to be obtained.
- 3. Representations.** In the assignment of claim, the seller is expected to make representations consistent with establishing the existence and validity of the claim without any third-party right of set-off or disallowance, consistent with the risk allocation between the seller and the buyer. The seller assumes the risk of the existence and validity of the claim and the buyer assumes the risk of the timing and rate of recovery on the claim.
- 4. Recourse.** Claim assignments typically include recourse by the buyer against the seller if the expected distribution is impaired, including situations where the claim amount is reduced or subordinated or where the dividends or distributions on account of the claim end up being proportionately less in amount or different in nature or timing than dividends or distributions payable to other holders of similar admitted claims against the estate. In such cases, the buyer would be entitled to a purchase price adjustment agreed under the claim assignment.



Vedder Price launched a new office in Miami as part of its continued strategy to locate in markets where our clients expand, attract top legal talent and strengthen the firm’s core practice areas.

In launching the Miami office location, Vedder Price is well positioned to continue to serve our Florida client needs in our largest practices, Finance, M&A/ Private Equity and Global Transportation Finance, while continuing to expand our Capital Markets footprint.

Thought Leadership

John Pearson from our London office recently co-authored “[The Aircraft Leasing Community and the Carbon Markets](#),” a discussion on how investments in the carbon markets can assist the leasing industry in the transition to net zero.

Russia Sanctions Overview

The Global Transportation Finance team has been at the forefront of discussions on the legal fallout from Russia’s invasion of Ukraine for the transportation sector. Set out below is our latest update shared with clients and friends. If you have any questions on how the Russia Sanctions impact your company, do not hesitate to contact our Global Transportation Finance attorneys.

<https://www.vedderprice.com/united-states-and-coalition-partners-commence-maritime-services-policy-and-adopt-oil-price-cap-exception-relating-to-seaborne-russian-oil/#overview>

Past Updates:

[OFAC Issues Preliminary Guidance on Safe Harbor for Maritime Services if Russian Oil is Sold at or Below Price Cap](#)

[BIS Revokes AVS License Exception for Belarusian Air Carriers; Updates List of Aircraft Reexported to Russia and Belarus in Violation of Licensing Requirements](#)

5. Timing of Payment. If the creditor’s claim against the insolvency estate has been proven, fixed and allowed prior to execution of the trade confirmation, payment of the purchase price will typically be made at closing. In contrast, if the claim to be sold has not been allowed and is thus still potentially subject to objection, payment is routinely delayed until such time as the claim becomes an allowed claim. As a result, having an allowed claim is preferable, although not necessary, to complete a claims trade.

6. Post Completion. Post-signing of the assignment of claim, the buyer would need to be registered as the creditor of record in respect of the relevant insolvency estate.

If you have any questions about claims trading, do not hesitate to contact our Global Transportation Finance attorneys.



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Vedder Price Reception in Dublin

The Global Transportation Finance team of Vedder Price hosted a reception in connection with the Airline Economics Growth Frontiers Dublin 2023 at Urban Brewing. Our attendees enjoyed a fun evening of socializing and networking with their peers.



EU Releases Fifth Round of Russian Sanctions: Impacts for Aviation and Maritime

BIS Issues Administrative Orders Temporarily Denying Export Privileges of Three Russian Air Carriers

BIS Identification of Aircraft Reexported to Russia in Violation of Russia-Belarus Licensing Policy

Memorandum of Russia Sanctions for the Aviation and Maritime Industries

International Sanctions Widen as Ukraine Crisis Deepens

Honors & Awards



Vedder Price Recognized in Chambers Global Asset Finance (Aviation & Rail) – Global Market Leaders in 2023

Chambers Global 2023 ranked the Global Transportation team Band 2 in the category of Asset Finance (Aviation & Rail). *Chambers Global 2023* recognized **Gavin Hill** and **Jeffrey T. Veber** as Band 3 and **Geoffrey R. Kass** as Band 4.



Vedder Price Global Transportation Finance Team Wins Airline Economics Recognition Through Private Placement Transaction

Airline Economics recently awarded the Vedder Price Global Transportation Finance team with the Capital Markets Deal of the Year recognition in connection with the recent closing of the **MAST 2022-1’s commercial aircraft portfolio financing transaction**. The recognition was given as part of the Global Aviation 100 Deals of the Year awards that were recently announced in Dublin, Ireland.

UCC 2022 Amendments – Final Version Now Being Considered By State Legislatures

What Equipment Leasing and Financing Parties Should Be Considering Now

In our [April 21, 2022 Newsletter](#), we reported to you that a special committee was in the process of amending the Uniform Commercial Code (the “**UCC**”) to reflect emerged and emerging technologies and trends. The technology-related amendments addressed, among other things, transactions involving distributed ledger technology, virtual currencies, nonfungible tokens and other digital assets. The amendments of particular interest to equipment leasing and financing parties are intended to reflect emerged and emerging industry practices. The referenced *emerged* industry practice is the creation and vaulting of equipment leasing and financing transactions existing only in electronic format. The *emerging* industry practice is the offering of financing products related to “bundled” transactions, which bundle a sale or lease of equipment, together with, among other things, a related software license, maintenance or other services, consumables or other related property, services or rights.

As explained in our previous article, the UCC is a “model commercial code which serves as the basis for state laws that govern most commercial transactions originated in the United States.” It facilitates sales, leases, secured financings and other transactions involving personal property by providing a uniform approach by states to the various legal considerations relating to these transactions. The practical benefit intended by this uniform approach is that the outcome of disputes among parties to, or impacted by, these transactions should be equitable and predictable.

Significant amendments to the UCC are made very infrequently, and are typically driven by a recognized need to align the UCC’s coverage of transactional matters with evolved or evolving market circumstances, trends and practices. As noted in our previous article, a special committee of commercial lawyers began the process of amending the model UCC in 2019 when it became clear that the existing model version did not cover, either adequately or at all, certain emerged and emerging technologies and trends. Since then, the amendments were finalized and are currently being considered for enactment by the states.¹

The final version of the amendments—generally.

The UCC is the legal underpinning for structuring, documenting, syndicating, securitizing and enforcing the spectrum of equipment finance and capital markets transactions. Accordingly, the amendments could have an impact on these transactions upon becoming effective in the various states, especially in New York because New York governing law is often the popular choice for many domestic and foreign transactions. Upon enactment, the amendments could afford certain market advantages if leveraged, or disadvantages if ignored.

The amendments that are likely to be of greatest interest to equipment finance providers relate to “chattel paper,” a category of collateral covered by revised UCC 9,² and to “hybrid leases,” a newly recognized category of true leases covered by revised UCC 2A. The digital asset laws created by the amendments are provided in a new UCC 12 and in revisions to UCC 9.³ Executive summaries of these amendments are provided below.

Chattel paper amendments.

Background.

References to “*chattel paper*” refer to a category of collateral covered by UCC 9. Although UCC 9 is typically associated with secured transactions, in addition to covering loans secured by collateral, it also covers *purchases of chattel paper*, including syndications, securitizations, and other capital markets transactions involving equipment leases and/or financings. Currently, “*chattel paper*” refers to the tangible or electronic original of an equipment lease or financing designated by the parties as being the “chattel paper” original. Whether in the context of a secured financing or purchase of the receivables evidenced by a related lease or financing, the secured lender or purchaser must satisfy the applicable UCC 9 requirements in order to establish the priority of its interest in the associated chattel paper. Perfection may be achieved by either physical possession of the tangible copy, or control of the electronic record, of the designated chattel paper originals of the related lease or secured financing documents. Establishing that a secured party or purchaser has validly perfected its interest in any associated chattel paper original is a very significant focus of most capital markets transactions.



Vedder Price Singapore Distinguished by The Legal 500 Asia Pacific 2023

The Legal 500 Asia Pacific 2023 has recognized the Global Transportation Finance team in Singapore in Asset Finance: Foreign Firms as Tier 3. In addition, Geoffrey R. Kass, Ji Woon Kim and Bill Gibson were Editorially Recommended.



Vedder Price Recognized in Chambers Asia-Pacific Guide 2023

Chambers Asia-Pacific 2023 ranked the Global Transportation Finance team in Singapore Band 4 for the Aviation Finance practice and ranked the team Band 4 in a new category for 2023: Asia-Pacific Region: Aviation Finance. *Chambers Asia-Pacific 2023* recognized **Ji Woon Kim** and **Bill Gibson** as Band 4 for Aviation Finance.



Vedder Price Is Recognized in Multiple Deal of the Year Awards at Airline Economics Aviation 100 Asia-Pacific Awards 2022

Airline Economics recognized the Vedder Price Global Transportation Finance team for the role they played in advising clients in three transactions recognized at its annual “Aviation 100 Asia-Pacific Deals of the Year Awards,” which recognize the foremost aviation finance transactions in the Asia-Pacific region.

Amended Definition of Chattel Paper.

The amended definition of “chattel paper” under UCC 9 now relates to the payment right of a lessor or secured party, *not* the paper or electronic record evidencing that right.

Specifically, Section 9-102(a)(11) has been amended to read as follows:

“‘Chattel paper’ means:

- (A) a right to payment of a monetary obligation secured by specific goods, if the right to payment and security agreement are evidenced by a record; or
- (B) a right to payment of a monetary obligation owed by a lessee under a lease agreement with respect to specific goods and a monetary obligation owed by the lessee in connection with the transaction giving rise to the lease, if:
 - (i) the right to payment and lease agreement are evidenced by a record; and
 - (ii) the predominant purpose of the transaction giving rise to the lease was to give the lessee the right to possession and use of the goods. (emphasis added)

But, as was the case before being amended, the term “chattel paper” does not include certain other payment rights, including with respect to a vessel charter or the use of a credit or charge card.

Official Comments and Examples. Although the “Official Comments” and related examples which follow Section 9-102(a)(11) are not legally binding, they provide useful as context for the intentions of the drafting committee when considering the text of the amended definition.

Official Comment 5(b) is particularly helpful, and includes the following explanation: “*What distinguishes chattel paper from other rights to payment is the fact that the creditor has an interest in specific goods to enforce the right to payment. For example, the fact that a secured party also has an interest in other property does not prevent the right to payment from being chattel paper, provided that the specific goods are the primary collateral.*” (emphasis added)

Examples 8 and 9 and the related commentary regarding what might constitute “chattel paper” provide some further insight as to the practical circumstances contemplated by the drafting committee when amending the definition.

Example 8. “*To secure a loan, Borrower grants Lender a security interest in a specified item of equipment and a deposit account. The loan and the security interest are evidenced by one or more records. The right to payment is chattel paper, assuming the equipment is the primary collateral.*” In this example, the inclusion of some incidental collateral, such as a deposit account, does not prevent the characterization of the Lender’s right to payment as chattel paper. Another typical example would be the inclusion of after-acquired replacement parts to be installed on the specified equipment.

Example 9. “*To secure a loan, Borrower grants Lender a security interest in all of Borrower’s existing and after-acquired inventory. The loan and the security interest are evidenced by one or more records. The right to payment is not chattel paper.*” In order to be chattel paper, a right to payment must be accompanied by a security interest in specific goods or a lease of specific goods. Accordingly, a right to payment secured by a security interest in inventory or similar rotating collateral is not chattel paper.

Achieving priority of interests in “chattel paper.”

In order to achieve priority over other parties claiming an interest in chattel paper either being pledged as collateral securing a loan or purchased in a capital markets transaction, a secured party or purchaser must “perfect” its interest by satisfying the applicable requirements in UCC 9. In larger capital markets transactions, perfection by possession or control by the purchaser of the related tangible or electronic records is often required because it could, together with the satisfaction of certain other criteria, afford the purchaser “superpriority” over competing third-party claims.

New Section 9-314A. New Section 9-314A amends the manner by which a purchaser or secured party may perfect the interest granted or conveyed to it with respect to chattel paper. Aside from filing a financing statement, a purchaser or secured party may also perfect its security interest by taking and retaining possession of each tangible (paper), and “control” of each electronic, “authoritative” copy or copies of the records evidencing the chattel paper. Official Comment 1 to new Section 9-314A explains the practical purpose underlying the differences in the perfection requirements when comparing new Section 9-314A to current Section 9-314 “[t]o accommodate current practices and future technology, parties are allowed considerable flexibility in determining the method used to establish whether a particular copy is authoritative, provided that third parties are able to reasonably identify the authoritative copies that must be possessed or controlled to achieve perfection.”⁴

Vedder Price was recognized in the following categories:

Asia-Pacific Supported Finance Deal of the Year

Vedder Price represented BNP Paribas, Singapore, in connection with the AFIC-supported financing of two Boeing 737 MAX 9s for AerDragon on operating leases to Aeromexico. The Vedder Price team consisted of **Ji Woon Kim** and **Benavon Lee**.

Asia-Pacific Editor’s Deal of the Year

Vedder Price represented the Export-Import Bank of the United States (EXIM Bank) in connection with the EXIM Bank-supported refinancing facility for Korean Air Lines. The Vedder Price team consisted of **Jeffrey T. Veber, Ji Woon Kim, Justine L. Chilvers, Mie Miura** and **Benavon Lee**.

Asia-Pacific Lease Deal of the Year

Vedder Price represented Castllake on a sale and leaseback transaction of two Boeing 787-800 and two Boeing 787-900 aircraft with award-winning low cost carrier Scoot. The Vedder Price team consisted of **Bill Gibson, Greg Whillis** and **Benavon Lee**.

Recent Speaking Engagements

February 15, 2023

John F. Imhof Jr. presented at the **21st Annual Marine Money Hamburg Ship Finance Forum**.

John interviewed Jens Mahnke, CEO of Elbe Financial Solutions (EFS), in a session entitled “Fund in Focus.” John and Mr. Mahnke discussed EFS as an alternative asset manager focused on sustainability-linked maritime and global infrastructure projects, and how EFS is assisting shipowners and investors with financing for these projects.

February 6 – 8, 2023

David M. Hernandez and **Edward K. Gross** spoke at the **Corporate Jet Investor (CJI) London 2023 conference**. Eddie moderated the session “Will the US keep leading the market?” where he led the conversation on how the market coped with sudden growth, what the future looks like for flight departments and if we are currently seeing a more balanced market. David served as a panelist for the session “From Russia With Sanctions.”

Essentially, perfection may be achieved by having either, or a combination of, tangible or electronic records so long as the party having possession or such control of records can establish that it is the “authoritative” copy of the tangible or electronic records that evidence the chattel paper. The revisions are intended to reflect current industry practices by certain lessors and financing providers who documents these using one or the other of paper or electronic records and either converting them to or supplementing them with records in the other medium. As is the case with references to “authoritative” in current UCC § 9-105(b) covering perfection by control of the authoritative copy of electronic chattel paper, the term “authoritative” is not defined, but is now also applied to tangible records.⁵ “Whether an electronic or tangible record evidencing chattel paper is authoritative depends on the facts and circumstances,” as noted in Official Comment 1 to new Section 9-314A, but some guidance is also provided in the Official Comment as to practices, systems and protocols that exist or may be developed to determine which copies of a record are authoritative and which are not.⁶

Amended Section 9-105. For the purposes of perfection by “control” under new Section 9-314A, a secured party must establish control under the general test in Section 9-105(a), including by satisfying the safe harbor tests in subsection (b) or (c) of Section 9-105. Subsections (a) and (b) are substantially unchanged by the amendments. Subsection (b) has been retained to assure viability after the amendments are enacted regarding systems for control of chattel paper evidenced by electronic records. Because subsection (b) would be inapplicable when the relevant record is maintained on a distributed ledger, subsection (c) has now been included and generally follows the conditions for control of controllable electronic records under new Section 12-105.⁷ Compliance with the conditions in subsection (c) would satisfy the conditions in subsection (b).⁸

Amended Section 9-330. Under amended Section 9-330(b), a purchaser may achieve *superpriority* over a security interest in chattel paper claimed other than merely as proceeds of inventory subject to a security interest if the purchaser gives new value (e.g., pays the purchase price), takes possession of each authoritative tangible copy of the record evidencing the chattel paper and obtains control under Section 9-105 of each authoritative electronic copy of the record evidencing the chattel paper, in good faith, in the ordinary course of the purchaser’s business, and without knowledge that the purchase violates the rights of the secured party. A mostly similar superpriority status may be achieved by a purchaser over a security interest in chattel paper claimed merely as proceeds of inventory by satisfying the requirements in Section 9-330(a).

Why the chattel paper amendments matter to the equipment finance industry.

Participants in these transactions, whether as originators, purchasers, lenders or investors, should be considering related changes to their equipment finance, loan and capital markets documents, transaction practices, and technology systems, so that they might take advantage of the amended laws. Upon enactment, certain transition rules will address prospective application of the UCC 9 amendments relating to post-enactment transactions involving chattel paper, or require compliance by a specified adjustment date with the amendments, in order to protect the perfection and priority of existing security interests.⁹

Hybrid lease amendments.

Background.

The UCC amendments included a new category of (true) leases covered by UCC 2A—a “hybrid lease.” Creating this new category of lease for inclusion within the scope of UCC 2A was responsive to industry requests that leasing law be amended to better address the respective rights and remedies of parties to so-called “bundled transactions.” Transactions involving a lease of goods (i.e., the spectrum of equipment types) together with a related agreement by a lessor to provide something else to a lessee represent a growing trend in the vendor finance market. The growing popularity of these transactions is attributable to demand by customers seeking to acquire the use of certain equipment together with other related aspects of the transactions. Generally, these customers are seeking a “solution” transaction documented by a single contract, entered into with a single counterparty to whom the customer will make a single periodic payment.

Certain of these transactions include an integrated lease of equipment, but the predominant purpose is something other than the lessee’s use and possession of the equipment. By way of example, cloud services and other “...as a service” transactions sometimes include an integrated lease of the related technology or other equipment, with the associated rent payments being included in the total payment for whatever constitutes the service. Other bundled transactions may be more obvious as to the predominance of the integrated equipment lease over the other aspects of the transaction. But in either case, equipment finance participants (“**observers**”) involved in the amendment drafting process sought to have the scope of UCC 2A amended so that the lessor-favorable provisions could apply to all or (at least) the equipment lease provisions of UCC 2A.

What is a “hybrid lease”?

New Section 2A-103(1)(h.1) defines “**hybrid lease**” as “a single transaction involving a lease of goods and; (i) the provision of services; (ii) a sale of other goods; or (iii) a sale, lease, or license of property other than goods.”

January 26, 2023

Edward K. Gross presented at the Helicopter Town Hall: The Helicopter Leasing Market in 2023, hosted by Corporate Jet Investor (CJI) and Aero Asset. The town hall served as a follow-up event from the London Conferences, and featured speakers from around the world sharing the latest insights into the current helicopter market



Deal Corner

Vedder Price Represents GA Telesis, LLC in Launch of New Direct Aviation Lending Platform

Vedder Price represented GA Telesis, LLC, (“GAT”) in connection with the launch of HALO AirFinance (“HALO”), a direct aviation lending platform. The new lending platform is a joint venture between GAT and Tokyo Century Corporation (“TC”). HALO will effectively serve as the exclusive debt origination channel for GAT and TC, with a strong emphasis on secured direct lending to airlines, lessors and investors, covering the collateral spectrum from new to mid-life aircraft. HALO is launching its first fund HALO One, in partnership with InterVest Capital Partners. HALO One will benefit from a revolving credit facility led by Citigroup as Structuring Agent and Co-lead Arranger and Fifth Third Bank, National Association, as Co-lead Arranger.

In addition to Geoffrey R. Kass, the Vedder Price legal team on the transaction was also led by Shareholders Adam R Beringer, Joseph H. Kye and Cody J. Vitello and Associates Joel R. Thielen, Gabriela D. Demos, John G. Munyon, Kevin M. Maedomari, Miri Joo and Adam S. Goldman.

Vedder Price Advises DLL Finance LLC in \$850 Million Securitization Transaction of Agricultural, Golf Course and Turf Equipment Contracts

Vedder Price represented DLL Finance LLC (DLL Finance), as originator, sponsor and servicer, in connection with the DLLAD 2023-1 securitization that closed recently. The four classes of notes issued by DLLAD 2023-1 LLC are secured by a pool of loans and leases with respect to agricultural, golf course and turf equipment. Global Transportation Finance Shareholder Edward K. Gross and Capital Markets Shareholder Kevin A. MacLeod led a team that also included Tax Shareholder Matthew P. Larvick and Associates Conor A. Gaughan, Francisco Koishi Ishino and Sandy W. Chen.

As previously mentioned, the Official Comments and related examples typically provide useful insight as to the purpose and construction of each of the UCC provisions, as is the case with this new definition. As an example of what might constitute a “hybrid lease,” the Official Comments include one of the most common examples: a lease of a copier, together with a sale of paper, staples and toner, with routine maintenance and repair services, all in return for periodic payments by the lessee. There are other examples, but the customer’s predominant purpose of having the use of the copier when compared to the consumables and services is obvious.

The related Official Comment also explains that whether a bundled transaction constitutes a “hybrid lease” will be a fact-specific determination. Among one of the most important considerations is whether the purported hybrid lease is a *single transaction*. This is an essential factor in the definition in new Section 2A-103(1)(h.1), which specifies that a hybrid lease “means a *single transaction*.” Further to that, the Official Comments make clear that if the *goods aspect* “is unrelated to the other aspects of the transaction,” and the terms of the single agreement relating to the goods are “readily severable” from the terms of the agreement relating to the other aspects of the transaction, then the document would not create a hybrid lease. In other words, it must be a “bundled” transaction.

What does it matter if a lease is a “hybrid lease”?

Among the implications of the amendments to UCC 9 regarding chattel paper mentioned above is that the revised definition now includes payment rights under a “hybrid lease” of specific equipment. That amendment is particularly useful in capital markets transactions involving a purchase or financing of leases which might constitute hybrid leases. Industry observers advocated for that amendment so as to address uncertainties as to how those transactions might be characterized in the representations, warranties and other provisions in capital markets documents involving portfolio sales or financings. Having hybrid leases being deemed chattel paper also provides clarity as to how purchasers and secured lenders may perfect and achieve priority with respect to their interests in the associated payment rights.

Other than the creation of the defined term “hybrid lease,” the primary amendment was to expand the scope (i.e., *what’s covered*) provision in Section 2A-102.

Under existing Section 2A-102, UCC 2A applies to any transaction, regardless of form, that creates a lease. As amended, UCC 2A will also provide for the application of UCC 2A to hybrid leases to the extent provided in new subsection (2) of amended Section 2A-102. Subsection (2) (a) addresses the application of UCC 2A with respect to hybrid leases if the lease-of-goods aspects do not predominate, and in that event, only the provisions of UCC 2A “*which relate primarily to the lease-of-goods aspects*” will apply. Under subsection 2(b), UCC 2A will apply to both the *lease aspects* and the *other aspects* (e.g., services, consumables, software licenses, etc.) of a hybrid lease “*if the lease-of-goods aspects... predominate.*”

Industry observers participating in the amendment drafting process were particularly focused on having hybrid leases be covered by UCC 2A because of what could be considerable advantages for lessors, financing providers and investors. Underlying the pursuit of expanding the scope of UCC 2A was the hope that its lessor-favorable provisions might be applied to all or (at least) part of a bundled transaction. Although, at first, the drafting committee was skeptical about the need to consider the expansion, including because certain of the members were either unfamiliar with this industry practice or it did not arise because of emerging technology, they ultimately recognized the beneficial market implications and included the related amendments.

Although, as noted above, UCC 2A is considered to be generally lessor-favorable, the UCC 2A protections available to lessors with respect to a “*finance lease*” are even more desirable. Pursuant to Section 2A-103(1)(g), a lease is likely to be a “finance lease” if the lessor is merely providing acquisition financing structured as a true lease, and is not the supplier, of the leased equipment. The ultimate goal industry observers sought to achieve was “finance lease” treatment with respect to all of the transactions constituting a hybrid lease, or (at least) the integrated equipment lease.

If an equipment lease that is integrated into a hybrid lease transaction is a UCC 2A “finance lease,” Section 2A-407 which makes statutory the “*hell or high water*” nature of a lessee’s rent obligations, will apply to the entire transaction, not just the lease if the lease-of-goods aspects predominate the transaction. But, even if the lease-of-goods aspects do *not* predominate, this statutory “hell or high water” protection will still apply to the lessee’s promise to pay rent as consideration for leasing the equipment.

By way of example, consider the “finance lease” implications associated with the hybrid copier lease mentioned above. That hybrid lease included an integrated lease of a copier together with a sale of paper, staples and toner, and an agreement to provide routine maintenance and repair services, all in return for periodic payments (including the lease rentals) by the lessee. Assuming that the lease of the copier aspects of that integrated transaction *predominate*, and that the copier lease is a “finance lease,” the lessee’s obligation to pay the entire amount due under the hybrid lease may be deemed to be “hell or high water” upon the lessee’s acceptance of the copier. However, even if the lease of the copier aspects *do not predominate*, but the integrated copier lease is a “finance lease,” the lessee’s obligation to pay the copier rent portion of the periodic payments could be deemed to be “hell or high water.” In either case, the lessor’s ability to monetize all or at least part of the revenue associated with a hybrid lease will be greatly enhanced.

Why the hybrid lease amendments matter to the equipment finance industry.

The Official Comments to Section 2A-102 provide some helpful guidance as to structuring and documenting hybrid leases so as to support a determination that the lease-of-goods aspects predominate. The Official Comments mention that the characterization of a transaction for the purposes of Section 2A-102 is a “question of fact,” as well as those transaction attributes that might support the predominant purpose for both UCC 9 chattel paper treatment and UCC 2A lease coverage. Per the comments, relevant factors include: “*the language of the agreement and the portion of the total price that is attributable to the lease of goods.*”

Further, the comments provide what could be considered as structuring and drafting hints. Among other things, the comments note that an “*agreed-upon allocation [of the price to the possession and use of the goods] is ordinarily binding on the parties.*” Accordingly, lessors desiring to achieve this favorable characterization should consider including some or more of the following in their hybrid lease documents: lessee acknowledgments supporting the lease-of-goods aspects as the predominant purpose; the “finance lease” treatment of the integrated lease; and/or the extent to which payments in a non-predominant hybrid lease relate to the use and possession of the leased goods.

New UCC 12—Digital assets, etc.

What are digital assets?

As previously noted, existing and contemplated changes in the marketplace were the impetus for the new amendments, especially to address the gap in existing commercial law regarding digital assets. The UCC amendments address that gap by including a new UCC 12 and revising certain other Articles with the intention of providing a uniform commercial law approach to transferring and collateralizing these assets. The amendments also cover the commercial law implications of existing and new technologies by which transactions may be conducted, like blockchain and other distributed ledger technology (“DLT”) platforms.

The digital assets covered by new UCC 12 are referred to as “controllable electronic records” (“CERs”), including virtual currencies, nonfungible tokens and other CERs that have been assigned an economic value. New UCC 12 also creates a new type of digital asset—CERs that have embedded payment rights for goods or services *which are exercisable by the owner*. Tethered payment rights meeting certain criteria in UCC 12 are referred to as “controllable accounts” or “controllable payment intangibles.” A number of the relevant considerations associated with monetizing these tethered payment rights pursuant to new UCC 12 are similar to the considerations when monetizing accounts receivables associated with a sale of goods or services pursuant to current UCC 9.

Essentially, the pertinent provisions of new UCC 12 and related revisions to UCC 9 should facilitate selling or financing these digital payment rights evidenced by electronic records on a distributed ledger platform. The new or amended UCC provisions afford “take-free” rights for “qualified purchasers,” establish the rights and duties of the account debtors, and the perfection and priority of security interests in these assets. The effect of these amendments should be to provide greater certainty as to the CER account debtor’s obligation to pay a purchaser or collateral assignee, and to afford CERs “negotiability” status (i.e., free of defenses, etc.) similar to the status afforded to a tangible negotiable instrument under UCC 3.

Why the digital asset amendments matter to the equipment finance industry.

As the equipment finance industry continues to evolve, equipment leases and financings are likely to involve transactional aspects addressed in new UCC 12 or the related amendments. Examples could include: transactional aspects evidenced by smart contracts; payments by virtual currencies; full or collateral assignments of CERs with embedded payment rights (e.g., a CER evidencing the right to receive software license payments); nonfungible tokens representing collateral; or escrow arrangements managed on a DLT platform.

Conclusion.

Enactment, Effective Date and Transition Rules.

As mentioned above, the amendments were finalized in July 2022, and are currently being considered for enactment by the states.¹⁰ When enacted, the amendments will include an effective date as determined by that state, as well as transition rules providing for prospective application of the amendments, with certain exceptions regarding new UCC 12 (digital assets) and amended UCC 9 (perfecting and obtaining priority of security interests). The transition rules will include a uniform adjustment date of January 1, 2025 (or if later, one year after the effective date), intended to provide sufficient time for a person to achieve perfection or priority of a security interest under the amendments following the effective date, or to protect its established priority before the priority might otherwise be lost on the adjustment date.¹¹ These compliance requirements must be carefully considered and addressed by document and systems strategies so as to protect any existing interests that might be impacted by the amendments.

Leveraging the Advantages Afforded by the Amendments.

The systems and practices associated with sales or financings of receivables evidenced by tangible or electronic leases or secured financings of specific equipment, could require adjustments by the parties to those transactions so as to achieve the desired priority status. The amendments relating to digital assets, including new UCC 12, should facilitate transacting on distributed ledger platforms, financing digital payment rights, and relying on virtual currencies as an exchange of value will be facilitated and accelerated. Lastly, lessors who originate bundled transactions so as to accommodate the greater demand for those transactions could achieve significant advantages by structuring and documenting those transactions to conform to the UCC 2A scope amendments regarding hybrid leases.



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Missed Delivery: Peregrine Aviation v Laudamotion

Cases resulting from the pandemic continue to work their way through the English courts, and *Peregrine Aviation Bravo Limited (the Lessor) and Laudamotion GmbH (the Lessee)*¹ is a recent decision that takes us back to the beginning of the shutdown of the airline industry due to the pandemic in 2020, when lessors and lessees were negotiating rent deferrals and rescheduling deliveries of aircraft.

The case is a useful exploration of the delivery process for used aircraft and will have interested parties in the industry examining the delivery provisions in their leases.

The facts

As part of a series of lease agreements between related parties, the Lessor and the Lessee contracted for the delivery of certain Airbus A320-200 aircraft (the **Aircraft**) to enter service with the Lessee beginning March 2020. Typical with many aircraft leases, the leases for the Aircraft provided that:

- (A) the Lessor would notify the Lessee of the time for delivery of the Aircraft to the Lessee “in a timely manner” and further, the Lessor agreed to “consult with the Lessee” prior to determining the exact date on which the Aircraft would be delivered to the Lessee, as well as to provide “Lessee with reasonable notice in respect of such date;”
- (B) the Aircraft would be delivered at a maintenance facility where the Lessor was also to accept redelivery of the Aircraft from the prior operator of the Aircraft, flynas. It was a condition of the delivery of the Aircraft to the Lessee that such redelivery had occurred from flynas;
- (C) each lease contained detailed technical requirements relating to the condition of the Aircraft, including technical records, at delivery (the **Delivery Condition Requirements**). If the Aircraft did not comply with any Delivery Condition Requirement in any material respect, the Lessee had the right to refuse to accept the Aircraft until such deviation was corrected, at the Lessor’s cost;
- (D) if the delivery of the Aircraft had not occurred on or before a long-stop date for delivery (including as a result of the Aircraft not complying with the Delivery Condition Requirements), the leasing could be terminated by either party on 10 business days’ written notice;
- (E) in addition to meeting the Delivery Condition Requirements, there were standard conditions precedent to the leasing of the Aircraft, including the provision by the Lessor of an Export Certificate of Airworthiness for the Aircraft; and
- (F) any failure by the Lessee to accept delivery of the Aircraft within five business days of it being validly tendered would result in the occurrence of an event of default.

Preparations for delivery commenced several months ahead of the proposed delivery date for the first Aircraft in March 2020, with the Aircraft undergoing maintenance to ensure it complied with the Delivery Condition Requirements and the Lessee inspecting the technical records as they became available, as part of the delivery process (among other steps taken, including the exchange of some of the conditions precedent documentation).

As the effects of the pandemic reached Europe in mid-March 2020, the parties initially continued to work towards delivery of the Aircraft but then correspondence between the two parties turned to whether delivery should proceed and if the Lessor would accept rent reductions and/or deferrals.

At the end of March 2020, correspondence between the parties presented to the court suggested an understanding between the Lessor and the Lessee that delivery of the Aircraft would occur during June 2020, pursuant to a global amendment agreement that was prepared (but not executed) in relation to the leases of the Aircraft.

In late April 2020 however, the Lessee sent a letter to the Lessor notifying the Lessor that it would not accept delivery of the Aircraft – in court, the Lessee indicated that this was part of a negotiation strategy it was undertaking with all of its lessor counterparties². Additionally, the Lessee instructed its technical consultants that they should cease to work on the delivery of the Aircraft.

In response to the letter from the Lessee, the Lessor served a notice on the Lessee on or around 1 May 2020 that said the date for delivery of the first Aircraft would be 7 May 2020 and the Aircraft was tendered for delivery by the Lessor to the Lessee on 7 May 2020. However, the Lessee refused to accept delivery and the Lessor declared an event of default for failure to take delivery of the Aircraft when validly tendered.

The Lessee contested that the Aircraft had not been validly tendered on the basis that:

- (A) the Lessor did not “consult with the Lessee” prior to the Lessor determining that the Aircraft would be delivered on 7 May 2020 and did not provide the Lessee with “reasonable notice” of the date on which the Aircraft would be delivered; and
- (B) the Aircraft did not meet the Delivery Condition Requirements when it had been tendered, including the failure by the Lessor to provide an Export Certificate of Airworthiness for the Aircraft.

The court considered each of these points in turn:

The requirement to consult and provide reasonable notice

The court found that the Lessor was obliged to consult with the Lessee regarding the date for delivery of the Aircraft and to provide reasonable notice of the delivery to the Lessee, and that the Lessor had not done so. This decision is interesting given the Lessee appeared to disengage from the delivery process, had ceased to cooperate in the delivery process for the Aircraft and had informed the Lessor that it did not intend to take delivery of the Aircraft.

The court was persuaded that the Aircraft having been ready for delivery in March was irrelevant and no constructive notice could be constituted that would have dispensed with the requirement for reasonable notice. Further, the Lessee was under no duty to cooperate pursuant to the terms of the lease, and such a duty could not be implied by the court.

Failure to meet the Delivery Condition Requirements

The court found that the failure to provide the Export Certificate of Airworthiness for the Aircraft meant the Delivery Condition Requirements were not satisfied by the Lessor and therefore, the Lessor could not be said to have validly tendered the Aircraft for delivery on 7 May 2020³.

The court rejected the Lessor's contention that the Export Certificate of Airworthiness would have been provided at delivery if the Lessee had been cooperative – this appears to be correct as otherwise the Lessee could have been forced to accept an aircraft which does not comply with a material Delivery Condition Requirement on the basis that the Lessee was uncooperative (noting the court had found that the Lessee was under no duty to be cooperative).

Additional considerations

The court dismissed the Lessor's principal claim, but did consider two additional matters that are of note⁴:

- (A) the Lessee sought to claim that as the Aircraft was still on lease to flynas at the time the Aircraft was tendered for delivery to the Lessee, the Aircraft could not have been validly tendered – this was rejected by the court on the basis that the lease with flynas was readily terminable by the Lessor. Indeed, the Aircraft had only been kept on lease with flynas to ensure its maintenance, storage and insurance pending delivery to the Lessee; and
- (B) the Lessee sought to claim that it was able to reject the Aircraft if it “was able to demonstrate” a material deviation from the Delivery Condition Requirements, which it contended meant that the deviations existed and it was capable of demonstrating the deviations, even if it had not actually demonstrated they existed – this was rejected by the court as well. The Lessee would have needed to provide details of the material deviations in order to allow the Lessor to rectify them.

Delivery provision considerations

It remains to be seen if the decision will be successfully appealed, but lessors may wish to consider tweaks to their delivery provisions to guard against some of the issues arising here:

- including or enhancing any cooperation obligations on a lessee in relation to the delivery process to ensure such lessee cannot avoid accepting a tendered aircraft by virtue of it having failed to engage in the process;
- including fixed timelines for any notice provision in relation to delivery, rather than have “reasonable” notice periods; and
- clarifying “failure to take delivery”-type events of default to include instances of the lessee stating it will not accept delivery.



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Global Transportation Finance Holiday Dinner

The Global Transportation Finance team hosted their annual holiday dinner at Sparks Steakhouse in New York. It was a great evening filled with networking among colleagues and friends.



Women in Aviation

The Women of the Global Transportation team along with Natixis Corporate & Investment Banking, Macquarie Group, Goldman Sachs and Sun Country Airlines hosted the Women in Aviation Reception, where guests enjoyed a festive networking event celebrating women in the industry.



Maritime Team Dinner

Vedder Price Maritime team hosted a dinner at Del Frisco's Double Eagle Steakhouse in connection with the 2022 Marine Money Ship Finance Forum in New York City. It was a wonderful evening of networking with clients and colleagues in the maritime industry.



Endnotes

UCC 2022 Amendments – Final Version Now Being Considered By State Legislatures

What Equipment Leasing and Financing Parties Should Be Considering Now

¹ As of the date of this publication, bills have been introduced in 18 state legislatures for the purpose of enacting the UCC amendments.

² The UCC is segmented into "Articles." Each of these segmented Articles contains the statutory coverage and official comments pertaining to a specific type of commercial transaction, but also recognizes any related provisions in the other Articles of the UCC. Article 1 of the UCC is not transaction specific, and includes definitions and provisions which generally pertain to the other Articles of the UCC. References in this article to "UCC 2A", "UCC 9", "UCC 12" and the like, refer to the corresponding Article of the UCC, either in its pre-amendment form, or as amended or now included; e.g., Article 2A (true "leases"), Article 9 (secured transactions) and Article 12 (digital assets).

³ One impetus for amending the UCC to cover the commercial law implications of digital assets was to avoid inconsistencies that would result in a non-uniform approach to these issues by state legislatures adopting non-uniform digital asset laws. The amendments also cover the manner by which security interests in these assets may be established, perfected and afforded priority.

⁴ See Official Comment 1 to new Section 9-314A.

⁵ *Id.*

⁶ *Id.*

⁷ Controllable electronic records and other digital assets are discussed in our below summary of new UCC 12.

⁸ See Official Comment 2 to revised Section 9-105.

⁹ See the Conclusion for a further discussion of the transition rules.

¹⁰ As of the date of this publication, bills have been introduced in 21 state legislatures for the purpose of enacting the UCC amendments.

¹¹ See new UCC Article A.

Missed Delivery: Peregrine Aviation v Laudamotion

¹ *Peregrine Aviation Bravo Ltd & Ors v Laudamotion GmbH & Anor* [2023] EWHC 48 (Comm).

² The court also considered if a letter from the Lessee to the Lessor stating that the Lessee would not make payments would constitute an Event of Default on the basis that it had "*threaten[ed] in writing to suspend payments with respect to all of any of Lessee's debts or other payment obligations*" but found that this provision could not be broadly construed, that the Lessee's statements were not unequivocal and the Lessor had ignored the statements ahead of tendering the Aircraft for delivery in May 2020.

³ The Export Certificate of Airworthiness for the Aircraft was only issued on 12 May 2020 (and seems never to have been delivered to the Lessee, in any event).

⁴ It should be noted that because these matters did not fall for consideration within the main claim, which was dismissed, these matters are *obiter dicta*.

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Global Transportation Finance

The Vedder Price Global Transportation Finance team is one of the largest, most experienced and best recognized transportation finance practices in the world. Our professionals serve a broad base of clients across all transportation sectors, including the aviation, aerospace, railroad, general equipment and marine industries, and are positioned to serve both U.S.-based and international clients who execute deals worldwide.

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