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Abogados Sierra Events and Sponsorships.

Assignment v. Novation – Local and International Aspects.  
by Jessi Saba

FEBRUARY NEWS on Mexican Aviation

COELUM: Pronunciation: 'che-l&m, is Latin for airspace or sky. The Romans began questioning the rights they had in the space above the land they owned and to how high above did that right extended to. Ad coelum et ad inferos, they discussed, meaning that their right of property would extend as high up to the heavens and down to hell.

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### III EMLA Women Aviation Leaders, Latin America and Caribbean

On February 28, 2018 was held the III EMLA-Women Aviation Leaders, Latin America and Caribbean, organized by the International Aviation Women’s Association (IAWA). Abogados Sierra S.C. had the privilege to be one the sponsors of the forum.



The forum analyzed the current situation of the aerospace and aviation industries in Mexico and Latin America, and the new technologies out there that impact them. Aspects related to gender equality, the difficulties of recruitment and the inclusion of new generations were also addressed.

### IATA Legal Symposium 2018 Bangkok, Thailand

Abogados Sierra S.C., once again, has attended and sponsored the IATA Legal Symposium 2018 which was held from February 27 until March 1 2018 at the Shangri-La Hotel in Bangkok, Thailand. The IATA Legal Symposium is the world’s premier annual aviation law event, with a reputation for insight, relevance and value among in-house counsel, private practitioners and government lawyers alike. The event is well known for its engaging subject matter, outstanding speaker and lively debates.



## Assignment v. Novation – Local and International Aspects.

by Jessi Saba.

A thorough analysis regarding whether a lease assignment or a lease novation is the correct approach to conduct the transfer of rights of the lessor in respect of an aircraft lease has been published in previous Coelum editions. This article will cover the basic aspects of each legal figure, comparing the same under the light of Mexican law against the Cape Town Convention.

It is important to recognize that both figures fully recognize a transfer of rights, and Mexican law allows for the parties to freely draft their agreement (novation or assignment) without any mandatory provisions to be included; yet, each transaction must be analyzed individually to determine which figure fits best. The main difference between the two, is that a novation agreement supposes the termination of a previous obligation and the origination of a new one, while the assignment supposes only the transfer of rights from the assignor to the assignee, with the initial obligation sustained under the same contractual relation as initially agreed.

In contrast, the Cape Town Convention defines an assignment as a contract which, whether by way of security or otherwise conferred on the assignee associated rights with or without a transfer of the related international interest.<sup>1</sup> As a general rule (unless otherwise agreed by the parties) an assignment also transfers to the assignee the related international interest.<sup>2</sup> The Cape Town Convention does not define the term novation, therefore, in accordance with the Official Commentary to the Cape Town Convention, the determination of whether an agreement constitutes an assignment or a novation, should be interpreted from its nature without reference to applicable law, provided that national laws differ very much on this point.<sup>3</sup> As further guidance, the Official Commentary establishes the following<sup>4</sup>:

- A new agreement between all three parties (debtor, creditor, and assignee) which replaces the original agreement would constitute a novation.
- A transaction in which the creditor transfers its rights and related international interests without reference to its obligations would constitute an assignee.
- A 'hybrid' transaction is one in which the creditor assigns its rights under the agreement and transfers its obligations (totally or partially) would be considered as an assignment under the Cape Town Convention, regardless of the characterization given by national law as a novation agreement.

*“...a novation agreement supposes the termination of a previous obligation and the origination of a new one, while the assignment supposes only the transfer of rights from the assignor to the assignee, with the initial obligation sustained under the same contractual relation as initially agreed.”*

Going back to Mexican law, the consideration of whether an agreement constitutes an assignment, or formally a novation can also raise an issue regarding taxes.

A transfer of an aircraft between two foreign entities does not have any tax consequences in Mexico (no sales or use tax, VAT, capital gains or any other tax) unless (i) the country of residence of the parties involved in the transfer is Mexico, or (ii) the place where the payment obligations of purchaser must be fulfilled within Mexican territory. Additionally to the above, it must be considered that when material delivery of an aircraft is conducted within the territory of Mexico, the transaction would be considered to have

1.- Article 1(b) of the Cape Town Convention.

2.- Article 31 (1) (a) of the Cape Town Convention.

3.- Official Commentary to the Cape Town Convention. Paragraph 2.43

4.- Official Commentary to the Cape Town Convention. Paragraph 2.44

occurred within Mexican territory and would be subject to a 16% VAT. This same rate applies when (i) the title of transfer takes place between tax residents of Mexico, even if the aircraft is not located in Mexican territory at the time of transfer. In addition, article 10 of the VAT law, specifically states that the transfer of assets bearing Mexican registration marks will be considered to be conducted within Mexican territory even when such transfer is conducted outside of Mexico, as long as the seller is a resident of Mexico.

When the right of possession of an aircraft on the other hand is handed by lessor to lessee under a lease, the material delivery of the aircraft would need to occur outside of the territory of Mexico in order not to generate VAT on rental payments.

Therefore, when a novation agreement is entered into the extinction of the prior obligation (for this purpose, the original lease agreement) that is being terminated would occur to give way to a new obligation under a new lease agreement. The termination of the original lease, would imply the termination of the right of possession by the lessee or operator of the aircraft, and hence, the aircraft would implicitly be delivered again to the lessee by the assignee, or new lessor. A new delivery of the aircraft under the new lease agreement to be conducted within Mexican territory would cause VAT to be applicable to rental payments at a rate of 16%<sup>5</sup>. The assignment on the other hand, as it is only a mere transfer of the rights under the existing lease, does not imply its termination and the right of possession by the lessee or operator will not be interrupted. No tax consequences will exist therefore, even if the aircraft is located in Mexican territory at the time of the transfer.

The above described 'new delivery' that a novation would create would be considered to occur within Mexican territory even when the aircraft might be physically placed outside of Mexico for the purposes of closing. This is considering that while the aircraft can be physically outside of the country it would still remain registered in Mexico and temporarily imported by the original lessee. In other words, to prevent a new delivery being considered to be occurring, the aircraft would need to be 'physically' and 'legally' exported from Mexico before the new lease shall enter into effect.

Back to the international sphere, when registering an assignment or a novation at the International Registry, the implications are completely different. In respect to the assignment, a registration is made as an "assignment of international interest" and the associated file number of the original international interest to be transferred must be related at the time of the registration. On the other hand, when registering a novation agreement, the already registered international interest constituted by the original lease agreement, would have to be discharged, and a new registration evidencing the lease agreement between the assignee and lessee would need to be registered in order for a Priority Search Certificate to evidence the termination of the prior lease and the celebration of the new one.

Even though the Official Commentary states, as discussed above, that for Cape Town purposes the assignment and novation should be determined by their nature regardless of national law. Specifically, for the case of Mexico, a novation should always be expressly agreed between the parties as such, as a novation cannot be presumed by interpretation<sup>6</sup>, and when it shall be stated expressly this would give way to the potential tax risk described above.

In many instances, assignment agreements are entered into, registered as such with the Mexican Aeronautical Registry, only to be registered with the International Registry as novation agreements. Having contradictory registrations at local and international level is misleading, as the Priority Search Certificate for the corresponding aircraft would evidence the termination of a prior obligation and the celebration of a new one, while a local law search would state that an assignment of rights was effected. When celebrating an assignment, the proper way to register the same before the International Registry is to register an 'assignment of international interest' referencing the original international interest that is being assigned, rather than having the original one international interest discharged.

It is important to analyze the transaction deeply, and determine the figure that fits best, and keep all registration compatible in order to avoid any misinterpretation or misleading transaction information.

5.- Article 1 and 21 of the VAT Law ("*Ley del Impuesto al Valor Agregado*")

6.- Article 2215 of the Federal Civil Code: "*A novation is never presumed, it must be expressly stated*"

## **Mexico pondering placing armed U.S. air marshals on flights.**

After 9/11 attacks on the United States, Mexico agreed to place Mexican security agents on certain flights but said it would never allow U.S. officials on board its commercial airlines, let alone armed. Now both countries are studying the convenience of negotiating an agreement for the deployment of Federal Air Marshals on commercial flights. <https://www.reuters.com/article/us-usa-mexico-security-exclusive/exclusive-u-s-mexico-explore-placing-armed-u-s-air-marshals-on-flights-idUSKBN1FJ04J> February 01, 2018.

## **Airlines complain about Mexico passenger arrival fee increase read.**

Aviation industry groups are pressing Mexico's government to reverse a January fee increase for international passengers arriving in Mexico City, claiming it is hurting the airlines and the country's economic competitiveness. The International Air Transport Association (IATA) and the Latin America and Caribbean Air Transport Association (ALTA), which represent airlines, opposed the increase, saying it made the existing Mexico City airport less competitive. <https://www.channelnewsasia.com/news/business/airlines-complain-about-mexico-passenger-arrival-fee-increase-9943288> February 09, 2018.

## **Balanced Approach to Aircraft Noise Management.**

The Ministry of Communications and Transport published a draft of Official Mexican Standard (PROY-NOM-036-SCT3-2017) to regulate the maximum permissible noise limits produced by aircraft. It is an update to the current regulations that seeks to adapt the national regulation with international standards in the matter, derived from the operation of new generation aircraft. <http://a21.com.mx/normatividad/2018/02/13/mexico-busca-actualizar-norma-sobre-ruído-de-aeronaves> February 13, 2018.

## **Mexico's Ground Handlers Plan for Expansion.**

Over the years new companies have been created and some have specialized in different airport services such as security, catering, cargo, ground handling and passenger services, resulting in national record of more than 82 registered companies operating within the Mexico City International Airport. Like the rest of the aviation industry, aircraft ground handling in Mexico is experiencing significant growth in recent years and has resulted in more proficient services as a result of the growing competition. <http://www.aviationpros.com/article/12391494/mexicos-ground-handlers-plan-for-expansion> February 14, 2018.

## **Safran and Albany inaugurate third plant for LEAP engine in Mexico.**

Safran and Albany have inaugurated a third joint manufacturing plant in Mexico, to make composite parts for the LEAP aircraft engine. This third joint plant is similar to and complements the two existing plants in Rochester, New Hampshire (United States), and Commerce (eastern France), inaugurated in 2014. It involved a total investment of about US\$100m. <https://www.avitrader.com/2018/02/22/safran-albany-inaugurate-third-composite-fan-blade-production-plant-leap-engine-mexico/> February 22, 2018.

## Human Trafficking: Hidden In Plane Sight.

The participation of Youla A. Haddadin, Advisor on Trafficking in Persons to the Office of the United Nations High Commissioner for Human Rights (OHCHR), has opened the door to the development joint ICAO-OHCHR human trafficking cabin crew guidelines on training. This will help improve the understanding of why trafficking happens, what the various types of trafficking are, who the victims and traffickers are, and what signals might indicate a case of trafficking. Critically, this document will also provide cabin crew with the reporting and response procedures should they find themselves confronting a potential trafficking situation. <http://www.unitingaviation.com/strategic-objective/safety/preventing-human-trafficking/> February 23, 2018.

## Human capital, the next challenge for the aerospace sector in Mexico.

The Mexican aerospace sector, which has experienced accelerated growth in recent years, faces the challenge of guaranteeing the training and qualification of specialists and technicians in order to keep up with the rapid development of the Industry. Paradoxically, the growth experienced in recent years could lead to a crossroad if specialized engineers and technicians are not trained for the future. <http://a21.com.mx/aeronautica/2018/02/26/capital-humano-el-proximo-reto-del-sector-aeroespacial-en-mexico> February 26, 2018.

## Rise of aviation fuel will increase the prices of plane tickets.

The increase in the price of aviation fuel and the volatility in the exchange rate during 2017 had a negative impact on the profits of Mexican airlines. Fuel for aircraft increased 14.27 percent in 2017, compared to the 12.41 pesos per liter of the previous year. In 2015, the average price of jet fuel was 6.53 pesos, an increase of 90.05 percent, compared to last year. Fernando Gómez Suárez, analyst of the air sector, indicated that the increase of aviation fuel that affected Mexican airlines could impact an increase of up to 18 percent in plane tickets. <https://heraldodemexico.com.mx/mer-k-2/alza-de-turbo-sina-pega-las-aerolineas/> February 27, 2018.

## Gender equality, the challenge of the aeronautical industry in 2030.

Within the framework of the III EMLA-Women Aviation Leaders, Latin America and Caribbean held in Mexico City, industry leaders analysed the current situation of the aerospace and aviation industries in Mexico and Latin America, particularly with regards to the progress of implementation of resolution A 39-30 issued by ICAO. State efforts were shared in order to reach the industry goal of achieving equal participation between men and women by the year 2030. <http://a21.com.mx/aeronautica/2018/02/28/igualdad-de-genero-el-reto-de-la-industria-aeronautica-en-2030> February 28, 2018.

## Airline fleet orders, Mexico: Airbus order books continue to drive solid growth for LCCs.

Aircraft deliveries to Mexico's airlines should peak in 2018; CAPA's fleet database shows the country's airlines are projected to incorporate 52 aircraft in their respective fleets. Mexican low cost airlines are leading aircraft deliveries for 2018. Combined, those operators are scheduled to accept more than 30 Airbus A320neos. <https://centreforaviation.com/insights/analysis/airline-fleet-orders-mexico-airbus-order-books-continue-to-drive-solid-growth-for-lccs-403231> February 28, 2018.

*In this month extract was prepared by J. Estrada, C. Espinosa, L. Caballero, R. Figueroa and J. Dorantes.*

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