



VALIDITY UNDER ITALIAN LAW OF A BERMUDA MORTGAGE ON AN AIRCRAFT REGISTERED IN BERMUDA EXCERPT FROM A LEGAL OPINION AFTER THE BLUE SKY ENGLISH CASE

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ABSTRACT: The article is excerpted from a legal opinion is based on the Blue Sky English Case, under which the validity of a mortgage on an aircraft must be determined on the basis of the law in force in the country where the aircraft is located at the time of conclusion of the mortgage – and not on the basis of the law of the country of registration of the aircraft. On the basis of this assumption, the opinion addresses the validity under Italian law of a mortgage drafted under the laws of Bermuda. In particular, formal requirements of the mortgage are examined as well as its validity with respect to the Italian prohibition of the agreement of forfeiture.

KEYWORDS: Blue Sky Case, Mortgage, Aircraft, Mortgage by demise.

RESUMEN: El artículo se basa en una opinión profesional sobre el caso inglés "Blue Sky", según la cual la validez de una hipoteca sobre una aeronave debe determinarse sobre la base de la legislación aplicable en el país en que la aeronave se encuentra en el momento de la celebración de la hipoteca y no sobre la base de la legislación aplicable en el país de matrícula de la aeronave. Teniendo en cuenta estas premisas, la opinión se refiere a la cuestión de la validez en Italia de una hipoteca constituida en virtud de las leyes de Bermudas, sobre todo en relación con los requisitos formales de la hipoteca y con su validez en relación con la prohibición del acuerdo de confiscación.

PALABRAS CLAVE: *Blue Sky Case*, Hipoteca, Aeronave, Acuerdo de Confiscación.

1. *The facts*

AAA SA (the "Client") is the operator of one BBB aircraft with manufacturer's serial number CCC (the "Aircraft") pursuant to an operating management agreement dated DDD (the "Management Agreement") between the Client and EEE (the "Owner"), a Bermuda company.

In order to refinance the acquisition of the Aircraft, the Owner entered into a loan agreement with FFF Ltd. (the "Lender") dated GGG, as security for which the Owner granted the Lender a first priority mortgage over the Aircraft (the "Mortgage").

The Aircraft is Bermuda registered and the Mortgage is governed by Bermuda law and registered at the Bermuda Department of Civil Aviation.

The Owner is now in default under the loan agreement and also owes the Client approximately Euro HHH million under the Management Agreement. As a consequence, the Client has detained the Aircraft at III airport.

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2. The Blue Sky case

In the *Blue Sky One Limited and Others v Mahan Air and Another* case (the "Blue Sky Case") of 2010, the English High Court refused to apply the law of the State of registration of the aircraft and confirmed that the validity of an English law aircraft mortgage is to be determined by the law of the place where the aircraft is situated (the "*lex situs*") on the date that such English law aircraft mortgage is executed¹.

The High Court further explained that the reference to the *lex situs* is to the domestic law of the place where the aircraft is situated, and not to its entire law including its choice of law rules, so that the doctrine of *renvoi* does not apply.

This position contrasts the traditional view that the creation, validity and effects of voluntarily created rights in aircraft should be governed by the laws of the "flag State". This view was rooted in the fact that the aircraft has a real connection with the state of registry. Moreover, aircraft by their own nature change location between different jurisdictions and, therefore, application of the laws of the "flag State" allows a much easier criterion to select applicable law than the *lex situs*.

This decision has been criticized, therefore, "as extensive legal research has established the opposite. The *lex rei sitae* conflict of laws rule finds no support at all in specialized English writings dealing with aviation financing law"². Some authors and practitioners believe that this decision may even be overruled in the next future.

However, if one is to consider the *Blue Sky* case as an applicable authority, it seems that, notwithstanding the selection of a specific governing law of the mortgage deed, the English courts (and any court applying English law) will

¹ [2011] All ER (D) 107 (May); [2010] EWHC631 (Comm). The case may be read on the internet at <http://www.bailii.org/ew/cases/EWHC/Comm/2010/631.html>. This case related to several Boeing 747-422 aircraft. One of the aircraft was owned by an English special purpose company and was leased to an Armenian company, Blue Airways LLC. The latter was registered with the Armenian Civil Aviation Authority. The aircraft was then chartered to Mahan Air, an Iranian company. The English special purpose company subsequently mortgaged the aircraft in favour a US Company. The mortgage deed was expressed to be governed by English law but was entered into at a time when the aircraft was physically situated in the Netherlands.

² Honnebier (2012), "The devastating 'Blue Sky' judgment compels the member states of the European Union to adopt the Cape Town convention", *Aviation & Space Journal*, 2/2012, p. 13. See also: Honnebier (2011), "The English Blue Sky Case about the Enforcement of Aircraft Mortgages and its Impact on the Global Financial Market", *Zeitschrift für Luft- und Weltraumrecht*, 1/2011, p. 47; Id. (2012), "The Netherlands is blacklisted due to its ambiguous aviation financing laws and only the Cape Town Convention can solve this problem", *Journaal LuchtRecht/Netherlands Journal of Aviation Law (JLR)*, 2/2012, p. 48; Id. (2011), *Rectified contribution to Contemporary Issues and Future Challenges in Air and Space Law*, Leiden, November 2011; Id. (2011), "The English "Blue Sky" case Shows that the Aircraft Finance Practice Needs Uniform International Substantive Mortgage Laws as the Existing Conflict Rules Fail", *Tijdschrift Vervoer & Recht*, 2/2011, p. 70; Wilberforce (1948), "The international recognition of rights in aircraft", *International Law Quarterly*, 2/1948, p. 425; Lalive (1955), *The Transfer of Chattels in the Conflict of Laws, treatise*, Cambridge University Press, Cambridge, p. 191; Goode (2007), *International interests in mobile equipment and the Cape Town Convention and Aircraft Protocol: adding a new dimension to international law-making*, in Id., *Transnational commercial law: text, cases, and materials*, Oxford University Press, Oxford, p. 434. Cuming (1989), *International regulation of aspects of security interests in mobile equipment*, UNIDROIT, Study LXXII, pp. 16 and 38.

assess the validity and enforceability of a mortgage deed under the laws of the jurisdiction where the aircraft is located³.

3. *Opinion required*

Given that the judgment in the Blue Sky Case will be persuasive (even if not binding) in the courts of Bermuda, and given that at the time of execution of the Mortgage the Aircraft was situated in Italy, the Client asked advice as to whether the Mortgage will create a valid security interest over the Aircraft under Italian law.

The following opinion is limited only to the object as defined in this § 3 and will not, therefore, deal with any other issue that may arise with respect to the said mortgage, its validity under other legislations, its extension, its object, its enforcement *etc.*

4. *Legal Opinion*

Based on the foregoing and having regard to the relevant laws of Italy, we are pleased to render the following opinion.

4.1. *Nature of the mortgage*

Under art. 1027.1 of the Italian Code of Civil Navigation, “*on aircrafts is only possible to register voluntary mortgages*”⁴.

The Mortgage Deed is vested into a deed between the parties and is, therefore, a “voluntary mortgage” under Italian law.

4.2. *Form of the mortgage*

Under art. 1027.2 of the Italian Code of Civil Navigation “*a mortgage may be created only by public deed or private written deed containing the specific particulars to identify the aircraft*” (on the specific issue relating to the authentication of the private written deed see below, under § 4.3.2).

In case of violation the mortgage would be null and void (see also art. 2821.1 of the Italian civil code). Under art. 750.3 of the Italian Code of Civil Navigation, the identification of an aircraft is made by reference to its registration marks and manufacturer’s serial number.

³ On this issue see also Dicey, Morris & Collins (2006), *The Conflicts of Law*, 14th ed., Sweet & Maxwell, London, and in particular Rule 120, Exception 2, under which a civil aircraft may be deemed to be situated in its country of registration if the aircraft is “*either over the high seas or over or on territory which is not under the sovereignty of any State*” at the time the mortgage is created (the so-called “Dicey Morris exception”). An Author points out that “*as there is no Bermuda... or English case law specifically on this point, options 3 and 4 are not without risk*” (McLean, “A Year Later: the Practical Consequences of Blue Sky One Limited”, which may be read on the internet at http://www.conyersdill.com/publicationfiles/229_11_04_26_A_year_later_the_practical_consequences_of_blue_sky-one_limited.pdf, April 2011, p. 2).

⁴ Marini (1996), “Sul principio della volontarietà nell’ipoteca navale”, *Trasporti*, 68/1996, p. 91; Fragali (1965), “L’ipoteca penale e l’ipoteca sull’aeromobile”, *Dir. Aereo*, 1965, p. 1. See also Spasiano (1972), “Ipoteca navale e aeronautica”, *Enc. Dir.*, XXII, p. 873; De Marchi (1987), “L’ipoteca navale: considerazioni e raffronti con l’ipoteca immobiliare”, *Vita not.*, 1987, p. 63; Righetti (1992), “Ipoteca navale ed aeronautica”, *Dig. Comm.*, VII, p. 535; Berlingieri, *I diritti di garanzia sulla nave, l’aeromobile e le cose caricate*, Cedam, Padova, 1965, pp. 282 ff.; Ripert (1952), *Droit maritime*, 4th ed., II, Dalloz, Paris, pp. 9 ff.

The Mortgage Deed is vested in a written document that clearly identifies the Aircraft and therefore it complies with the said requirement so it complies, under this profile, with Italian law.

4.3. Registration requirements

Under Italian law (art. 1030 of the Italian Code of Civil Navigation) a mortgage is validly constituted only after it is registered in the relevant public registry and recorded in the registration certificate (on the specific issue relating to the record on the registration certificate see below, under § 4.4).

If a mortgage deed is not registered in the relevant registry, no mortgage is created either against third parties or between the parties to the mortgage deed⁵.

This rule raises two different questions.

4.3.1. Relevant registry

The first question relates to the relevant registry where the mortgage is to be registered.

As a matter of fact, under Italian law a mortgage on an aircraft is to be validly registered in the Italian “Registro Aeronautico Nazionale – RAN” (i.e.: National Aeronautic Registry), which is managed by the “Ufficio Registro Aeromobili – URA” (i.e.: Aeronautic Registry Office) within the “Ente Nazionale per l’Aviazione Civile – ENAC” (i.e.: the Italian Civil Aviation Authority).

However it is our view that this requirement of Italian substantive law does not have any relevance with respect to the principles expressed in the Blue Sky case. As a matter of fact, under Italian law the valid constitution of a mortgage requires the mortgage deed to be registered in the relevant public registry – which happens to be the Italian RAN if the aircraft bears Italian marks⁶.

There is no doubt that, in accordance with Italian law, a mortgage filed in a foreign public registry (where the aircraft is firstly registered) would be recognised as valid and effective *even if that same mortgage is not registered in the Italian RAN*.

A final consideration on this point. The Blue Sky doctrine would be useless if it required, for a mortgage to be valid, to be registered with the aviation authority of the State where the aircraft was located at the time of execution of the mortgage deed. Any national registry, in fact, allows registration of a mortgage only insofar as it refers to an aircraft registered in that same national registry and bearing that nation’s registration marks.

Therefore, it is our view that it is not necessary that the Mortgage Deed under reference is registered in the Italian RAN in order for the mortgage to be valid and effective and that the registration in the Bermuda Register is compatible with such validity and effectiveness.

⁵ Spasiano (1972), “Ipoteca navale”, in *Enciclopedia del diritto*, XXII, Milano, p. 885; Rubino (1956), “L’ipoteca immobiliare e mobiliare”, in Cicu & Messineo (eds.), *Trattato di diritto civile e commerciale*, XIX, Milano, pp. 212 ff.; Pugliatti (1957), “La trascrizione. La pubblicità in generale”, in Cicu & Messineo (eds.), *Trattato di diritto civile e commerciale*, XIV-I, t. I, Milano, pp. 432 ff.; Berlingieri (1965), *I diritti di garanzia sulla nave, l’aeromobile e le cose caricate*, Cedam, Padova, pp. 272 ff.

⁶ Art. 1031 of the Italian Civil Navigation Code clearly states that “request for publication must be filed with the office where the aircraft is registered”.

4.3.2. The requirement of authentication of the private written deed

The second question raised by the principle set forth above under § 4.3.1 relates to the requirements provided under Italian law for registration of the mortgage.

Under Italian law a private deed is not sufficient to validly create a mortgage, since such a validity depends on the registration of the mortgage deed in the Italian RAN and the Italian RAN does not accept filing of private deeds if the signature of the parties thereto is not “legally ascertained” – i.e.: are not authenticated by a Notary Public (or equivalent officer).

We note that neither the Entry of Priority Notice or the Entry of Aircraft Mortgage appear to include a formal authentication of the signature of Mr JJJ, on behalf of FFF Ltd.

It is a question of Bermuda law whether the apposition of such signature in front of a DCA officer equals the authentication of the signature by a Notary Public (or equivalent officer).

In this connection, however, it might be relevant to clarify if the lack of such authentication may be considered as a formal irregularity of the Mortgage Deed under Italian law.

We note that in Italian law the authentication of the signatures is not a requirement of validity of the Mortgage Deed but it is only a condition for the mortgage to be filed in the Italian RAN, instead.

This is clear under art. 2702 and 2703 of the Italian civil code, where it states that authentication is only one of the techniques allowed to have legal certainty of the author of the signature (the other being, for example, the recognition of the signature by its author, under art. 2702 of the Italian civil code) but is not a requirement for the validity of the deed⁷.

The Italian ENAC clearly recognises this principle in its day-by-day activity. Mortgage deeds for aircrafts entered into in international practice are usually long several tens of pages and are written in English and their filing with RAN would request them to be translated into Italian. Therefore, the Italian ENAC allows the parties to file with the RAN only a so-called “short form” mortgage, in Italian, duly authenticated, only for the purpose of the registration of the mortgage. Allowing this practice ENAC recognises that the requirement of authentication is not provided for the validity of the mortgage deed but only for the document to be filed and that, therefore, it relates to the rules of functioning of the ENAC instead of the rules of validity of the contract.

Given that the competent registration authority is the Bermuda DCA, Italian law only requires, for the mortgage to be valid and effective, that the Mortgage Deed is registered in the relevant register and does not question whether filing in that register imposed requirements that may not correspond to what is required for filing a mortgage with the Italian RAN (which relates to the functioning of the office, not to the validity of the mortgage).

Therefore, we believe that there was no need that the signatures of the parties in the Mortgage Deed under reference were authenticated by a Notary Public (or equivalent officer) in order for the mortgage to be valid and effective,

⁷ Cass., 7 July 1988, n. 4469, *Giur. it.*, 1989, I, 1, p. 258, holding that “the transfer of immovable assets by a private deed without authentication of the signatures is valid between the parties but ineffective as regards the registration in the applicable registry”; Cass., 26 November 1971, n. 3445.

since the deed was, eventually, registered in the relevant register (The Bermuda DCA).

4.4. Record on the registration certificate

We do not have evidence that the mortgage was recorded in the registration certificate of the aircraft (which is required by art. 1030 of the Italian Code of Civil Navigation, as noted above, under § 4.3). We assume it was.

However, even if it was not, the lack of record in the registration certificate would not deprive the mortgage of its validity and effectiveness.

In fact, under art. 869.2 of the Italian Code of Civil Navigation, it is possible that at the moment of filing of the mortgage, the registration certificate is not delivered to the ENAC (this happens if the aircraft is currently elsewhere). In this case, the mortgage is considered as validly created and the law only requires that the record on the registration certificate is made in a further moment.

As a matter of fact, the creation of the mortgage only requires its registration in the registry (art. 870 and 256 of the Italian Code of Civil Navigation) and the recording in the registration certificate is only the compliance with a specific obligation with respect to a mortgage already created.

4.5. Consequences of the (supposed) contrast with the Italian discipline of the “*patto commissorio*”

As far as this opinion is concerned, the *Blue Sky* case dealt with the validity of a mortgage deed shaped following English law but governed by Dutch law. Here the problem is that under English law it is allowed to mortgage a property by conveying it to the creditor, with a condition that the property will be returned on redemption. Mortgage deeds are drafted accordingly⁸.

In most civil law jurisdictions, on the other hand, such a mortgage by a conditional transfer of ownership would be invalid under the prohibition of the so-called “*patto commissorio*” (“*pacte comissoire*”) – notwithstanding such a prohibition appears to be declining as a consequence of international commercial law and practice⁹.

⁸ This is referred to as a “mortgage by demise”, where the mortgage is transferred, by the mortgagor, ownership of the mortgaged property. Once the loan is repaid or other mortgage obligations are fulfilled, the mortgagor has a right to be returned the mortgaged property. Mortgages by demise were the original form of mortgage, and continue to be used in many jurisdictions, and in a small minority of states in the USA. Many other common law jurisdictions have either abolished or minimised the use of the mortgage by demise – as it happened in England and Wales as regards registered interests in land (see sect. 23 of the Land Registration Act 2002).

⁹ This was noted, as regards Italian law, by Alb. Candian (2005), “Le garanzie finanziarie dopo il d.lg. 170/2004”, in Berlingieri (a cura di), *Temi e problemi della civilistica contemporanea. Venticinque anni della Rassegna di diritto civile*, ESI, Napoli, 40. The best evidence of such a tendency comes from France. The Code Napoléon, that was the model for the Italia prohibition of the “*patto commissorio*” [Bussani (2000), *Il problema del patto commissorio*, Giappichelli, Torino, pp. 6 ff. and 97 ff.], was recently amended by the *ordonnance n. 2006-346 du 23 mars 2006 relative aux sûretés*, so that now the *pacte comissoire* is allowed. Under art. 2348.1 of the French *Code Civil*, in fact, “*il peut être convenu, lors de la constitution du gage ou postérieurement, qu'à défaut d'exécution de l'obligation garantie le créancier deviendra propriétaire du bien gagé*”. The law provides, however, that the creditor cannot enrich out of the *pact comissoire*. Therefore, art. 2348.2 of the French *Code Civil* provides that, at the time of transfer, the conveyed asset must be estimated by the parties or an expert appointed by the

In Italy there exists a prohibition of the “patto commissorio” with respect, among others, to mortgages: “it is null and void any agreement under which, if payment is not made within the agreed term, ownership of the mortgaged asset is transferred to the creditor ...” (art. 2744 of the Italian civil code)¹⁰.

It is true that art. 5.3(c) of the Mortgage Deed, read along with art. 8.2(k) and 9 (Receivership), under some profiles may be found to violate the “divieto del patto commissorio”, if one interprets the powers of the Receiver as including also the power to acquire ownership of the mortgaged asset.

Art. 8.2(d) of the Mortgage Deed, however, confers the right “to sell, call in, collect and convert into money the Aircraft with all such powers in that respect as are conferred by applicable law ...” and appear, therefore, in compliance with the law.

It is necessary, therefore, to assess if any invalidity of art. 5.3(c), 8.2(k) and 9 may affect the validity of the Mortgage Deed.

Under Italian law nullity may affect either the whole contract or a single part thereof.

In particular, the contract is null if the nullity affects the contract as a whole (e.g.: it lacks the required form under art. 1418.2 and 1325 of the Italian civil code). This is not the case here, because the violation of the “divieto del patto commissorio” is limited to single clauses and in itself does not affect the Mortgage Deed as a whole and in its function.

In the other cases, the nullity affects only the relevant single clause within a wider contract (art. 1419 of the Italian civil code) – as it is the case here, where the violation of the “divieto del patto commissorio” is included, as a severable provision, in the wider Mortgage Deed.

court (“la valeur du bien est déterminée au jour du transfert par un expert désigné à l'amiable ou judiciairement”). If the debtor fails to repay and the creditor keeps ownership of the asset, under art. 2348.3 of the French *Code Civil* the difference between the value of the asset and the guaranteed amount must be returned to the debtor (“lorsque cette valeur excède le montant de la dette garantie, la somme égale à la différence est versée au débiteur ou, s'il existe d'autres créanciers gagistes, est consignée”). It is to be noted, incidentally, that under Italian law the creditor may keep the asset mortgaged only if the estimation is made after the debtor defaults (so called “patto marciano”). If an estimation is provided at the time of transfer, the agreement is null unless the debtor is allowed to prove that the value of the mortgaged asset at the time of default is different from that at the time of transfer. On French law after the *ordonnance n. 2006-346* see Briolini (2007), “La riforma del diritto delle garanzie in Francia”, in *Banca, borsa e titoli di credito*, 2007, II, p. 226; Fiorentini (2006), “La riforma francese delle garanzie nella prospettiva comparatistica”, in *Europa dir. priv.*, 2006, p. 1155; Simler (2006), “La réforme du droit des sûretés”, in *La semaine juridique*, n. 13, 2006, p. 124.

¹⁰ On the “divieto del patto commissorio” see Anelli (1996), *L'alienazione in funzione di garanzia*, Giuffrè, Milano; C. M. Bianca (1957), *Il divieto del patto commissorio*, Giuffrè, Milano; Alb. Candian (1999), “Appunti dubbiosi sulla “ratio” del divieto di patto commissorio”, in *Foro it.*, 1999, I, c. 175; Carnevali (1982), “Patto commissorio”, in *Enc. dir.*, XXXII, Milano, p. 505; Bussani (2000), *Il problema del patto commissorio. Studio di diritto comparato*, Giappichelli, Torino; Cipriani (2000), *Patto commissorio e patto marciano. Proporzionalità e legittimità delle garanzie*, ESI, Napoli; Di Paolo (1995), “Patto commissorio”, in *Digesto (disc. priv.)*, Utet, Torino, pp. 309 ss.; Girino (1991), “Garanzie sui finanziamenti: le insidie del patto commissorio”, in *Amm. e fin.*, 1991, 15, p. 819; Lojacono (1952), *Il patto commissorio nei contratti di garanzia*, Giuffrè, Milano; Luminoso (1990), “Alla ricerca degli arcani confini del patto commissorio”, in *Riv. dir. civ.*, 1990, I, p. 219; Sassi (1999), *Garanzie del credito e tipologie commissorie*, ESI, Napoli.

When one peruse the capability of an incidental “patto commissorio” to affect the validity of the whole Mortgage Deed, one realizes that in Italian legal theory two alternatives are proposed.

Under art. 1419.2 the nullity of the single clause could never determine the nullity of the whole contract since the “patto commissorio” would be automatically substituted by the legal provisions applicable to the mortgage (i.e.: artt. 2808 ff. of the Italian civil code) and by the discipline of “divieto del patto commissorio” itself (art. 2744 of the Italian civil code), in application of art. 1339 of the Italian civil code (“*clauses ... imposed by the law ... are included in a contract by law, even in substitution of clauses agreed by the parties which do not comply with the clauses imposed by the law*”)¹¹.

Under the art. 1419.1 the nullity of the single clause could determine the nullity of the whole contract if, and only if, it is proved that both parties would have not created the mortgage without the “patto commissorio”¹². We did not receive any direction in this sense, in our telephone conversation I anticipated this point and received no instructions with respect to this hypothesis and, moreover, this case seems quite academic in the context of a mortgage.

As regards the issue of the violation of the “divieto del patto commissorio”, therefore, we note that the violation of the “divieto del patto commissorio” applicable to single clauses of the Mortgage Deed, if any, would not affect the whole deed that would, therefore, remain valid and effective as a whole – the relevant clauses being substituted by the legal discipline of mortgages and narrowed by the legal “divieto del patto commissorio”.

For the sake of completeness, we highlight that some Authors believe that the creditor would be entitled to oppose an *exceptio doli* (an equitable remedy against fraud) against the debtor who tried to have the mortgage deed declared null and void only because of the “patto commissorio” contained therein¹³.

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¹¹ Pratis (1976), “Della tutela dei diritti – dei privilegi”, *Commentario del codice civile*, II, Utet, Torino, p. 95.

¹² Andrioli (1955), “Della responsabilità patrimoniale”, in Galgano (ed.), *Commentario del codice civile Scialoja-Branca*, 2nd ed., Roma, p. 53.

¹³ Roppo, *Trattato Rescigno*, 2nd ed., XIX, Utet, Torino, 1985, p. 573.