



By Devendra Pradhan

# Aviation Industry in Nepal

## Need to adhere to Geneva and Cape Town Conventions

**I**n 2007, Nepal earned a gross foreign exchange of US\$230 million from tourism sector which makes tourism one of the major foreign exchange generating industries in the country. Needless to say that tourism plays a significant role in the economic growth of the country. Being a landlocked country wherein 64 percent of the total land area is hilly or mountainous, air transport is the only reliable mode of transportation for domestic and international travel.

Nepali civil aviation industry has a troublesome history. The national flag carrier Nepal Airlines Corporation (NAC) that has been in the business for about half a century has very controversial history. It had a monopoly over the domestic sector for three and half decades. Despite that NAC failed to create and protect a niche in the market. While the national flag carriers of other countries that started in the same decade with NAC (such as Thai Airways International and Singapore Airlines) have emerged as the most prestigious air carriers internationally, the NAC's situation is degrading day-by-day and it is in a shambles now. NAC has only two jet aircraft in its fleet compared to Thai International's more than eighty-five and Singapore Airline's more than one hundred.

Even private sector airlines, except a few, do not have an exciting track record. With the collapse of once well operating airlines like Nepal Airways, Necon Air, Everest Air, Lumbini Airways and Shangrila Air within the past fifteen years, a big question arises: who is to blame for the sorry state of the aviation industry of the country? the government? or the private sector? The records indicate that those private sector airlines that have collapsed were, at some point, the most successful airlines as they were also the highest tax paying domestic airlines.



### Regulation

Air transport service is one of the highly regulated areas anywhere in the World. International laws relating to civil aviation are very complex. The civil aviation laws of the country must comply with the guidelines and requirements of International Civil Aviation Organisation (ICAO).

But Nepal's Ministry of Tourism and Civil Aviation (MoTCA) has shown a total disregard towards civil aviation sector despite a vital role this sector plays in the national economy. Except for enacting a National Civil Aviation Policy and few basic civil aviation legislations, the government has failed to provide proper attention towards the promotion of civil aviation sector. The government introduced the first Civil Aviation Policy in 1993 and implemented an "open sky policy" encouraging private sector participation in the aviation sector. In 2006, the government introduced a revised Civil Aviation Policy that adopts a "liberal sky policy" and encouraged private participation through domestic

and foreign investment in the area of air transport operation by allowing foreign investment up to 80 percent in the international sector and up to 49 percent in the domestic sector. The new Policy aims to develop Nepal as a regional air transit hub for Asia and the Asia-Pacific region.

The new Policy envisages for such changes in the civil aviation sector that if they are achieved, no doubt, the Nepali aviation industry would be one of the best in the Asian continent. However, it is too good to be true. The MoTCA has not done anything remarkable in this sector to achieve the goals prescribed by the Policy.

Nepal is facing the challenge of developing a new international airport equipped with modern facilities. With the increasing number of domestic airlines and tremendous increase in air traffic in the past few years, the only international airport (though it does not deserve this adjective due to the infrastructure and facilities not available there) of the country (Tribhuvan International Airport –TIA) is not going to be able to handle the air traffic in near future. For one the 10,000 feet runway is too small. Also the apron has a capacity to handle not more than 10 jet aircraft. Except for an ADB's technical assistance project (financed by the government of Japan) to evaluate the capacity of airports of Nepal, there is no project in pipeline for construction of another international airport. It is certain that Nepal will not see another international airport at least for another half a decade and will have to rely on TIA. In such situation, it is questionable whether the government would really be able to develop Nepal as a regional transit hub for Asia and the Asia-Pacific region as sought by the Policy. The government should focus on the plans and programs which are technically feasible and practically achievable.

The only regulatory body of this sector, the CAAN, set up in 1998 as an autonomous body to administer and regulate overall civil aviation in the country and to make air transport safe, regular, standard and efficient, also failed to make any noteworthy contribution to achieve the goals sought by the Policy and implement the aviation laws of the country in its a decade-long existence. Except for promulgating few basic regulatory manuals required by the ICAO, the CAAN has failed to make any advancement in the civil aviation sector. It has been too late for the CAAN to act towards protection of air passengers' rights and to implement directives and guidelines in the area of Passengers' Bill of Rights, lost and damaged baggage,

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handicapped access, compensation for delayed flights and cancelled flights, charter flights etc. While the civil aviation regulatory bodies of other countries (as well as their other regulatory bodies) routinely publish their directives and regulatory materials on their website for public use and information as a part of their duty to the public, it is very surprising that the CAAN, which has a duty to inform people about the development of the civil aviation in the country, charges hefty fees in US dollars from the public to issue copies of regulatory materials.

Nepal has lost internationally credible airlines like Lufthansa, Austrian Airlines, Singapore Airlines and some other airlines that used to fly into Nepal in the past. Both the MoTCA and the CAAN have failed to put enough endeavour to attract other credible international airlines into the country. Neither the MoTCA nor the CAAN seems to have a definite plan and programme for the near future which is technically feasible and practically achievable.

**Creditworthiness**

Creditworthiness of domestic airlines (except a few) in the international aviation industry is not impressive. Nepali civil aviation industry has seen sudden rise and sudden demise of several domestic airlines in the past. Almost all of the domestic airlines that collapsed in the past had trouble in financial dealing with the foreign aircraft leasing companies. While the laws of other developed jurisdictions primarily protect the interest of aircraft owners in asset-based aircraft lease transaction, Nepali civil aviation laws do not provide adequate protection to foreign aircraft owners and leasing companies. Foreign aircraft leasing companies find the Nepali market very risky and take great deal of caution in putting their valuable machine in the hands of Nepali air service operators. To make the matter worse, our judiciary including the Supreme Court, has been passing interim orders against foreign aircraft owners and leasing companies preventing them from taking possession of their aircraft from the defaulting domestic operators and to take those aircraft back from Nepal upon termination of the aircraft lease agreement. We have seen such examples in the past in the case of *AerCap Ireland Ltd. v. Cosmic Air Pvt. Ltd.* and *AerCo Ltd. v. Cosmic Air Pvt. Ltd.* Our honourable justices must take consideration of

international legal practices and also must make themselves adequately familiar with the legal aspects relating to cross-border asset-based aircraft financing and leasing transactions while dealing on such sensitive issues and passing an order that would adversely impact the faith on our judicial system in the international field. The domestic air service operators had already been experiencing loss of credibility in the international aviation market, our judiciary's action in the above-mentioned litigations certainly gave a blow to the development of aviation industry in the country. Now it will certainly take a great length of time for our aviation industry to regain the confidence in the international aviation market. Recent departure of Air Arabia, from the only cross-border joint venture airline company in the country, from the Nepali sky after a short duration of time is another major setback for Nepali aviation industry.

Despite the troubled history, the Nepali aviation industry has huge potentials. The problem of domestic aviation industry is not the lack of adequate domestic and international market but it is the lack of availability of enough number of aircraft. Unlike other industries, operation of an airline requires a huge investment.

But Nepali private sector airlines are not financially capable enough to purchase jet aircraft through their own investment. Except for consortium loan by few domestic commercial banks that financed aircraft purchase by a domestic airline, our domestic airlines are solely relying on leasing of aircraft from foreign aircraft owners and leasing companies. At the bright side, amidst such troubled domestic aviation market, Buddha Air was able to secure financing from the international institution like IFC which is noteworthy indeed.

### **International Conventions**

The MoTCA and the CAAN certainly must take immediate steps to preserve the integrity of aviation industry of the country in the international market. First, they must implement adequate legal measures so that foreign aircraft owners and leasing companies feel comfortable leasing their aircraft in Nepali aviation market. Second, a proper regulation must be enacted immediately under the aviation

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laws creating provision for a separate National Registry within the CAAN for registration of conveyances, bills of sale, mortgages, contracts, and other instruments affecting interest in or title to an aircraft for the purpose of recording and obtaining a lien on aircraft. The provisions of recording of deed and mortgages under the Civil Code with the local Land Revenue Offices cannot fulfil the purpose of asset-based financing like aircraft sale and financing. For this purpose, Nepal must ratify and adhere to the Geneva Convention on the International Registration of Rights in Aircraft. Finally, the government must ratify and adhere without any delay to the Convention on International Interests in Mobile Equipment and the Protocol to Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment (collectively known as the "Cape Town Convention"). The Cape Town Convention applies to the sale, financing and leasing of aircraft, aircraft engines and helicopters. This Convention has been enforced in order to provide adequate assurance primarily to lessors that the assets that they have leased or financed will be secured by a guaranteed security interest with international recognition. The Cape Town Convention creates an international interest that is recognised in all contracting states and provides creditors with a range of default remedies. This Convention creates a uniform international regimen facilitating

the creation, perfection and enforceability of security interest, title reservation and leasing rights in aircraft, aircraft engines and helicopters.

The Cape Town Convention is not only beneficial to lessors but is also beneficial to lessees. It is more beneficial to developing countries like Nepal where the existing legal regimes may not currently be sufficiently responsive to the need of creditors to feel secure. Several banks including the US Exim Bank have announced a discount on asset-based aircraft financing in countries that sign, ratify and implement the Cape Town Convention. Ratification of the Convention would be an excellent gesture from the government of Nepal to clear the gloomy image of Nepali aviation industry in the international aviation market.

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