REPORT

Toronto, Ontario
August 22, 2001
(Updated February 28, 2002)

I - INTRODUCTION

A – Request to the ULCC

[1] In August 2000, the Department of Justice of Canada sought the assistance of the Uniform Law Conference of Canada (ULCC) to prepare a uniform act to implement both the *Convention on International Interests in Mobile Equipment* (hereinafter the *Convention*) and the *Protocol on matters Specific to Aircraft Equipment* (hereinafter the *Aircraft Protocol*).

[2] At the time of the request, the texts of the *Convention* and *Aircraft Protocol* were still being negotiated and it was anticipated that the instruments would be submitted to a Diplomatic conference that was likely to take place in South Africa in May 2001. On that basis, it was agreed that it was possible to complete the uniform act for presentation at the ULCC in August 2001 while taking into account the final version of *Convention* and *Aircraft Protocol* as adopted by the Diplomatic conference. The ULCC agreed that it was appropriate to start working on this project as soon as possible since: (1) it is a high priority for Canada; (2) that Canada has been a leader in this project since the beginning; and, (3) that it was important not to loose the momentum resulting from the five Canadian-wide consultations undertaken by the Department of Justice in order to move as quickly as possible into implementation.

[3] The Working Group started its work on that basis on February 15, 2001. On March 13, 2001 the ICAO Council decided to hold the Diplomatic conference from October 29 to November 16, 2001. Further to this turn of events, it was decided to carry on the work undertaken. The project could be presented to the ULCC in August 2001 and submitted for adoption subject to a date after the Diplomatic Conference after a new version of the uniform act incorporating modifications resulting from the Diplomatic conference would have been distributed to ULCC jurisdictional representatives.

[4] A Diplomatic Conference held from October 29 to November 16, 2001 finalised and adopted a *Convention on International Interests in Mobile Equipment* and a *Protocol on Matters specific to Aircraft Equipment*. The Working Group resumed its work on the Uniform Act in order to adapt it to the final texts of the *Convention* and *Aircraft Protocol*.

B – Mandate of the Working Group

[5] The mandate of the Working Group was to draft in both official languages and mindful of Canada's two legal traditions – Civil Law and Common Law – a uniform act to implement the *Convention* and the *Aircraft Protocol* in Canada. A draft uniform act was presented at the ULCC's August 2001 Annual Meeting for discussion and adoption subject to a date after the

Diplomatic Conference. The draft Uniform Act has been revised in order to take into account the changes made to the *Convention* and *Aircraft Protocol* at the Diplomatic Conference. The Working Group'mandate was to contemplate drafting a uniform act that could allow the inclusion of additional Protocols (*i.e*., Railway Rolling Stock and Space Objects Protocols). The instructions given to the Working Group to draft this uniform act included providing comments or explanations for each provision of the act and also preparing a Working Group Report. The Report should describe the *Convention* and the *Aircraft Protocol*, the methodology followed to implement them, including an assessment of the declarations and options allowed under the terms of the *Convention* and *Aircraft Protocol* and recommendations as to the options available to Canada under both instruments at the time of accession.

II – OVERVIEW OF THE CONVENTION AND THE AIRCRAFT PROTOCOL[1]

A – Historical Background

[6] This project is the result of a proposal by Mr. T.B. Smith Q.C., formerly with the Department of Justice of Canada and the Canadian member of the Governing Council of Unidroit, shortly after the conclusion in Ottawa of both the 1988 Unidroit Convention on International Financial Leasing and Convention on International Factoring. Studies by Professor Ronald C. Cuming, University of Saskatchewan College of Law, and Unidroit established both the need for and the feasibility of such project. Thus in 1992 a study group was set up by the Governing Council of Unidroit to carry the project forward.

[7] In early 1999, the texts of the Convention and Aircraft Protocol were submitted for review to a Joint Unidroit-ICAO Session of governmental experts. The Session met in Rome, February 1st-12, 1999, in Montreal, August 24 to September 3, 1999 and in Rome, March 20-31, 2000. The texts of the instruments were then submitted for review to the Legal Committee of ICAO sitting in Montreal, August 28 to September 8, 2000. The texts were adopted at a Diplomatic Conference hosted by South Africa in Cape Town, October 29 to November 16, 2001.

B – The Project and its Contexts

1 – General Thrust and Principal Features of the Project (par. 10-11)

[8] The purpose of the Convention is to facilitate and thereby encourage international asset-based financing, *i.e.* financing using the value of property and most commonly of equipment as security for payment thus reducing financial risk and costs and making greater levels of credit available. In general terms the Convention/Protocol provides rules for the constitution and

[1] The text found under this title, more specifically under titles B-C, is drawn from paragraphs 10-173 of the Report of the Rapporteur on International Interests in Mobile Equipment (Aircraft Equipment) tabled at the 31st Session of the Legal Committee of the International Civil Aviation Organisation, Montreal, 28 August - 8 September 2000, LC/31-WP/3-4 (23/06/00) and updated by the Working Group to take into account the changes made to the *Convention* and *Aircraft Protocol* at the Diplomatic Conference (it is not an official commentary on the Convention and Protocol). The paragraph numbers in parentheses beside sub-titles refer to paragraph numbers found in the Report of the Rapporteur.

effects of international interests in aircraft equipment. It provides in effect a substantive internationally endorsed regime for asset-based financing in respect of aircraft equipment.

[9] The Convention establishes rules designed to be applicable to international interests in a number of categories of equipment. The term "international interest" (or in French, "*garantie internationale*") is used in the Convention/Protocol to designate an interest or right in an object which is conferred by a person who is in fact in the position of a debtor. That right is intended as security for the payment of a debt, in other words it is intended to guarantee payment. Although typically created under domestic law, to qualify as an international interest, the interest must meet certain Convention standards. The Convention is concerned with three types of international interest:

1) those granted under a security agreement;
2) those held under a title reservation agreement; and
3) those vested in a person who was lessor under a leasing agreement.

[10] In addition to aviation equipment, described in the Convention as airframes, aircraft engines and helicopters, the Convention contemplates that it will apply one day to interests in railway rolling stock and space property. The final provisions of the Convention even provide for assessments to be made in due course of the feasibility of extending the application of the Convention through further protocols to any other category of high-value mobile equipment. In summary, the draft Convention:

1) sets formal requirements for the creation of an international interest;
2) sets out basic default remedies;
3) establishes registration rules;
4) deals with the effect of an international interest as against third parties (priority rules, rules to preserve the efficacy in the event of bankruptcy);
5) contains provisions on assignments; and
6) deals with registrable national interests.

2 – The Convention/Protocol Framework (par. 28)

[11] The Convention/Protocol structure proposed is quite unusual and, in the view of some, it is without direct precedent. The structure consists of a base Convention that has little effect of its own. Its legal force depends on the presence of an equipment-specific Protocol that is in force. The Convention contains general rules thought to be potentially applicable to many types of equipment. It is intended to be accompanied by one or more equipment-specific protocols that will give the Convention a practical existence while varying its rules to suit the market conditions for that type of equipment.

3 – The Context of the International Financial Architecture (par. 15-19)

[12] In its broadest sense, this project is about assisting States in getting the most out of their economies and thereby helping the battle against inequality. It is believed that a significant part of the financial differential between more developed and less developed countries can be

accounted for by the legal framework which they provide for granting of credit. According to one author “when the law permits lenders to effectively take collateral, a more efficient loan market results. Where creditors can get collateral for their loans, they will make larger loans, for longer periods of time, and at lower interest rates.”[2]

[13] In official studies of the International Financial Architecture prompted by the recent international financial crisis that began in Asia but soon appeared on other continents it was recognised that major improvements to domestic legal frameworks for financial transactions were required.[3] A report of a Working Group on International Financial Crises prepared under the aegis of the G-22 endorses certain key principles and features of effective insolvency and debtor-creditor regimes and encourages further efforts in countries and in the relevant fora to strengthen existing insolvency and debtor-creditor regimes.[4] The Working Group found that “effective debtor-creditor laws create a legal framework that allows for loans to be extended at lower interest rates and at less risk while facilitating the diversification of credit risk and fostering non-bank financial intermediation.”[5]

[14] The framework features identified by the Working Group for effective debtor-creditor regimes are relevant to the current efforts to evolve a regime to encourage asset-based financing. They are worth quoting:

1) Creation of Security Interests
2) Priority
3) Registration of Security Interests
4) Enforcement

[15] It therefore appears that the Convention/Protocol at least in its thrust favouring asset-based financing and principal features encompassing the establishment of an international interest, a registration system, a priority rule and prompt remedies including self-help reflects features propounded in respect of the new financial architecture. Aircraft, it will be recalled, represent 4% of the world’s moveable equipment[6]. An impressive starting point for reform.

<u>4 – The Context of International Aviation Finance (par. 20)</u>

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[2] Heywood, W. FLEISIG, "The Proposed Unidroit Convention on mobile equipment: economic consequences and issues", 1999-2 *Unif. L. Rev.* 253, 255.

[3] In response to the crisis, Finance Ministers and Central Bank Governors from a number of systemically significant economies met to examine issues related to the stability of the international financial system and the effective functioning of global capital markets. Three working groups were formed to contribute to the international dialogue on how to proceed in these areas.

[4] *Report of the Working Group on International Financial Crises*, October 1998, pp. vii, 14-18, 40, 44-47. The report is available at < http://www.worldbank.org/html/extdr/ifa-reports/index.htm >.

[5] *Idem*, p. 17.

[6] Heywood. W. FLEISIG,, *supra*, note 2.

[16] It seems clear that from a macro-economic point of view the present project is in line with the most up-to-date thinking and that instruments with features like the ones contemplated in the Convention/Protocol would be viewed as beneficial from that standpoint. But there is of course a more immediate and more concrete standpoint. This project is also about buying and selling and making efficient use of aircraft and aircraft equipment. Its goal is to make financing available where it is not and, where it is, to permit one to buy and sell more cheaply through financing that minimizes the risks of financial loss. Concomitantly, this project is about relieving pressure on governments to finance aircraft and aircraft equipment purchases or to guarantee them. It will be realized that the latter aspect also affects the privatisation objectives of certain States. It will also support the policies of others in respect of off-shore financing structures. Modern aviation financing can be divided roughly into three options: equity financing; debt financing; lease financing.

5 – Financing Participation in Civil Aviation Industry Development and Aviation Safety (par. 27)

[17] International aviation financing is the lifeblood of international civil aviation, in particular in respect of fleet renewal. The absence or shortage of financing may have an immediate and direct impact on an aircraft operator's ability to participate in industry development and remain fully focused on safety. This importance of finance was no doubt in the minds of the framers of the Chicago Convention, the principles and arrangements of which were agreed in order *inter alia* “that international air transport services may be established on the basis of equality of opportunity and operated soundly and economically”.[7] The opportunity now presents itself for Member States to participate effectively in a process designed to facilitate fleet renewal and thus significantly contribute to the sound and economic development of civil aviation. The adoption and implementation of the rules of this Convention/Protocol are designed to facilitate the cost efficient acquisition and use of aircraft equipment, whether new aircraft or parts. This should enable operators to acquire modern enhanced and environmentally friendly equipment and remain more easily focused on safety.

C – The Texts of the Convention/Aircraft Protocol

1 – Sphere of Application and General Provisions (par. 39-46)

[18] Chapters I of the Convention (Articles 1 to 6) and I of the Protocol (Articles I to VIII) contain, as their titles indicate, provisions of a general nature including provisions on sphere of application.

[19] In brief, the Chapters set out a large number of definitions. Then, the Convention posits what is meant by an international interest. It is an interest which conforms to the Convention's scope and creation criteria: it is an interest in certain limited types of equipment (aircraft objects, railway rolling stock or space property) granted under certain limited types of agreement (security agreements, title reservation agreements and leasing agreements). The Convention also

[7] Preamble to the Convention on International Civil Aviation signed at Chicago on 7 December 1944.

applies to a limited class of proceeds of the equipment. The Protocol adds that the Convention/Protocol also applies to contracts of sale.

[20] The Convention/Protocol specifies that it applies to helicopters, airframes and engines; the effect of this is to say that it applies to helicopters as a whole but that in respect of other aircraft it applies to engines and airframes separately. This distinction was agreed upon because of the high value of aircraft engines (they can constitute 25% of the value of the composite aircraft) and the fact that they are frequently financed separately from an aircraft. Furthermore engines are often pooled and interchanged between aircraft and among airlines.

[21] The Convention applies when the debtor is situated in a Contracting State and has rules that determine where the debtor is situated. The situation (or *locus*) of the creditor is not a factor. This is important because it means that creditors will be able to participate in the benefits of the Convention even though their State is not in a position to commit to it. The Protocol adds that the Convention/Protocol will also apply when the aircraft appears on the aircraft register of a Contracting State. It will also apply when the parties stipulate that the aircraft will appear on the registry of a Contracting State and does so appear.

[22] Certain States having indicated the desirability of an option to exclude purely internal transactions from certain aspects of the Convention, the possibility of making a declaration to that effect appears in Article 50 of the Convention and Article XXXI of the Protocol. A definition of internal transaction is presented in Article 1 of the Convention, which is further refined in respect of aircraft objects in the Protocol. It should be noted that this opt-out provision is without prejudice to the first-to-file rule, and, accordingly, the parties to an internal transaction will enjoy the facility of having their national interest noted on the international register.

[23] The Convention contains a set of general rules on its interpretation that appear to be standard fare in the case of private international law instruments. The Convention also deals with the applicable law in general (that designated by the forum State's rules of Private International Law) and also in the case of multijurisdiction States such as federal States. The Protocol reminds one that the parties to a transaction may determine the domestic law applicable in whole or in part to their contractual relations and obligations under the Convention.

<u>2 – Constitution of an International Interest (par. 61)</u>

[24] Article 7, the sole article in Chapter II of the Convention, sets out the formal requirements for an interest to qualify as an international interest under the Convention. The instrument creating or providing for the interest must be in writing. The debtor must have the power to dispose of the object. The instrument must contain an identifying description which in the case of an aircraft object, according to Article VII of the Protocol, is determined to consist of the manufacturer's serial number, the name of the manufacturer and the model designation. If the agreement is a security agreement, it must enable the secured obligations to be determined, but it need not state the sum or maximum sum secured. The presence of a statement of such a sum in compliance with national law or other additional information in the security agreement will not affect its validity as an international interest.

3 – Default Remedies (par. 63-76)

[25] Chapter III of the Convention and a good portion of Chapter II of the Protocol (Articles IX to XVI) are concerned with the remedies available to creditors in the event of the debtor's default. These provisions are of capital importance. They respond to the call for rapid and cheap enforcement that characterises the asset-based financing seen as an integral part of the proposed International Financial Architecture. Similarly, they respond to the prompt enforcement principle.

[26] Under the Convention, the debtor and creditor are permitted to agree on the events that constitute default. Failing such agreement, the Convention provides that default means a substantial default. The Convention distinguishes the default remedies available to the different types of creditors: the chargee under a security agreement, the conditional seller under a title reservation agreement and the lessor under a lease. Unless States declare otherwise, the remedies are to be exercised in conformity with the procedure applicable under the laws of the place where the remedy is to be exercised.

[27] The chargee may with the agreement of the chargor (a) take possession or control of the object, (b) sell or grant a lease of it and (c) collect any income or profits arising from the management or use of the object. The Protocol adds that with the consent of holders of higher ranking interests, the chargee may also (d) procure the deregistration of the aircraft and (e) procure the export and physical transfer of the aircraft object from the territory in which it is situated. As provided under Article 54 of the Convention, a State is at liberty to declare that no leases may be granted in its territory in respect of an object controlled from its territory. According to that same provision, States are required to declare whether or not these remedies are to be exercised only with leave of the court.

[28] Under the Protocol all these remedies must be exercised in a commercially reasonable manner and they are deemed to be exercised in a commercially reasonable manner where they are excercised in conformity with a provision of the agreement except where such a provision is manifestly unreasonable. When a sale or lease is contemplated, the chargee must give certain interested persons (the debtor, a surety and other persons who have notified their interest in the object) 10 days notice unless a longer period has been agreed. Sums received as the result of the exercise of a remedy must, of course, be applied toward the discharge of the debt. If those sums exceed the debt and reasonable costs, then unless a court orders otherwise, the surplus is to be paid to the next ranking creditor and if there is none, to the chargor. All these prescriptions are mandatory and therefore cannot be contracted out of.

[29] The Convention also contains rules on the vesting or transfer to benefit of the chargee of the right of ownership or other interest of the chargor in the object. Such vesting can occur after default with the consent of the chargor and all interested parties. Also, under a rule that cannot be derogated from, a court may order such vesting in satisfaction of the secured obligation, but only if the amount of the secured obligation is reasonably commensurate with the value of the object and payments to be made by the chargee to interested persons. When the object is sold or vested in the chargee in accordance with the above rules, the title is clear of any lower ranking interest.

[30] At any time after default but before sale or vesting, the chargor or any interested person may discharge the security interest by satisfying the obligation in full, subject to any lease granted in the meantime. If a person other than the chargor satisfies the obligation, that person is of course subrogated to the rights of the chargee. These rules are mandatory.

[31] The rules relating to title reservation agreements and leases are much simpler. They provide that the conditional seller or the lessor may simply terminate the agreement and take possession or control of the object. If a State has declared under Article 54(2) that those remedies may only be exercised with leave of the court, then the conditional seller and the lessor must of course apply for a court order granting the remedies.

[32] The Protocol contains rules on de-registration and export authorisation which must be specifically agreed to by State by way of a declaration made under Article XXX(1) of the Protocol. The rules provide that a document known as an Irrevocable De-Registration and Export Request Authorisation issued by the debtor must be registered on the aircraft register upon the debtor's request. The person in whose favour the document is issued will be the only one entitled to procure de-registration of the aircraft and the export and physical transfer of the aircraft object from the territory in which it is situated. This is to be done only in accordance with the terms of the authorisation and applicable safety legislation. The authorisation may be revoked and removed from the registry but only with the consent of its beneficiary. The authorities are required to co-operate with the beneficiary in the exercise of the latter's remedies.

[33] The Convention also contains provisions on interim relief, *i.e.* **speedy** relief to be accorded pending a final determination of the creditor's claim. These rules apply in respect of security agreements, title reservation agreements and leases. According to Article X of the Protocol, States are at liberty to declare that they will not apply these provisions in whole or in part. Furthermore, the debtor must have consented to the application of the rules on interim measures. Under the Protocol, States have the option of declaring in terms of calendar days what constitutes speedy relief.

[34] Under the Convention/Protocol, the interim relief will take the form of one or more of the following court orders as the creditor requests: (a) preservation of the object and its value; (b) possession, control or custody of the object; (c) immobilisation of the object; (d) lease or management of the object and the income therefrom; and (e) sale and application of the proceeds therefrom. This last form of relief stems from the Protocol and States need not be bound by it, according to Article XXX(2) of the Protocol. The same applies to all Protocol provisions relating to interim relief. Before making an order for interim relief, the Court may require that notice of the creditor's request be given to interested persons. Other forms of interim relief may be granted in accordance with applicable domestic law.

[35] In granting an order for interim relief, the court may impose the conditions it considers necessary to protect interested persons in the event the creditor fails to perform any of its obligations to the debtor under the Convention or the Protocol or fails to establish its claim on final determination. This provision applies where it has not been excluded by States. Under a

rule in the Protocol which is subject to State approval, the provision where available may be derogated from by agreement between the creditor, the debtor and any other interested person.

[36] The Protocol provides, as in the case of normal relief under a security agreement, that when the object is sold, title is acquired clear of any lower ranking interest. Under a further rule that requires States' acceptance by way of a declaration, registry and other administrative authorities would be compelled to make available the procurement of de-registration of aircraft and the procurement of export and physical transfer of aircraft within a number of days (yet to be specified) from the granting of interim relief.

[37] Additional remedies permitted by applicable law may be exercised to the extent they are not inconsistent with the mandatory provisions of Chapter III of the Convention.

4 – The International Registration System (par. 81-83)

[38] An International Registry is established by the Convention for the registration of a number of types of interest. Primarily, it will register international interests, prospective international interests and registrable non-consensual rights and interests. Also registrable are assignments and prospective assignments; acquisitions of international interests by subrogation; subordinations of interests; sales and prospective sales; and finally notices of national interests. Different registries may be established for different categories of object and associated rights.

[39] A Supervisory Authority to be identified in the Protocol is created *inter alia* to establish and oversee the operation of the Registry, appoint and dismiss a Registrar (unless otherwise provided in a Protocol), make regulations (with the initial ones entering into force on the date of entry into force of the Protocol), establish a procedure for receiving complaints, set the fee structure and report to Contracting States. It is given the power to enter into agreements including a headquarters agreement with the Host State. The Registrar is to ensure the efficient operation of the Registry. The Protocol indicates that the Registrar should be appointed for five years at a time.

5 – Modalities of Registration (par. 87-93)

[40] The Convention provides that the Protocol and regulations are to specify the requirements for registration, for making searches and issuing certificates and for ensuring confidentiality. Those requirements are not to include evidence that the requisite consents to registration have been given. The Protocol specifies that the search criteria for aircraft objects shall be the manufacturer's serial number supplemented as provided in the Regulations.

[41] Under the Convention/Protocol, a Contracting State may designate an entity in its territory as a channel for certain registrations destined for the registry, to wit, international interests in, or sales of, helicopters and airframes for which it is the State of Registry, registrable non-consensual interests created under its law and notices of national interests.

[42] Registration is to be effected in chronological order of receipt at the International Registry database. A registration takes effect when the requisite information is entered in the

database so as to be searchable. When a prospective international interest becomes an international interest that interest is treated as registered as of its registration as a prospective interest. A comparable rule applies in respect of prospective assignments. The Convention also contains rules on who may register different rights and interests and who must consent to the registration. In the case of an international interest it is the debtor who registers or consents to registration. Registrations are effective until discharged or until the period specified in the registration if any has expired.

[43] Any person may, in the manner prescribed, make or request a search of the Registry. The Registrar will, upon request, provide search certificates that constitute *prima facie* proof of their authorship and content. Lists of non-consensual rights or interests declared by Contracting States are also to be searchable.

[44] The beneficiary of a registered right or interest must procure de-registration of that right or interest once the secured obligations or conditions have been fulfilled. Likewise the intended beneficiary of a registered prospective international interest or a prospective assignment of an international interest must procure de-registration when so requested by the intended debtor or assignor before the beneficiary has given value or incurred a commitment to give value. Similarly the creditor of a duly discharged obligation secured by a notified national interest must upon demand of the debtor procure the discharge of the registration.

6 – Privileges and Immunities of the Supervisory Authority and the Registrar (par. 103)

[45] Chapter VI of the Convention consists of a single Article. Paragraph 1 assures the Supervisory Authority of legal personality on the plane of International Law. Although, there is no obligation to do so, individual States and no doubt the Host State will, in accordance with practice, ensure that the Authority has the personality on the plane of domestic law which it requires to fulfil its functions.

7 – Liability of the Registrar (par. 110)

[46] Article 28 of the Convention stipulates that the Registrar is to provide insurance or a financial guarantee covering its liability to the extent provided by the Protocol. The Protocol provides that they will cover all the liability of the Registrar. The liability of the registrar is limited to compensatory damages. Punitive or exemplary damages are excluded. The cause that may generate the compensable loss would be an error or omission of the Registrar or a malfunction of the international registration system except where the malfunction is caused by an event of an inevitable and irresistible nature, which could not be prevented by using the best practices in current use in the field of electronic registry design and operation, including those related to back-up and systems security and networking.

8 – Effects of an International Interest as against Third Parties (par. 112-122)

[47] The effects of an international interest as between the parties to the agreement creating it are dealt with primarily in the terms of the agreement and, where referred to by the Convention/Protocol, in rules of national law. The Convention/Protocol regulates the effects of

an international interest as against third parties in general and, in certain respects, in insolvency proceedings.

(a) – Priority of competing interests

[48] In a very simple rule that constitutes the very *raison d'être* of the international registry, the Convention provides that a registered interest in an object has priority over any other interest subsequently registered and over an unregistered interest. The priority extends to select proceeds of the object. This rule, known as the first-to-file rule, is absolute. It applies even when the first registered interest was acquired with actual knowledge of other interests and also in respect of fresh advances made on a first interest with knowledge of a second interest. Likewise the buyer acquires its interest subject to any interest already registered but free of unregistered interests even if it has knowledge of them. The holders of competing interests are at liberty to vary their priority as between themselves and change the order of subordination; should the holder of the subordinated interest decide to assign that interest, the subordination will not affect the assignee unless it was registered prior to the assignment.

(b) – Effects of Insolvency

[49] The Convention poses the rule that an international interest duly registered before the commencement of insolvency proceedings is to be given full effect in insolvency proceedings against the debtor. Therefore a secured creditor's rights in an object will be recognised as valid in such proceedings. If local law was more generous to the creditor, *e.g.* by not requiring prior registration, then local law is preserved.

[50] The Protocol provides for two sets of special remedies on insolvency, labelled Alternatives “A” and “B”. In accordance with Article XXX(3) of the Protocol, States may choose to apply one or the other, or neither. If they select one or the other, their courts and administrative authorities will be expected to co-operate with foreign courts and administrative authorities in carrying out the alternative to the fullest extent permitted by law.

[51] **Alternative “A”** presupposes of course the existence between the debtor and the creditor of an international interest in an aircraft object duly registered before the commencement of insolvency proceedings. Within a determined period of time following the commencement of insolvency proceedings or of a moratorium on the exercise of a creditor's rights to institute insolvency proceedings or to exercise its rights under the Convention, the creditor is to be given possession of the aircraft object, if all defaults have not been cured. The period of time will be the shorter of the waiting period set by States in a declaration or the period that would otherwise be applicable; the latter could be a period that had been contractually agreed between the debtor and the creditor.

[52] During the interim period described above, the continued use of the aircraft object is not precluded, but the debtor and insolvency administrator are under an obligation to preserve and maintain the aircraft and its value. The creditor may apply for additional interim relief as contemplated by applicable law. At the expiration of the interim period, not only is the creditor entitled to possession, assuming the defaults have not been cured, but the relevant authorities

would be compelled to make available the procurement of de-registration of aircraft and the procurement of export and physical transfer of aircraft within a number of days (to be specified in a State declaration) from receipt of notice that the creditor has been given possession. Finally, it should be noted that the insolvency administrator may terminate the agreement between the debtor and the creditor but may make no changes to it without the creditor's consent.

[53] **Alternative "B"** is less explicit in the formulation of the protection of the creditor's interests. Upon the occurrence of an insolvency-related event, the creditor may, upon proof of its claim and the registration of its interest, call upon the debtor or the insolvency administrator to take one of the following courses of action: either cure all defaults and agree to perform all future contractual obligations, or give the creditor the opportunity to take possession of the aircraft in accordance with applicable law. The applicable law may authorise a court to impose additional steps or the provision of additional guarantees. If the debtor or insolvency administrator fails to follow either course of action, the creditor may apply to a court for a grant of possession. The Court may order the taking of additional steps or the provision of additional guarantees. The aircraft object may not be sold pending a judicial decision regarding the claim or the international interest.

9 – Assignments of Associated Rights and International Interests; Rights of Subrogation (par. 131-133)

[54] Chapter IX of the Convention sets out the requirements for the constitution of an assignment of associated rights and the related international interest. According to that Chapter, the assignment must be in writing. It must enable the contract to which the associated rights relate to be identified. If the assignment is by way of security, it must enable the secured obligations to be determined in accordance with an applicable protocol, but it need not state the sum or maximum sum secured. The Protocol does add to the list of validity requirements that the assignment must be consented to in writing by the debtor. The consent may be given in advance and need not identify the assignee.

[55] To the extent agreed by the parties the assignment of associated rights transfers to the assignee the related international interest and all the interests and priorities of the assignor under the Convention. The determination of the defences and rights of set-off that the debtor may exercise against the assignee is left to local law. However the debtor is permitted to waive such defences and rights of set-off, with the exception of defences arising from fraudulent acts committed by the assignee. When obligations secured by an assignment have been discharged, the associated rights as may subsist, revert to the assignor, the original creditor.

[56] A debtor who under the Protocol has agreed to an assignment in advance, is bound by it and has to act according to it, if it has been given notice of it by the assignor and the notice identifies the associated rights. A debtor who pays in accordance with notification is discharged to the extent of the payment. The Convention rules applicable to default on security agreements apply to assignments, *mutatis mutandis*. Likewise, the Convention rules concerning competing interests apply to competing assignments, *mutatis mutandis*.

[57] It is worth noting that an assignment of associated rights which is not effective to transfer the international interest is outside the scope of the Convention.

<u>10 – Non-consensual Rights or Interests (par. 139-141)</u>

[58] The Convention deals with the issue of priority vis-à-vis non-consensual interests, *i.e.* interests that derive their existence not from agreements but from the law itself. These would include interests such as repairers' or suppliers' liens, tax liens, wage liens, privileges upon moveable property, the priority of the seizing creditor. Article 39 (1) b) of the Convention provides specifically that nothing in the Convention shall affect the rights of a State or a State entity, intergovernmental organisation or other private provider of public services to arrest or detain an object under the laws of that State for payment of amounts ought to such entity, organisation or provider directly relating to those services in respect of that object or another object.

[59] An international interest enjoys priority over an unrecorded or a subsequently recorded non-consensual interest, unless those interests don't have to be recorded. However in all cases non-consensual interests must somehow be brought to the attention of the international financing community. The Convention allows Contracting States to ensure the recognition of categories of non-consensual interests by way of a declaration that can be made at any time. In making such a declaration States may divide their non-consensual interests into two types: categories that will not require registration to retain their priority and categories that will. Interests of the latter category may be registered by the holder and will follow the rules for international interests. They take rank according to their order of registration.

[60] On the other hand those in a category declared not require registration shall have priority over registered interests. The rule applies in or out of an insolvency of the debtor. It is worthy of note that a declaration relating to non-registrable non-consensual interests may be expressed to be prospective in the sense that it may be expressed to cover categories that are created after the deposit of the declaration.

<u>11 – Application of the Convention to Sales (par. 145-147)</u>

[61] The Convention itself contains very few rules pertaining to sales. It considers sale as a remedy upon default, even an interim one, but not as a transaction except to say that sales and prospective sales may be registered to the extent that a protocol states that the Convention is applicable to sales and prospective sales of relevant objects. The Protocol does this by implication when it states not that the Convention, but that the Convention's rule on its scope of application applies in relation to a sale, and that "agreement" includes a contract of sale and “debtor” means a seller. The Convention/Protocol provides that a sale may be registered by or with the consent of the seller. It also provides that a registration may be extended by or with the consent of the same person. This latter provision should not have frequent application as the request for registration of a sale is unlikely to contain an expiration period, unless it is a prospective sale. The rules on discharge of registration applicable to security agreements and title reservation agreements apply in respect of sales. The Convention's priority rules will apply in relation to sales including those that would be applicable in the case of insolvency proceedings

against the seller. The priority of duly declared non-registrable non-consensual interests applies in respect of sales.

12 – Jurisdiction (par. 150-154)

[62] The first jurisdiction rule advanced by the Convention is founded on party autonomy subject to the public policy of the competent State. The parties to a transaction may agree which court will be competent to hear any claim under the Convention provided their agreement is valid under applicable law. The court selected need not have a connection with the parties or the agreement.

[63] Applications for interim relief by way of (a) preservation of the object and its value, (b) possession, control or custody of the object and (c) immobilisation of the object, may also be heard by two other courts, that of the State where the object is situated and that chosen by the parties, provided those States are Contracting States. Furthermore, applications for interim relief by way of lease or management of the object and the income therefrom may be made to the courts agreed by the parties or those where the debtor is situated, provided those courts are in Contracting States. The special jurisdictions in respect of interim relief referred to in this paragraph may be exercised even if the determination of the final relief may fall to a court of another State or an arbitral tribunal. A general jurisdiction provision is also included in the Convention.

[64] The issue of the enforcement of waivers of sovereign immunity is often perceived to be a difficult one. The Convention/Protocol provides explicitly that a waiver of sovereign immunity from a jurisdiction designated by its rules, shall be binding and, if other conditions for jurisdiction have been met, it shall be effective. However, such a waiver must be in writing and contain a description of the aircraft object. As a restraint on immunity from enforcement does not necessarily flow from a restraint on immunity from jurisdiction, the Convention/Protocol specifically applies comparable rules and conditions in respect of immunity from enforcement of rights and interests relating to an aircraft object.

[65] In principle, the Registrar is immune from legal process and thereby from the jurisdiction of the courts. There are however a few cases where the Registrar is amenable to the jurisdiction of the courts of the place where it has its centre of administration and of those courts alone. This is the case in respect of actions in damages brought against the registrar. Also, when a person has a right to a discharge or amendment of a registration and is not able to obtain it through the usual channels, the Court has jurisdiction to give the Registrar the appropriate orders to set matters right. This latter rule is not intended to grant the court jurisdiction to resolve the merits of a dispute, that being left to the general jurisdiction rules summarised above.

13 – Relationship with other Conventions (par. 159-163)

[66] The Convention/Protocol sets the relationship between itself and four other international instruments (one still in draft form) which could affect international interests in aircraft equipment.

1) The *Unidroit Convention on International Financial Leasing*, opened for signature at Ottawa on 28 May 1988
2) The United Nations *Convention on Assignment of Receivables in International Trade* adopted in July 2001
3) The *Convention on the International Recognition of Rights in Aircraft* opened for signature at Geneva on 19 June 1948
4) The *Convention for the Unification of Certain Rules Relating to the Precautionary Attachment of Aircraft* opened for signature at Rome on 29 May 1933

14 – Final Provisions (par. 165-173)

[67] Chapters XIV of the Convention and VI of the Protocol contain a number of usual Final Provisions including a federal State ratification clause and interpretation clause.

[68] As already noted throughout our examination of the text, the Convention/Protocol permits an impressive number of declarations to be made in respect of different provisions. It is noteworthy however that no declarations are permitted except those expressly authorised. The Protocol contains useful rules for a State wishing to make a declaration subsequent to the entry into force. An effectiveness period of six months is applicable unless a longer period is provided in the declaration. The declaration will not apply to rights and interests arising prior to its effective date. A declaration and a reservation may be withdrawn; an effectiveness period of six months is indicated.

[69] In respect of transition from the existing rules to the new international ones, the Convention's rules in general do not apply in respect of pre-existing rights or interests. However, States can make a declaration and specify a date, not earlier than 3 years after the date on which the declaration becomes effective, when the Convention and Protocol will become applicable to pre-existing rights and interests. The period is reckoned from the date the Convention entered into force in respect of the State where the rights or interests were created. If they were not so registered, the Convention would treat them as any other unregistered interest.

III – CANADIAN ACCESSION AND IMPLEMENTATION

A – The Convention and the Aircraft Protocol – A Priority for Canada

[70] As Canada has played a key legal role in this project since its beginning many States have been looking to Canada in the preparation of those instruments and they will be looking to Canada in their preparation of implementing legislation. For one thing Canada is an important actor in the development of air law. ICAO and the International Air Transport Association (IATA) who have played an important role in the preparation of these instruments, have their headquarters in Montreal. In addition, during the last ten years Canada has been modernising its security laws and has emerged as a leader in the area of electronic registries for secured interests. Finally, as the Civil Code of Quebec is probably one of the few civil law system in the world that provides for movable hypothecs Canada brings a unique contribution to the preparation of the draft Convention and Protocol as a country of both civil law and common law traditions, both

practised in French and in English and both familiar with the concept of interests in mobile equipment.

[71] Economically, the draft Convention and its related Protocols could apply and be of benefit to industries such as air and maritime transport, to railway rolling stock and satellite industries that are very important to the Canadian economy. Asset-based financing and leasing activities in relation to mobile equipment allow the risk involved with such activities to be lowered in comparison with conventional non-asset-based financing and leasing activities. Lower risk will usually result in lower financial and leasing rates, thereby increasing the availability and/or reducing the cost of that equipment. In summary, such economic gains could give Canada interesting economic competitive gains.

B – Ongoing Consultations with regard to the Negotiations

[72] Since the beginning of the project, the Government of Canada has held five Canada-wide consultations. They were held in the Fall of 1998, Spring/Summer 1999, Winter 2000, Spring/Summer 2000 and Winter/Spring 2001. On these five occasions, the Government of Canada has been consulting simultaneously (1) the provincial and territorial governments, and (2) interested Canadian authorities, industries and practitioners on the Convention and Protocol (i.e. members of the aviation industry and legal practitioners or academics with an interest in areas such as air law, corporate and financial law, private international law, securities, bankruptcies and electronic registries). The consultations have indicated that the texts of the instruments meet the needs of Canadian industry and essential aspects of the Canadian legal framework.

C – Consultation on Canadian Accession and Implementation

[73] Consultations with the provinces and territories regarding Canada's accession to the Convention and Protocol and their implementation will be taking place in the coming year.

D – Form of Implementation: Amending Legislation or Stand-alone legislation

1 – Amending Legislation

[74] In its discussions regarding the form of implementation of the Convention and the Protocol, the Working Group first compared the option of legislation amending Personal Property Security Acts (PPSAs), and other legislation as necessary, to the option of stand-alone legislation implementing the Convention and the Protocol. After a short discussion, it became clear that the regime that is to be implemented is exceptional in nature as it will apply to a very limited number of objects and as it will be used by a small number of sophisticated parties. It was for these reasons that it was decided to implement it through stand-alone legislation. This solution would also have the advantage to keep intact the general PPSAs framework and to have a transparent international interests regime for aircraft equipment.

2 – Provincial and Federal Jurisdiction over Implementation – Mirror Legislation

[75] Then the Working Group discussed the need to have federal legislation implementing the Convention and the Protocol. It was clear from the discussion that all substantive provisions of both instruments would need to be implemented at the federal level because of their possible relevance to a Federal Bank Act Security and because of their direct link to bankruptcy and insolvency, and privileges and immunities.

[76] A majority of Members of the Working Group suggested preparing mirror image implementing legislation for the adoption of the federal and provincial governments in order to prevent constitutional arguments based on the division of powers with regard to implementation. In their view, the federal power over aeronautics in this particular case may not be settled. Thus if an issue covered by a particular provision of the Convention/Protocol would happen to fall within exclusive federal jurisdiction, pursuant to power over aeronautics, then provincial implementing legislation standing alone would not be enough to support implementation of the Convention/Protocol in domestic law. Furthermore, if Canada ever becomes a party to the Railway Rolling Stock Protocol the Convention would have to be implemented at the federal level in any event. Thus likewise if an issue covered by a particular provision of the Convention/Protocol would happen to fall within exclusive provincial jurisdiction, pursuant to the law of contracts for example, then federal implementing legislation standing alone would not be enough to support implementation of the Convention/Protocol in domestic law. These same Members of the Working Group thought that it was important not to second guess what is arguably of federal jurisdiction and what is of provincial jurisdiction. Instead, they were of the view that including all substantive provisions in mirror legislation enacted at both levels of governments would prevent making any division of powers argument to declare the federal or provincial legislation *ultra vires*.

3 – Separate Legislation Implementing the Convention and the Aircraft Protocol or Stand-alone Legislation Implementing both Instruments

[77] Then the Working Group discussed whether there should be separate legislation implementing the Convention and the Protocol or stand-alone legislation implementing both instruments. Members of the Working Group favoured the latter. In their opinion, implementing the Convention and the Protocol separately would defeat the objective of Article 6(1) of the Convention which states that the Convention and the Protocol shall be read and interpreted together as a single instrument. On that occasion, many members of the Working Group voiced their frustrations with the current Convention/Protocol structure as it is hard to work with and may lead to some uncertainties. To address this issue, the Diplomatic Conference invited the Secretariats of Unidroit and ICAO to draft a consolidated text to facilitate the use of the instruments (Final Act of the Conference, Resolution n. 1).

4 – Consequential Amendments (Provincial and Federal)

(a) - Federal

[78] The Working Group agreed that despite the enactment of mirror legislation there would be a need to amend the Bankruptcy and Insolvency Act in order to implement Alternative “A” of Article XI of the Protocol and that there could be some actions required at the federal level in

order to implement Article 27 of the Convention with regard to privileges and immunities. In order to keep intact the mirror effect of the legislation between the federal and provincial jurisdictions, it was agreed not to include those amendments in the uniform act.

(b) - Provincial

[79] At the provincial level, the Working Group discussed the possibility of making consequential amendments to the PPSAs and judgement enforcement legislation. Further to an analysis conducted by Ron Cuming, Michel Deschamps and Catherine Walsh, it was decided not to provide for consequential amendments to that effect at this point. However, this conclusion could be reviewed after the Diplomatic Conference. An analysis of consequential amendments with regard to registrable non-consensual rights and interests and non-registrable non-consensual rights and interests (Articles 7, 29, 39 and 40) can be found at paragraphs [91]-[109] of this Report.

[80] In order to keep intact the mirror effect of the legislation between the federal and provincial jurisdictions, it was agreed not to include those amendments in the uniform act.

5 – The Implementation of Future Protocols

[81] The Working Group discussed whether the uniform act could be used to implement other protocols in the future. Without taking a final decision on the subject, it has agreed to incorporate in the commentaries to the provisions of the uniform act language and/or directions to that effect.

E – Implementation Methods used in Canada

[82] Generally, there are three methods - options - by which international treaties are implemented in Canada.[8]

[83] Option (1) - The treaty can be incorporated in a short act which expressly gives the force of law to the treaty or certain of its articles. Then the treaty or such articles may be set out as a schedule to the act (e.g.: The *Foreign Missions and International Organisations Act*, C.S.C., c. F-29.4, C.S. (1991), c. 41; and, the ULCC *Uniform International Commercial Arbitration Act*, 23B.1-1).

[84] Option (2) - The treaty may be implemented by an act which may employ its own substantive provisions to give effect to the treaty, the text of which is not directly enacted or referred to (e.g.: Section 7(2.2) of the *Criminal Code* implementing the *Convention for the Suppression of Unlawful Acts against the Safety of Maritime Navigation*, opened for signature at Rome on March 10, 1988).

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[8] Verdon, Christiane, "Le Canada et l'unification internationale du droit privé" (1994) 32 Can. Y.B. Int'l L. at 30; and Brownlie, Ian, *Principles of Public International Law*, 2nd ed. (Oxford: Clarendon, 1973) at 50.

[85] Option (3) - Even where the treaty is referred to in the long and short titles of the Act and also in the preamble and schedule for dissemination purposes, the Act may not expressly give the force of law to the treaty. Rather, contents of the provisions will allow the enforcement of the treaty in domestic law as is necessary to comply with the obligations imposed on the State without expressly giving the force of law to the treaty as Option (1) does. However, the provisions of the act implement the treaty in domestic law (e.g.: *An Act to Implement NAFTA*, C.S.C., c. N-23.8, C.S. (1993), c. 44 and the ULCC *Uniform Settlement of International Investment Disputes Act* implementing the *ICSID Convention*).

[86] The Working Group discussed the three options. The third option was rejected from the start. During its discussion of the two remaining options, a Member of the Working Group made a suggestion for a fourth option that would have consisted in preparing a single act reproducing in its own body the consolidated text of the Convention/Protocol itself. This fourth option was described as an alternative to Option (1) . This new alternative had the advantage of respecting the decision of the Working Group to prepare stand-alone legislation . While being attracted by the user-friendly and transparent characteristics of this option the Working Group resisted it on several practical grounds. First, as this option would have been a precedent it would have required the approval of the Conference. Secondly, it was the view of the Working Group that it was not appropriate to enact a different text than the ones which would be signed and ratified by Canada, as the Diplomatic conference adopted the dual Convention/Protocol structure. Thirdly, the Working Group did not want to take the risk that the consolidated text of the Convention/Protocol be adjusted so that it would comply with domestic law and domestic legislative drafting conventions. Those adjustments could have implied the addition and the deletion of provisions, thus resulting in a renumbering the Articles, or it could have implied changes of terms. It was the view of the Working Group that such adjustments could lead to uncertainties. On the basis of those three arguments, one Member of the Working Group indicated that in order to favour uniform international interpretation of the Convention and Protocol it was important for all courts to refer to the same provision numbers and to uniform substantive law. The fourth option would defeat this important objective that is included in Article 5 of the Convention. Those same arguments favoured Option (1) over Option (2). In addition, the Working Group favoured Option (1) because it was: the best option to meat the transparency objectives; the simplest to produce; and, the most appropriate option in order to prepare mirror legislation.

[87] In this context, it is the recommendation of the Working Group that the most appropriate, simple and effective means of implementing the Convention and the Protocol in Canada would be through the method described in Option (1) (see paragraph [83]).

F – Implementation Principles Followed

[88] The Working Group adopted the following implementation principles from the collective work edited by Professor Hugh Kindred and others from Professor Ian Brownlie:

> "[T]o what extent may international legal principles be relied upon as imposing legally enforceable obligations, or conferring legally enforceable rights, on individuals that they may use in their domestic system ? This question is, in some

contexts, referred to as the "direct applicability" or "direct effect" of international law in the domestic legal system. [...] In Canada, [...] [a] good argument may be made [...] that Canada is adoptionist in respect of customary international law and transformationist in respect of conventional law - the latter clearly springing from following the British legal tradition that treaties must be enacted into law by Parliament before they will affect private rights."

"Implementation is the process of giving effect to a treaty within the national legal system. In Canada, the vast majority of treaties have to be implemented by legislation. This requirement is the result of the constitutional separation of powers. Although the executive in exercise of the royal prerogative may conclude a treaty, it cannot make law. That is the responsibility of the legislature. As a result, a treaty made by the federal government will bind Canada as a country, but its provisions do not affect internal law until they have been implemented by legislation. [...] [J]urisdiction to adopt laws for the purpose of implementing treaties is determined by the ordinary rules governing the division of legislative powers under the constitution."[9]

"It is only in so far as the rules of International Law are recognised as included in the rules of municipal law that they are allowed in municipal courts to give rise to rights and obligations. [...] [I]nternational law has no validity save in so far as its principles are accepted and adopted by our own domestic law."[10]

G – Implementation Analysis of the Convention/Protocol

1 – Texts set out in the schedules to the Act

[89] The Working Group agreed that the texts that will be signed and ratified by Canada will be the texts that will have the force of law in domestic law. Furthermore, the Working Group agreed that those texts would be appearing in the Schedules to the Act. Because the consolidated version of the Convention/Protocol is not the text that wouldbe signed and ratified by Canada, it could also appear in the Schedules to the Act but only for interpretation purposes.

2 – General implementation comments

[90] The Working Group suggested making as few declarations as possible in order to make the application of the Convention and Protocol as simple as possible, as uniform as possible across Canada and to make Canada an attractive place to conduct business.

3 – Implementation Analysis of the Declarations and Options

[9] Kindred, Hugh M., et al., *International Law Chiefly as Interpreted and Applied in Canada*, 5th ed., Toronto, Edmond Montgomery, 1993, at 147-48.

[10] cf. Brownlie, Ian, *Principles of Public International Law*, 4th ed., Clarendon Press, Oxford, 1990, at pp. 47-48.

(a) – Article 39 of the Convention - General or specific declaration as to non-registrable non-consensual rights and interests

and

(b) – Article 40 of the Convention - Declaration as to the categories of non-consensual rights and interests which shall be registrable

Interface with Existing Law

[91] The Convention priority regime is comprehensive, covering priority conflicts between (1) registered international interests; (2) a registered international interest and an unregistered interest (whether or not an international interest); (3) a registered international interest and the rights of an insolvency administrator; (4) a registered international interest and a registered or unregistered non-consensual interest; (5) a registered or an unregistered interest (whether or not an international interest) and the interest of a buyer of the relevant object. The Convention definition of "unregistered interest"- applicable to priority conflicts within categories (2) and (5) - is drafted so as to apparently include unregistrable interests created by consensual agreement. A consensual interest may be unregistrable, even though it is a security interest or the interest of a lessor or conditional seller, because it has not been constituted as an international interest in the specific manner provided in Article 7. For example, the agreement may not meet the collateral description requirements of Article 7. Alternatively, it may be unregistrable because it is an interest arising out of a consensual relationship that does not involve a security agreement, lease or conditional sale. The result is that any consensual proprietary interest (whether registrable or unregistrable) created under non-Convention provincial or federal law that is not expressly referred to in section 29 or in the Protocol can be defeated by a prior or subsequent registered international interest or by a subsequent buyer of the property subject to the interest. The vulnerable consensual interest need not be one created under a type of transaction referred to in Article 2.

[92] Existing domestic registration requirements will also need to be examined to determine whether interests in the nature of a security interest, or the interest of a lessor or conditional seller, should be exclusively constituted under and regulated by the Convention, or whether alternative or dual constitution and registration should be permitted as a matter of domestic law.

[93] However, the impact of the Convention on the priority status of non-consensual interests arising by operation of Canadian law requires further consideration. Under the priority scheme of the Convention, non-consensual interests are subordinate to a registered interest unless the Contracting State expressly preserves them via a declaration pursuant to Article 39 or 40 of the Convention.

[94] The federal government, and the provinces and territories will each need to reach their own policy decisions on what domestic non-consensual interests they wish to preserve, and whether this should be accomplished through Article 39 or Article 40. However, the Working Group thought that every attempt should be made to secure uniform treatment in all Canadian declarations on the most significant and universal class of non-consensual interests: creditors

who secure a money judgment against a debtor who is a chargor, conditional buyer, or a lessee under a transaction subject to the Convention.

[95] Under existing provincial and territorial law, a judgment creditor can acquire a proprietary right or interest in the assets of a judgment debtor in varying ways. In some jurisdictions, the judgment debtor's assets become "bound" by a judgment through the judgment enforcement process, with the typical triggering event being actual seizure of the asset. In other jurisdictions, the judgment creditor can attach the debtor's assets simply by registering notice of the judgment or notice of a judgment enforcement writ.

[96] The judgment creditor's "lien" so constituted fits within the definition of "non-consensual interest" in Article 1 of the Convention as being a "right or interest conferred by law to secure the performance of an obligation" (the obligation in question being payment of the judgment debt).

[97] As already emphasized, a non-consensual interest is subordinated under the Convention to a registered interest unless the non-consensual interest is listed explicitly in a declaration made by a Contracting State under Article 39 or 40. If no declaration is made, the interest loses whatever preference it would otherwise enjoy under domestic law.

[98] According to the Working Group, the judgment creditors of the owner of an aircraft object deserve protection in cases where a consensual interest under the Convention is created and registered after the creditor obtains judgment. Otherwise the Convention could become a means for aircraft owners to shield a valuable asset from the claims of their judgment creditors by charging the asset in favour of a single "preferred" creditor. Admittedly, this risk arises in the case of a subsequent charge against the debtor's existing assets, as opposed to the situation where the aircraft object comes into the debtor's patrimony only after the fact pursuant to a leasing or conditional sales agreement. However, the priority scheme of the Convention, including the priority scheme in Articles 39 or 40, does not permit distinctions to be drawn between competitions involving a charge, and those involving leases and conditional sales (purchase money financing). So the problem must be solved uniformly, or the rights of judgment creditors would not be preserved at all.

[99] With that caveat in mind, the question is whether Article 39 or 40 provides the most appropriate mechanism for protecting the rights of judgment creditors.

[100] A declaration under Article 39 enables a Contracting State to list those non-registrable interests that are to have priority over a registered interest. It is the most disadvantageous approach from the perspective of the aircraft financing industry since it means prospective financers cannot place exclusive reliance on the international registry to assess their priority risk. Indeed, it is an unworkable approach in the context of existing Canadian domestic law, at least in the case of those Canadian jurisdictions in which the judgment creditor's property and priority rights arise through registration as opposed to seizure. Prospective financers cannot realistically be expected to search each separate provincial registry for outstanding judgments.

[101] To meet the risk assessment concerns of aircraft financers, the Canadian declarations made under Article 39 could protect only those judgment creditors who effect physical seizure of the aircraft object before the competing consensual interest is registered under the Convention. There would have to be a further caveat that the seizure be effected in circumstances in which, under the relevant domestic law, the seizure would give the judgment creditor priority over the holder of an unregistered interest of the kind in question. This caveat is required by the wording of Article 39 and is needed to fully protect unregistered conditional sellers and lessors who are not necessarily subordinated under all provincial laws to the claims of the lessee's or buyer's judgment creditors. Presumably, prospective financers could verify with relative ease whether seizure has taken place. Nonetheless, this approach imposes an inquiry burden beyond the international registry itself, and may require consequential amendments to domestic law to be workable.

[102] The alternative solution would be to declare the interest of judgment creditor to be a registrable interest pursuant to Article 40 of the Convention so as to trigger the first to register priority rules of the Convention. Prospective aircraft financers would then be able to rely exclusively on the results of a search of the international registry.

[103] The Working Group initially had some concerns with this solution in so far as it would trigger the Convention's first-to-register rule even where the judgment creditor's interest came into conflict with the interest of a conditional seller or lessor of an aircraft object. What if the rights of a judgment creditor registered before the object was even delivered to the buyer or lessee pursuant to the sale or lease? Might the first to register rule not result in unfairly depriving the subsequently registering seller or lessor of their ownership rights? On reflection, the Working Group decided that this was not a real concern. First, it is very unlikely that a judgment creditor would be able to register ahead of the seller or lessor since the Convention requires a serial number description and this would be difficult if not impossible for the judgment creditor to obtain in advance of delivery of the object to the judgment debtor. Second, conditional sellers or lessors can easily protect themselves by registering in advance of the execution of the actual lease or sale (registration of prospective interests being permitted under the Convention). However, there are significant policy issues associated with this solution.

[104] First, if the seller or lessor failed to register or registered tardily, the holder of a registered judgment would take priority even though under Canadian domestic law this result would not necessarily follow in the equivalent scenario, e.g. in the case of those jurisdictions (Ontario and Quebec) which do not require registration of "true" leases as a condition of third party effectiveness, and also in those jurisdictions (most) which give the lessor or seller a grace period for effecting registration without loss of priority to an intervening judgment after delivery of the object to the buyer or lessee.

[105] Second, under current provincial and territorial law, a judgment creditor who enforces its rights against specific assets of the judgment debtor generally must share the fruits of enforcement with the debtor's other creditors (pursuant to the Creditors' Relief Acts in the common law provinces and to some extent, pursuant to the *Civil Code* in Quebec). The Convention, in contrast, rank registrable non-consensual interests on a first to register basis with the result that competing registered judgment creditors would be ranked on a "first come first

served" basis. A similar policy question arises in the bankruptcy context. Although the position remains somewhat unclear, it seems that a judgment "lien" acquired under provincial or territorial law prior to bankruptcy is terminated by the bankruptcy and the asset vests in the trustee for distribution among all creditors according to the ranking scheme of the Bankruptcy and Insolvency Act. In contrast, under Article 30 of the Convention, a registered interest is ipso facto effective against the bankruptcy trustee.

[106] It may be that this second policy concern could be accommodated by amending the relevant provincial, territorial and federal laws to provide that the priority rights of a judgment creditor acquired by registration under the Convention are subject to collective sharing pursuant to the relevant provincial or territorial system. Alternatively, it may be felt that an exception to the collective sharing principle in favour of a "race to the swift" principle could be acceptable in the limited context of aircraft financing. As for the bankruptcy issue, again it would be possible to amend the BIA to provide that in the event of bankruptcy, the judgment debtor's bankruptcy trustee succeeds to the priority of a registered interest acquired by a judgment creditor in assets covered by the Convention for the benefit of all creditors.

[107] There is a third, conceptual, concern, with the Article 40 solution. Under current domestic law, a creditor who obtains a judgement does not thereby obtain any property right in the debtor's assets. As noted earlier, it is only through seizure or registration in a provincial registry that a judgment "lien" attaches. An Article 40 declaration declaring the interest of a judgment creditor to be a registrable interest would therefore need to be accompanied by amendments to domestic law to provide that a judgment creditor who so registers ipso facto acquires a "judgment lien" in the relevant asset. Otherwise the judgment creditor's interest would not qualify as a non-consensual interest within the definition of the Convention, *i.e.*, an interest created by operation of the law of the Contracting State to secure an obligation.

Working Group Recommendation - Article 39 Declaration

[108] Members of the Working Group were of the view that a list of non-registrable non-consensual rights and interests should be kept to a minimum or should not even exist. The main objective should be to avoid secret liens. As this is matter of policy for each enacting jurisdiction, Members of the Working Group nevertheless agreed that there should be a general or specific declaration as to non-registrable non-consensual rights and interests. The Working Group recommended that if a list of those non-registrable non-consensual rights and interests should be prepared in domestic law it would be by way of regulation. The content of this list would then be the subject of a Declaration. It is worthwhile to note that Article 39 (1) b) of the Convention provides specifically that nothing in the Convention shall affect the rights of a State or a State entity, intergovernmental organisation or other private provider of public services to arrest or detain an object under the laws of that State for payment of amounts ought to such entity, organisation or provider directly relating to those services in respect of that object or another object.

Working Group Recommendation - Article 40 Declaration

[109] Members of the Working Group agreed that there should be a declaration as to the categories of non-consensual rights and interests that shall be registrable (e.g., tax liens, airport liens, mechanics liens, repairers liens). The Working Group recommended that a list of those categories of non-consensual rights and interests be prepared in domestic law by way of regulation. The content of this list would then be the subject of a Declaration.

(c) – Article 53 of the Convention - Declaration as to the "court" or "courts" for the purposes of Article 1 and Chapter XII de la Convention

[110] Members of the Working Group agreed that the act should provide for the "court" or "courts" having jurisdiction for the purposes of Article 1 and Chapter XII of the Convention. That "court" or those "courts" would then be identified in a declaration. Members of the Working Group were of the view that such jurisdiction should be given to Superior courts in both federal and provincial legislation as it is done under bankruptcy and insolvency laws.

(d) – Article 50 of the Convention - Declaration as to the exclusion of purely internal transactions

[111] Members of the Working Group agreed that provinces, territories and the federal should not exclude from the scope of the Convention purely internal transactions. Since what could be a purely domestic transaction from the outset could become an international transaction, because of refinancing purposes for example, the Working Group was of the view that avoiding uncertainties with regard to the transition from a domestic regime to an international one was essential. For example, it was noted that it could create uncertainties with regard to prior only domestically registered interests. Therefore, by including purely internal transactions, a transition provision for that purpose would not have to be implemented in domestic law. Finally, since the number of purely internal transactions for aircraft equipment is very small, there would be very little impact on the current regime to cover these transactions by the Convention ant the Protocol. To do otherwise would result in high costs and little benefits for the industry.

(e) – Article 54(1) of the Convention - Declaration as to the prohibition of a chargee's right to grant a lease

[112] Members of the Working Group agreed that we should not prohibit a chargee's right to grant a lease for the administration of the equipment when the chargor is in default. This is in conformity with domestic law.

(f) – Article 54(2) of the Convention - Declaration as to the exclusion of self-help remedies

[113] Members of the Working Group agreed that Common Law jurisdictions in Canada do not need to exclude self-help remedies. As these remedies are not generally available in Quebec members of the Working Group agreed that Quebec may consider requesting Canada to make a declaration excluding self-help. In the absence of such Declaration, the self-help remedies would be available for the purpose of the Convention/Protocol.

(g) – Article 55 of the Convention - Declaration as to the (partial) non-applicability of Article 13 of the Convention

[114] Members of the Working agreed that Article 13 as it stands is in conformity with Canadian Law. Therefore, there is no reason to make a declaration under Article 55 of the Convention.

(h) – Article X of the Protocol - Declaration as to the applicable period constituting "speedy relief" (See the declaration pursuant to Article 13 of the Convention and XXX(2) of the Protocol)

[115] The Working Group agreed that each jurisdiction will have to decide whether it can implement this provision with a delay imposed on the judiciary. Some Rules of Court or civil procedures may allow this where others may not. In that later case, since those rules are usually prepared by the judiciary they may not be readily amendable. In that case, jurisdictions that may not be in a position to give the force of law to Article X(1) and (2) will have to exclude the application of those provisions. The rest of Article X is in conformity with domestic law.

(i) – Article XI of the Protocol (Alternative A, par. 3, Alternative B, par. 2) - Declaration as to the applicable period constituting the "waiting period"

[116] Members of the Working Group recommend the implementation in federal law of Alternative A and would recommend a waiting period of 60 days. This would level the playing field between Canadian and the United States industry that already has the benefit of a similar provision in American law.

(j) – Article XIX of the Protocol - Declaration as to the designation of entry points to the International Registry (See Article 18(5))

[117] Members of the Working Group recommend not to provide for the designation of entry points. Since the number of transactions for aircraft equipment is very small, there would be very little impact on the current domestic registration facilities if these transactions could be registered directly with the International Registry. To do otherwise would result in high costs and little benefits to the industry.

(k) – Article 52 of the Convention and Article XXIX of the Protocol - Declaration as to the territorial units to be covered by the instrument

[118] The Working Group is of the view that no provision is needed in the act to provide for the territorial application of the instrument. The mere fact of enacting implementing legislation and requesting that the application of the instrument be extended to the jurisdiction is sufficient for that purpose. But for transparency purposes some jurisdictions may prefer to include such provision.

(l) – Article XXX(1) of the Protocol - Declaration as to the application of Articles VIII, XII and XIII of the Protocol

[119] Members of the Working Group recommended to implement Articles VIII and XII as they are both in conformity with domestic law. Article XIII that falls under federal jurisdiction will not be implemented at this stage as it does not conform with domestic law.

(m) – Article XXX(2) of the Protocol - Declaration as to the (partial) applicability of Article X of the Protocol

[120] See (h) above.

(n) – Article XXX(3) of the Protocol - Declaration as to the application of Article XI Alternative A or Alternative B

[121] See (i) above.

4 – Interpretation

[122] The Working Group has decided not to include the usual interpretation provision that states that “This Act shall be interpreted in good faith in accordance with the ordinary meaning to be given to its terms in their context and in light of its object and purpose”. The Working Group was of the view that it was unnecessary as this is a motherhood statement and that such provision may not be combined that easily with Article 5 of the Convention. In any event, Articles 31 and 32 of the Vienna Convention on the Law of Treaties, Can. T.S. 1980 No. 37 are accepted in Canadian law by recent court decisions. In Thomson v. Thomson, [1994] 3 S.C.R. 551, at pp. 577-578, the Justice La Forest wrote “[i]t would be odd if in construing an international treaty to which the legislature has attempted to give effect, the treaty were not interpreted in the manner in which the State parties to the treaty must have intended. Not surprisingly, then, the parties made frequent references to this supplementary means of interpreting the Convention, and I shall also do so. I note that this Court has recently taken this approach to the interpretation of an international treaty in Canada (Attorney General) v. Ward, [1993] 2 S.C.R. 689”.

[123] The Working Group has decided to provide in that Act that in applying or interpreting the Convention and the Protocol recourse may be had to:

[124] The Explanatory Report and Commentary on the Cape Town Diplomatic Conference to Adopt a Mobile Equipment Convention and an Aircraft Protocol, October 29-November 16, 2001 and the Consolidated Aircraft Convention, being the Convention as amended by the Aircraft Protocol, the text of which was prepared by the International Civil Aviation Organization (ICAO) and the International Institute for the Unification of Private Law (Unidroit).

[125] This provision is in addition to the treaty interpretation principles. Enacting jurisdictions may simply indicate references for these United Nations and Unidroit documents in their legislation. Alternatively, some jurisdictions could also publish these documents in their Gazette for

dissemination purposes or make reference to the documents as published in the Canada Gazette for dissemination purposes

5 - privileges and immunities

[126] Articles 27 of the Convention dealing with privileges and immunities will be set out in federal legislation and therefore the Uniform Act will not deal with such.

6 – Ratification

[127] It is necessary to provide when the Convention and the Protocol will have the force of law for the enacting jurisdiction. It is important to provide for an effective and simple provision to co-ordinate the entry into force of the Convention and Protocol for Canada at the international level, the coming into force of domestic implementing legislation and regulation, and giving the Convention and the Protocol the force of law. Proclaiming the implementing legislation in force on the day the Convention and Protocol come into force for Canada is not recommended since this may not suit the legislative agendas of all jurisdictions. Instead, it is recommended that the legislation implementing the Convention and Protocol come into force on Royal Assent. The Act is drafted such that the Convention and Protocol are given the force of law domestically only from the date they come into force at the international level for Canada and the jurisdictions declared pursuant to Article 52 of the Convewntion and Article XXIX of the Protocol. That date is either the first day of the month following the expiration of three months after the date (1) of the necessary number of instruments of ratification or (2) of the deposit of Canada's instrument of ratification. Note that in the case of jurisdictions adopting implementing legislation after the coming into force of the Convention and Protocol for Canada, the Act provides that the Convention and Protocol have the force of law, not from their entry into force in accordance with Article 49 of the Convention and XXVIII of the Protocol, but rather on the entry into force of the declaration extending the application of the Convention and of the Protocol to that jurisdiction in accordance with Article 52 of the Convewntion and Article XXIX of the Protocol. Finally, it is important to provide for the eventuality where declarations could be substituted before the Convention and Protocol come into force at the international level for Canada.

H – Miscellaneous Issues

1 – Address of Unidroit's website

[128] < http://www.unidroit.org >

2 – Address of ICAO's website

[129] < http://www.icao.int >

3 – Other useful documents

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PANAHY, Dara A., et Raman MITTAL, "The prospective Unidroit Convention on international interests in mobile equipment as Applied to space property", (1999) 2 *Unif. L. Rev.* 303.

ROSEN, Howard, "Creating an international security structure for Railway rolling stock: an idea ahead of its time?", (1999) 2 *Unif. L. Rev.* 313.

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STOUFFLET, Jean, « L'avant-projet de Convention d'Unidroit: Réflexions sur son insertion dans le système juridique français », (1999) 2 *Rev. de D. Unif.* 361.

WEBER, Ludwig, et Silvério ESPÍNOLA, "The development of a new Convention Relating to international interests in mobile equipment, in particular aircraft equipment: a joint ICAO- Unidroit project", (1999) 2 *Unif. L. Rev.* 463.

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IV – THE ULCC INTERNATIONAL INTERESTS PROJECT WORKING GROUP

[130] A list of the Members of the Working Group is attached to this Report for information (additional members participated in the Working Group during its work to bring the Uniform Act in line with the Convention and Protocol and were therefore added to the list).

V – RECOMMENDATION

[131] That this Report and the attached Uniform Act be discussed and adopted in principle.

[132] That further to the October 29 to November 16, 2001 Diplomatic Conference the Report and the Uniform Act be modified accordingly and formally adopted according to a March 30, 2002 Rule, or later.