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# Analysis of Non-Consensual Rights and Interests under Article 39 of the Cape Town Convention

John Pritchard and David Lloyd\*

*This article will analyse how Article 39 entitled 'Rights having priority without registration' should be understood and applied under the Convention to aircraft objects. It begins with a review of the general history and policies behind both generic and aircraft-specific non-consensual rights and interests, and rights of detention with respect to aircraft, and how they have related in terms of priority to consensual interests. The article discusses the Article 39 policy objectives and conflicts within the purposes and intended benefits of the Convention and the Aircraft Protocol. It then compares the priority rules in Articles 29, 39 and 40 in relation to non-consensual rights and interests and describes how Article 39 works within the Convention. We then focus on the differing categories of non-consensual rights or interests that have been declared to date and conclude with policy suggestions for Contracting States in making their declarations under Article 39. The final section analyzes practical examples of enforcement of the Convention where non-consensual rights or interests may arise.*

## 1. Introduction

The purpose of this article is to analyse how Article 39 of the Convention,<sup>1</sup> which is entitled 'Rights having priority without registration' should be understood and applied within the sphere of application<sup>2</sup> of the Convention to 'aircraft objects' as defined in the Aircraft Protocol.<sup>3</sup> Article 39 of the Convention, the

non-consensual rights or interests defined in Article 1(s) of the Convention and declarations of Contracting States will be the main focus since Article 39 deals with preferred priorities without registration. However, attention is also given to Article 40 on 'Registrable non-consensual rights or interests' as its principles are helpful to illustrate the contrast with Article 39. This Article also provides suggestions to Contracting States in making their declarations or subsequent declarations<sup>4</sup> in Article 39.

Article 39 reads:

Article 39 — Rights having priority without registration

1. A Contracting State may at any time, in a declaration deposited with the Depositary of the Protocol declare, generally or specifically:

- (a) those categories of non-consensual right or interest (other than a right or interest to which Article 40 applies) which under that State's law have priority over an interest in an object equivalent to that of the holder of a registered international interest and which shall have priority over a registered international interest, whether in or outside insolvency proceedings; and

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<sup>1</sup> Convention on International Interests in Mobile Equipment adopted in Cape Town, 16 November 2001.

<sup>2</sup> See Convention Articles 2 and 3; See Roy Goode, *Convention on International Interests in Mobile Equipment and Protocol Thereto on Matters Specific to Aircraft Equipment: Official Commentary* (hereinafter, 'Official Commentary') (3<sup>rd</sup> edn UNIDROIT 2013) para 2.18.

<sup>3</sup> Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment (Cape Town, 2001), in force from 1 March 2006. Other Protocols are not covered in this article.

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<sup>4</sup> Article 57.

(b) that nothing in this Convention shall affect the right of a State or 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 owed to such entity, organisation or provider directly relating to those services in respect of that object or another object.

2. A declaration made under the preceding paragraph may be expressed to cover categories that are created after the deposit of that declaration.

3. A non-consensual right or interest has priority over an international interest if and only if the former is of a category covered by a declaration deposited prior to the registration of the international interest.

4. Notwithstanding the preceding paragraph, a Contracting State may, at the time of ratification, acceptance, approval of, or accession to the Protocol, declare that a right or interest of a category covered by a declaration made under sub-paragraph (a) of paragraph 1 shall have priority over an international interest registered prior to the date of such ratification, acceptance, approval or accession.

The definition in Article 1(s) reads:

‘non-consensual right or interest’ means a right or interest conferred under the law of a Contracting State which has made a declaration under Article 39 to secure the performance of an obligation, including an obligation to a State, State entity or an intergovernmental or private organization.

For convenience, in this article, we use the term ‘NCRI’ to mean non-consensual right or interest.

Article 39 brings order to the treatment of priorities between national law conferred NCRIs that are declared (and any that are not declared) by a Contracting State and international interests that would not, without the use of Article 39, have any basis for consistent interpretation by courts of that Contracting State. In order to accomplish that ordering of priorities, the Convention does not create, and does not permit the Contracting States to create, a new right or interest or a new priority but merely permits them to choose whether to declare that a category of

local NCRIs that already have priority over consensual interests (which are equivalent to an international interest of the same type as such consensual interests in an aircraft object in that Contracting State) should have the same priority against registered international interests constituted under the Convention within that Contracting State.<sup>5</sup>

Section 2 of this article covers the general history and policies behind both generic and aircraft-specific NCRIs, such as mechanic’s liens and rights of detention with respect to aircraft,<sup>6</sup> and how they have related in terms of priority to consensual interests, such as security interests, and the resulting conceptual basis for the treatment of these NCRIs under the Convention. Section 3 discusses the Article 39 policy objectives and conflicts within the purposes and intended benefits of the Convention and the Aircraft Protocol. It then compares the priority rules of Articles 29, 39 and 40 in relation to NCRIs and describes how the Convention defines NCRIs and how Article 39 works within the Convention. Section 4 focuses on the differing categories of NCRIs that have been declared to date and concludes with policy suggestions for Contracting States in making their declarations under Article 39 and, to some extent, Article 40. Finally, Section 5 summarizes practical examples of enforcement of rights in the context of the Convention where NCRIs are involved and provides guidance to a practitioner or a court when applying the Convention and the Aircraft Protocol to these issues, including the discharge of NCRIs that should not have been registered on the International Registry.

<sup>5</sup> If a state does not declare a particular category, then such a non-consensual right or interest would not have such a preference against a registered international interest although it would remain valid against unregistered interests to the extent provided by law. See Section 3(b)(ii) below for further discussion.

<sup>6</sup> This article will generally speak in terms of ‘aircraft’ but the analysis applies equally to all aircraft objects: airframes, aircraft engines and helicopters which are defined in the Aircraft Protocol.

## 2. The historic framework of non-consensual rights or interests and their priority

The history and policy underpinnings of (1) generic and aircraft-specific liens and rights of retention, which are the basis for categories that may be declared in relation to aircraft objects under Article 39(1)(a), and (2) generic and aircraft-specific rights of detention (as opposed to retention), which may be preserved pursuant to a declaration in relation to aircraft objects under Article 39(1)(b), provide context for the policies of NCRIs that are reflected in Article 39, the understanding thereof and the current and future considerations by Contracting States in the making of declarations and subsequent declarations as to categories of such nationally preferred NCRIs.

### (a) *Generic non-consensual rights and interests*

The defined term ‘non-consensual right or interest’ is intended for use under the Convention with any object that may be subject to a Protocol. The term is defined as being a ‘right or interest conferred under the law of a Contracting State ... to secure the performance of an obligation ...’. The Official Commentary points out that the terms ‘right’ and ‘interest’ are not defined in the Convention, and ‘in general an interest denotes a right *in rem* in an asset whilst a right is a personal right of possession or control of ...an asset in which the holder [of the right] has no interest (as in the case of a right of detention of an aircraft for airport dues...),<sup>7</sup> and further notes that it is ‘a right or interest created by law, not by agreement’.<sup>8</sup> Even if a court approves a contract it does not mean the right or interest has been conferred by law. The Official Commentary explains that the NCRI cannot include a court-approved secured loan made to a debtor-in-possession in insolvency proceedings despite the need for court approval because the loan and its security are consensual and created by agreement.<sup>9</sup>

<sup>7</sup> Official Commentary, Goode (n 2) para 2.33.

<sup>8</sup> Ibid, para 2.33(4).

<sup>9</sup> Ibid.

The most common examples of Article 39(1)(a) NCRIs are ‘non-consensual liens in favour of repairers for repairs to objects in their possession or for unpaid wages due from insolvent employers (which, though usually unsecured, are in some States given priority even over the claims of secured creditors)’ and liens for unpaid taxes and charges related to such objects.<sup>10</sup> For the review of the historical and policy development of generic NCRIs, we will focus on the sources of generic liens (mostly under the laws of England and the United States) and rights of retention (in respect of which we make mention of that concept in civil code countries) in favour of repairers and service providers in relation to goods and finally on the source of rights of detention in England.

### (i) *Generic liens and rights of retention*

The possessory lien concept developed in the common law countries, while the right of retention appears to have developed in the civil code influenced countries as a parallel concept. The workman’s lien was recognized in England, as described in old documents, when liens were upheld in favour of innkeepers on a guest’s baggage and in favour of a tailor on gowns made for a customer.<sup>11</sup> The lien expanded over the centuries to cover all types of work, including repairs of goods and other trades and services that no longer exist today. The rationale was commercial convenience to help ensure workmen were paid especially in times when their bargaining power was low. The workman’s lien was a remedy by way of self-help and it has been cited as a remedy *in rem* upon the goods.<sup>12</sup>

Generic liens and other rights of third parties with respect to chattels developed in other common law countries in favour of the ‘furnisher of services’ who had a right to hold

<sup>10</sup> Ibid, para 4.271, Appendix XIIC.

<sup>11</sup> Graham McBain, ‘Codifying Common Law Liens’ (2007) 20(4) *Commercial Law Quarterly* 3, 5, referencing reports prior to 1465.

<sup>12</sup> Ibid 6.

the property of his customers which came into his possession until he was paid.<sup>13</sup>

The right of retention in civil code countries was described in similar terms. One commentator stated that the right of retention ‘refers to cases in which a creditor, that holds an asset belonging to its debtor, may refuse to restitute it as long as it remains unpaid, in the understanding that such asset has not been given as a guaranty’.<sup>14</sup>

Other sources cite older commentaries to describe the development from a right to refuse to surrender possession with no right to sell the property into a right to sell the property which became called a ‘particular’ lien in common law countries.<sup>15</sup> At common law in England, the general lien developed<sup>16</sup> as ‘a right to retain the property of another on account of a general balance due from the owner’.<sup>17</sup> In addition to commercial convenience, the rationale behind the general lien developed as a way to satisfy a need for financing of industrialization and increasingly complex transactions involving multiple parties in the multi-step process of manufacturing and finishing goods in industries, such as textiles, that had a chronic lack of credit and a rudimentary banking system.<sup>18</sup> Over

time, the number of general liens declined, and McBain concludes from a review of cases that the general lien no longer exists as to goods and that only the common law particular lien remains as a common law possessory lien in England. The general lien was developed for economic reasons as a form of financing, and accordingly came to an end due to the combination of changes in the industries it supported and the inequitable advantage that it provided to certain creditors against the creditors as whole for whom the debtor’s estate should be distributed proportionately.<sup>19</sup>

Other examples of the development of liens to support growth and industrialization existed in the United States. A wide variety of state statutes created or reinforced service liens in the 1800’s and the early 1900’s and they were aimed at helping service industries that were important to the local economy. Often the different state statutes would simply copy the common law lien into a statutory lien and it would be adapted to the economic needs of the industry involved.<sup>20</sup>

The trend through the development of liens in both England and the United States appeared to be tied closely to various economic reasons, both as the liens were created and used and as they were decided to be no longer needed. The supporting reasons that one can derive from the above summary include the evolution of other forms of financing or other forms for securing payment for services and the rationale that the liens were counterproductive to efficient economic development.

Turning to the issue of priority of liens as against security interests in the same property, Professor Gilmore in the 1950’s analyzed how the different jurisdictions in the United States had dealt with the issue of priority between the statutory lien and the security interest under the relevant statutes at the time as the lengthy state by state process of adopting the Uniform Commercial Code (‘UCC’) in the United States was begun. He divided

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<sup>13</sup> Grant Gilmore, *Security Interests in Personal Property* (Little Brown & Company 1965) 873-75, citing examples of the workman’s lien, warehouseman’s lien on stored goods and common carrier’s liens on shipped goods; McBain (n 11) 5.

<sup>14</sup> Manual Borja Soriano, ‘Teoría General de las Obligaciones’ (21st ed. Porrúa 2012) 523, citing other civil code commentators from other civil code countries. In particular Borja Soriano cites Bonnacese who explains that the right of retention cannot be considered as a right *in rem*, as it lacks the required organic elements and explains that the credit that is vested in the right of retention should be considered an unsecured credit. (Under the Convention, it does not matter in respect of the term non-consensual right or interest whether it is secured or unsecured and this flexibility of the definition in the Convention is a necessary part of it being applicable on a global basis.)

<sup>15</sup> McBain (n 11) 5.

<sup>16</sup> *Ibid* 4, 6.

<sup>17</sup> *Ibid*.

<sup>18</sup> *Ibid* 10-11.

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<sup>19</sup> *Ibid* 13-14.

<sup>20</sup> Gilmore (n 13) 874.

the different states into three groups: one group (perhaps as many as half of them) had no position on the issue of priority, another group subordinated the statutory liens to the security interests in the same equipment, and a third group provided that the statutory lien had priority over existing, perfected security interests. There was no single guiding principle within these three groups that would allow prediction as to how the different jurisdictions would act.<sup>21</sup> The new UCC section on secured transactions provided a rule as to priority between such liens and security interests that solved the variance among the state statutes by providing a fall back rule giving the local possessory lien on goods that secured payment or performance of an obligation for services or materials priority over a security interest unless a local statute provided otherwise.<sup>22</sup> Much later in the 1990's, the UCC provided the same type of fall back rule as to priority between such possessory liens and the rights of lessors.<sup>23</sup> This evolution illustrates that there can be a development of systems with regard to priority between holders of possessory liens and security interest holders and lessors on generic equipment that provides a greater level of predictability to equipment asset based finance while also allowing for variance among jurisdictions.

(ii) *Generic Rights of Detention*

A detention right, unlike a lien or a right of retention, is not based on possession nor does it seek to prevent other parties with an interest from having access to the asset. In England, the idea of a right of detention can be traced to maritime port laws under the Merchant Shipping Act 1894, where a number of different situations may permit the dock owners to exercise a right of detention. For example, where damage had been caused by a foreign ship to the docks or piers or other port infrastructure, the vessel may be

detained.<sup>24</sup> The Air Navigation Act 1920 incorporated this concept which was then copied into the Civil Aviation Act 1949.

Courts, in early cases considering the rights of dock owners to detain ships for outstanding payments for dock maintenance and other services, held that it was a statutory right of the dock owners to detain the ships and that the right of detention was their only protection for the payment of dues.<sup>25</sup> The era in which these rights of detention were created in the 1800's and applied in the case above in 1905 was one in which steamships were moving in and out of port and going long distances and were not easily tracked. The point of the detention right at that time is more supportable than the right of detention for aircraft airport charges today since the airport has a great deal more control over who uses their services and more information on where they can be located. In addition, these rights of detention are in most cases only against the vessel that incurred the charges and not against a fleet of vessels no matter who owns them.<sup>26</sup>

(b) *Aircraft non-consensual rights and interests*

Aircraft-related NCRIs developed from the existing generic liens and rights of retention on other goods and equipment and maritime port rights of detention that are discussed in summary form above. Here we focus briefly on aircraft mechanic's liens, whether called

<sup>24</sup> The Merchant Shipping Act 1894 was preceded by three previous statutes. The Liverpool Dock Act, 1855, s. XXIX is an example and provided: 'In every case in which any Damage shall be done to any Lock, Gate, Bridge, Pier, Landing Stage, Jetty, Platform, Quay, Wharf, Warehouse...such Vessel may be detained until such Damage shall have been paid for or a Deposit shall have been made....' (emphasis added).

<sup>25</sup> See *The Emilie Millon* [1905] 2 KB 817, 821. Note, legal commentary on this case also refers to *The Emilie Millon* as *Mersey Docks*, the name of one of the parties.

<sup>26</sup> Graham McBain and Julian Acrapopulo, 'Aircraft Fleet Liens Under English Law', para 7, in Graham McBain (ed), *Aircraft Liens and Detention Rights* (Sweet & Maxwell 2012) (hereinafter "McBain in *Aircraft Liens*").

<sup>21</sup> Ibid.

<sup>22</sup> Uniform Commercial Code, section 9-333.

<sup>23</sup> Ibid, section 2a-306.



possessory common law liens or rights of retention in aircraft, on statutory lien filing systems that have been created, and on how the NCRIs in aircraft relate to the Geneva Convention and to the development of the Convention and the Aircraft Protocol. Then we consider briefly the controversial area of rights of detention of aircraft and of fleet liens.

(i) *Mechanic's liens and rights of retention on aircraft*

Mechanic's liens in common law jurisdictions and rights of retention in civil code and other jurisdictions, in each case with respect to repair or other services enhancing or preserving the value of the aircraft, are derived from a long history of such liens and rights with respect to other goods and other industries that have already been described above. Similarly other non-consensual liens and interests with regard to aircraft, such as tax liens, are based on the law applicable to all types of goods and assets and the law has been adapted in many cases to the aircraft industry.

A brief look at the book by Graham McBain on *Aircraft Liens and Detention Rights*,<sup>27</sup> which has chapters on the law on aircraft liens and detention rights in over 80 countries, reveals that the concept of some type of possessory lien or right of retention exists in most jurisdictions; and it is not surprising that the Official Commentary in Appendix XIIC shows that most Contracting States that declared specifically rather than generally as to NCRIs included a form of repairer's lien. Being possessory in most cases means that they are largely secret liens or rights of retention unless one knows that the aircraft is undergoing repair or maintenance at the time. Systems have developed to fit the liens into filings that are public in some jurisdictions, but even in the case of the United States described below, this has not eliminated possessory liens for repair.

This is the case with the filing system of the Federal Aviation Administration ('FAA') in the United States for aircraft mechanic's and similar liens on FAA-registered aircraft. It applies the

state law liens and priorities, along with any notice or filing requirements under state law, to the filings to be made at the FAA Aircraft Registry. The FAA adopted a procedure that enabled state law created notice filings to be made at the FAA when a state statute provided satisfactory provisions for filing, but which did not apply to a possessory lien where there was no state filing statute.<sup>28</sup>

In the FAA system, the priority position of the mechanic's lien as against a security interest or a conditional sale or a lease or a title transfer was settled by the local state jurisdictions so that once filed at the FAA an interest in an aircraft had the priority established under applicable state law with the exception of liens as to which a party had actual notice (unlike the Convention in which knowledge is not a factor).<sup>29</sup> The local state laws would determine if a NCRI had priority over a filed mortgage on an aircraft.

But the question of how the priority among different national jurisdictions with respect to mortgages and leases of aircraft as they related to NCRIs was not resolved. The issue of recognition by Country B of a NCRI that arises and is effective in Country A is generally considered under the conflicts of law rules of the forum.<sup>30</sup> Apart from references to priority rules under the Geneva Convention which is described in subsection (b)(ii) below or to the Convention, the general approach (described in many of the different jurisdictions in the McBain book on *Aircraft Liens and Detention Rights*)<sup>31</sup> to the question is first one as to recognition and then as to priority. Recognition of liens is similar in many jurisdictions to the principles of recognition of judgments and usually one of not being in violation of public policy or being illegal

<sup>28</sup> 46 Fed.Reg. 61,528 (Dec 17, 1981), following state law as to lien coverage and as to whether it was recordable, in order to 'assure uniformity'.

<sup>29</sup> *Philko Aviation, Inc. v Shacket*, 462 U.S. 406 (1983).

<sup>30</sup> Official Commentary, Goode (n 2) paras 4.269, 4.270.

<sup>31</sup> McBain in *Aircraft Liens* (n 26) paras 16.1, 16.2.

<sup>27</sup> *Ibid.*

under the laws of the forum. The question of priority between a foreign aircraft lien and a domestic one is often considered procedural, and it is stated that it may be determined by a court under its priority rules as a matter of procedure.<sup>32</sup> The completely unpredictable nature of the priority that an international interest or a sale would face against a NCRI with respect to an aircraft object in other jurisdictions is what the Convention aims to solve in Contracting States by Article 39.

(ii) *The Geneva Convention*

The first international convention to attempt to regularize the recognition and priority of interests and rights in aircraft was signed in 1948 in Geneva and named the Convention on the International Recognition of Rights in Aircraft ('Geneva Convention').<sup>33</sup> Today, 89 countries are parties to the Geneva Convention, and it is now being eclipsed by the Convention and the Aircraft Protocol. The Aircraft Protocol provides in Article XXIII, as between Contracting States to the Convention, that the Geneva Convention is superseded 'as it relates to aircraft' and aircraft objects, except that 'with respect to rights or interests not covered or affected by the present Convention' (which of course includes the Aircraft Protocol), the Geneva Convention 'shall not be superseded'. Below, we discuss very briefly whether any part of the Geneva Convention has not been superseded as to NCRIs because if so, it would therefore continue to be part of the laws on aircraft NCRIs outside of the Convention.

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<sup>32</sup> Ravi Nath, 'India' in Graham McBain (ed), *Aircraft Liens and Detention Rights* (Sweet & Maxwell 2012); Nicolai Vella Falzon, 'Malta' in *Aircraft Liens and Detention Rights* (2010) paras 16.1, 16.2; Federico Santacruz, 'Mexico' in *Aircraft Liens and Detention Rights* (2011) paras 16.1, 16.2; John Pritchard, 'United States of America' in *Aircraft Liens and Detention Rights* (2011) paras 16.1, 16.2; Restatement (Second) of Conflict of Laws §§ 187, 251 cmt. f & g, 253 cmt. c (1971).

<sup>33</sup> Convention on the International Recognition of Rights in Aircraft (signed June 19, 1948) ICAO Doc 7620 (Geneva Convention).

The Geneva Convention begins by stating that 'it is highly desirable in the interest of the future expansion of international civil aviation that rights in aircraft be recognised internationally'. The immediate question is which 'rights' in aircraft is the Geneva Convention saying should be recognised?

Article IV of the Geneva Convention addresses rights conferred under the law of a Contracting State for claims in respect of salvage and extraordinary expenses indispensable for the preservation of the aircraft and states that these would have priority over any other interest for a period of three months without any recording. Thereafter the claim would need to be recorded. As noted above, to the extent that the Geneva Convention does address NCRIs such as the rights of salvage and extraordinary preservation expenses above, in a case where the relevant parties to a priority issue are Contracting States to both the Geneva Convention and the Convention, then the Geneva Convention would be superseded with respect to such rights or interests pursuant to Article XXIII of the Aircraft Protocol.

Where there is a Geneva Convention Contracting State that is not also a Contracting State under the Convention, the Convention Official Commentary states that the Convention and Aircraft Protocol should be applied where the law of a Convention Contracting State is the applicable law for purposes of that Geneva Convention priority determination. Non-consensual rights or interests under the Convention would be included if there were such an application.<sup>34</sup> For our discussion, perhaps the most important aspect of the Geneva Convention is that it did not expressly or clearly cover any NCRIs other than the salvage and extraordinary and indispensable expenses referenced above. In particular, the lack of ability to protect other rights was a reason for the public reservations made by Mexico as to its inability to recognize the priority of fiscal claims of the government

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<sup>34</sup> Official Commentary, Goode (n 2) paras 5.104, 5.106.



and claims arising out of work contracts. Additionally, in the process of adopting the Geneva Convention, the right to prefer fiscal claims, such as tax and other charges, was dropped due to perceived exposure of security interests to such claims.<sup>35</sup>

It is generally considered that the inability to protect these and other non-consensual preferred rights or interests such as the right of detention were among the reasons why some other jurisdictions, England among them, did not ratify the Geneva Convention. The drafters of the Convention were aware of these defects, among others, in the Geneva Convention and, as discussed below in subsection (c), set out to permit the recognition of preferred national NCRIs should a Contracting State desire to do so in its own jurisdiction.

(iii) *Rights of detention in aircraft*

A detention right over an aircraft may be exercised in a variety of circumstances such as: airport charges, air navigation charges, licensing, customs, noise and aircraft emissions, patents, public health, unpaid tax, and under laws that do not come under the Convention, such as those for crimes, war or national emergency. Accordingly, the primary purpose for a detention right can vary considerably. Depending on the circumstances, a detention right may also permit the sale of an aircraft or the forfeiture of an aircraft. For example, an aircraft can be sold for the non-payment of international air navigation charges, such as Eurocontrol charges.<sup>36</sup>

A recent case, *Global Knafaim Leasing Limited & CGTSN Limited v. The Civil Aviation Authority, BAAA Limited*,<sup>37</sup> relied on the *Emilie Millon*<sup>38</sup> in support of its ruling that both

Eurocontrol and the Civil Aviation Authority properly exercised their rights of detention. With respect to titleholders, the *Global Knafaim* court quoted from a Canadian case, *In re Canada 3000 Inc.*,<sup>39</sup> in stating that legal titleholders are in a better position to protect themselves against losses than airport authorities or other governmental or quasi-governmental agencies because they ‘can select airlines they are prepared to deal with and negotiate appropriate security arrangements as part of their lease transactions with airlines.’<sup>40</sup> The court did not take into account the economic development and modern techniques that should today permit an airport authority or other governmental agency to monitor and charge its users of services for their payment obligations or on the other hand the inability of lessors and lenders to be able to deal with airlines or other users with whom they have leasing or finance contracts since the former do not have immediate online access to the amounts of fees as they are incurred or build up. These points are made in Section 4(c) of this article as part of a more extensive discussion, and the archaic nature of the right of detention for such charges is noted in subsection (a) (ii) above.

(c) *Development of Article 39 and 40*

Articles 39 and 40 were developed early in the process of drafting the Convention. The early proposals in 1995, and then as part of the first drafts provided, were remarkably close to the final product.<sup>41</sup> In the 1995 conceptual memo it was stated that the proposed convention ‘should embody a system in which maximum information is provided to financiers and lessors

<sup>35</sup> G. Nathan Calkins Jr., ‘Creation and International Recognition of Title and Security Rights in Aircraft’ (1948) 15 *Journal of Air Law and Commerce* 156, 169-171; R.O. Wilberforce, ‘The International Recognition of Rights in Aircraft’ (1948) 2 *The International Law Quarterly* 421, 480-481.

<sup>36</sup> McBain in *Aircraft Liens* (n 26).

<sup>37</sup> [2010] EWHC 1348.

<sup>38</sup> *Emilie Millon* (n 25).

<sup>39</sup> [2006] 1 SCR 865.

<sup>40</sup> *Global Knafaim* (n 37) 17.

<sup>41</sup> Study Group for the Preparation of Uniform Rules on International Interests in Mobile Equipment: Sub-Committee for the Preparation of a First Draft, ‘Memorandum Prepared Jointly by Airbus Industrie and the Boeing Company on Behalf of an Aviation Working Group’, UNIDROIT 1995, Study LXXII – Doc 16, Rome, May 1995, 20-22 (hereinafter ‘1995 Study Group Memorandum’).

in order for them to calculate legal risks and appropriately price such risks in transactions'. To do this the memorandum proposed that each country must record with UNIDROIT the categories of its preferred creditors and that changes would only have prospective effect. It was only very late in the process that the alternative in Article 39(4) was added introducing the concept that by declaration a State could elect that the categories of NCRIs in that State would, if so provided under national law, have priority over international interests registered before the declaration. Article 39(4) has only been declared by eight States.

In 1996, a Report of the Study Group for the Preparation of Uniform Rules on International Interests in Mobile Equipment stated that the drafting done by the Aviation Working Group was based on the premise that the future Convention 'should provide a clear rule for the settlement of priority disputes between the holders of international interests and the holders of non-consensual national interests of whatever kind but in particular those held by preferred lien creditors, for example, the revenue authorities.'<sup>42</sup> The Study Group report included a discussion of the proposals and noted that 'one of the principal reasons why certain States had not become Parties to the ...Geneva Convention...was the way in which that Convention had the effect of overreaching the claims of local tax authorities'.<sup>43</sup>

In the 1997 Preliminary Draft of the Convention by the Study Group after its November session in Rome,<sup>44</sup> the then draft of the text of the future Article 39 expressly

provided that the national law priority of the NCRIs would be a priority over a registered interest 'of the same type as the international interest'.

The text of the Report of Second Joint Session in 1999<sup>45</sup> included a revised draft from the drafting group in Attachment F and on page F-26 Article 38 contained a full revised draft of the future Articles 39 and 40. In that revision, the words from the 1997 draft that read 'type as the international interest' were deleted and instead it said 'registered international interest'. The language of the Article already dealt with this concept in another way as it still contained the language we now see which includes 'an interest in the object equivalent to that held by the holder of an international interest'. The words 'equivalent to that held' are to be read literally when looking at how the applicable national law would decide if the NCRI had priority. To be equivalent one would have to determine which type of an international interest, one under a security agreement, a title reservation agreement or a lease agreement, applied under such applicable law. Accordingly, the deletion of the words did not change the result even if it no longer had the 'type' wording reminding a reader of how important national law was to understanding the words 'equivalent'. This language can be used to reach the same result which is to ensure that the NCRI declared only has that priority over those types of agreements that are also subject to priority by NCRIs and that other types of international interests were not affected. As discussed in Section 3(b)(ii) and Section 4(b)(5), the type of international interest that is subordinated under local law is an issue today with some declarations that are themselves so terse in their drafting that they could mislead a reader

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<sup>42</sup> Study Group for the Preparation of Uniform Rules on International Interests in Mobile Equipment, 'Report', UNIDROIT 1996, Study XLII – Doc 27, Rome, July 1996, para. 79.

<sup>43</sup> *Ibid*, para 81.

<sup>44</sup> Study Group for the Preparation of Uniform Rules on International Interests in Mobile Equipment, 'Preliminary Draft UNIDROIT Convention on International Interests in Mobile Equipment', UNIDROIT 1998, Study LXXIII – Doc 1, Rome, January 1998, [XV].

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<sup>45</sup> UNIDROIT Committee of Governmental Experts for the Preparation of a Draft Convention on International Interests in Mobile Equipment and a Draft Protocol Thereto on Matters Specific to Aircraft Equipment, 'Second Joint Session Report', ICAO Ref. LSC/ME/2-Report, UNIDROIT CGE/Int. Int./2-Report, Montreal, September 1999.

who is a potential financier or lessor as to what the law is in that Contracting State.

One last point to extract from the Convention legislative history is the comment by the Greek representative, Professor Voulgaris, in a debate reported from a session of the Governing Council of UNIDROIT in 1998, when he said that it was important that the declaration category 'list only be effective within the country which deposited it...lest otherwise other Contracting States might be prejudiced'.<sup>46</sup> There was no rebuttal of this comment, and it illustrates how it was always intended that the effect of the priority of the categories declared under Article 39 for NCRIs should only be effective within the relevant Contracting State.

### **3. Analysing Article 39 within the framework of the policy objectives and development of the Convention and of non-consensual rights or interests and rights of detention**

To analyze what the Convention means in its use of the term 'non-consensual right or interest' and how Article 39 should be understood, this Section of the article: (1) discusses the Article 39 policy objectives and conflicts within both the purposes and intended benefits of the Convention and the Aircraft Protocol, and the context of the historical framework of NCRIs and rights of detention described in Section 2 above; (2) compares the priority rules of each of Articles 29, 39 and 40 of the Convention as they relate to NCRIs; and (3) explains how Article 39 is applied to such rights and interests that are declared and focuses on specific issues such as how such declared preferred rights are not applicable outside of the declaring State.

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<sup>46</sup> 1998 Governing Council meetings 16–20 Feb 1998, pages 19–20.(b), Discussion Professor Voulgaris.

#### *(a) Article 39 Policy Objectives and Conflicts*

The cost of a modern commercial aircraft or spare engine is substantial.<sup>47</sup> As a consequence, operators conserve cash by obtaining the ownership or use of a large majority of their aircraft through: (1) secured debt financing, in which the operator remains the economic owner and title holder of the equipment; (2) finance leasing, which is effectively a debt financing in which the lender (finance lessor) takes title to the equipment for security purposes but the operator remains the economic owner by virtue of a bargain purchase 'option' at the end of the term<sup>48</sup>; or (3) operating leasing, in which a third party has title to, and economic ownership of, the equipment and leases it to the operator for a period substantially less than the equipment's remaining useful economic life.<sup>49</sup> All of these structures can be implemented at the time the equipment is delivered by the applicable original equipment manufacturer ('OEM') or at the time of later financing or leasing with respect to used equipment.

In each such structure, the operator provides an indemnity to the lender or operating lessor with respect to any and all expenses incurred in the use and operation of the aircraft until, as the case may be, the secured debt is repaid, the finance lease bargain purchase 'option'

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<sup>47</sup> Although final prices are typically subject to negotiation, Boeing recently published its 2013 list prices in which the 737 Family ranged from \$76.0 to \$109.9 million; the 747, 767 and 777 Families ranged from \$185.8 to 357.5 million; and the new 787 Family ranged from \$211.8 to 288.7 million. See [www.airfinancejournal.com/Article/3244428/Boeing-increases-list-prices.html](http://www.airfinancejournal.com/Article/3244428/Boeing-increases-list-prices.html), accessed 5 September 2013.

<sup>48</sup> For simplicity, in this section the term 'lender' refers to both a lender in a traditional loan secured through a mortgage lien on the applicable aircraft and a finance lessor secured through a title retention arrangement.

<sup>49</sup> An operating lessor may, in turn, finance its acquisition of equipment through a secured loan or a finance lease structure. This article ignores that structural possibility because, for purposes of this discussion, the impact of NCRIs on such lenders is the same as when a loan or finance lease is made directly with the operator.

is exercised or possession of the aircraft is returned to the operating lessor. Certain of these expenses can give rise to NCRIs which the operator is obligated to discharge in a timely manner.

NCRIs impact the expectations of lenders and operating lessors differently. In the case of secured debt financings and finance leases, the aircraft should be seen as collateral securing the obligation of the operator to pay the debt service/'rent' from which the lender recoups the loan balance and obtains a fair return on that investment. In these transactions, the financing party only needs to ensure that, if there is a default by the operator, the then realizable value of the aircraft after discharging any prior ranking NCRIs is likely to be sufficient to cover the operator's remaining payment obligations.<sup>50</sup> To provide a buffer against NCRIs that may be present at the time of a foreclosure, a lender typically advances less than the full value of the aircraft (i.e., a loan-to-value ratio of less than 1.0). A lender's exposure to NCRI risk is further mitigated because such loan-to-value ratio generally declines during the term of the financing inasmuch as the loan balance normally amortizes more rapidly than the value of the aircraft depreciates.

By contrast, an operating lessor does not recover its full investment in the aircraft and a fair return through the lease rentals alone, but rather depends for that on realizing the residual value of the aircraft through a subsequent lease or sale. Accordingly, NCRIs not discharged or indemnified by the operator will erode the asset value anticipated by an operating lessor on a dollar-for-dollar basis. This risk is particularly acute following a lease default when the operating lessor desires to mitigate its losses by repossessing and redeploying the aircraft as quickly as possible. To do so, the operating lessor may be forced to discharge NCRIs for debts incurred by the operator when there may be little prospect that the operator will honor its indemnification obligation under the lease.

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<sup>50</sup> To be fully repaid, the lender must also consider how long realization of the collateral could be delayed.

In general, the Convention and the Aircraft Protocol foster the foregoing principles and assumptions underlying the various forms of aviation financing and leasing by committing Contracting States to enforce the contractually agreed creation and priorities of registered international interests. By doing so, a Contracting State stands to advance the policy objective of increasing the availability, and reducing the cost, of aviation financing and leasing for its operators. Article 39 establishes a significant exception to that framework by allowing a Contracting State to identify, generally or specifically, categories of unregistered NCRIs that take priority over registered international interests. This exception reflects a countervailing policy decision that affording certain creditors the protection of priority NCRIs will facilitate the smooth day-to-day provision of aviation services to the public. As noted above, the laws of many jurisdictions grant priority to NCRIs covering fees accrued by operators that fund governmental services such as air traffic control and airport operations as well as expenses incurred by operators for equipment maintenance.<sup>51</sup>

Article 39 balances these conflicting policy objectives by making a Contracting State's universe of granting priority to NCRIs reasonably transparent so that financing parties have a fair opportunity to factor the resulting risk and uncertainty into decisions about whether to provide support to the State's operators and at what price and on what terms and conditions.<sup>52,53</sup> Thus, Article 39 stipulates that

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<sup>51</sup> Of the 40 jurisdictions that have made Article 39 declarations, 22 have specifically declared unpaid governmental taxes and charges as NCRIs under Article 39(1)(a) and 30 jurisdictions have declared under Article 39(1)(b) that the Convention does not affect the right of governmental or private providers of public services to arrest or detain an aircraft object in accordance with applicable domestic law for payment directly relating to such services in respect of such object [or another object].

<sup>52</sup> 'The basic principle is that of retention or restriction of priority by publicising preferred NCRIs, thus permitting financing parties to assess and price these risks.' Official Commentary, Goode (n 2) para 4.270.

a State<sup>53</sup> must set forth in its declarations, either generally or specifically, those categories of unregistered NCRIs that will have priority over registered international interests. There are also aspects of Article 39 that protect international interests. Several elements of Article 39 make clear that no such NCRI has a greater priority over a registered international interest than it would have over an 'equivalent' interest under the State's law. Indeed, a State has the ability to restrict the priority of an NCRI for purposes of the Convention.

Further, as noted by paragraph 4.269 of the Official Commentary:

the priority is not a Convention priority but one given by the law of the declaring State. It is therefore not entitled to recognition in another Contracting State unless the conflict of laws rules of the State so require.

Similarly, paragraph 3 protects an international interest against being primed by an NCRI given priority by a declaration deposited by the Contracting State after establishment of such international interest, unless, in accordance with paragraph 4, at the time of ratification, acceptance, approval of, or accession to the Aircraft Protocol the State reserved the right to make such *post facto* changes in priority. Even paragraph 4 is consistent with the general Article 39 principle of transparency.

*(b) The priority rules of Articles 29, 39 and 40 within the Convention*

*(i) Principle of Article 39 and the declared but unregistered non-consensual rights or interests and rights of detention*

The basic principle of Article 39 is the transparent preservation within a Contracting State's jurisdiction of those rights of detention and of the priority of those preferred national law rights and interests which the Contracting State has chosen to declare applicable so as to permit

them priority conferred by its laws over registered international interests, and has deposited that declaration with UNIDROIT.<sup>54</sup> In Section 4 below, we discuss how the declarations are phrased and should be phrased where possible.

By making a declaration under Article 39(1)(b), a Contracting State can preserve its local law rights of arrest and detention for non-payment of charges for public services related to an aircraft object or, as will be discussed later, 'another object', without registering these rights in any registry but with the transparency of the UNIDROIT category publication system of such declarations under Article 23 described in the next paragraph.<sup>55</sup> Similarly, under Article 39(1)(a), a Contracting State can choose in its declarations which categories of its local law conferred NCRIs (that have priority under that law over interests equivalent to one or more types of registered international interests) shall have, after the date of deposit of that declaration with UNIDROIT, that same priority over subsequent registered (and therefore unregistered) international interests of that type under Article 39(3)<sup>56</sup> without registration of such NCRI under the International Registry priority system of the Convention. An Article 39(4) declaration would permit priority to be given under the terms of Article 39(1)(a) over an international interest registered even prior to the deposit of the declaration, but this earlier priority does not mean that the declaration alters any of the other limitations on Article 39(1)(a) since all it does is override Article 39(3).

The Article 39 preferred national law rights are described as an exception to the Convention registration priority system. While other exceptions exist,<sup>57</sup> most importantly the exception with respect to pre-existing rights or interests under Articles 60(1) and

<sup>54</sup> International Institute for the Unification of Private Law ("UNIDROIT").

<sup>55</sup> See Section 3(b) below.

<sup>56</sup> Article 39(3) and (4).

<sup>57</sup> Roy Goode, 'The Priority Rules Under the Cape Town Convention and Protocols' (2012) 1 *Cape Town Convention Journal* 95, 98.



(2),<sup>58</sup> none of those exceptions are, or have a need to be, placed by the Convention into the transparent system of online reporting of all declared categories that is required to be supported by UNIDROIT. UNIDROIT receives all deposits of declarations as to categories of NCRIs under Articles 39 and 40 and is required under Article 23 to record and publicize such priority categories by making the declarations as to categories searchable on their website in the name of the declaring Contracting States and to make them available to anyone who requests them.<sup>59</sup>

This online NCRI category system and further availability upon request, allows for a greater degree of transparency and therefore predictability with regard to what NCRIs a financing party or other interested party may encounter in a declaring Contracting State which have priority over a registered interest than has ever been available before now. In fact, parties already use this system to plan transactions and to study local law categories that are declared. It is likely parties will expand that use as it becomes better understood that if a declaration is not made as to a category then that category will not be a preferred right or interest as against international interests within that declaring Contracting State. The Convention's principled and textual support of that non-declaration principle is set forth immediately below. While one still has to have advice as to what the underlying law of a Contracting State is as to declared categories, a holder of an international interest should be able to ascertain that its registered international interest is superior in all Contracting States to NCRIs that were not in declared categories.

*(ii) Principle of Article 29 and the unregistered interest*

The Official Commentary's first comments on Article 29 fully support this perspective on its priority principles:

This Article lays down a set of priority rules governing a registered interest in relation to other registered interests and to every kind of unregistered interest, whether or not registrable, except a non-consensual right or interest covered by a declaration by a Contracting State under Article 39(1)(a) (see paragraphs 4.269 *et seq.*) and a pre-existing right or interest (see Article 60 and paragraphs 4.348 *et seq.*).<sup>60</sup>

Under Article 29(1), the Convention provides its basic rule that a 'registered interest has priority over any other interest subsequently registered and over an unregistered interest'. Nowhere in Article 29 is there any exception referencing Article 39 NCRIs that are not registered, and on its face it would appear that the text of Article 29 is inconsistent with the foregoing Official Commentary since Article 29 makes a registered interest superior to all unregistered interests.

However, the definition of unregistered interest intentionally excludes Article 39 interests as seen below, and Article 29(1) imports that definition into its priority rule:

'unregistered interest' means a consensual interest or non-consensual right or interest (other than an interest to which Article 39 applies) which has not been registered, whether or not it is registrable under this Convention.

This raises the logical question of what happens if there is a nationally conferred NCRI with local law priority (even without any registration in its jurisdiction), but the Contracting State elects not to declare that category of NCRI under Article 39. In that case, the undeclared NCRI comes within the definition of 'unregistered interest' and will lose in a priority match with a registered interest pursuant to Article 29(1). The Official Commentary on that definition makes this point as to the priority system and registered interest versus unregistered interest definitions very clear:

'unregistered interest' means any interest, whether consensual or nonconsensual, which has not been

<sup>58</sup> Ibid 100.

<sup>59</sup> Official Commentary, Goode (n 2) para 4.159.

<sup>60</sup> Official Commentary, Goode (n 2) para 4.183.



registered in the International Registry, *whether or not it is registrable, except for a non-consensual interest which a Contracting State declares under Article 39 is to have priority, without registration, even over a registered international interest.* The essential point is that under Article 29(1) a registered international interest has priority over an unregistered interest as defined above. *The fact that the unregistered interest may not itself be capable of protection by registration is irrelevant; the superior ranking of the registered international interest lies at the heart of the protection which the Convention is designed to provide.*<sup>61</sup>

The foregoing principles described in the Official Commentary clearly exclude from the Article 29 priority regime the preferred nationally conferred NCRIs that are declared under Article 39 and include in the Article 29 regime all NCRIs that are not declared under Article 39 whether or not registrable under Article 29.

All Contracting States are subject to Article 39 whether or not any declaration is made. This point follows directly from the discussion about the Article 29 priority system and is the reason why Article 39 is regarded as an exception. By ratifying the Convention, all Contracting States are subject to Article 39 in each Contracting State and its declarations of priority under its national laws. We discussed above the principle that for any nonconsensual rights or interests that a Contracting State does not make category declarations, they will be unregistered interests subject to Article 29 and so subordinate to any registered interests on the International Registry.

If a Contracting State makes no Article 39 declarations, then under Article 29 in that State all NCRIs in an aircraft object that may arise under its laws will be subordinate to any registered international interest no matter when made. While NCRIs have priority even over unregistered international interests,<sup>62</sup> a question can be asked whether it would be true in reverse that undeclared NCRIs would be subordinate to unregistered international

interests since they are subordinate to registered interests. However, Article 29 'does not regulate priority between competing unregistered interests',<sup>63</sup> and Article 39 only applies to NCRI categories which have been declared under Article 39 so that non-declared rights or interests come under Article 29 as set forth above in Section 3(b)(ii). Consequently, subordination in this case would be left to national law.

*(iii) Principle of Article 40 and the registrable non-consensual right or interest*

A registrable NCRI is defined in Article 1(dd) to mean: 'a non-consensual right or interest registrable pursuant to a declaration deposited under Article 40'. As with a NCRI declared under Article 39, this also must still be a valid right or interest under the declaring Contracting State's law. The Official Commentary states that it is:

a right or interest created by the law of the Contracting State, as opposed to agreement, which by virtue of a declaration made by that State under Article 40 can be registered as if it were an international interest. A typical example is the lien of a judgment creditor.<sup>64</sup>

The declarations of the categories that may be registrable by the Contracting State under Article 40 bring the registrable rights and interests in such categories within the Convention for priority purposes as if they were an international interest. Once registered on the International Registry and even if not so registered (thereby having no priority rights against other interests that are registered), the registrable rights or interests under Article 40 are subject to the first in time registry priority rules to which all Contracting States adhere and will have effect in actions and priority disputes in all Contracting States.<sup>65</sup> This is

<sup>63</sup> Ibid, para 4.196.

<sup>64</sup> Ibid, para 4.36.

<sup>65</sup> Article 40 states, 'A Contracting State may at any time in a declaration deposited with the Depositary of the Protocol list the categories of non-consensual right or interest which shall be registrable under this

<sup>61</sup> Ibid, para 4.45 (emphasis added), para 4.200 (Illustration 22).

<sup>62</sup> Ibid, para 2.214.

different than Article 39, which declares rights and interests that do not need registration, are not subject to the first in time priority rules and do not have effect in other Contracting States.

*(c) How Article 39 applies and is to be analysed*

The following subsections review different issues that arise when applying and analysing Article 39.

*(i) Intended limitations of the defined term non-consensual rights or interests*

A non-consensual right or interest is defined in Article 1(s) using the words 'right or interest conferred under the law of a Contracting State'. The limit of 'a right or interest' to being conferred by law is key to understanding Article 39 and Article 40 of the Convention. The right or interest is not contractually or consensually created. Each of Articles 39 and 40 refers to declaring only 'categories' of NCRIs. Consequently, the effect of Articles 39 and 40 must be limited in effect to only those rights or interests 'conferred under the law of a Contracting State' and which fit into a category described in that State's declaration, if any, under that Article.

One of the further limitations within the definition of the NCRI is that the particular Contracting State whose law governs is the one 'which has made a declaration under Article 39'. Accordingly, only the law of the particular Contracting State is relevant to ascertaining the validity and meaning of a particular NCRI.

In an international convention such as this, an express limitation to one applicable law selected by the Convention terms is itself meaningful and indicates the express intention of the Convention to limit the breadth of the NCRI validity and effect thereof under the Convention to that governed by the law of the declaring Contracting State, unless modified by

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Convention as regards any category of object as if the right or interest were an international interest and shall be regulated accordingly. Such a declaration may be modified from time to time.'

a further express provision such as the Article 40 provisions that allow for the registrable NCRI to be registered and, whether or not so registered, to then be 'regulated accordingly'.

Finally, the right or interest in the NCRI definition is qualified as being a right or interest 'to secure the performance of an obligation'. The words 'to secure the performance of an obligation' are immediately after the words 'which has made a declaration under Article 39'. Does this mean that the Contracting State had to declare that the right or interest was intended to secure the performance of an obligation? That is clearly not what the text can mean. The phrase simply limits the right or interest under the Contracting State's national law to one that is created under that national law 'to secure the performance of an obligation'. Additionally, this includes 'an obligation to a State, State entity or an intergovernmental or private organisation' so that the breadth of these obligations (which must be conferred under the law and not be contractual) is not limited but inclusive of obligations to governments and other organisations. Indeed, there does not seem to be any basis on which these would be limited to just payment obligations and so performance obligations would be included by these words.<sup>66</sup>

The definition of registered interest<sup>67</sup> includes a registrable NCRI, and as a result those NCRIs that fit within the categories declared under Article 40 are inserted by the declaring Contracting State into the Article 29 Convention regime of priority. This completely separates the registrable NCRI

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<sup>66</sup> McBain has said and cited Goode for the proposition that although common law liens 'can cover obligations other than debts it appear[s] that the majority (and, perhaps, all) common law liens have only covered debts, in practice'. McBain (n 11)[n 19]; Roy Goode, *Hire-Purchase Law and Practice* (2<sup>nd</sup> edn Butterworths 1970).

<sup>67</sup> A registered interest is defined in Article 1(cc) as follows: 'an international interest, a registrable non-consensual right or interest or a national interest specified in a notice of a national interest registered pursuant to Chapter V.'

from the NCRI, apart from establishing the underlying validity of the right or interest under the declaring Contracting State's law. After that validity is established, the interests differ insofar as a registrable NCRI can have its priority established according to the Article 29 registration system within the Convention for purposes of all Contracting States, while the NCRI can have its priority based on the Article 39 system where the priorities of the declaring Contracting State are brought within the Convention for purposes of use only within that Contracting State.

(ii) *Types of equivalent interests under national law*

The first part of sub-paragraph (a) of Article 39(1) refers to declarations of 'those categories of non-consensual right or interest ... which under that State's law have priority over an interest in an object equivalent to that of the holder of a registered international interest... and which shall have priority...'.<sup>68</sup>

The word 'equivalent' requires that the interest under that State's law must have a meaning under that law that is equivalent to a registered international interest. How does one determine if an interest is equivalent to an international interest when an international interest can be constituted and described in Article 2(2) pursuant to one of three different agreements: (1) a security agreement, (2) a title reservation agreement or (3) a leasing agreement? Article 2(4) answers this when it says that the applicable law determines whether an interest to which Article 2(2) applies falls within one of the three interests under the respective types of agreements that constitute an international interest. This is the very important characterization that is to be used by the parties and, if needed, by courts as to which type of international interest is applicable when considering remedies under the Convention. There, this determination of the characterization of the international interest is relevant because Articles 8 and 9 deal only with remedies in favour of a chargee under a security agreement and Article 10 deals only with a conditional seller under a title reservation agreement or a

lessor under a leasing agreement. The remedies are very different.

Similarly in the applicable Contracting State, the differences in priorities between the various categories of NCRIs and the different types of interests in aircraft objects under which an international interest may be characterized can create an important difference in result: in some cases the NCRI will have priority over one type of international interest under the applicable national law and in some cases it will be subordinate to another type of international interest.

Under Article 5(3), references to applicable law are to the domestic rules of the law applicable by virtue of the conflict rules of the forum State. Using the law determined as applicable by the forum State, which in the case of a NCRI determination of priority should be in the relevant declaring State, a court would determine which of the different types of agreement was applicable and then whether a NCRI of the declared category would have priority over the particular type of the interest.

The Official Commentary discusses the equivalent types of interest as follows:

An equivalent interest is an interest under a charge or held by a person who is a conditional seller under a title reservation agreement or a lessor under a title reservation agreement. A State may retain or restrict its nationally preferred rights or interests arising by law, but may not use the Convention to expand these preferred rights. For example, if nonconsensual rights or interests, while having priority over charges under a Contracting State's laws, do not have priority over the rights of conditional sellers under title reservation agreements, a declaration purporting to cover the latter would not be permitted by Article 39.<sup>68</sup>

The national laws of the Contracting State are fundamental to the interpretation of not only the NCRI and its priority over an equivalent national law interest, but also as to what should be the characterization of the type of international interest.

<sup>68</sup> Official Commentary, Goode (n 2) para 2.210; see text to 45 and declaration issues at Section 4(b)(5).

*(iii) Insolvency*

The final phrase of sub-paragraph (a) of Article 39(1) reads ‘whether in or outside insolvency proceedings’. When Article 39(1)(a) is declared generally, as the lead-in paragraph of Article 39(1) permits, then all categories that have the priority described in such sub-paragraph (a) will apply to have priority in or outside insolvency. But, in some countries, the declarations apply only in insolvency proceedings and while Article 39 does not give specific guidance as to limiting the application to insolvency, if the categories declared only have application during an insolvency then such a declaration should be so limited. This is better than issuing a misleading declaration as to legal priority that does not exist in that jurisdiction. Even if a declaration is not limited to insolvency proceedings, if the categories have priority only in insolvency proceedings in that jurisdiction, then that limitation would apply and there would not be any greater priority just because of the declaration. As the Official Commentary states, ‘the Convention may not be used as a vehicle to expand such preferred rights’.<sup>69</sup>

*(iv) Effect of Article 39 in Contracting States other than the declaring State*

As discussed in Section 3(b)(i) above, each of sub-paragraphs (a) and (b) of Article 39(1) permits a Contracting State to preserve nationally preferred rights under the laws of that State. In sub-paragraph (a) it is the priority of the NCRI against a registered international interest so long as the State’s law provides that such right or interest would have such a priority over an equivalent interest to the international interest, and in sub-paragraph (b) it is the right of the Contracting State or an entity of the State, intergovernmental organization or other private provider of public services that has a right to arrest or detain the aircraft object under the laws of the State for payment of directly related unpaid amounts owed to

it. These are all rights of priority under State law pursuant to sub-paragraph (a) and rights of arrest or detention under State law pursuant to sub-paragraph (b), which in each case are effective as a result of the declaration in the Contracting State against other interests under the Convention in that State. But this does not have an effect in other Contracting States, and there is no textual support for these rights to be effective in other Contracting States. This is in accord with the Official Commentary and its comment that ‘the priority [of sub-paragraph (a)] is not a Convention priority but one given by the law of the declaring State. It is therefore not entitled to recognition in another Contracting State unless the conflict of laws rules of that State so require.’<sup>70</sup> Similarly, the Official Commentary makes the same exact comment as to sub-paragraph (b) rights of detention or arrest.<sup>71</sup> And, Illustration 48 (paragraph 4.281 of the Official Commentary) posits the airport authority of one Contracting State attempting to arrest an aircraft in another Contracting State for unpaid landing fees in respect of the relevant aircraft against which it would have a right of arrest or detention within its jurisdiction. The result is that the conflicts of laws rules of the forum Contracting State would be the basis for making the determination of whether to recognize the right of detention.

Another example is given by the Official Commentary with respect to the taking of Article 8 remedies after an event of default in Illustration 7 (paragraph 4.91) which makes a very clear case along with the discussion in paragraph 4.89 that both show how a prior ranking NCRI will have priority over all registered international interests. The actual text of the example and the discussion does not indicate in what jurisdiction the events would take place and so it could have been read as saying that this priority reaches to any Convention jurisdiction and has a wider effect than expected. This would in

<sup>69</sup> Ibid, para 4.270.

<sup>70</sup> Ibid, para 4.269.

<sup>71</sup> Ibid, para 4.272.

particular contradict the Official Commentary paragraphs commenting on Article 39 in, for example, paragraph 4.269 and Illustration 48 at paragraph 4,281 discussed above. Upon inquiry, Professor Goode responded that he was not concerned at that point of the analysis with the effect of a NCRI in other jurisdictions, and everything is assumed to be local. This helps make consistent analysis of the basic point that the Article 39 priorities take effect only under the laws and jurisdiction of the declaring State.

*(vi) Application of Article 39(1)(b)*

Article 39(1)(b) has already been discussed in terms of not being effective outside of the declaring State under subsection (v) above and under Section 3(b)(i) above where the transparent preservation of Article 39(1)(b) rights of arrest or detention by category declaration was an important principle supporting a system of greater predictability and uniformity. It has also been made clear that, in the same manner as sub-paragraph (a) of Article 39(1), that sub-paragraph (b) is not a provision that could or should expand the laws of the declaring State with respect to the rights of the State or a State entity or a intergovernmental organization or provider of public services to arrest or detain an aircraft for failure to pay amounts due that are directly related to such public services in respect of that object 'or another object'.

The last four words and numerous variations of them are the focus of concerns over the potential use of the term in a declaration just because it was in Article 39(1)(b). The Official Commentary also confirms the savings clause nature of sub-paragraph (b) that may preserve rights of arrest or detention given by the law of the declaring State and states 'but may not expand these'. It continues:

In that regard UNIDROIT in its Declarations Guide to the Convention and Aircraft Protocol, has encouraged Contracting States not to include the words 'or another object' in their declarations where, as is the case in most jurisdictions, there is no fleet-wide right of detention under national law'.<sup>72</sup>

<sup>72</sup> Ibid, para 2.216. See paras 2.215, 4.272-3.

Unfortunately, as noted in Section 4(a)(v) below, only four nations out of 30 that declared a version of Article 39(1)(b) excluded any kind of another aircraft or another object language. This might have been in some cases due to the simplicity and ease of declaring a right of detention as a precautionary matter notwithstanding that it is not clear such a right is relevant or even exists under local law. As explained in Sections 4(b) and (c), the declaration of a right or interest that does not exist may have a negative economic impact on the declaring State's aviation industry. It appears that a further study of the actual laws as to fleet liens and coverage of other aircraft globally may be needed to explore this point.

Meanwhile, in Section 4(c), as well as in Sections 4(a) and (b), this article has strongly encouraged Contracting States to carefully consider the full effect of their declarations and to consider making subsequent declarations to alter them, including as to the 'another object' language.

The Convention provides a Contracting State with alternatives. It can declare that a category of NCRIs in the form of rights of arrest or detention under its laws to secure payment of amounts due for such public services as airport landing fees or air navigation charges or other airport charges in respect of an aircraft specifically has priority under paragraph 1(a) of Article 39(1), and it can declare under paragraph 1(b) that it preserves the right to arrest or detain an aircraft for failure to pay for such public services provided to an aircraft. If the Contracting State declared and applied paragraph 1(a) it could do so only with respect to non-consensual, and not with respect to any contractual, rights or interests permitting it. If the Contracting State were applying a paragraph (1)(b) right of arrest or detention, it could include the contractual rights of arrest or detention given to a provider of public services. Even though the paragraph 1(b) rights can be contractual the Official Commentary points out that: 'the priority (in the case of 1(a)) or right of detention or



arrest (in the case of 1(b)) must arise under the national law of the declaring State.<sup>73</sup>

*(vii) Application of Article 39 to sales of aircraft objects*

The most important Convention term in Article 39(1)(a) is 'international interest'. As just described above that term may be characterized as an interest created by different types of agreements. It is also a proxy for a sale of an aircraft object when reading Convention articles on priority. As provided in Article 1(ss), the term sale means 'a transfer of ownership of an object pursuant to a contract of sale'.

Article III of the Aircraft Protocol entitled 'Application of Convention to sales', as permitted by Article 41 of the Convention, is the provision that made the registration and priority provisions of the Convention applicable to Chapter X, which contains Articles 39 and 40. It has become routine in Cape Town transaction practice that sales are treated as if they were international interests for purposes of registration of interests and priority. Sales of aircraft objects, like registered international interests are also subject to the priority of declared NCRIs under Article 39 in the declaring State's jurisdiction.

Since the Geneva Convention sets out rules requiring national aircraft registry filings for perfection and priority of 'rights of property' in aircraft (as opposed to individual aircraft engines), the Aircraft Protocol's Article III provisions as to sales incorporating Article 39 priorities will supersede the Geneva Convention as it relates to transfers of ownership of airframes and helicopters and the priority of any NCRIs as against such transfers. This will only be applicable when the relevant States are Contracting States under both Conventions as noted in Section 2(b)(ii) above. Under the Geneva Convention, only

claims for salvage and indispensable expenses of preservation have priority over recorded rights of property in aircraft. For a lienholder under a declared category, the superseding effect of the Convention combined with the Aircraft Protocol could give it a better position than it would have had in the same State solely under the Geneva Convention as against transfers of aircraft.

*(viii) Attachment of priority and enforcement actions*

The issue of timing of attachment of the NCRIs upon enforcement and its relation to the enforcement of international interests is discussed under Sections 5(a)(i) and 5(b) since Section 5 concerns the application of Article 39 in practice.

#### **4. Declarations under Articles 39 and 40: consistency, divergence and recommendations**

In a general sense, knowing what categories of NCRIs may exist with potential priority over international interests and sales, and having the greater level of predictability in each case provided by the public declarations of categories, are a major part of the benefits for both parties to asset-based financing and leasing transactions and to aviation industry participants intended by the declaration of categories made by Contracting States under Articles 39 and 40.

To the extent that these declarations are unclear, incorrect or confusing, these benefits are diminished. The weakening of financing benefits is not the only concern arising from inaccurate or misleading declarations. The loss of clarity as to what is being declared will hurt the holders of NCRIs in that Contracting State if their lien or right is not recognized by a party to a transaction and a local court then finds that the lienholder is not entitled to priority which it should have originally had under that jurisdiction's laws. Even if the lienholder ultimately prevails, the unnecessary cost of litigation and administrative time will have vitiated many of the benefits of a uniform

<sup>73</sup> Ibid, para 4.273. The Official Commentary in paragraph 4.276 has detailed comments on the types of governmental units or providers of public services, whether State, State entity, intergovernmental or private organization, and as to which rights to arrest or detain can be preserved.



set of rules for priorities that the Convention aims to provide to all parties. Hence, the stakeholders who should want to have clear declarations include the private lien holders, the government holders of rights and interests, the local airlines and other aircraft operators, financiers, lessors and sellers of aircraft objects in those countries and the courts that must adjudicate these issues.

The existing declarations of Contracting States may be amended to clarify the language or to narrow or eliminate categories in order to promote asset-based financing and leasing of aircraft in a Contracting State<sup>74</sup> and for the benefit of all of the above described stakeholders. As a whole, the Contracting States have followed the Article 39 and Article 40 declaration recommendations of UNIDROIT and the Aviation Working Group ('AWG') described below with only minor variations to reflect national laws, but issues that are noted below arise and numerous improvements could be made. Each Contracting State should consider making amendments to declarations for clarity or necessary correction or, on the other hand as spelled out in subsection (c) below, for the benefit of its aviation industry. Such amendments should be, and already are, routine under the Convention. The existence of a six month period before effectiveness after deposit with UNIDROIT<sup>75</sup> can be used to educate all relevant interests.

In subsection (a) below, we review a selection of the declarations currently on deposit with the Depository. In subsection (b) we note specific problems arising from divergent texts of the declarations. In subsection (c) we make general recommendations to Contracting States and give the rationale for narrowing the declarations further in particular as to the fleet lien.

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<sup>74</sup> Article 57.

<sup>75</sup> The six months run from the first day of the month following receipt of the notification of a subsequent declaration under Article 57(2) or a withdrawal of a declaration under Article 58(1).

*(a) Review of categories of declarations under Articles 39 and 40 and comparison to UNIDROIT Model Forms and AWG economically based recommended categories*

This is an analysis of some of the many declarations that were shown on the UNIDROIT website (and on the International Registry) as of the end of June 2013. It is intended to be illustrative and not exhaustive.

*(i) Introduction to review process to create Annexes on variations in declarations*

This part of the article discusses the declarations of different NCRIs, under Article 39 and that are registrable under Article 40, in terms of categories that have been declared to date. The research for this analysis consisted of comparing declarations made by Contracting States with model declarations. As background, UNIDROIT, as depository under the Convention and Aircraft Protocol, has issued model forms to assist Contracting States in making declarations in compliance with the terms of the Convention and Aircraft Protocol. UNIDROIT has issued five model forms for purposes of declarations made under Articles 39 and 40.<sup>76</sup> These forms generally consist of lead-in introductions to specific declarations issued by Contracting States. Similarly, the AWG has issued model forms for purposes of declarations that can be made under Articles 39 and 40. In contrast to the UNIDROIT forms, these forms provide language for the specific categories of some declarations recommended by the AWG to be made by Contracting States under Articles 39 and 40 for maximum economic benefit

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<sup>76</sup> UNIDROIT Secretariat, 'The System of Declarations Under the Convention of International Interests in Mobile Equipment and the Protocol Thereto on Matters Specific to Aircraft Equipment: An Explanatory Memorandum for the Assistance of States and Regional Economic Integration Organisations in the Completing of Declarations', UNIDROIT (2011), DC9/DEP - Doc 1 Rev 4, at <http://www.unidroit.org/english/documents/2011/depository/dc09-dep-01rev4-e.pdf>, accessed 29 August 2013.

under the Convention as applied to aircraft objects.<sup>77</sup> These UNIDROIT and AWG model forms have been compared with issued declarations, which are available via the UNIDROIT Depository website<sup>78</sup> and on the International Registry.

*(ii) UNIDROIT model forms of declarations and footnote guidance as to Articles 39(2), 39(3) and 39(4) declarations*

The UNIDROIT Model Form Nos. 1–4 pertain to declarations made under Article 39. Model Form No. 6 pertains to declarations made under Article 40. Model Form Nos. 2 and 4 provide models for general declarations that require no additional substantive input from Contracting States.<sup>79</sup> By contrast, Model Form Nos. 1, 3, and 6 provide models that invite Contracting States to input specific categories to be declared.<sup>80,81,82</sup> The forms have

<sup>77</sup> Aviation Working Group, ‘Declarations Matrix and Economically-Based Recommendations: Ratification of the Cape Town Convention and Aircraft Equipment Protocol’, at <http://www.awg.aero/assets/docs/matrixofrecommendeddeclarations.pdf>, accessed 29 August 2013.

<sup>78</sup> UNIDROIT, ‘Declarations Deposited Under the Cape Town Convention on International Interests in Mobile Equipment and Under the Protocol to the Cape Town Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment’, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/main.htm>, accessed 29 August 2013; see text to n 77 above.

<sup>79</sup> For example, Form No. 2 provides, ‘(Name of the State) .....declares that all categories of non-consensual right or interest which under its law have [and will in the future have] priority over an interest in an object equivalent to that of the holder of a registered international interest shall have priority over a registered international interest, whether in or outside insolvency proceedings [and whether registered before or after (name of the State)’s (ratification) (acceptance) (approval) (accession)].’ For Form No. 4, see text to n 85 below.

<sup>80</sup> For example, Form No. 1 provides, ‘(Name of the State) ..... declares that the following categories of non-consensual right or interest (list the relevant categories)..... have priority under its law over an interest in an object equivalent to that of the holder of

footnotes as to certain optional provisions and very helpful guidance so that States can also take advantage of options such as covering future rights and interests under Article 39(2) or past rights and interests under Article 39(4). They also offer advice such as to delete ‘or another object’ in declarations under Article 39(1)(b) if a State does not have a fleet lien concept or wishes to narrow existing law on the topic not to cover an existing fleet lien right of detention.<sup>81, 82</sup>

*(iii) AWG Model categories for declarations under Article 39(1)(a)*

AWG issues ‘Economically-Based Recommendations’ for declarations intended to enhance the economic benefits accrued to Contracting States derived from the Cape Town Convention. AWG recommends that, applying commercial criteria, declarations other than the model declarations should not be made. In contrast to the UNIDROIT forms, the AWG models provide for specific categories that Contracting States may use in making declarations, while recommending that any declarations be specific and quantifiable,

a registered international interest and shall have priority over a registered international interest, whether in or outside insolvency proceedings [and whether registered before or after (name of the State)’s (ratification) (acceptance) (approval) (accession)].’

<sup>81</sup> Form No. 3 provides, ‘(Name of the State) ..... declares that nothing in the Convention shall affect its right or that of (list the names of any relevant State entities, intergovernmental Organisations or other private providers of public services) ..... to arrest or detain an object under its laws for payment of amounts owed to it or to any such State entity, Organisation or provider directly relating to the services provided by it in respect of that object or another object (strike out the words ‘or another object’ if not wishing the declaration to apply in relation to rights under the State’s laws to arrest or detain an object for payment of amounts owed in respect of another object).’

<sup>82</sup> Form No. 6 provides, ‘(Name of the State) ..... declares that the following categories of non-consensual right or interest (list the relevant categories)..... shall be registrable under the Convention as regards any category of object as if the right or interest were an international interest and shall be regulated accordingly.’

limited to customary categories such as repairs, and limited to claims that arise following a declared default. Many jurisdictions have followed this advice and many others have made minor variations. AWG recommended two possible specific declarations (or categories) under Article 39: (1) liens in favour of workers for unpaid wages arising since the time of a declared default under a contract to finance or lease the relevant object<sup>83</sup> and (2) liens in favour of repairers of an object in their possession to the extent of service performed on and value added to that object.<sup>84</sup>

<sup>83</sup> Variations on this model declaration include, for example, '[E]mployee wages relating to service fairly allocated to the use of an aircraft object as from the date that remedies have been exercised under the Convention and Protocol by the holder of as registered interest' (Bahrain) and, '[T]he lien enjoyed by wage-earners by reason of the preferential rights accorded to the wages owed by the employer at the time of its default under a financing or lease contract regarding an object' (Cameroon & Congo). 'Declarations Lodged by the Kingdom of Bahrain Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Accession in Respect Thereof', 27 November 2012, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/bahrain.pdf>, accessed 29 August 2013; 'Declarations Lodged by the Republic of Cameroon Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Accession in Respect Thereof', 19 April 2011, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/cameroon.pdf>, accessed 29 August 2013; 'Declarations Lodged by the Republic of Congo Under the Cape Town Convention', 16 November 2001, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/congo.pdf>, accessed 29 August 2013.

<sup>84</sup> Variations on this model declaration include, for example, 'Any debt due to the holder of a possessory lien for the repair, preservation of the aircraft to the extent of the service performed on and value added to the aircraft' (Malta) and, '[L]iens in favour of repairers of an aircraft in their possession to the extent of amounts due for their services' (Togo). 'Declarations Lodged by Malta Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Accession in Respect Thereof', 1 October 2010, at <http://www.unidroit.org/english/conventions/mobile-equipment/>

*(iv) Declarations under Article 39(1)(b)*

UNIDROIT's Model Form No. 4 provides the structure for declarations made under Article 39(1)(b). These declarations pertain to the Contracting State's right to arrest or detain specified objects for payments owed to the State.<sup>85</sup> Thirteen Contracting States have issued declarations that match Model Form No. 4.<sup>86</sup> Other Contracting States have issued variations of this model.<sup>87</sup> While Model Form No. 4 retains the state's right to arrest or detain 'an object,' variations retain the state's right to arrest or detain 'an aircraft object' (USA) or simply 'an aircraft' (Togo).

*(v) Declarations under Article 39(1)(b): 'or another object'*

Variations on declarations issued under Article 39(1)(b) and modeled after UNIDROIT's

[depositaryfunction/declarations/bycountry/malta.htm](http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/malta.htm), accessed 29 August 2013; 'Declarations Lodged by the Togolese Republic Under the Cape Town Convention on 26 September 2011', at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/togo.htm>, accessed 29 August 2013.

<sup>85</sup> Form No. 4 provides, '(Name of the State) .....declares that nothing in the Convention shall affect its right or that of any State entity, any intergovernmental Organisation or other private provider of public services to arrest or detain an object under its laws for payment of amounts owed to it or to any such State entity, Organisation or provider directly relating to the services provided by it in respect of that object or another object.'

<sup>86</sup> Afghanistan, Canada, Kazakhstan, Kenya, Mongolia, Oman, Pakistan, Senegal, Singapore, South Africa, Turkey, and UAE have issued declarations under Article 39(1)(b) matching UNIDROIT Model Form No. 4.

<sup>87</sup> For example, Albania, Brazil, the Netherlands, Norway, and the United States of America have declared under Article 39(1)(b), '[N]othing in the Convention shall affect the right of [the state] or that of any entity thereof, any intergovernmental organization in which [it] is a member State, or other private provider of public services in [it] to arrest or detain an aircraft object under [its] law for payment of amounts owed to any such entity, organization, or provider directly relating to the services provided by it in respect of that object or another object.'

Model Form No. 4 include variations on which objects may be arrested or detained for payments owed to the State. Model Form No. 4 quotes directly from Article 39(1)(b) in providing that, ‘Nothing in the Convention shall affect [the Contracting State’s] right . . . to arrest or detain an object under its laws for payment of amounts owed to it . . . directly relating to the services provided by it in respect of that object or another object’ (emphasis added). Because these declarations do not expand the Contracting State’s law, a declaration made under Article 39(1)(b) should not cover ‘or another object’ unless the Contracting State’s law already so provides. Thirteen Contracting States that have issued declarations matching Model Form No. 4 make declarations covering ‘or another object.’<sup>88</sup> Another thirteen States had variations but all covering in some way ‘another object.’ By contrast, four Contracting States, including Bangladesh, Panama, the Russian Federation, and the United Arab Emirates, exclude the ‘or another object’ language from the declaration.

*(vi) Other categories of declarations made under Article 39*

Contracting States have made declarations concerning taxes or other unpaid charges under Article 39(1)(a), (which AWG recommended only to be made under Article 40). The taxes or other unpaid charges declared under Article 39(1)(a) are generally restricted to those arising since the time of a declared default under a contract to finance or lease the object in question.<sup>89</sup> Additionally, Ethiopia and

Kenya have made declarations under Article 39 concerning bailees.<sup>90</sup>

Certain Contracting States have also made unique declarations under Article 39 that have not been declared by any other Contracting States. These unique declared categories include:

- (1) Rights of the state government to arrest or detain an aircraft object for violation of safety-related or criminal law, provided that no such arrest or detention shall give rise to the power of sale or right to proceeds;<sup>91</sup>
- (2) Lien on goods in possession of home workers;<sup>92</sup>

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date of a written notice to the operator of specific intention to exercise rights under the IDERA in respect of a default would be the time of a ‘declared default’, but if no such IDERA notice was issued, the date of the last written notice of default to the operator by the IDERA holder would be the time of ‘declared default’. Bangladesh, as a different example, declared the following category under article 39(1)(a): ‘[L]iens or other rights of an authority of Bangladesh relating to taxes or other unpaid charges arising from or related to the use of that aircraft object and owed by the owner or operator of that aircraft object, arising since the time of a default by that owner or operator under a contract to finance or lease that aircraft object.’ ‘Declarations Lodged by the People’s Republic of Bangladesh Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Accession in Respect Thereof’, 15 December 2008, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/bangladesh.htm>, accessed 29 August 2013.

<sup>90</sup> ‘Lien created by bailees on goods in their possession.’ ‘Declarations Lodged by the Government of the Federal Democratic Republic of Ethiopia Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Ratification in Respect Thereof’, 21 November 2003, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/ethiopia.htm>, accessed 29 August 2013; ‘Declarations Lodged by the Government of the Federal Democratic Republic of Ethiopia Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Ratification in Respect Thereof’, 13 October 2006, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/kenya.htm>, accessed 29 August 2013.

<sup>91</sup> Declared by Bahrain. See text to n 83 above.

<sup>92</sup> Declared by Ethiopia. See text to n 90 above.

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<sup>88</sup> See text to n 86 above.

<sup>89</sup> The use of the words ‘declared default’ is widespread in declarations regarding preferred government liens for amounts owing after a ‘declared default’ in respect of the use of that aircraft as well as for amounts due to employees for unpaid wages. The Federation of Indian Airlines and the AWG sent a joint letter dated 17 July 2013 addressed to the EU-India Civil Aviation Cooperation Project proposing amendments to India’s Civil Aviation requirements that would reflect the intent of the Article 39(1)(a) declaration by India and clarify the position that the

- (3) Judicial costs incurred in respect of the sale of the aircraft and the distribution of the proceeds thereof pursuant to the enforcement of any mortgage or other executive title;<sup>93</sup>
- (4) Fees and other charges due to the Director General arising under applicable law of [the State] in respect of the aircraft;<sup>94</sup>
- (5) Wages and expenses for salvage in respect of the aircraft;<sup>95</sup>
- (6) A right or interest in respect of an aircraft which, if the aircraft had been a vessel, would have resulted in a maritime lien on the aircraft and its equipment for (a) salvage and (b) damage done by that aircraft;<sup>96</sup>
- (7) The right of the [State] to arrest, attach or confiscate mobile equipment and aircraft equipment in the event of breach of the customs or criminal laws of the [the State];<sup>97</sup>
- (8) Creditors' claims on current payments;<sup>98</sup>

- (9) Claims to cover costs for activities for the prevention of technogenic and/or environmental disasters or loss of life in cases where the termination of the debtor entity or its structural units may lead to technogenic and/or environmental disasters or loss of life;<sup>99</sup>
- (10) Claims, by individuals to whom the debtor is liable for causing injury to life or health, which are settled by means of capitalization of relevant periodic payments, as well as claims for compensation for moral damage;<sup>100</sup>
- (11) Claims for severance pay and remuneration of persons employed or working under an employment contract and for the payment of royalties to authors of intellectual property.<sup>101</sup>

*(vii) AWG recommended categories of declarations for Article 40*

AWG also issued 'Economically-Based Recommendations' for declarations that may be made under Article 40. AWG suggests again that there be a specific list and that the use of Article 40 for all categories of further NCRIs is preferred in order to bring them all into the first-to-file International Registry system.<sup>102</sup> AWG recommends three potential categories of declarations. AWG first recommends, 'Right of a person obtaining a court order permitting attachment of an aircraft object in partial or full satisfaction of a legal judgment.'<sup>103</sup> Second, AWG recommends, 'Liens or other rights of the government of {name of state} relating to taxes or other unpaid charges of

<sup>93</sup> Declared by Malta. See text to n 84 above.

<sup>94</sup> Declared by Malta. See text to n 84 above.

<sup>95</sup> Declared by Malta. See text to n 84 above.

<sup>96</sup> Declared by Pakistan. 'Declarations Lodged by the Government of the Islamic Republic of Pakistan Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Accession in Respect Thereof', 22 January 2004, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/pakistan.htm>, accessed 29 August 2013.

<sup>97</sup> Declared by Panama. 'Declarations Lodged by the Government of the Republic of Panama Under the Cape Town Convention and the Aircraft Protocol at the Time of the Deposit of Its Instrument of Ratification in Respect Thereof', 28 July 2003, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/panama.htm>, accessed 29 August 2013.

<sup>98</sup> Declared by the Russian Federation. 'Declarations Lodged by the Russian Federation Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Accession in Respect Thereof', 25 May 2011, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/russianfederation.htm>, accessed 29 August 2013.

<sup>99</sup> Declared by the Russian Federation. See text to n 98 above.

<sup>100</sup> Declared by the Russian Federation. See text to n 98 above.

<sup>101</sup> Declared by the Russian Federation. See text to n 98 above.

<sup>102</sup> See text to n 77 above.

<sup>103</sup> Variations on this model declaration include, '[T]he rights flowing from the arrest of an aircraft object in partial or complete performance of a judgment' (Cameroon & Congo). See text to n 83 above.



any type whatsoever (which is not covered by the declaration under Article 39(1)(a) of the Convention).<sup>104</sup> Third, AWG recommends, '[A]ny other non-consensual right or interest which is not covered by the declaration under Article 39(1)(a) of the Convention.'<sup>105</sup>

*(viii) Other variations of categories of declarations made under Article 40*

Certain Contracting States have declared categories concerning employees.<sup>106</sup> Nigeria has also declared three less common categories

<sup>104</sup> Variations on this model declaration include, '[L]iens or other rights of an authority of [the state] relating to taxes or other unpaid charges arising from or related to the use of an aircraft object and owed by the owner or operator of that aircraft object, arising prior to the time of a declared default by that owner or operator under a contract to finance or lease that aircraft object' (Bangladesh, India, & Malaysia). See text to n 89 above; 'Declarations Lodged by the Republic of India Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Accession in Respect Thereof', 31 March 2008, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/india.htm>, accessed 29 August 2013; 'Declarations Lodged by the Government of Malaysia Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Accession in Respect Thereof', 2 November 2005, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/malaysia.htm>, accessed 29 August 2013.

<sup>105</sup> Variations on this model declaration include, '[A]ny other category of NCRIs that are not subject to the declaration made under Article 39(1)(a) of the Convention and which are capable of being registered in the International Registry as if they were an international interest and capable of being treated as such' (Togo). See text to n 84 above.

<sup>106</sup> Bangladesh, India, and Indonesia declared the following category: '[L]iens in favour of airline employees for unpaid wages arising prior to the time of a declared default by that airline under a contract to finance or lease an aircraft object.' See text to n 89 and n 104 above; 'Declarations Lodged by the Republic of Indonesia Under the Cape Town Convention at the Time of the Deposit of Its Instrument of Accession in Respect Thereof', 16 March 2007, at <http://www.unidroit.org/english/conventions/mobile-equipment/depositaryfunction/declarations/bycountry/indonesia.htm>, accessed 29 August 2013.

under Article 40. These declared categories include (1) liens of a salvor for unpaid charges in respect of salvage services provided to an aircraft object when it is water borne, (2) liens of a person providing towage services to an aircraft object when it is water borne in respect of unpaid charges, and (3) liens of a bailee of an aircraft object in respect of unpaid charges for the bailment of the said aircraft object.

*(b) Divergent categories of declarations from best practices and recommendations*

Some examples of divergences found in the summary in subsection (a) above from UNIDROIT and AWG form declarations illustrate the ways in which new declarations can be improved and existing declarations can be amended or interpreted where possible in a Contracting State to achieve more uniform results of lien disputes and greater predictability within these jurisdictions.

Many of the declaration variations are different in detail and no change is suggested as a result of these differences. Different approaches to NCRIs are expected. And, the model declarations do not always fit the language or concepts of a national law created right or interest. However, here are some issues drawn from actual declarations that can make declarations fail to work as well as they should and the reasons why:

- (1) Lack of relevance to mobile equipment or to aircraft in particular. Declarations as to rights or interests that are not relevant in any way to mobile assets should be withdrawn.
- (2) Incomplete descriptions or inconsistent text that renders the declaration almost impossible to use.
- (3) Incorrect use of the exclusivity between Articles 39 and 40. Rights or interests that are repeated in both of Article 39(1)(a) (which by its terms excludes a right or interest as to which Article 40 applies) renders at a minimum the Article 39 declaration a nullity and may be so inconsistent as to exclude use of the Article 40 declaration.



- (4) Efforts at distinguishing the declaration under Articles 39 and 40 described in subsection (b)(3) above by reference to the time at which a charge arose, but in the two declarations the timing is incorrectly described.
- (5) Use of the general term of ‘international interest’ when only security interests or mortgages are subject to NCRIs under the national law in contrast to title reservation agreements and leases where the title holders such as lessors and conditional vendors would not be subject to NCRIs in that Contracting State, thereby misleading and creating uncertainty among potential financing parties and lessors. In this connection, a declaration may have actually been viewed as a positive declaration if the focus had been solely on the type of international interest for which the local equivalent was a security interest and then had confirmed the characterization of that type of interest in the declaration.<sup>107</sup> For this kind of declaration issue, it would be helpful if a revision to the existing declaration could be done as a technical amendment since it would add to the transparency as to national laws of NCRI priority that Article 39 declarations were designed to create.
- (6) Using language from the form, such as Form No. 4 with respect to ‘or another

object’ without changing the form language when the underlying law of the declaring State does not contain applicable fleet lien or detention rights, or since they are not in use they could be restricted at this time for the benefit of the aviation industry in that State.

*(c) Thoughts on Considerations in Making Article 39 Declarations to Maximize Convention Benefits*

As noted above, Article 39 gives a Contracting State the option to declare ‘at any time’ which NCRIs will enjoy up to the same priority with respect to registered international interests as such NCRIs have with equivalent interests under its internal law. A declaration may not create a new NCRI or accord it a greater priority than that under applicable internal law, but a declaration may restrict the priority of an NCRI vis-à-vis a registered international interest as compared with such NCRI’s priority with respect to an equivalent domestic interest. In all cases, a declaration under Article 39 may be general or specific in terms of identifying categories of NCRIs to be covered. By creating more uncertainty and risk for financing parties, a larger and/or less specific universe of NCRIs covered by a declaration reduces (or potentially eliminates) the willingness of potential financing parties to offer financing to the operators in the applicable Contracting State and tends to raise costs of such financing.

There is already extensive research and precedent under the Convention for the economic benefits to Contracting States of making declarations that are required by the OECD<sup>108</sup> in order to obtain the discounts available on export credit financing. The

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<sup>107</sup> See Section 3(b)(ii) discussion in depth; an example of the issue is in the Russian declaration. ‘Pursuant to subparagraph ‘a’ of paragraph 1 of Article 39 of the Convention, the Russian Federation declares that on the territory of the Russian Federation the following claims of creditors that are satisfied during insolvency proceedings shall have priority over a registered international interest...’. Russian Federation Declaration (n 98); however, after concerns were raised that the international interest would include title holders and lessors, it was confirmed that in insolvency proceedings the interests of the title holders under a conditional sale or a lease were not included in the debtor’s bankruptcy assets under local law and not subordinate to NCRIs so they could not be covered by the declaration.

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<sup>108</sup> The Organisation for Economic Co-operation and Development (OECD) provides a forum for world governments to work together to design policies that will improve the economic and social well-being of all people. See the OECD website at <http://www.oecd.org/>. For further discussion, Kristin Van Zwieten, ‘The Insolvency Provisions of the Cape Town Convention and Protocols: Historical and Economic Perspectives’ (2012) 1 *Cape Town Convention Journal* 53, [n 148-57].

declarations also support the capital markets options that Contracting States are only now beginning to see may be available as a result of proactive declarations made by Contracting States. Some of the limitations on declarations suggested in this article and in any event the correction of deficient declarations discussed earlier in this Section 4 can also be economically beneficial to the airlines and operators of a Contracting State and do justify a proactive stance on declarations by Contracting States.

Certain themes relevant to NCRI and rights of detention policy determinations emerge today from the historic framework outlined above in Section 2 of this article. In general, the law has tended to discourage creation of NCRIs and rights of detention except as necessary to ensure payment to furnishers of services, and then mostly where the value added to goods was specific to the debtor (e.g., repairers and tailors) or where the debtor was likely to be difficult to reach by the time other remedies could be pursued (e.g., maritime liens on foreign vessels alleged to have caused damages and liens in favour of innkeepers). Similarly, Section 2 of this article describes how English common law favoured particular liens over general liens and notes that general liens in the common carrier industry withered away due to changes in that industry and due to inequitable impacts from general NCRIs. Likewise, even when a case can be made for creation of an NCRI, Section 2 described Professor Gilmore's analysis of different relative priorities that can be accorded such liens.<sup>109</sup>

Against this historical context, three significant changes to the airline industry occurring over the last four decades have raised important issues that should inform how Contracting States approach their Article 39 declaration policy. First, most national NCRI regimes implicitly reflect an increasingly outdated aircraft operating model in which airlines were regulated and/or owned by the State. To assure adequate cashflow to existing airlines, regulators would typically treat airlines

like utilities and thus restrict competition, set fares, limit capacity and, particularly in the case of state-owned carriers, provide subsidies. Countries would support loss-making national carriers for various reasons including international pride, promotion of tourism, creation of airline-related jobs and maintenance of military capabilities. In that environment, insolvencies and failures were far less common than today, so lending and operating lease assumptions about asset values were not as exposed to unexpected diminution by NCRIs. The wide deregulation of airlines has benefited consumers with lower costs and greater choice, but the industry is now far more volatile; bankruptcies and restructurings are routine events. As a result, NCRIs create a much higher degree of uncertainty for, and can inflict greater injustices on, providers of financings and operating leases.

Second, an ever-increasing number and percentage of commercial aircraft are owned by third party lessors. When operators owned their aircraft, there was fairness in attaching the operator's assets for the benefit of creditors who had extended goods and services to it. Such creditors might include employees owed wages for work performed, governments and agencies owed accrued taxes and fees for air navigation and airport operations, maintenance and repair organizations ('MROs') owed for adding value to the operator's equipment through overhauls and repairs, and suppliers owed for providing essential consumables such as fuel and catering. With the exception of certain durable value added to aircraft equipment by MROs, the goods and services provided by operator creditors do not particularly benefit financing parties. Although lenders can, to some extent, create a buffer for NCRIs by reducing loan-to-value ratios, operating lessors bear the full brunt of NCRIs relating to costs, taxes and fees for which they were not responsible and are not in a better position to discourage and control than the immediate creditor.

Fleet liens, a particularly glaring remnant of the era of regulated airlines that owned their equipment, allow a government agency

<sup>109</sup> See Section 2 above; Gilmore (n 13) 874.

such as Eurocontrol to assert priority NCRI on a particular aircraft to recover charges attributable to the aircraft whose operation gave rise to the charges and in some instances, even charges created by operation of other aircraft in the same fleet as described in Section 2(b)(iii). This may have been more defensible when operators owned the applicable aircraft, but today this aspect of many NCRI regimes creates considerable risk to financing parties and is especially unfair to operating lessors. Nonetheless, Article 39 (1)(b) expressly preserves the possibility of NCRI to secure payment of amounts owed relating to services 'in respect of that object *or another object*' (emphasis added) if that reflects the underlying national law of the declaring State.

Third, for at least certain types of debts incurred in operation of an aircraft, technology could readily replace the old NCRI approach without sacrificing its intended policy objectives but achieving them without diminishing the Convention benefits and with far greater fairness. For example, until recently the recordkeeping required to process navigation charges and landing fees was cumbersome and inaccurate – there was a defensible analogy to liens in favour of innkeepers and carriers and to maritime port rights of detention. Now, technologies akin to automobile toll road fare collection devices could make accruals, even payments, for such small but regularly-occurring charges more rapid and accurate and obviate the need for NCRI, or at least their special priorities. Moreover, financing parties and operating lessors have a shared interest with other creditors in driving responsible airline financial practices and would be allies supporting timely payment of other creditors if given more transparent information on accruing arrearages.

Accordingly, in order to maximize the Convention benefits for their operators while protecting categories of creditors accorded special treatment through an NCRI regime, Contracting States should carefully consider limiting the scope of such NCRI, either in the relevant Article 39 declarations or in

related enabling legislation. With respect to aircraft objects that are operator-owned and subject to either a secured loan or finance lease, NCRI should not cause the lender's anticipated loan-to-value ratio to fall below that necessary to repay the applicable loan or finance lease balance. This could be accomplished by making declared NCRI subordinate 'only' to registered international interests in which case the beneficiaries of preferred NCRI would come ahead of other NCRI and the discharge of all NCRI would come at the expense of the owner-operator that incurred the applicable obligation. This would be a version of Professor Gilmore's second category of NCRI in which statutory liens were subordinated to security interests.<sup>110</sup> A variation of this approach would establish a fixed aggregate amount of priority NCRI, with any balance coming immediately after the lenders secured by the registered international interest. Such a distinction might be reserved for NCRI in favour of providers of services that keep the aircraft object airworthy, such as MROs and other repairers of aircraft.

Both to obtain for their operators the benefits intended by the Convention and for the sake of fairness, Contracting States should arguably not permit NCRI to encumber aircraft objects owned by title holders of aircraft other than the operator, such as operating lessors, with the possible exception of NCRI relating to services necessary for maintenance of airworthiness. Apart from such an exception, there is no justification for transferring value from the asset of an operating lessor to a creditor of an operator. As an example, take the operating lessor who did not incur the liability incurred by the operator and did not even know about it. Such a title holder is not in a better position to discipline the improvident incurrence of an obligation by its lessee or to cause the lessee to make payment of operational obligations and fees. A middle ground might be providing for a capped pool of NCRI allowable on

<sup>110</sup> Gilmore (n 13) 874.

leased aircraft, small enough that the operating lessor could require deposits or include lease covenants and periodic certifications that would protect its ownership interests. Above all, unless at least subject to these kinds of caps, Contracting States should only permit priority fleet liens on aircraft that are owned by the operator; the fleet lien option in Article 39(1)(b) for aircraft owned by parties other than the operator and subject to a registered international interest should not be elected.

Just as NCRI in other industries were revised or eliminated as technologies allowed, a Contracting State can today turn to alternative means of protecting its creditors that are currently benefiting from priority NCRI. For example, technology now readily enables air navigation and landing fees to be accrued and billed promptly with attribution to the proper operator and aircraft. Such technology also enables giving lenders and operating lessors greater real-time transparency into accruing liabilities that may give rise to liens. Making creditors aware of this threat to their collateral or asset would effectively enlist them in efforts to spur discharge of those liabilities by the operator. There is evidence that creditors who have the benefit of priority NCRI may be more inclined to let unpaid charges accrue rather than pursue timely collection, effectively transferring the risk of nonpayment to other creditors. To avoid this, consideration should be given to imposing time limitations on such NCRI benefit if meaningful enforcement efforts have not been taken by the creditor.

## 5. Application of Article 39 in practice

Articles 8 to 15 of the Convention and Articles IX to XIII of the Aircraft Protocol provide remedies that may be exercised by lessors, conditional sellers, and secured parties in respect of international interests. Such remedies generally provide that after a default a creditor may, in a commercially reasonable manner, repossess, deregister, or sell aircraft objects in which the creditor has an international interest. As a preliminary matter, the inquiry with respect to an asserted international interest

includes whether an international interest has been validly constituted with respect to an aircraft object, meets all the Convention formalities, the extent of the equipment to which the interest applies, and whether the interest has been registered on the International Registry and with what priority.

Article 39 adds another layer to the detailed examination that must be undertaken to determine the exercise of remedies in the domestic or international context because a typical enforcement scenario often involves the priority of an asserted international interest *vis a vis* a purported NCRI. Below, that analysis is broken down into theoretical examples and discussions of the effect of different NCRI types and then into practical issues to be considered by practitioners in local enforcement of remedies.

### *(a) Effect of Article 39 non-consensual rights or interests on the exercise of remedies in the domestic and international context*

#### *(i) Liens under Article 39(1)(a)*

The inquiry with respect to a NCRI asserted pursuant to Article 39(1)(a) involves determining whether a Contracting State has made a declaration (general or specific) that the particular type of NCRI has priority under the laws of that State, and, if so, whether such declaration became effective before or after the registration of the applicable international interest. The timing of declaration effectiveness is important because under Article 39(3) a NCRI conferred by national law with respect to which a Contracting State has made a declaration under Article 39 *may* have priority over a registered international interest only if the declaration concerning such NCRI was deposited with the Depository first. In the case of a declaration made pursuant to Article 39(4), the categories of NCRI declared will have priority even if they arose before the declaration because the Contracting State has said that they will have such a priority over an international interest.<sup>111</sup>

<sup>111</sup> Of the 39 countries that have made declarations through July 10, 2013 pursuant to Article 39(1)(a),

The declaration is no more than a statement as to types or categories of NCRIs that may be covered by each Article 39 provision. The declaration in and of itself does not create the underlying law and does not necessarily mean that the given NCRI is recognized by the national law of the declaring country or is accorded a special priority. Thus, the inquiry is not grounded solely in determining whether the international interest was registered first or the NCRI declaration became effective first. Indeed there is a more fundamental issue, that being whether there is an enforceable NCRI and whether in that Contracting State the NCRI has priority over interests equivalent to the registered international interest under that State's laws that is covered by the declaration. This would include analysis of whether a declaration has a limitation to certain international interests or other limiting language that would mean that the NCRI would be effective only prior to that particular type of international interest under that Contracting State's laws.<sup>112</sup>

As a *basic example*, presume that a maintenance facility located in a Contracting State seeks to enforce a mechanic's lien against an aircraft in the Contracting State and that under the laws of the Contracting State the mechanic's lien is a valid NCRI with priority over an interest equivalent to a registered international interest in the Contracting State. At the same time, a lessor is attempting to enforce its rights in the Contracting State to repossess the aircraft in which it has a registered international interest. In this instance, there should be no doubt that the NCRI has priority over the registered international interest. Changing the

example slightly: if the local law recognizes the mechanic's lien as a valid NCRI but does not recognize the priority of the mechanic's lien over an interest equivalent to the applicable registered international interest, then it should not be afforded priority under the Convention. Why? Because of the Convention's reliance on *both* the validity *and* priority of the NCRI under local law.

As a *second example*, presume that a maintenance facility located in Contracting State A seeks to enforce a mechanic's lien against an aircraft in Contracting State B and that after examination under the laws of Contracting State A it was determined that the mechanic's lien was a valid NCRI with priority over an interest equivalent to the applicable registered international interest in the Contracting State A. At the same time, a lessor is attempting to enforce its rights in Contracting State B to repossess the aircraft in which it has a registered international interest. Does it matter that the mechanic's lien is valid and has priority in Contracting State A and does it matter whether Contracting State B made a declaration under Article 39(1)(a) as to mechanic's liens? No, it would not matter. Consider the following reasoning.

If the NCRI were a treaty-based lien, then Country B would be obligated to recognize the mechanic's lien even if its own laws did not. Such is not the case, however. As has been recognized by Professor Goode in the Official Commentary, the declaration of a category and application of a NCRI may not expand a right beyond that permitted by the law of Country B.<sup>113</sup> In the enforcement context, when the law being considered is the law of the forum, the inquiry may be relatively straightforward and, assuming a valid NCRI with clear priority, would rest on whether the international interest was registered first or whether the NCRI declaration became effective first. But where the asserted NCRI arises under the law of a State different than that in which enforcement is sought, the Convention does not apply to this

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only eight of those countries declared Article 39(4) permitting such priority of a non-consensual right or interest covered by a declaration under Article 39(1)(a) over an international interest registered prior to the date of the ratification, acceptance, approval or accession of the Aircraft Protocol.

<sup>112</sup> For example, see subsection 4(b)(5) above for a discussion of declarations where the national law gives priority only over charges under security agreements and not title holders such as lessors and conditional vendors.

<sup>113</sup> Official Commentary, Goode (n 2) para 4.270.



question at all since the NCRI declaration was made solely by the one State for use within its own national law as it applies to international interests. Indeed, this is why Professor Goode states: '[T]he priority is not a Convention priority but one given by the law of the declaring State. It is therefore not entitled to recognition in another Contracting State *unless the conflict of laws rules of that State so require.*'<sup>114</sup> That a declaration made by a Contracting State under Article 39 is a declaration by the Contracting State as to categories with priority under its own law and not a declaration concerning the laws of another Contracting State is further supported by a comparison between Article 39 and Article 40. Whereas the former recognizes a Contracting State's right to declare the effectiveness of a priority under its own law, the latter recognizes a Contracting State's right to declare which categories of its NCRIs shall be registrable and capable of being registered as a registered interest, *i.e.*, a treaty-based right effective and recognized in all other Contracting States.

Nor does the specific wording of the opt-in provisions of declaring countries change this result. Indeed, the typical opt-in provision says something along the lines of: 'The following categories of NCRIs have priority under its laws over an interest in an aircraft object equivalent to that of the holder of a registered international interest and shall have priority over a registered international interest, whether in or outside insolvency proceedings, namely: . . .' The phrase 'under its laws' refers only to the laws of the declaring State.

A very important timing issue has been raised by Professor Goode. This is the further question as to under what conditions and when the priority of a right or interest covered under Article 39 attaches under the law of the declaring State.<sup>115</sup> Professor Goode states:

Outside insolvency Article 39 rights will almost always take the form of a lien or a right of arrest or

detention. Exercise of such a right is governed by the law of the declaring State but typically depends upon the aircraft object still being in the debtor's possession. Where that is the case the Article 39 priority will not be exercisable against the holder of a registered interest that has already availed itself of an enforcement remedy over the aircraft object. But if before then the holder of the Article 39 right or interest has taken possession of the aircraft object or has exercised a right to arrest or detain it, the attached priority of that right or interest must be respected by the holder of the registered international interest to the extent required by the law of the declaring State.<sup>116</sup>

Consider the above comments in the context of the earlier example of the maintenance facility seeking to enforce a mechanic's lien against an aircraft in the Contracting State while a lessor attempts to enforce its rights in the Contracting State to repossess the aircraft. If the lessor has 'already availed itself of an enforcement remedy over the aircraft object', then it will be determined under the law of the declaring State whether the maintenance facility is able to enforce its mechanic's lien. In particular, the law of the declaring State will need to determine to what extent the enforcement remedy will need to have progressed in order for the mechanic's lien to become subordinate and be required to respect the interest of the lessor who is the holder of a registered international interest. As described in greater detail in paragraph 2.218 of the Official Commentary, the issue of timing of attachment of either the Article 39 right or interest or of a registered international interest is derived in part from the principle that the holder of a registered international interest has a duty to respect priorities and this carries over to the role of actual enforcement. If the fact situation described were reversed and the mechanic's lien had been enforced against the aircraft object, then the right or interest would have attached and the holder of the registered international interest would have to respect such attached priority, once again to the extent required by the law of the declaring State.

<sup>114</sup> Ibid, para 4.269 (emphasis added).

<sup>115</sup> Ibid, para 2.83; see further discussion at Sections 3(c)(viii) and 5(b).

<sup>116</sup> Ibid, para 2.218.



(ii) *Right of arrest or detention under Article 39(1)(a) and under Article 39(1)(b)*

The foregoing discussion as to national law validity and priority of NCRIs within the context of the Convention holds equally true in the context of rights of arrest or detention pursuant to a declaration made pursuant to Article 39(1)(a). As recognized by Professor Goode, the rights of arrest or detention given by the law of a State for payment of amounts due to a provider of public services<sup>117</sup> can be covered by a declaration under Article 39(1)(a) if given priority under the relevant national law over interests equivalent to that of the holder of a registered international interest.<sup>118</sup> Alternatively, a Contracting State can make a declaration under Article 39(1)(b), which serves as a savings clause in so far as it protects rights of arrest or detention given by contract because such rights are not covered under Article 39(1)(a). Professor Goode recognizes that NCRIs covered under Article 39(1)(b) are not entitled to recognition in another Contracting State unless the conflict of laws rules of that State so require.<sup>119</sup>

Consider the following example of an Article 39(1)(b) declaration made by Country A:

Nothing in the Convention shall affect the right of Country A or that of any entity thereof, or any intergovernmental organization in which Country A is a member, or other private provider of public services in Country A, to arrest or detain an aircraft object under its laws for payment of amounts owed to the Government of Country A, any such entity, organization or provider directly relating to the service or services provided by it in respect of that object or another aircraft object.

Although this declaration is made pursuant to the Convention, the right of arrest/detention referenced in the declaration is given by the

law of Country A. Hence, as with a declaration made pursuant to Article 39(1)(a), the conflict of laws rules of a different forum state will determine the extent to which the NCRI may be recognized.

Using the foregoing declaration as a basis, let us take the example that an airport authority of Country A attempts to detain *three* aircraft, designated as Aircraft 1, Aircraft 2, and Aircraft 3, operated by a lessee operator based on unpaid fees due by the operator to such airport authority for Aircraft 1 in the amount of \$50,000 and for aircraft 2 in the amount of \$50,000. The airport authority asserts a right of detention based upon the Article 39(1)(b) declaration. The question is whether the lessor's right to repossess all three aircraft in the event of a default on rental payments for all three aircraft is superior to that of the airport authority's purported NCRI based on the unpaid fees.

In this example, for the airport authority to seek detention of all three Aircraft through an action in the courts of Country A, there are three essential points underlying the analysis. First, the declaration itself is not the actual right of detention.<sup>120</sup> Second, the Convention does not create a treaty-based detention right but recognizes Country A's declared detention right in Country A, which will be conditioned according to Country A's actual laws.<sup>121</sup> Third, the declaration addressing the right to detain 'another object' (which would provide the authority to detain an aircraft other than that on which the operator owes the aircraft fees) must have become effective before the lessor's registration of its interest.<sup>122</sup> Accordingly, provided that the declaration was effective prior to the lessor's registration of the international interest, *and* provided that the law of the declaring State permits the exercise of a lien on equipment other than that on which the fee is owed, then the aircraft authority *does* have the right to detain all three aircraft even though there are only fees due on two of the aircraft.

<sup>117</sup> Examples of 'public services' are services that result in airport and navigation fees, but not general taxes owed by the debtor. See Official Commentary, Goode (n 2) para 2.215.

<sup>118</sup> *Ibid*, para 4.272.

<sup>119</sup> *Ibid*, para 4.272. See discussion of the same issue as to Article 39(1)(a) at text relating to n 105.

<sup>120</sup> *Ibid*, para 4.272.

<sup>121</sup> *Ibid*, para 4.272.

<sup>122</sup> *Ibid*, para 4.278.

Consider a second example where Aircraft 1 is located in Country B, whose laws do not permit any liens arising out of unpaid airport fees. The airport authority of Country A seeks to detain Aircraft 1 by commencing an action in the courts of Country B. Here, in addition to the three essential underlying points referenced in the foregoing paragraph, there is the additional consideration that the Convention does not recognize Country A's declared detention right in another country. Instead, as noted above, the Convention does no more than recognize that Country A has made a declaration that claims for unpaid airport fees will have priority over an international interest. In this scenario, the court of Country B is under no obligation to recognize the right of detention under the laws of Country A. Instead, we would expect that the court of Country B would engage in a choice-of-law analysis to determine whether it would permit the arrest/detention sought by the airport authority of Country A. Given that its own laws do not permit such an arrest, it appears unlikely that the court of Country B would order the arrest/detention.

There are few court decisions to date on Convention applicable international interests or NCRIs. There is one decision that illustrates in a partial way the point that Article 39 of the Convention does not create a treaty-based detention right that could be utilized outside of the declaring State. In *Corporate Aircraft Funding Company LLC v. Union of India & ORS, W.P.(C) 792/2012*, High Court of Delhi at New Delhi, March 14, 2013, the High Court determined that powers under the Customs Act of India, which appear to have included a power of detention, could not be exercised when the subject aircraft was outside of India. The case also included a clash between the government agency's right of detention and the right of a creditor to deregistration under an irrevocable deregistration and export request authorization (IDERA). In that case, a petitioner mortgagee had made a loan to the owner of the aircraft which was secured by a mortgage on the aircraft. It appears to have been a Convention

applicable international interest, but that was not the main point at issue. The instrument of mortgage conferred on the mortgagee the right to seek deregistration of the aircraft from the jurisdiction of the State Registry, defined as the national jurisdiction in which the aircraft was registered. Here, the State Registry was India. The lessee executed an irrevocable power of attorney empowering the mortgagee to seek deregistration of the aircraft and an IDERA pursuant to Article XIII of the Aircraft Protocol.

Following the termination of the lease between the owner and lessee and the default of the owner on the loan, the mortgagee sought its right of deregistration. The deregistration was challenged by India's Director General of Civil Aviation (DGCA) at the behest of the Directorate of Revenue Intelligence (DRI) on the basis that the lessee had not paid certain customs fees in connection with the importation of the aircraft into India. At the time that the mortgagee sought to exercise its right of deregistration, the aircraft was located in London.

The mortgagee asserted that the DGCA's refusal to effect deregistration violated the Convention and the Aircraft Protocol and that under Article XIII of the Aircraft Protocol the DGCA had the duty to assist the mortgagee in exercising its available remedies, including deregistration of the aircraft. The mortgagee further asserted that the Customs Act had no applicability because the aircraft was located outside the territory of India.

As a basic premise, the Court found that under Articles IX and XIII of the Aircraft Protocol, the DGCA ordinarily would be obligated to assist the mortgagee in obtaining deregistration. But the Court stated that such obligation needed to be considered in connection with India's instrument of accession, which empowered the detention or arrest of an aircraft with the object of recovering an amount owed to the government or any inter-governmental organization or private provider of public services in India under the extant laws in respect of services provided to

the aircraft. Referencing the general opt-in declaration of India under Article 39(1)(b),<sup>123</sup> the Court stated:

A bare perusal of the said provision would show that the power conferred therein is with regard to arrest and detention of the aircraft and not to prevent its deregistration. Admittedly, the Aircraft is no longer available in India, having flown out of India. . . . Therefore, the DGCA cannot now, in my opinion, do indirectly what it cannot achieve directly. The argument advanced on behalf of the DRI that, since there is no reason to believe that the aircraft (being 'goods', within the meaning of the Customs Act), is liable to be confiscated on account of the fact that the conditions of exemption notification were violated cannot be accepted as the Aircraft, i.e., goods in issue, are no longer available within the territorial jurisdiction of India. The power under Section 110 of the Customs Act cannot extend beyond the territorial jurisdiction of India.

Within this quote and the opinion, the Court focused on a number of different points concerning the non-consensual right of detention under Article 39(1)(b), the relation of such right (or power as they call it) to the IDERA, and the limit of the national law conferring such right to the territorial jurisdiction of India. With regard to the Convention and India's Article 39(1)(b) declaration, it made clear the distinction that the 'power conferred therein is with regard to arrest and detention of the aircraft and not to prevent its deregistration.' Since the aircraft was then outside of India, the Court extensively discussed its reasoning that the government did not have power to extend its territorial jurisdiction outside of India in regard to the

Customs Act that conferred the actual right of confiscation. It also emphasized that the government could not then indirectly affect the aircraft by preventing the DGCA from honoring its obligations to deregister an aircraft pursuant to the Convention. Finally, it also said there was no power under the Customs Act by which the government could order the DGCA to desist from deregistering the aircraft and issued a writ of mandamus directing the DGCA to deregister the aircraft.

The Court's reference to India's Article 39(1)(b) declaration under Form No. 4 as the right of arrest or detention being a 'power conferred therein' might be construed as meaning that the Convention conferred the right or that the declaration conferred the right, but that is not correct since, as noted earlier, the NCRIs and the rights of arrest and detention declared under Article 39(1)(b) are conferred only by national law.<sup>124</sup> Article 39(1)(b) preserves the existing right of arrest or detention that exists in the declaring State.

*(iii) Interested persons*

Attention must be paid to the definition of 'interested persons' as defined in Article 1(m) sub-paragraphs (i), (ii) and (iii) of the Convention. Included in Article 1(m)(iii) of the multi-part definition of 'interested persons' is 'any other person having rights in or over the object.' As recognized by Professor Goode, this broad category includes, among others, holders of NCRIs under Article 39 and holders of registrable NCRIs under Article 40 who have not registered their interest.<sup>125</sup> If such a holder had registered its registrable NCRI, it would have broad notice rights under the Convention as a debtor under Article 1(m)(i).<sup>126</sup>

<sup>123</sup> India's Article 39(1)(b) declaration under Form No. 4 states: 'Nothing in the Convention shall affect its right or that of any entity thereof, or any intergovernmental organization in which India is a member, or other private provider of public services in India, to arrest or detain an aircraft object under its laws for payment of amounts owed to the Government of India, any such entity, organization or provider directly relating to the service or services provided by it in respect of that object or another aircraft object.' See text to n 95 above.

<sup>124</sup> Official Commentary, Goode (n 2) paras 4.270, 4.272. The Official Commentary notes that a declaration cannot create a non-consensual right or interest or a right of arrest or detention.

<sup>125</sup> *Ibid*, para 4.19, 2.87.

<sup>126</sup> Article 1(j): a debtor includes 'a person whose interest in an object is burdened by a registrable non-consensual right or interest'. An object would be

When holders of NCRIs and registrable NCRIs that have not been registered are ‘interested persons’, they must receive notification under Article 8(4)(b) of an intended sale or lease of a charged object by a charge, provided such persons ‘have given notice of their rights to the chargee within a reasonable time prior to the sale or lease’. Interested persons under sub-paragraph (iii) also must give their consent under Article 9(1) to the vesting of the object in the chargee in satisfaction of the debt in the absence of a court order and must be given notice if required by a court order entertaining a request from a creditor for advance relief under Article 13.<sup>127</sup> Because Articles 9(1) and 13 do not have the same provision as Article 8.4(b) that the sub-paragraph (iii) holders must have given reasonable notice of their existence to a creditor, we must look further to understand what duty a creditor may have to obtain knowledge as to the existence of holders of which it is not aware at the time of enforcement by the creditor.

Interpretation as to the extent of this duty would fall within Article 5 rules of interpretation of the Convention. Under Article 5(1) when interpreting the Convention, ‘regard is to be had to its purposes as set forth in the preamble, to its international character, and to the need to promote uniformity and predictability in its application’. Article 5(2) states that matters not expressly settled by the Convention ‘are to be settled in conformity with the general principles on which it is based, or, in the absence of such principles, in conformity with the applicable law.’<sup>128</sup> Here, the duty of inquiry, if any, by the creditor

should, in the interest of uniformity and predictability under the Convention, follow the rule in Article 8(4)(b) to the extent that it makes sense within the contexts and the purposes of Articles 9(1) and 13 and the Convention.

*(b) Practical issues in dealing with government authorities and Article 39(1)(a) and (b)*

Under the Convention, an enforcing creditor, which can include the holders of NCRIs, must respect priorities.<sup>129</sup> As such, from an enforcing creditor’s perspective, one of the more important aspects of dealing with government authorities may be one of timing. As recognized by Professor Goode, there is a need to establish the point at which the NCRI priority attaches.<sup>130</sup> An Article 39 priority will not be exercisable against a lessor who is the holder of a registered international interest that has already availed itself of an enforcement remedy over the aircraft object if the national law of the Contracting State that declared such NCRI category recognizes the priority of the rights of an enforcing lessor over the NCRI holder.<sup>131</sup> Why? Because the exercise of a NCRI is ‘governed by the law of the declaring State.’<sup>132</sup> In countries where an Article 39 declaration of arrest/detention has been made, the timing issue creates a tension between when a lessor should advise airport authorities that it is seeking its rights of enforcement and a lessor’s usual preference to be discrete about its enforcement plans so that the lessee does not have an opportunity to remove the aircraft object to a different jurisdiction.

As a basic premise, the lessor should determine whether it plans to proceed by judicial or non-judicial remedies. Certainly, if a lessor believes that an airport authority may have a right to arrest/detention under Article 39, and if the lessor proceeds by judicial remedies, then it

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considered ‘burdened’ by a non-consensual right or interest if the right or interest has been a registered on the International Registry so that concerned parties would have notice of it.

<sup>127</sup> Official Commentary, Goode (n 2) paras 4.19, 4.88, 2.87(3).

<sup>128</sup> Article 5(3) further provides that references to the applicable law are to the ‘domestic rules of the law applicable by virtue of the rules of private international law of the forum State.’

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<sup>129</sup> Official Commentary, Goode (n 2) para 2.83.

<sup>130</sup> *Ibid*, para 2.83; see Sections 3(c)(viii) and 5(a)(i).

<sup>131</sup> *Ibid*, para 2.218.

<sup>132</sup> *Ibid*, para 2.218.

may wish to proceed as quickly as possible to initiate the action in the local court of a law that will recognize that action as giving the lessor priority. It is possible under local law that a lessor will be deemed to have ‘already availed itself’ of its enforcement remedies by virtue of such court action, even if the court has not actually issued an order directing the return of the aircraft object. Thus, consultation with local counsel is paramount to determine the laws of priority under the Contracting State and of course to aid in the practical issues of communicating with airport authorities.

Trickier is the case where a lessor elects to proceed by non-judicial remedies. In that instance, the lessor will need to consider several factors, the first of which is whether the Contracting State permits non-judicial remedies under Article 54(2) of the Convention. But beyond that, and the truly challenging part, is that in the absence of a court order, it will likely be necessary for a lessor to involve the airport authorities in attempting to repossess an aircraft object that is within the confines of that airport authority’s jurisdiction. In that instance, the airport authority may have an argument that the lessor has not ‘already availed itself’ of its enforcement remedies at the time when it seeks to enlist the aid of the airport authority. And of course, as such, the airport authority will also be notified of the potential ‘adverse’ interest of the lessor.

*(c) Removal of non-consensual rights or interests from the International Registry*

When pursuing remedies, one of first steps will be a search of the International Registry, and if a NCRI turns up the question will arise if it is valid or should be registered at all. The registration of interests on the International Registry is completed online through the registry website.<sup>133</sup> The consent of all named

parties must be provided through the website by means of a digital signature. For Article 40 registrable NCRIs, consent of all concerned parties would not make sense and so a holder can effect that registration on its own. Such a registrable NCRI as the name suggests does not require the consent of any party other than the holder of the interest.

Registrations of alleged registrable NCRIs purportedly made under Article 40 are not some defect on the part of the International Registry. As the Official Commentary points out, the system is ‘purely electronic and involves no human intervention at the Registry end. So the Registrar has no role to play in relation to a discharge dispute and can act only on the order of the court’.<sup>134</sup> Such invalid registrations create problems for the holder of title of the aircraft as they may be considered a cloud on title and delay or prevent the passing of unencumbered title to a potential purchaser in an ordinary sale or in a non-judicial sale following the pursuit of remedies. The steps below would likely need to be taken. In a judicial sale, some shortcuts may be possible as the creditor should be able to obtain an order from the same court that can be used to speed up the discharge of the registration.

*(i) Steps in aid of discharge*

Article 25 and Article 44 of the Convention provide guidance on procuring the removal of invalid registrations from the International Registry. The Official Commentary has an extensive discussion<sup>135</sup> of the court approaches. There are many aspects of a removal process to be considered and these are beyond the scope of this article. Below is a brief summary but it should not be viewed as complete.

*(a) Article 25 demand for discharge*

Article 25 provides that where either the obligations secured by a registered interest have been discharged, or where a registration

<sup>133</sup> The International Registry is maintained and managed under Article 17 of the Convention by the Registrar. The contract to do so is awarded for a five-year term. The Irish company Aviareto successfully tendered for the first contract from 2006 to 2011 and this contract was subsequently renewed for a further five years until 2016.

<sup>134</sup> Official Commentary, Goode (n 2) paras 2.142, 2.143.

<sup>135</sup> *Ibid*, paras 4.298–4.304, 2.231.



should not have been made or is incorrect, the person in whose favour that registration was made shall procure its discharge (or amendment) after written demand by the debtor. Accordingly, a party seeking discharge may send a written request for discharge to the holder of the interest at the address stated in the registration.

*(b) Article 44 court order*

If the debtor's Article 25 request is not complied with, the debtor may need to seek a court order directing the beneficiary to procure the discharge of the registration. The court making the order must have jurisdiction under the Convention. If the parties have entered into agreement that the courts of a Contracting State have jurisdiction over the claims, then the debtor may bring the claims in that court. If not, then the debtor may seek the order in a court having jurisdiction pursuant to its rules.

Articles 44(2) and 44(3) permit a debtor to seek an order directing the Registrar to discharge a registration. Under Article 44(1), the courts of the place in which the Registrar has its centre of administration have exclusive jurisdiction to make awards of damages or orders against the Registrar. Section 7 of the International Interests in Mobile Equipment (Cape Town Convention) Act 2005, the legislation implementing the Convention in Irish law, provides that the Irish High Court is the court with jurisdiction in disputes under the Convention.<sup>136</sup> The Registrar must be named as a respondent with respect to any relief affecting registration on the Registry.<sup>137</sup>

<sup>136</sup> The Rules of the Superior Courts were amended by Statutory Instrument No. 31/2008 to allow cases involving the Registrar to be brought in the Commercial Division of the High Court, which was established in 2004 to allow commercial cases to be handled in a more time-efficient manner. Whether an applicant decides to pursue the claim in the more time-efficient but more costly Commercial Court or the regular High Court is a decision to be made by the applicant.

<sup>137</sup> Donal Gallagher, 'Procuring the Discharge of Problem or Improper Registrations on the International

*(ii) Irish Court decisions addressing discharge*

Two recent Irish Court decisions, *PNC Equipment Finance LLC v Aviareto Limited and Link Aviation LLC*<sup>138</sup> and *TransFin-M, Ltd. v Stream Aero Investments S.A. and Aviareto Limited*,<sup>139</sup> provide insight into the process of seeking discharge of another party's registration. These cases demonstrate the willingness of Irish courts to assert jurisdiction over registry disputes even if the litigating parties do not have other connections to the jurisdiction.

In both cases, the courts directed the discharge of purported registrable NCRIs on the basis, among other points, that the countries relevant to the disputes had not made Article 40 declarations. In *PNC*, the two parties, the aircraft, and the lease agreement were all connected to the United States, which has not made any declaration under Article 40. In *Transfin-M*, the holder of the purported registered NCRI was based in Panama, which has not made any Article 40 declaration, and the aircraft was registered in the United Kingdom, which is not a Contracting State.

These cases appear to set a framework for the approach that Irish courts will take in cases of problematic or improper registrations.<sup>140</sup> But the practitioner should note that these cases were not particularly challenging for the courts because the claims were uncontested by the purported interest holders and the registrations were invalid on their face because countries relevant to the disputes had not made Article 40 declarations or were not Contracting States. It remains to be seen how Irish courts would rule in more contentious cases.

Registry – Expediting the Process' (16<sup>th</sup> Annual Global Corporate Aircraft Transactions Forum, New York, 13-14 June 2013) 7 (hereinafter Gallagher).

<sup>138</sup> Unreported, High Court, 19 December 2012.

<sup>139</sup> Unreported, High Court (Commercial Division), 18 April 2013.

<sup>140</sup> Gallagher notes that the Irish courts 'essentially assumed ultimate jurisdiction in matters related to registration on the International Registry.' Gallagher (n 113) 11.



## 6. Conclusion

The Article 39 provisions are fully in accord with the basic objectives and principles stated in the third Preamble paragraph of the Convention which are: ‘The need to ensure that interests in such [mobile] equipment are recognized and protected universally’. This Preamble paragraph ‘goes to the very *raison d’etre* of the Convention, namely to provide a uniform set of rules for the creation, perfection and priority of international interests in such equipment, in order to overcome the serious problems arising from differences among legal regimes on these issues and the inadequacy of the traditional *lex rex sitae* principle when applied to equipment constantly moving from one State to another’.<sup>141</sup> By discussing the historical development of non-consensual rights or interests, the need for legal principles to apply to priority between these interests and international interests formed throughout Convention Contracting States and the policies underlying the economic benefits to be obtained, this article has attempted to support the application and understanding of Article 39 that best meets the foregoing objectives and principles of the Convention.

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<sup>141</sup> Official Commentary, Goode (n 2) para 4.3.