

The Power to Dispose under the Cape Town Convention and Aircraft Protocol

Roy Goode*

An essential ingredient of the constitution of an international interest under the Cape Town Convention on International Interests in Mobile Equipment is that at the time of the agreement the debtor has power to dispose. 'Power to dispose' is wider than right to dispose, covering also situations in which, by exception to the nemo dat rule, the debtor can transfer a greater interest in the equipment than he himself possesses. This article examines the meaning of 'power to dispose' and follows the author's series of Official Commentaries on the Convention and its Protocols in arguing that a necessary implication of the registration provisions under Article 29 of the Convention is that the power to dispose can arise under the Convention itself, not merely under national law.

The 2001 Convention on International Interests in Mobile Equipment (the 'Cape Town Convention' or 'Convention' or 'CTC'), together with its associated Aircraft Protocol (the 'Protocol'), contains a set of uniform rules governing, among other things, the creation, perfection and priority of international interests in aircraft objects. An international interest is an interest granted by a chargor under a security agreement or vested in a person who is the conditional seller under a title reservation agreement or a lessor under a leasing agreement (collectively 'the debtor'). An aircraft object is an airframe, aircraft engine or a helicopter. The Aircraft Protocol extends the Convention, other than the default provisions, to outright sales.¹ The primary method of perfecting an international interest or an outright purchase is by registration in the International Registry, which is based in Dublin, operated by Aviareto Limited (the 'Registrar') and supervised by the Council of the International Civil Aviation Organization (ICAO), which at a later stage joined the initiating organisation, the International Institute for the Unification of Private Law (UNIDROIT) in sponsoring the Cape Town Project.

The conditions for constituting an international interest are prescribed by Article 7 of the Convention and for a sale by Article V of the Protocol.

* Professor Sir Roy Goode QC, Emeritus Professor of Law at the University of Oxford and Emeritus Fellow of St John's College, Oxford. I am indebted to Kenneth Gray for his comments on an earlier draft of this paper. I have accepted Mr Gray's point on the protection of the sub-lessee under Article 29(4) of the Convention – indeed, his position was that taken in my Official Commentary, para 2.166, a point that he was too polite to mention – and have expanded the treatment of power to dispose to reinforce my reasoning, disputed by Mr Gray, that a power to dispose can arise not only under national law but under the Convention.

¹ This is true also of the Space Protocol. By contrast the Luxembourg Protocol, covering railway rolling stock, and the draft mining, agricultural and construction ('MAC') equipment Protocol do not apply to outright sales and merely permit registration of a notice of sale having no Convention effects but designed to give notice of the existence of the sale for the purpose of priority rules under national law.

Article 7 provides as follows:

Article 7 — Formal requirements

An interest is constituted as an international interest under this Convention where the agreement creating or providing for the interest:

- (a) is in writing;
- (b) relates to an object of which the chargor, conditional seller or lessor has power to dispose;
- (c) enables the object to be identified in conformity with the Protocol; and
- (d) in the case of a security agreement, enables the secured obligations to be determined, but without the need to state a sum or maximum sum secured.

Article V is in similar terms except that it states the necessary elements of a contract of sale instead of the constitution of an international interest.

Non-compliance with any of these provisions means that no international interest comes into existence and registration of the purported interest will be of no effect.² Indeed, insofar as such registration casts a shadow on the title of the owner or of another, lawful, registrant it may be actionable. For example, under English law a wrongful registration made maliciously, that is, without an honest belief of entitlement to make it, and causing pecuniary loss to the claimant constitutes the tort of slander of title, attracting a right to damages and, in the case of a Cape Town Convention registration, an order requiring the defendant to procure discharge of the registration. Irish law is similar, and in the absence of an order from a court outside Ireland, and to overcome lacunae in Article 44 of the Convention,³ the Irish High Court has invoked its general jurisdiction rules as regards torts committed in Ireland to make an order *in personam* against the registrant to discharge the registration and then, in exercise of its Convention jurisdiction under Article 44(1), has directed the Registrar to discharge the registration.⁴

The requirements of Article 7 paragraphs (a), (c) and (d) are reasonably clear, but there has been much discussion of the meaning of ‘power to dispose’ under paragraph (b) and it is to this issue that the present article is directed.

I. ‘Dispose’

The word ‘dispose’ has a wide meaning, covering every form of grant of a property interest by the debtor or outright seller, including a sale (whether outright or under reservation of title), a lease, a sub-lease, an assignment of a lease or sub-lease, a charge or sub-charge (whether by a transfer of title under a mortgage or sub-mortgage or by a hypothecation or sub-hypothecation⁵), an assignment of a charge or sub-charge or the delivery of possession under a pledge, contractual lien or other kind of bailment. For this purpose delivery of possession may be actual (direct, physical) or constructive (indirect), for example, by giving control of the contents of a warehouse through possession of the keys or the delivery of possession to a third party who agrees to hold the object to the order of the grantee. But the grant must confer a property interest of some kind; the conferment of a mere contractual right to buy, take a lease, etc, unaccompanied by the delivery of possession is not a disposition.

² Requirements (a), (b) and (d) do not apply to a prospective international interest, as defined in Article 1(y) of the Convention, but since the registry is asset-based it is necessary that the equipment be identifiable in conformity with the Protocol.

³ See Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and Protocol thereto on Matters Specific to Aircraft Equipment* (3rd edn, UNIDROIT 2013) paras 2.226-2.228.

⁴ *Transfin-M v Stream Aero Instruments SA and Aviareto Ltd* 2013 No 112 MCA. See Goode, *Official Commentary* (n 3) para 2.228.

⁵ See the definition of ‘security agreement’ in Article 1(ii) of the CTC read with that of ‘debtor’ in Article 1(j).

The only relevant disposition is one by the debtor or outright seller, but the debtor may also be a creditor, as where a lessee grants a sub-lease or a chargor grants a sub-charge.

II. Power to dispose and right to dispose

The phrase 'power to dispose' includes but is wider than a right to dispose, extending to the legal power to dispose even where there is no right to do so. A power to dispose exists either where there is a right to dispose or where the applicable law or the Convention gives effect to the disposition even though the person making it has no right to do so.

III. Right to dispose

The right to dispose exists where the grantor, whether the debtor or an outright seller, either transfers no greater interest than it has or, if transferring more, obtains the consent of the party or parties whose interests would be affected by the disposition. There are two main cases:

- (1) the debtor or seller is the unencumbered owner, or
- (2) though the debtor or seller is not the unencumbered owner the disposition is made with the consent of the owner and of the holder of any other interest which the disposition, if effective, would override.

Case (1) needs no explanation. Examples of case (2) are dispositions by an agent acting within his actual authority, express or implied; sales by a mortgagee pursuant to a power of sale contained in the mortgage; transfers of a mortgage; and sub-mortgages or sub-charges by a mortgagee or chargee. Further, a right of disposal suspended while the holder has granted an interest to another which is incompatible with exercise of the holder's rights⁶ if not made subject to those rights may be revived by the termination of that interest under the applicable law.⁷ Also within case (2) are dispositions of no greater interest than the grantor has, for example, second and subsequent mortgages or charges by a mortgagor or chargor and assignments or sub-leases by a lessee where not prohibited by the lease.

Examples under the Convention are dispositions by a chargee⁸ who has exercised a right of repossession, sale or grant of a lease under Article 8 (a right which under that Article is dependent on the chargor's agreement), the vesting of ownership in the chargee under Article 9 (which requires the agreement of the debtor as an interested person⁹) and lawful termination of the agreement by a conditional seller or lessor under Article 10 in accordance with an agreement concluded under Article 11. In all these cases the right of disposal is consensual and the disposition does not transfer greater rights than those of the person by whom or on whose behalf it is made.

⁶ As on the grant of a lease, where the lessee has a right of quiet enjoyment against its lessor and any person whose interest was not registered prior to the registration of the lessor's interest (Protocol, Article XVI(1)(a); Convention, Article 29(4)(b)).

⁷ An interesting question arising under English law is the effect on an authorised sub-lease of termination of the head lease. Curiously there appears to have been no reported case on this question, nor is it discussed in textbooks on bailment or personal property. The writer has expressed the view that, subject to any conditions imposed by the lessor on the right to grant a sub-lease this continues in force, the sub-lessee becoming the direct lessee of the lessor on the terms of the sub-lease. See Roy Goode, *Goode on Commercial Law* (Ewan McKendrick ed, 5th edn, Penguin Random House UK 2016 and LexisNexis 2016) para 28.28 and n 50. This conclusion derives support from the decision of the Privy Council in *The Pioneer Container* [1994] 2 AC 324 dealing with the binding effect of a sub-lease on the head lessor. On this basis the lessor's power of disposal would remain in suspense despite termination of the head lease in the absence of conditions attached to the grant of the sub-lease.

⁸ Which under Article 1(ii) includes a mortgagee.

⁹ Article 1(m).

IV. Power to dispose

A power to dispose goes much wider than a right to dispose, covering every case in which, by exception to the *nemo dat* rule,¹⁰ the debtor or seller can confer an interest greater than that which it holds and without the consent of the holder of superior interests. Such an exception may arise either under the applicable law or, by necessary implication, under the Convention as extended by the Protocol.

V. Exceptions to the *nemo dat* rule under the applicable law

Most common law systems while taking the *nemo dat* rule as their starting point, provide exceptions. English law examples include dispositions by: an agent beyond his actual authority but within the scope of his ostensible authority; a non-owner who is held out as the owner by the true owner; a mercantile agent in possession with the consent of the owner;¹¹ a seller who remains in possession with the consent of the buyer;¹² and a buyer who obtains possession with the consent of the owner.¹³ In almost all these cases¹⁴ the effectiveness of the disposition is dependent on its being made to one who takes in good faith and without notice of the prior title. Outside these exceptions the *nemo dat* rule prevails. So a lessee has no power to sell or even to grant a sub-lease where this would be in breach of the leasing agreement. Civil law systems by contrast have a different starting point, adopting the general principle that *en fait de meubles, la possession vaut titre*,¹⁵ pursuant to which a person who is not the owner but holds possession with the consent of the owner can transfer title to one taking possession in good faith. Here the effect of the applicable law is that the person effecting the transfer has a power of disposal within Article 7 of the Convention and this includes power to make an outright sale, grant a mortgage or charge or assign a lease or grant a sub-lease despite a prohibition in the lease agreement.

VI. What is the applicable law?

This question is not answered by the Convention, which leaves the matter to be determined by the domestic rules of private international law of the forum State.¹⁶ Under most legal systems, including English law, the proprietary effects of a dealing in tangible movables are governed by the *lex situs* (*lex rei sitae*), that is, the law of the situation of the asset at the time of the disposition in question.¹⁷

VII. Exceptions to the *nemo dat* rule under the Convention and Protocol

A power to dispose can also arise under the Convention as extended by the Protocol. Under Article 29 of the Convention the first to register an interest acquires priority¹⁸ and this is so even if the registrant of the second, unauthorised, interest took with actual knowledge of the prior unregistered

¹⁰ *Nemo dat quod non habet*, also rendered in civil law jurisdictions as *nemo plus juris ad alium transferre potest quam ipse habet*.

¹¹ Factors Act 1889, s 2(1).

¹² *ibid*, s 7; Sale of Goods Act 1979, s 24.

¹³ Factors Act 1889, s 9; Sale of Goods Act 1979, s 25. See generally Goode, *Goode on Commercial Law* (n 7), chapter 16; Michael Bridge, *The Sale of Goods* (3rd edn 2014), chapter 5.

¹⁴ Mortgages of registered ships and aircraft constitute an exception. See n 21.

¹⁵ See, for example, the French civil code, art 2279.

¹⁶ Article 5(3). This reflects an almost universal rule that conflict of laws issues are to be determined by the *lex fori*, which in this context means its domestic rules, excluding *renvoi*.

¹⁷ For English law, the latest case, concerning the law applicable to an aircraft mortgage, is *Blue Sky One Ltd v Mahan Air, PK Airfinance US Inc v Blue Sky Two Ltd* [2010] EWHC 631 (Comm).

¹⁸ Article 29(1).

interest.¹⁹ Similarly a second buyer from a seller in possession who registers its purchase before registration by the first buyer has priority even if taking with actual knowledge of the prior sale.²⁰ This rule is designed to protect the integrity of the registry system and to avoid factual disputes as to whether a party did or did not have knowledge. In national legal systems such knowledge would almost always make the second disposition ineffective except in the case of successive charges.²¹ It is thus implicit in the registration and priority provisions that a debtor in possession and a seller remaining in possession have power to dispose under the Convention, because otherwise Article 29(2) would be deprived of effect and Article 29(1) would be rendered otiose, at least as regards conditional sale and leasing agreements, since there would be no point in providing a facility for the conditional seller or lessor to register its international interest or the buyer to register its purchase in order to protect its priority.²² Three simple illustrations will demonstrate this.

Illustration 1

Under an agreement governed by English law and falling within the Cape Town Convention A leases an airframe to B, who wrongfully sells the airframe to C. B has no power to make the disposition under English law. A fails to register its international interest. If B were not to be considered to have a power of disposal under the Convention there would be only one international interest, that held by A. In this situation A would have priority over C, not under Article 29(1), which applies only if there is at least one registered interest, but because there is no valid competing interest either under the Convention or under the applicable law. So a conflict between competing international interests, the outcome of which is intended to be determined by Article 29, could never arise and Article 29(1) would be rendered otiose.

Illustration 2

The facts are as Illustration 1 except that B, instead of selling the airframe to C, grants C a sub-lease in breach of the leasing agreement. Again, B has no power under English law to grant the sub-lease, so if it were not to be considered to have a power of disposal under the Convention there would be no point in A registering its international interest as it would have priority anyway, making Article 29(1) redundant.

Illustration 3

A supplies an aircraft engine to B under a conditional sale agreement which reserves title until payment but fails to register the title reservation as an international interest in the International Registry. B wrongfully sells the goods to C who, knowing of A's title, registers the sale in the International Registry. C has priority over A under Article 29(1), and under Article 29(2) this is the case despite C's knowledge of A's prior interest and

¹⁹ Article 29(2).

²⁰ Protocol, Article XIV(1).

²¹ Since the chargor always remains free to deal with his reversionary interest. Moreover, registration systems governing aircraft mortgages may provide priority by registration regardless of actual or constructive notice of an unregistered mortgage. But Article 29 also applies to title reservation and leasing agreements, which in most countries (the US, Canada, New Zealand and Australia being the exceptions) are not registrable, so that a disposition to a third party taking with knowledge of a prior interest will have no effect.

²² See Goode, *Official Commentary* (n 3) para 2.65(4). It may be noted that this conclusion has been widely accepted. It was the position taken in the Official Commentary from the very first edition published in 2002 after extensive consultation with delegations and with the aviation industry, which has endorsed it. See, for example, *Practitioners' Guide to the Cape Town Convention and the Aircraft Protocol* (Legal Advisory Panel of the Aviation Working Group, 2015) 18 <<http://www.awg.aero/assets/docs/VED-Practitioners-Guide-9-9-15.pdf>> accessed 06 February 2018.

despite the fact that such knowledge renders the disposition to C ineffective under the applicable law.

So it is clear that a lessee in possession has a power of disposition under the Convention and if the lessee sells or charges the leased equipment to a third party who registers the sale or charge before the lessor has registered its international interest the third party has priority under Article 29(1) of the Convention. Similarly a sub-lease by the lessee not only creates an international interest in favour of the lessee²³ but also confers rights on the sub-lessee against both the sub-lessor and the head lessor²⁴ even if the sub-lease is in breach of a provision of the lease agreement. Again, a seller who is allowed by its buyer to remain in possession, perhaps for the purpose of remedying minor defects in the aircraft object, retains a power of disposal and if the seller makes a wrongful second sale to another buyer who is the first to register its purchase the second buyer has priority under Article 29(1) as applied to sales by Article III of the Aircraft Protocol.²⁵

There is one exception to this general priority principle, namely that a debtor cannot use the priority rules to impeach its own creditor's title and renounce its obligations under the agreement. So where an aircraft object is supplied under a title reservation agreement and the supplier registers its international interest and then charges the equipment to a third party, the supplier cannot rely on its registration to obtain priority over the chargee. Similarly, a lessee who grants a sub-lease cannot secure priority over his own lessor by registering his interest as sub-lessor before the lessor has effected registration of its own international interest. As the Official Commentary explains,²⁶ for the conditional seller to assert its prior registration would be inconsistent with the security interest it has granted to the chargee, while a lessee's claim to priority over its own lessor by virtue of having registered its international interest before the registration of the lessor's international interest would be inconsistent with its obligations under the lease and a denial of the lessor's title. However, its sub-lessee is protected by Article 29(4) of the Convention and Article XVI(1)(a) of the Protocol. Nevertheless the sub-lessee's position is not necessarily secure because if the head lease is terminated, whether by reason of the lessee's breach of its obligations under the head lease or otherwise, then it may be that its rights under the sub-lease come to an end.²⁷ That is a matter governed not by the Convention or Protocol but by the applicable law.

VIII. Representative capacities

Article VI of the Protocol provides as follows:

Article VI — Representative capacities

A person may enter into an agreement or a sale, and may register an interest in, or a sale, an aircraft object in an agency, trust or other representative capacity. In such case, that person is entitled to assert rights and interests under the Convention.

This provision is to be interpreted broadly as permitting a person acting as trustee to take any action under the Convention, including registration of an assignment or subordination, whether or

²³ Though not one which, on registration, will give him priority over his own lessor. See n 26.

²⁴ Convention, Article 29(4); Protocol, Article XVI(a). But see n 26.

²⁵ Article 29(1) of the Convention applies only where the two interests are in competition. So it has no application to a chain of sales where each buyer acquires its seller's title, which is thus displaced, so that it is usually the last buyer in the chain that acquires title.

²⁶ Goode, *Official Commentary* (n 3) para 2.171.

²⁷ As to the position under English law see n 7.

not covered by the express language.²⁸ This provision is important because the use of security and other trustees is very common in aircraft financing. The trustee may be trustee of the aircraft objects, leases granted by the debtor and other contract rights given in security by the debtor or may instead exercise control of the aircraft object through a special purpose vehicle which is wholly owned by the trustee and which holds title to the aircraft object, the trust being limited to security over the charge itself, any leases and other contract rights and insurances.

A. Dispositions under the Convention by a trustee

In order for Article VI to apply two conditions must be satisfied. First, the trust must have been established, and the trustee appointed, in conformity with the law governing the trust, usually the law expressly or impliedly designated in the trust instrument.²⁹ Secondly, an international interest must have been created, or a sale effected, though it is not necessary that it should have been registered. Where these conditions are satisfied and the interest or sale registered the trustee must, it is thought, be considered to have a power of disposal, a conclusion necessitated by the need to protect reliance on the International Registry. In the absence of registration, however, it is for the *lex situs* at the time of the disposition to determine whether this is effective, for example where the disposition was within the scope of the trustee's apparent authority or by virtue of some other exception to the *nemo dat* rule, as where delivery has taken place in a jurisdiction whose law adopts the *possession vaut titre* principle. Assuming the trustee to have been properly appointed under a valid trust, only the trustee, not the beneficiaries, can register the international interest or sale and exercise default remedies.³⁰

B. Dispositions under the Convention by an agent or other representative

Similar considerations apply to dispositions by an agent or other representative of the creditors.

IX. Disposition of an aircraft engine installed on a helicopter

An international interest can only be constituted and registered in relation to an aircraft object, that is, an airframe, an aircraft engine or a helicopter. There can be no separate registration of a component of one of these objects. An aircraft engine which is uninstalled or is or becomes installed on an airframe is a separate object for the purpose of the Convention and therefore capable of being the subject of an international interest. By contrast a purported disposition of an engine while installed on a helicopter has no Convention effects. This is because, as is clear from Article I(2) of the Protocol, such an engine is merely a component of the helicopter, not an aircraft object.³¹ Article I(2)(a) defines aircraft as 'aircraft as defined for the purposes of the Chicago Convention which are either airframes with aircraft engines installed thereon or helicopters', no reference being made either to helicopter airframes or to helicopter engines, while in the definition of airframes in Article I(2)(e) the reference to installed accessories expressly excludes aircraft engines but there is no such exclusion in the definition of helicopters. The practical solution to this problem is for the creditor to take and register an international interest over the helicopter, which includes the engine as a component, and at the same time to take and register a prospective international interest in the engine which will become

²⁸ Goode, *Official Commentary* (n 3), paras 2.67, 5.33.

²⁹ See the 1985 Convention on the Law Applicable to Trusts and on their Recognition, arts 6-8 (the 'Hague Convention'). The Hague Convention has been ratified by 14 States, including nine civil law jurisdictions, and provides the best guide to the treatment of trusts for the purpose of the Cape Town Convention and Protocol.

³⁰ Goode, *Official Commentary* (n 3) paras 2.67, 5.33.

³¹ Goode, *Official Commentary* (n 3) paras 3.8, 3.10.

a completed interest the moment it leaves the helicopter, registration (and accordingly priority) dating back to the time of registration of the prospective international interest with no requirement of further registration.³²

X. Party having neither a right to dispose nor possession

A party who has neither a *right* to dispose nor actual or constructive possession has no power of disposal under the Convention and any purported grant of an international interest or sale under the Convention will be ineffective unless a power of disposal arises under the applicable law. So a lessee who has not yet taken delivery of an aircraft object and thus has no right *in rem*, merely a contractual right to delivery under the terms of the leasing agreement, has no power of disposal under the Convention, the power remaining with the lessor, while the power of disposal of a seller who delivers possession to the buyer is extinguished. In such cases the power of disposal of a party not in possession depends on the applicable law. For example, under many systems disposal by an agent within the scope of his apparent authority will be effective even if the agent is not in possession, and this power will meet the Convention requirement.

On the other hand, it is not necessary for the aircraft object to have been delivered to the buyer from a lessee in possession or the second buyer from a seller in possession in order to secure priority for the buyer under the first-to-register rule. Delivery of possession may be necessary for an effective disposition under the applicable law, as with some of the exceptions to the *nemo dat* rule under English law described above, but it is not an element of a disposition in exercise of a power to dispose under the Convention.

³² Convention, Articles 16(1)(a), 18(3), 19(4). See Goode, *Official Commentary* (n 3) para 3.10.