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STUDY GROUP FOR THE PREPARATION OF  
UNIFORM RULES ON INTERNATIONAL INTERESTS IN MOBILE EQUIPMENT :  
WORKING GROUP TO CONSIDER THE LEGAL AND TECHNICAL ISSUES  
RAISED BY THE ESTABLISHMENT OF AN INTERNATIONAL REGISTER

*EXPLORATORY REPORT*

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# **AN INTERNATIONAL REGISTRY FOR INTERNATIONAL INTERESTS IN MOBILE EQUIPMENT ;**

## **EXPLORATORY REPORT**

prepared by Professor R.C.C. Cuming  
(University of Saskatchewan)\*

### **I. BACKGROUND**

The Unidroit project to develop a Convention on International Interests in Mobile Equipment originated in a proposal presented in 1988 to the Unidroit Governing Council by the Canadian member of the Council.<sup>1</sup> The Governing Council authorised the preparation of a study of the area in order to permit it to assess the feasibility of the Canadian proposal,<sup>2</sup> and the preparation of a follow-up questionnaire<sup>3</sup> that was sent to equipment suppliers, equipment buyers, equipment financiers and government agencies all over the world. The outcome of the study and the questionnaire was a decision on the part of the Governing Council in May 1991 to set up a restricted exploratory working group to examine the feasibility of the proposed project. The Group, composed of experts in secured financing of large equipment, met in March 1992 and concluded that the project was both useful and feasible.<sup>4</sup> A Study Group was convened and it held its first meeting in March 1993. In 1994 and 1995 a sub-committee of the Study Group held three meetings during which the various issues associated with the proposed Convention were addressed

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\* Significant assistance with matters relating to the registration of interests in aircraft was provided by Mr. J. Wool, Attorney, Norton Rose, Paris, on secondment from Perkins Coie, London Office and Affiliate Professor of Law, University of Washington. However, the author takes full responsibility for the contents of the report.

<sup>1</sup> Reproduced in part in Cuming, "International regulation of aspects of security interests in mobile equipment," (1990-91) *Uniform Law Review* 63-65.

<sup>2</sup> See Unidroit 1989 Study LXXII - Doc. 1, *International regulation of aspects of security interests in mobile equipment: Study*, reproduced in (1990-91) *Uniform Law Review* 63.

<sup>3</sup> See Unidroit 1989 Study LXXII - Doc. 2, *International regulation of aspects of security interests in mobile equipment: Questionnaire*. See also 1991 Doc. 3, *Analysis of the replies to the Questionnaire on an international regulation of aspects of security interests in mobile equipment* (prepared by the Unidroit Secretariat), and 1992 Doc. 4, *Basic issues identified in responses to the Questionnaire* (prepared by R.C.C. Cuming).

<sup>4</sup> See Unidroit 1992 Study LXXII - Doc. 5, *Report of the March 1992 meeting of the Restricted Exploratory Working Group to examine the feasibility of drawing up uniform rules on certain aspects of security interests in mobile equipment*, pp. 2-3, paras. 5-6.

and draft Articles (Appendix A) were considered.<sup>5</sup> At the 1994 meeting the Sub-committee of the Study Group invited Airbus Industrie and the Boeing Company to convene a working group, the Aviation Working Group, to comment on the proposed Convention to the extent that it might affect interests in aircraft. In 1995 the Aviation Working Group submitted a detailed memorandum containing a set of recommendations.<sup>6</sup> Some of the implications of these recommendations are addressed in the body of this report and in Appendix B. The draft Articles as amended along with draft supplementary rules and associated materials relating to aircraft to be prepared by the Aviation Working Group<sup>7</sup> will be presented to the next meeting of the Study Group to be held in April 1996.

The draft Articles provide for an international registry for "interests" in "objects"<sup>8</sup> and specify some of the basic characteristics of the system within which the registry would function.<sup>9</sup> Nevertheless, the Sub-committee decided that it would be necessary to commission a separate study of registration matters and to undertake consultation with potential users of an international registry<sup>10</sup> and governmental regulators responsible for existing registry systems. This exploratory report is the first step in this process.

## II. THE CONTEXT

There exists no precedent for an international registry for interests in mobile equipment. However, several Canadian provinces have established personal property security registry systems having characteristics which are similar although, of course, not identical to those that would be required of a registry system of the kind contemplated by the draft Articles. The Canadian systems

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<sup>5</sup> *Revised proposals for a first set of draft articles of a future Unidroit Convention on International Interests in Mobile Equipment*, Unidroit, 1995, Study LXXII - Doc. 18 and *Study Group for the preparation of uniform rules on international interests in mobile equipment: Sub-committee for the preparation of a first draft*, Unidroit 1995, Study LXXII - Doc. 21 (Summary report of third session, 11-13 October 1995), November 1995, (hereinafter, "the draft Articles").

<sup>6</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, 1995. See also Doc. 21, *supra*, note 5, paras. 10 and 39.

<sup>7</sup> The draft rules and materials relating to interests in aircraft were not available to the author of this report when the report was being prepared.

<sup>8</sup> The Sub-committee decided at its October 1995 meeting to attempt to find a substitute for the terms "interest" and "equipment." See Doc. 21, *supra*, note 5, para. 8. The amended draft Articles refer in Article 4(e) to an "interest in or over an object." However, in this report, the terms "interest" and "equipment" are retained in order to avoid confusion and to maintain the links between the report and prior published documents on this project.

<sup>9</sup> Chapters II and IV.

<sup>10</sup> See Doc. 21, *supra*, note 5, para. 39.

are the most modern of their kind in the world and have been in place long enough (in some provinces at least 10 years) to demonstrate their functionality. The author of this report has had extensive experience with these systems and has drawn on this experience when preparing this report.

The proposals set out in this report are not to be viewed as a prescription of the characteristics of an international registry for interests in mobile equipment. The report has been designed to serve three functions: (i) to describe (principally in the light of the Canadian experience) what is feasible; (ii) to explore the policy choices that must be made when determining the characteristics of the registry system; and (iii) to provide a context within which any special considerations associated with the transactions to which the proposed Convention would apply can be identified and addressed.

### III. CHARACTERISTICS OF THE REGISTRY

#### 1. Introduction

Set out below is a description of the characteristics of a registry system that, in the opinion of the author, could function in the context of the draft Articles. The report does not address technical matters that fall within the expertise of computer systems designers and operators. However, many of the specific proposals set have been implemented in Canada without difficulty. Accordingly, their technical feasibility is not in doubt.

#### 2. An international registry

A few existing international Conventions provide for the registration of rights in specified types of mobile equipment. However, none of them provides for a truly international registry for the rights to which they apply. For example, under the *Geneva Convention on the International Recognition of Rights in Aircraft*, 1948, rights arising under a mortgage, hypothèque or other security device are to be recorded in a public record of the Contracting State in which the aircraft is registered as to nationality.<sup>11</sup> Under the *Geneva Convention on the Registration of Inland Navigation Vessels*, 1965, rights *in rem* in vessels to which the Convention applies are registered in a registry in the State from which the operation of the vessel is habitually directed, the State in which the owner is habitually resident or of which the owner is a national, or, in the case of a corporation, the State in which it has its registered office or principal place of business.<sup>12</sup> Under both Conventions, registration is to be effected in national registries, albeit ones that might have been designed to function specifically in the context of the Conventions.

Rights arising under the proposed Convention would be international in that they would draw life not from the national law of one of the parties or from the law of the *situs* of the

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<sup>11</sup> Article 1(1)(d)(i)-(ii).

<sup>12</sup> Article 3(1).

collateral, but from the Convention itself. Logically, therefore, registration of the rights should be in an international registry established pursuant to the proposed Convention.

There are logistical reasons why an international registry is required. Since the type of property falling within the scope of the proposed Convention is by nature highly mobile and, consequently, has no *situs* that is relevant for registration purposes, third party<sup>13</sup> protection necessitates registration in a location that third parties can be expected to search. They cannot be expected to search national registries throughout the world before acquiring interests in equipment.<sup>14</sup> This is logistically unworkable and commercially unreasonable.

Even if the problem described in the preceding paragraph could be overcome, all difficulties would not be eliminated. In the absence of a single international registry, it would be necessary for all States that are parties to the proposed Convention to establish and maintain national registries that meet the requirements of the Convention and to provide easy and effective (electronic) access to these registries from locations throughout the world. While this may be easily within the capability of some States, this will not be the case universally. The provision of such facilities should not be a pre-requisite to a State becoming a party to the proposed Convention. This would have the effect of unnecessarily limiting the acceptability of it. What is required is a single, international administration that provides registration facilities capable of fulfilling the requirements of the proposed Convention.

An aspect of the structure of the international registry that will have to be given further study is whether or not existing registration facilities can be employed in conjunction with or as part of the international registry. This approach is of particular relevance in the context of registrations affecting interests in aircraft.<sup>15</sup> Almost all States currently have a recording office operated by a civil aviation authority as required by the *Chicago Convention on International Civil Aviation*, 1944 where aircraft are registered as to nationality. Further, States that are party to the *Geneva Convention on the International Recognition of Rights in Aircraft*, 1948 use these offices as registries for interests recognised by that Convention. In addition, some States have central national registry offices for interests in aircraft created under domestic law.<sup>16</sup> Use of

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<sup>13</sup> In this context, "third party" refers to someone, such as a potential buyer of the equipment or a potential chargee, to whom the chargor, buyer or lessee offers the equipment fraudulently representing that he or she has unencumbered ownership of it.

<sup>14</sup> This generalisation would not apply to aircraft that must be registered as to nationality under Articles 17 and 19 of the *Chicago Convention on International Civil Aviation*, 1944. If national "satellite" registries for rights in aircraft were to be established, a third party would know that a search might be made in the registry office of the State in which the aircraft was registered as to nationality.

<sup>15</sup> See Doc. 16, *supra*, note 6, p. 23, para. 9.2. It is important to note that the Aviation Working Group has stressed the point that "[t]he existence and role of the satellite offices would not, however, detract from the concept of a 'central' filing system; a filing, including one made through an eligible satellite office, (would have) continuing force, and (would) remain effective, notwithstanding changes from time-to-time in the physical or legal ... location of the aircraft." *Ibid.*

<sup>16</sup> A recent paper prepared for the Commission of the European Union contains a recommendation that consideration be given to the creation of a European-wide aircraft registry. Should such a registry be established, it



existing facilities as satellite offices for the international registry and access to existing regulatory expertise may minimise disruption to the regulatory systems applicable to aircraft interests while at the same time enhancing the efficacy of the international registry.<sup>17</sup>

The concept of satellite offices need not be confined to the registration of interests in aircraft. It is conceivable that some States will want to establish within their borders one or more satellite offices, which would have electronic access to the data base of the international registry and which any user could visit in order to effect a registration, conduct a search or obtain expert advice (possibly backed by guarantees of accuracy) with respect to registrations and searches. Some States may decide that access to the international registry by their nationals should be available only through such offices. It is also conceivable that business organisations will want to create agencies having as their sole function the provision of registry-related services to members of the organisations. These agencies could make the necessary arrangements with the international registry so as to be able to act as agents for their members in effecting registrations and obtaining search results.

The draft Articles provide that the international registry shall be located in such place and managed by such body as shall be determined from time to time by the Governing Council of the International Institute for the Unification of Private Law (Unidroit).<sup>18</sup> They also provide that the administrative details associated with the functioning of the registry, including the managerial and operational control of it, are to be set out in rules promulgated from time to time by Unidroit.<sup>19</sup> The use of rules rather than provisions in the proposed Convention dealing with the details of the registry and its operations is a very important feature of the proposed structure. The Canadian experience has been that numerous modifications to the rules governing a registry system must be made in order to ensure that the system operates at an optimum level and can meet new needs as they arise. The necessary flexibility would be lost should the details of the operation of the registry be included in the proposed Convention.

### **3. A computerised registration system**

It is inconceivable that the international registry would be other than fully computerised. The cost and inefficiency associated with a manual system dictate this conclusion. All information submitted to the registry would be stored electronically and retrievable from one or more data bases. While registration documents could be submitted to the registry in hard copy format, information contained on the documents would be reconfigured to electronic format and stored in a data base. As noted below, the registry would provide for remote electronic access to the extent

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could constitute a satellite office which would provide exclusive access to the international registry established under the proposed Convention for registrations relating to interests in aircraft.

<sup>17</sup> As to the special role these offices might continue to play in the context of transfers of ownership interests in aircraft, see Appendix B.

<sup>18</sup> Draft Article 5(2). This should not be read as precluding the use of national or regional satellite offices.

<sup>19</sup> *Ibid.*

contemplated by the proposed Convention. Consequently, it would be possible to transmit electronically registration information to the registry data base (i.e. register it) and to retrieve electronically information in it from remote locations. Both functions would be done without administrative involvement by registry personnel.

#### 4. The role of the registrar

The role of the registrar under a system of the kind described in this report would be almost exclusively administrative. The registrar would not be responsible for, or make judgments as to the regularity, validity or even existence of the transaction to which a registration relates.<sup>20</sup> Nor would the registrar have the responsibility to ensure that the parties named in a registration notice are the persons who they purport to be or that the person named as chargor, buyer or lessee in fact has consented to the registration as required by the draft Articles.<sup>21</sup> So long as a tendered registration notice meets the requirement of the registration rules, the registrar would be required to effect the registration. The registrar would not have the power to amend or discharge a registration without the proper formal demand of the appropriate party. Where registration is effected electronically, there would be no opportunity for registrar involvement since the information set out in the electronic registration notice would be automatically entered into the registry data base without any involvement of registry personnel.

#### 5. The languages of the international registry

The international registry would function in the context of a Convention to which a large number of States would be parties. It can be expected that the users of the registry will speak different languages. While there is nothing to preclude the publication of "unofficial" versions of the registry rules in several languages, it is very likely that it will be impractical for the registry to function in all the languages spoken by its users. Consequently, it will be necessary to set the "official languages" of the registry. The Canadian experience has demonstrated that a sophisticated, modern registry system can function effectively in two languages: English and French.

The extent of the language problem is reduced in the context of the information to be included in registration notices (see 7. **Notice registration**, *infra*) by the fact that a great deal of international commercial activity involves the use of "Arabic" numbers and the Latin alphabet. These characters are commonly used to record serial numbers on items of large equipment of the kinds to which the proposed Convention would apply.

Government-operated satellite offices and agencies created by business organisations could have a significant role in ameliorating the problems associated with language. Users of the system

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<sup>20</sup> However, the role of registry officials at satellite offices may be somewhat broader. See discussion of transfers of ownership interests in aircraft in Appendix B.

<sup>21</sup> See draft Articles 14(1) and (2).

who cannot function in one of the official languages of the system should be able to get assistance from a satellite office or business organisation agency.

The draft Articles provide that a registration notice shall include the name of the chargor, buyer or lessee, although this name is to be treated as a registration-search criterion in a very limited context.<sup>22</sup> It is impractical and unreasonable to expect parties to "translate" their names into another language. In any event, there may be no equivalent words in one of the official languages of the registry. Nevertheless, search results<sup>23</sup> must disclose names and addresses. For this to be done, this information in some form would have to be entered into and retrievable from the data base of the registry. It is most unlikely that a computer programme can be developed at acceptable cost that would recognise all the characters of all the languages of users of the system. An acceptable alternative measure would have to be employed.

Under the Canadian systems, a high-volume user (i.e. chargee) may request an identification number. This number takes the place of the name of the user in all registrations in which that user is the chargee. This system could be used in a modified form in the context of the international registry. Users with untranslatable names (and any other user who requests the service) would be assigned an identification number. [In this context, the term "users" includes chargees and chargors, lessors and lessees, sellers and buyers]. When a request for an identification number or identification numbers<sup>24</sup> is made, the requesting party would have to provide the requisite address or addresses in computer recordable form.

Where the relevant search criterion is the serial number of specific items of equipment (i.e. where the person searching is a potential buyer, lessee or chargee), the search would always disclose the existence of a registration based on that serial number as the registration criterion, and the disclosure of identification numbers for chargors, buyers or lessees rather than their names would be a minor inconvenience. The person who obtains the search result would be able to obtain the full name from the registry should this be necessary. Government-operated satellite offices and agencies created by business organisations could provide the necessary assistance to users in obtaining registration numbers and converting addresses into computer-readable form. However, in the limited situations where the chargor's name is the relevant search criterion the use of identification numbers for chargors adds an additional complication. (See 8. The registration-search criteria, *infra*).

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<sup>22</sup> See text accompanying note 32, *infra*.

<sup>23</sup> The term "search result" is used in this report to refer to the information supplied by the registry to a person who has requested a registry search using the appropriate search criterion.

<sup>24</sup> A registering party may be required to obtain a registration number for all parties to the transaction and would be required to provide in computer-readable form the addresses of all such parties.

## 6. Access to the international registry

Rules dealing with registrations and searches of the registry data base would provide that registration documents and search requests could be delivered in hard copy format to the registry using traditional delivery methods such as postal services, courier and facsimile transmission. Search results issued by the registry will be delivered to persons requesting them using the same methods.

Available technology makes it quite possible to allow alternative methods of accessing the registry in order to effect a registration or to search the data base. The experience with the Canadian system demonstrates that remote, electronic access to a public registry entails no insuperable logistical or security problems. Consequently, it is quite possible to design a system that permits users (registering parties and persons wishing to search the registry) to have direct electronic access to the data base without any administrative intervention by registry officials. However, it is very likely that direct access would be attractive only to frequent users of the system since it must be preceded by arrangements for the payment of fees and entails special measures (e.g. secret user-identification methods) to ensure the integrity of the data in the system.

Infrequent users may wish to have the benefits of electronic access to the registry and at the same time welcome the intervention of administrative personnel who have the necessary expertise to provide guidance in effecting registrations or conducting searches. As noted above, the full range of registry-related services could be provided to such users through government-operated satellite offices or agencies established by business organisations.

Security concerns must be addressed under a system that provides for remote electronic access to the data base, particularly if that access is available other than through a government-run registry office. These concerns relate to the possibility that an unauthorised person may gain access to the data base and discharge or amend registrations or effect registrations that have no legal basis.<sup>25</sup> Again the Canadian experience is instructive. Under some of the Canadian systems, electronic access to the data base is limited to persons who have been issued with special identification numbers.<sup>26</sup> In order to ensure that these identification numbers do not readily get into the hands of unauthorised persons, arrangements are made to have the numbers automatically changed at frequent intervals (e.g. daily). In addition, verification notices are used in Canada as a back-up security measure. (See 13. **Registration verification**, *infra*.)

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<sup>25</sup> Of course, it is not possible to design a registry system, whether electronic or manual, that completely eliminates the possibility of fraudulent conduct on the part of unauthorised persons. Where registrations, amendments or discharges are in hard copy form, there is no way a registrar can be assured that the documents presented for registration have been authorised by a person with requisite legal authority. A signature or corporate seal guarantees nothing since it can be replicated and placed on documents without authority. Advances in technology used in the reproduction of printed materials have made it almost impossible to distinguish an original from a copy of a document.

<sup>26</sup> These identification numbers are separate from the identification numbers referred to in 5. **The Languages of the International Registry**.

## 7. Notice registration

Modern computerised registry systems generally provide for notice registration and not agreement filing. What is submitted to the registry, either in hard copy or electronic format, is a notice in a form prescribed by regulations (referred to in the draft Articles as a "registration notice"<sup>27</sup>) that sets out basic information relating to the transactions to which it relates. The written documents used in the transaction are not delivered to the registry. The draft Articles provide for this approach to registration.<sup>28</sup>

The principal reason why notice registration must be used is that document filing precludes effective use of a computerised data base. Agreements to which the proposed Convention would apply (security agreements, title retention agreements and leases) can be extensive and the cost of data entry, storage and retrieval of large numbers of these documents would be prohibitive.<sup>29</sup>

Document registration is not a necessary feature of an effective registry system. The most important aspects of the information set out in a registration notice (and, consequently, included in the registry data base) are the identity and location of the registering party (chargee, title retention seller or lessor), the identity and location of the chargor, buyer or lessee, the type of transaction to which the registration relates and a description of the subject-matter of the transaction. Other terms of the agreement between the parties need not be stored in the data base and disclosed in a search result. If it is important to a person who obtains a search result to determine what these terms are, it can obtain this information directly from the registering party or through the chargor, buyer or lessee. The registry would contain sufficient information as to the existence and nature of a registered interest to permit the person who obtains a search result to take the steps necessary to avoid loss when dealing with the chargor, buyer or lessee in possession of the equipment. At the same time a significant level of confidentiality would be maintained since details of the contractual relationships between the parties (e.g. interest and leasing rates)<sup>30</sup> would not be disclosed unless one of the parties to the transaction was prepared to have it disclosed.

## 8. The registration-search criteria

All computer programmes that operate in conjunction with electronic data bases are designed to focus on categories of information when storing and retrieving information. These are often referred to in the Canadian systems as registration-search criteria. Canadian personal property registries use two registration-search criteria: the debtor's name and an item description

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<sup>27</sup> Draft Article 14(2).

<sup>28</sup> *Ibid.*

<sup>29</sup> However, see Appendix B as to the possibility of including registrations of ownership transfer and assignments of leases of aircraft and the role that government satellite offices might play as repositories of hard copy documents relating to ownership transfers.

<sup>30</sup> This feature of the proposed system should appeal to parties to transactions who often go to great lengths to seek the omission of confidential financing terms from publicly registered transaction documents.

of the collateral (required where the collateral is in a list of kinds of collateral that can be reliably described by a serial number or an equivalent). Registered information in the data bases can be retrieved through the use of either the chargor's name or a description of the collateral as the search criterion. Each registration-search criterion has its own advantages.

Systems that employ the chargor's name as the relevant registration-search criterion are generally ones that accommodate security interests in collateral that cannot practically be described on an itemised basis. For example, where the collateral is inventory or accounts separate itemisation is not feasible both because of the large number of separate items of collateral that are likely to be involved and because the security interest is likely to extend to collateral to be acquired by the chargor at a time after registration.

Where a unique collateral identifier can be used as a registration-search criterion, the registry can be more effective than it can where the chargor's name is the only registration-search criterion. The problem with a chargor name registration-search system is that it does not give protection to a third party who is not in a position to obtain a search of the registry based on the chargor's name because the existence or identity of the chargor is unknown to that person. This problem is demonstrated in the following scenario. B gives a security interest in collateral to A who registers a registration notice in a registry system under which B's name is the requisite registration-search criterion. In violation of the security agreement, B sells the machine to C who then offers it for sale to D. D is unaware of the identity or existence of either A or B. Before purchasing the collateral, D searches the registry using C's name as the search criterion. This search does not disclose A's registration since it is indexed under B's name and recoverable only by using B's name as the search criterion. If on the strength of this search D then buys the collateral, he acquires it subject to A's security interest. The only realistic solution to this problem is to provide D with a search criterion that will permit him to discover A's registration. If a unique collateral identifier, such as the serial number of the machine, were to be used as a registration criterion (i.e. included on A's registration notice), it would be available to D as an effective search criterion the use of which would disclose A's registration.

The proposed Convention would apply to rights in specified kinds of equipment, items of which can be separately identified by serial number or an equivalent identifier.<sup>31</sup> There is no provision in the proposed Convention for registration of rights in movable property that is not identifiable at the date the registration is effected. Consequently, for the most part, there is no need to use the chargor's, buyer's or lessee's name as a registration-search criterion. However, the Sub-committee of the Study Group decided that it was possible to envisage "a separate debtor-based register as an alternative means of perfecting an international interest against the debtor's trustee in bankruptcy and unsecured creditors. Entry in such a registry would, however, not affect other types of third parties such as buyers and subsequent secured creditors."<sup>32</sup> The draft Articles make provision for the use of chargors', buyers' or lessees' names as registration-search criteria in

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<sup>31</sup> Draft Article 2(1) and Doc. 21, *supra*, note 5, para. 9.

<sup>32</sup> *Ibid.*, para. 14.

this limited context.<sup>33</sup> If, as suggested earlier in this report, it proves necessary to use chargor, buyer or lessee identification numbers to address the problem of differences in the languages of the users of the system, an additional feature will have to be added to the registry. This feature would involve a separate index of these names and the number allocated to each of them. When a search is requested by a creditor or trustee on the basis of a name, it will be necessary for the registry to obtain from the name index the number corresponding to the name. This number would then be used as the search criterion in the general data base of the registry. As a result, searches using the chargor's, buyer's or lessee's name would involve two steps. While the second step would be automated, allowing remote, direct access searching, it remains to be seen whether or not the same approach can be used in connection with the first step.

## **9. Duration of registration**

Older, paper-based registry systems limit the duration of registrations to set periods of time. These periods are generally between three and five years. Consequently, registering parties must make sure to renew their registrations if the agreements to which those registrations relate extend beyond the prescribed registration period. The reason for placing limits on the time registrations are effective (and, consequently, exposing registering parties to the considerable risk of loss of legal rights by failure to renew their registrations) is to respond to the need to ensure that the system does not retain registrations that are not related to extant agreements. It is often difficult to persuade registering parties to discharge registrations once the agreements to which they relate have been performed. This is particularly so where a discharge fee must be paid. The cost of storage of hard copy registration documents can be very significant and further dealings with the property to which the registration relates can be hampered if registrations relating to the property are unnecessarily maintained.

The Canadian registry systems do not set arbitrary periods for the effectiveness of registrations. The registering party is given the right to choose the period of time for which it wants its registration to be effective. Any period of registration in multiples of one year up to 25 years or infinity can be selected. The registration automatically expires (and is deleted from the data base) upon the expiry of the period selected by the registering party unless, prior thereto, the registration has been renewed. The problem of undischarged, irrelevant registrations is addressed in Canada by measures designed to encourage registering parties to discharge their registrations voluntarily. These measures include allowing discharge without a registry fee and providing a computer-generated form (sent to the registering party along with the verification notice described below) that can be used to discharge the registration. As a result most costs associated with discharge are eliminated including the clerical cost of preparing a discharge notice. These measures have worked very well and undischarged, irrelevant registrations create few problems.<sup>34</sup>

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<sup>33</sup> Draft Article 5(3)(b).

<sup>34</sup> In addition, most of the Canadian systems give to the person named as chargor in a registration that does not relate to an extant security agreement the power to force the discharge of the registration without having to invoke court proceedings.

Since the international registry is to be computerised, it is quite possible to employ the Canadian approach and avoid the necessity to have a set duration for registrations. The Subcommittee of the Study Group concluded that the duration of a registration was a matter to be left to the parties.<sup>35</sup> This decision is reflected in the draft Articles.<sup>36</sup>

#### 10. Effecting a registration

If the international registry were to permit direct, remote, electronic access to the registry data base, a registration would be effected as soon as it was transmitted to and accepted by the data base programme of the registry. However, where other methods are used to deliver a registration notice to the registry, different considerations are involved. If, for example, the registering party were to deliver a registration notice (in proper form) to the registry by mail, facsimile or courier, registry clerks would have to key edit the information set out in the registration notice. Only then would it be entered into the data base.

A practical question arises as to whether the registration is to be treated as being effected when the registration notice is received by the registry or when it is searchable (i.e. after it has been key edited and entered into the data base). If it is treated as being registered when it is received by the registry, there will be a period of time between the date of receipt and the date of entry into the data base during which the registration is deemed to exist but during which it is not searchable. Under this approach, the risk of loss resulting from the delay in entry of the registration information would be borne by persons who rely on information disclosed in search results issued by the registry. These people must accommodate the possibility that the search results they obtain from the registry do not disclose registrations that legally exist. This risk can be reduced somewhat by including on search results the date after which undisclosed registrations may exist.

The alternative approach ( i.e. registrations must be searchable to be effective) places the risk of loss associated with delay in entry of registration information into the data base on the registering party. The registering party can control this risk by refusing to advance credit or release possession of sold or leased goods until a search result is obtained demonstrating that the registration has been effected.

If the international registry is very efficiently operated, it should not matter a great deal which approach is used since the period between receipt of registration data and entry of that data will be short. The result would be that the risk involved would be so small that it could be allocated to the registering party or the person searching the registry without much concern to either of them.

Most of the Canadian systems initially employed the former approach since remote access to the data bases was not permitted and, in all cases, registration notices had to be delivered

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<sup>35</sup> Doc. 21, *supra*, note 5, para. 27.

<sup>36</sup> Draft Article 14(4).



physically to the registries. Search results issued by the registries stated the date (referred to as the "currency date") after which undisclosed registration could have existed. Most of these systems have switched to the latter approach. There are two reasons for the change. The first is that, when a person searching the registry can safely assume that a search result displays all existing registrable claims against property, subsequent transactions involving the property need not be delayed. Under the former approach completion of such transactions would generally be delayed until expiry of the period between the date of the transaction and the currency date on the search result. The second reason is that the great bulk of registrations are now effected through electronic transmission of registration data with the result that, as soon as these registrations are effected, they are searchable. This being the case, persons who obtain search results generally assume that all registrations are disclosed and are less likely to appreciate the significance of a currency date set out on the search result. It was considered to be commercially unacceptable to subject business activity to a small, but, nevertheless, significant risk that an undisclosed registration might exist. Registering parties who want to avoid the risk of delay in the entry of registration information they provide to the registry can go to a government-operated regional registry office or private service provider and register using the electronic access system.

The draft Articles do not clearly opt for one or the other of the approaches noted above. They provide that registration takes effect when a registration notice is received by the international registry and a registration number and date are assigned.<sup>37</sup> If the registration number, date and time are assigned automatically by the computer programme, registration is effected when the data are entered into the data base and become searchable. If the registration number, date and time are manually assigned by a registration clerk immediately upon receipt of the registration notice, the registration is effected at that point even though it may not be searchable for hours or days later.

There are two related but separate issues. The first of these is whether or not there should be a period of temporary, deemed registration following upon the execution of an agreement or the delivery of equipment to a chargor, buyer or lessee. Under the Canadian systems, a chargee who has provided money or credit to the chargor to acquire the collateral is given a 15-day "grace period," starting when the chargor obtains possession of the collateral, within which to effect a registration. If the security interest is registered within this period, it is deemed to have been registered from the date of execution of the security agreement.

There is good evidence to indicate that the concept of a "grace period" originated at a time when communication with registries was slow and it was thought impractical to require a chargee who takes a security interest in newly-acquired collateral to effect a registration before the chargor obtains possession of the collateral. However, where remote, instantaneous access to the registry is possible, as it is in most Canadian provinces (and as it could well be under the proposed Convention), it is doubtful whether there is any justification for a grace period. The obvious problem with a grace period is that the convenience given to the registering party comes at the expense of persons who obtain search results and rely on the information they contain. This has been recognised, at least in part, in Canadian legislation which provides that deemed registration

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<sup>37</sup> Draft Article 14(3) and Doc. 21, *supra*, note 5, para. 23.

gives the chargee priority with respect to other chargees and unsecured creditors, but not over good faith buyers of the collateral. The result is that such buyers can rely completely on the information provided in search results issued by the registry and need not be concerned lest they might acquire the collateral subject to an extant, but not searchable, security interest. There is no provision in the draft Articles for grace periods.

The second related issue is whether the system should allow a registration to be effected by a registering party before the agreement to which the registration relates has been executed. The Canadian systems expressly permit pre-agreement registration. As a result, a chargee can effect a registration in relation to a possible future transaction and, when the transaction is concluded, immediately release the collateral to the chargor, or in the case of a secured loan, the funds to the chargor, since the chargee has by that time a valid registration and an established priority position.

The draft Articles do not permit pre-agreement registration, however, they do not require that the chargor under a security agreement have an *in rem* interest in the equipment before a registration in relation to the agreement can be effected. If a security agreement, leasing agreement or title reservation agreement provides that the chargor, lessor or seller will acquire rights in the subject-matter of the agreement at a future time, a registration notice may be registered and the priority of the interest dates from the date of registration and not from the date the interest arises.<sup>38</sup> This feature is of particular importance in the context of situations in which chargees are providing loan credit to chargors. A secured lender may not be willing to release loan funds to the chargor until it is satisfied that a registration notice relating to its secured loan transaction with the chargor is registered and its priority status is established. A chargor will not be able to acquire an *in rem* interest in the equipment until the funds are released.

## 11. The role of notice and knowledge

While the draft Articles do not so provide, it is clear that deemed or constructive notice would not play a role in the priority structure of the proposed Convention. The priority position of an interest that is registered in the international registry would arise from the fact of registration, not from the assumption that the holder of a subsequent interest in the same equipment has notice of the interest as a result of the registration. Under the priority rules of the draft Articles, the lack of knowledge of the existence of a prior unregistered interest is not a pre-requisite to priority. A registering party which is first to effect a registration is given priority over a prior unregistered interest of which it has full knowledge.<sup>39</sup> The same approach is applied to the position of buyers of equipment. A buyer of equipment takes free from an unregistered international interest even though the buyer is aware that the equipment being purchased is subject to that interest.<sup>40</sup> While this approach would appear to reward conduct that falls below acceptable levels of commercial morality, it can be justified in the context of modern commercial law regimes and accepted business practices. These regimes have been designed to increase legal predictability. This policy

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<sup>38</sup> Draft Articles 4(b), 6, 17 and 19(5).

<sup>39</sup> Draft Article 19(2) and Doc. 21, *supra*, note 5, para. 33.

<sup>40</sup> Draft Article 19(3) and Doc. 21, *supra*, note 5, para. 34.

objective can be frustrated if the outcome of a priority competition between a prior unregistered interest and a subsequent, competing, registered interest held by a business corporation is dependent upon difficult findings of fact such as the state of knowledge of the relevant officers of the business corporation.

There is one situation in which a priority status depends upon the knowledge of the party claiming priority. This is where future advances are involved.<sup>41</sup> It is clear that in this situation what is contemplated is actual knowledge and not deemed or constructive notice resulting from registration.<sup>42</sup>

## 12. Errors in registration information

It is inevitable that at least a few registering parties will make mistakes when entering information that is required to be included on registration notices. The legal significance of such mistakes will be conditioned by the type of information to which the mistakes relate. A mistake in recording information that constitutes the prescribed registration-search criterion (i.e. the serial number of the equipment) can be expected to have greater significance than a mistake in recording the address of the chargor. The reason for this is that a mistake in recording the serial number of the equipment may have the effect of rendering the registration unretrievable by a person who obtained a search result using the correct serial number of the equipment as its search criterion. An error in the address of the chargor will not have this effect.

The Canadian experience has demonstrated, however, that an error in recording a registration criterion on a registration notice need not automatically invalidate a registration since it need not preclude retrieval of the registration when an error-free search criterion is used. In Canada, computer programmes are used which are capable of retrieving registrations involving registration criteria that "closely match" the search criteria used in searches. The result is that the person requesting the search will be informed that, while there are no registrations having registration criteria that exactly match the search criterion used, there are one or more other identified registrations having registration criteria that are "close matches." The number and kinds of registrations that are disclosed as "close matches" vary depending upon the computer programme used by the registry.

The Canadian approach can be seen as having been adopted by the draft Articles which provide that the validity of a registration is not affected by an irregularity in the registration notice unless the irregularity is seriously misleading.<sup>43</sup> The information that is disclosed to the person who obtains the search result may be such that the person cannot reasonably be seen as having been seriously misled by the error in the registration criterion since the registration was disclosed as one of the "close matches." The draft Articles make it clear that the test to be applied is

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<sup>41</sup> See draft Article 19(1) and Doc. 21, *supra*, note 5, para. 32.

<sup>42</sup> *Ibid.*

<sup>43</sup> Draft Article 14(5) and Doc. 21, *supra*, note 5, para. 24.

objective, not subjective. They provide that an irregularity may be seriously misleading whether or not anyone is actually misled by it.<sup>44</sup> An objective test ensures that all persons who obtain search results from the registry are treated in the same way and that priorities are not determined on the basis of the subjective knowledge of such a person. Endemic to a subjective test is the potential for circular priority problems. If A's defective registration is effective against B because B was aware of the existence of A's interest but ineffective against C because he was not, a circular priority problem arises if both B and C have registered interests. A has priority over B but not over C; B has priority over C because its interest was registered before that of C, but C has priority over A.

### 13. Registration verification

Registration verification is a feature of most Canadian registry systems that should be considered for the international registry. Under the Canadian systems, when a registration is effected, modified or discharged, a verification notice is printed automatically by the computerised system and sent to the registering party. The verification notice sent when a registration is effected replicates exactly the information that has been recorded in the data base of the registry. The verification notice gives the registering party the opportunity to compare the information in the registry data base with the information the registering party intended to have registered when it transmitted its registration notice. This comparison allows the registering party to identify errors on its part or on the part of the registry and to avoid potential future complications from these errors by having them expeditiously corrected. However, under Canadian law, the registering party who receives a verification notice is not estopped from later claiming compensation from the registry for errors in the registration caused by the registry but disclosed in the verification notice.

It is quite possible to extend the Canadian approach to provide that registration verification notices be sent not only to registering parties but as well to the chargors, buyers or lessees, as the case may be, identified in registrations. Under most Canadian systems the obligation to inform chargors of registrations affecting their property is placed on the chargee and not on the registry. This is simply an economy measure and not a necessary feature of the systems.

Verification notices can play an important role as anti-fraud measures. Under the Canadian systems, when a registration is modified or discharged, the registering party is informed of this by a verification notice. If the modification or discharge was not authorised by the person legally entitled to do so, this fact can be brought to the attention of the registrar and the registration will be restored. Some of the Canadian Personal Property Security Acts provide that, if a discharged registration is restored within 30 days from the date of a discharge, the priority status of the registration is also restored except as against interests that were acquired during the period between discharge and restoration.<sup>45</sup>

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<sup>44</sup> *Ibid.*

<sup>45</sup> For a brief discussion of a possible role for verification notices in the registration of ownership transfers, see Appendix B.

#### 14. Amending a registration

The draft Articles provide for amendment to a registration by transmission or delivery of a registration amendment notice.<sup>46</sup> (As to what constitutes registration, see 10. **Effecting a registration**, *supra*). The draft Articles also provide that an amendment to a registration can have only prospective effect.<sup>47</sup>

#### 15. Court jurisdiction over the registry

A very important question that must be addressed in the context of the international registry is: which court or courts, if any, have jurisdiction over the registry? The Canadian experience demonstrates that there are two categories of situations in which courts are likely to be called upon to deal with matters directly or indirectly related to a registry. The first category is comprised of situations where the issue before the court involves a priority competition between competing claimants; and the second is comprised of situations in which the court is asked to issue an order binding on the registrar.

By far the greatest number of cases arising under Canadian systems have involved the question whether or not the registration requirements have been met and, if not, what are the priority consequences of non-compliance. These cases fall into the first category noted above. Under the Canadian systems, the registrar plays no role in assessing the adequacy of information contained in a registration statement that is tendered for registration. So long as the registration document appears on its face to comply with the registration regulations, the registration is effected. Consequently, the issue of adequacy arises when a competing interest holder claims that a prior registration is invalid as a result of the inadequacy of the information set out in the registration document (e.g. the chargor's name or the serial number of the collateral has not been properly recorded).

The initial determination in any case involving the issue of validity of a registration is the interpretation to be placed on the wording of the relevant legislation and registry regulations. Consistency is important in this context. Clearly, a registry system cannot function properly where there are inconsistent interpretations of the registration requirements of that system since these requirements are directly related to the priority status of the interests involved. Every person who uses the system should be subject to the same requirements and should be able to determine what those requirements are. Once the meaning of the applicable legislative provision or registration regulation is established, the next question is whether or not there has been compliance in a particular case. Complete consistency is less of a concern at this level, although it would be anomalous if, on substantially identical facts, litigants in different courts obtained differing results.

The second category of issues are those in which a court order is directed to the registrar. In a Canadian context, this would involve cases where a registration is no longer valid for one

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<sup>46</sup> Draft Article 15(1)(a) and Doc. 21, *supra*, note 5, para. 25.

<sup>47</sup> Draft Article 15(2).

reason or another. The most common reason will be that the security interest has ceased to exist since the obligation it secured has been performed or otherwise discharged. There will also be cases in which the registrar has refused to register a registration statement on the ground of non-compliance with the registration requirements and the registering party, contending that there has been compliance, seeks a court order requiring the registration. Clearly, it is not desirable in any of these situations to have two or more judicial rulings ordering the registrar to do inconsistent things.<sup>48</sup>

The above-noted considerations are not unique to the Canadian systems. They must be addressed as well in the context of the international registry.<sup>49</sup> Solutions are easily identified where a national registry is involved since it is possible to specify in that context the court or courts that have jurisdiction in the matters. Conflicting rulings are addressed through appeals. Where an international Convention and international registry are involved, the solutions are not as obvious.

This matter was examined by the Sub-committee of the Study Group at the October 1995 meeting. Five approaches were identified: (i) to provide for a choice of jurisdiction rule in the proposed Convention under which national courts having jurisdiction can be identified; (ii) to create a special international tribunal which has exclusive jurisdiction; (iii) to make no provision for jurisdiction and leave the matter to national courts which would have only *in personam* jurisdiction over the litigants but no power to issue orders binding on anyone else or orders affecting the registry which the registrar would be required to obey; (iv) to leave the matter of jurisdiction to agreement between the parties to a security agreement, title retention agreement or lease that they will submit themselves to the jurisdiction of a particular forum for the purposes of issues relating to registration; and (v) to give to the registrar the power to make decisions in the light of all the circumstances, in particular any *in personam* court orders that may have been made.<sup>50</sup>

## 16. Liability for errors or omissions in the operation of the registry

Designers of the Canadian systems concluded that if the law is to force secured parties to register their interests in order to protect their priority positions and if it is to induce persons to rely on the registry system when assessing the legal risk involved in business transactions, the registry systems must be reliable. Registering parties must be guaranteed that, if they comply with registration requirements, their interests will be promptly and accurately registered. Persons who obtain search results from the registry must be guaranteed that the information disclosed on search

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<sup>48</sup> A third category of situation in which court involvement would be sought would be where a claim was made against the registrar for errors or omissions in the operation of the system. (See *infra*, 16. Liability for errors or omissions in the operation of the registry.)

<sup>49</sup> In addition, court jurisdiction over the registry would be invoked in a situation where it was claimed that the registration was invalid because it was not authorised by the putative chargor as required by draft Article 14(1)(b). See also Doc. 21, *supra*, note 5, para. 22.

<sup>50</sup> See Doc. 21, *supra*, note 5, para. 27.

results is accurate in that it is identical to the information submitted by registering parties. Consequently, all the Canadian Personal Property Security Acts give a statutory right of compensation for loss suffered by a chargee whose interest has not been registered, or not registered properly as required by law and for loss suffered by a person who obtained search results from the registry that are inaccurate or misleading as a result of an error in the operation of the registry system. Some provinces place upper limits on the amount of damages recoverable by aggrieved users; however, these limits are generally adequate to cover most cases of loss.

A guarantee of the proper operation of a registry is not a *sine qua non* of the existence of the registry. It is possible to have a registry system that places all risk of loss resulting from failures in the system on its users, thus requiring the users to self-insure or purchase insurance against this risk. If the reliability of the registry is very high with the result that the risk of loss to users of it is very low, the lack of a guarantee of its proper operation is not an important consideration to users. The experience in Canada is that losses have been so infrequent that it is very likely that the statutory guarantees could be eliminated without a significant diminution in public support for the systems. By the same token, the fact that the losses are so infrequent means that generous guarantees can be offered by the governments that operate the systems since the chances that they will be called upon to compensate any significant number of users are very small.

A decision will have to be made as to whether or not it is necessary or feasible to provide guarantees to users of the international registry similar to those provided under the Canadian legislation.<sup>51</sup> If guarantees are to be provided, it will be necessary to identify a source of funds that will be used to pay losses or to purchase insurance against loss (assuming that private insurers are prepared to carry the risk). If the international registry is to provide the guarantee and if insurance principles are applied, each user of the system would bear the cost of the insurance by paying as part of the registration fee or searching fee an amount that represents the appropriate premium to cover the potential loss to that user resulting from an error or omission in the operation of the system. This would result in a graduated fee structure. If the registry is not to be the vehicle for providing the insurance, each user would purchase its own insurance or would self-insure.

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<sup>51</sup> *Ibid.*, para. 29





## APPENDIX A

### *FIRST SET OF DRAFT ARTICLES OF A FUTURE UNIDROIT CONVENTION ON INTERNATIONAL INTERESTS IN MOBILE EQUIPMENT*

(established by the Drafting Group on 19 December 1995  
pursuant to the decisions taken by the Sub-committee at its third session) <sup>1</sup>

#### CHAPTER I

#### SPHERE OF APPLICATION AND GENERAL PROVISIONS

##### *Article 1*

1. – This Convention provides for the creation and effects of an international interest in mobile equipment. The international interest shall be of an autonomous character and shall have effect throughout the territories of Contracting States.

2. – For the purposes of this Convention an international interest in mobile equipment is an interest in an object of a kind listed in Article 2:

- (a) granted by a chargor under a security agreement;
- (b) retained by a seller under a title reservation agreement; or
- (c) retained by a lessor under a leasing agreement.

##### *Article 2*

1. – This Convention applies in relation to objects of any of the following kinds:

- (a) aircraft;
- (b) aircraft engines;
- (c) [ registered ships ];
- (d) oil rigs not intended to be permanently immobilised;
- (e) containers [ with a cubic capacity of not less than x ];
- (f) railway rolling stock;
- (g) satellites;
- (h) [ other? ].

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<sup>1</sup> The use of an asterisk (\*) against a particular provision indicates that the provision in question is envisaged as part of the Final Clauses of the future Convention.

\* 2. – [ Add provision for amendment from time to time of list set out in Article 2 (1) by designated procedure pursuant to Article X ]

### *Article 3*

[ Add provision on connection to a Contracting State]

### *Article 4*

In this Convention:

- (a) "international interest" means an interest to which Article 1 applies;
- (b) "prospective international interest" means an interest that will come into existence as an international interest upon the chargor, seller or lessor acquiring rights in the object to which the agreement providing for the interest relates;
- (c) "object" means an object of a kind listed in Article 2 (1);
- (d) "agreement" means a security agreement, a title reservation agreement or a leasing agreement;
- (e) "security agreement" means an agreement by which one person ("the chargor") grants to another person ("the chargee") an interest ("security interest") in or over an object to secure the performance of an existing or future obligation;
- (f) "title reservation agreement" means an agreement by which one person ("the seller") agrees to sell an object to another person ("the buyer") on terms that ownership does not pass until performance of the buyer's obligations;
- (g) "leasing agreement" means an agreement by which one person ("the lessor") leases an object (with or without an option to purchase) to another person ("the lessee") for a period of not less than [ three ] years;
- (h) "Rules" means rules laid down by the body referred to in Article 5 (2);
- (i) "registered" means registered in the international register against the object or objects to which the agreement providing for an international interest relates [or, for the purpose only of Article 19 (4), registered either against such object or objects or against the name of the chargor, buyer or lessee];
- (j) "unregistered" means not registered as stated in the preceding subparagraph;
- (k) "registrar" means the registrar of the International Registry;
- (l) "registration notice" means the notice in writing referred to in Article 14 (2);
- (m) "registration amendment notice" means the notice in writing referred to in Article 15 (1);

(n) "registration discharge notice" means the notice in writing referred to in Article 15 (3);

(o) "writing" means an authenticated record of information (including information sent by teletransmission) which is in tangible form.

## CHAPTER II

### THE INTERNATIONAL REGISTER

#### *Article 5*

1. - An international register shall be established for the purpose of registering international interests in conformity with this Convention.

2. - The international register shall be located in such place or places and managed by the registrar under the direction of such body as shall be determined from time to time by the Governing Council of the International Institute for the Unification of Private Law (Unidroit) and shall be operated in accordance with the Rules.

3. - The international register shall be arranged so as to accommodate:

[ (a) ] registration by reference to the serial number or other identification mark of the object to which the international interest relates [; and

(b) for the purpose only of Article 19 (4), registration by reference to the name of the chargor, buyer or lessee of the object ].

4. - [ Other provisions to be inserted ].

## CHAPTER III

### CONDITIONS FOR THE APPLICATION OF CHAPTERS IV - VII

#### *Article 6*

Subject to the provisions of Article 17, Chapters IV to VII of this Convention apply in relation to an international interest only where the agreement providing for the interest:

- (a) is in writing;
- (b) relates to an object in which the chargor, seller or lessor has rights;
- (c) describes the object in a manner sufficient to enable it to be identified;
- (d) in the case of a security agreement, states the obligations secured.

## CHAPTER IV

### EFFECTS OF AN AGREEMENT FOR AN INTERNATIONAL INTEREST AS BETWEEN THE PARTIES

#### *Article 7*

##### *[ Alternative I*

1. – This Chapter applies to an agreement only where the parties have so agreed in writing, whether in the agreement or otherwise.

##### *Alternative II*

1. – The parties may agree in writing to exclude, wholly or in part, any right or remedy conferred on the chargee, seller or lessor by this Chapter.

\* 2. – ] This Chapter has effect subject to the provisions of the Unidroit Convention on International Financial Leasing where applicable.

#### *Article 8*

The parties may provide in their agreement as to what constitutes default giving rise to the remedies specified in Articles 9 to 11.

#### *Article 9*

1. – In the event of default by the chargor under a security agreement, the chargee may:

- (a) obtain a court order for sale of any object charged to it and payment of the proceeds to the chargee, or otherwise obtain the proceeds and other benefits of realisation of the object;
- (b) take possession of any such object; or
- (c) sell or grant a lease of any such object on reasonable terms.

2. – At any time after default by the chargor, the parties may agree or the court may on the application of the chargee order that ownership of any object charged to it shall vest in the chargee in full satisfaction of all or any part of the chargee's claims under the security agreement.

3. – In exercising its powers under the preceding paragraph the court shall have regard on the one hand to the value of the object to be vested in the chargee and on the other to the amount of the obligation which is to be satisfied by the vesting.

\* 4. - A Contracting State may at any time make a declaration specifying the courts or tribunals (including arbitral tribunals) empowered to make an order under paragraph 2.

5. - At any time before sale of the charged object or the making of an order under paragraph 2, the chargor may redeem it by paying the full amount secured by the security interest, subject to any lease granted by the chargee under sub-paragraph (c) of paragraph 1.

6. - A sale by the chargee in exercise of its rights under paragraph 1 or pursuant to an order of the court under that paragraph shall pass title to the buyer free from any other international interest over which the chargee's international interest has priority under the provisions of Article 19. Where such a sale results in a surplus above what is due to the chargee, the surplus shall be paid by the chargee to the holder of any other registered international interest ranking immediately after the chargee's international interest or, if there is none, then to the chargor.

#### *Article 10*

In the event of default by the buyer under a title reservation agreement or by the lessee under a leasing agreement, the seller or lessor, as the case may be, may take possession of any object to which the agreement relates.

#### *Article 11*

The parties may agree upon any additional remedies for default by the chargor, buyer or lessee to the extent that they are consistent with the preceding provisions of this Chapter and are permitted by the applicable law.

#### *Article 12*

1. - Any remedy provided by this Chapter shall be exercised in conformity with the procedural law of the place where exercise of the remedy is sought.

\* 2. - A Contracting State may declare at the time of signature, ratification, acceptance, approval or accession that where the charged object is situated within its territory:

(a) the chargee may exercise the remedy conferred by Article 9(1)(b) only pursuant to an order of the court;

(b) the provisions of Article 9(1)(c) shall not apply to such an object.

*Article 13*

Except as provided by the preceding provisions of this Chapter the rights of the parties to an agreement shall be governed by the applicable law.

CHAPTER V

REGISTRATION OF AN INTERNATIONAL INTEREST

*Article 14*

1. – An international interest may be registered in the international register where:
  - (a) the agreement relating to it conforms to the provisions of Article 6; and
  - (b) in the case of a security agreement, the chargor has consented in writing to the registration.
2. – A party to an agreement wishing to register an international interest shall transmit or deliver to the registrar in conformity with the Rules:
  - (a) a notice in writing ("registration notice"); and
  - (b) in the case of a security agreement, a copy of the chargor's written consent to the registration.
3. – Registration of an international interest shall take effect when a registration notice has been received by the registrar and the international registration system has allotted a registration number and recorded the date and time of registration.
4. – Registration of an international interest shall remain effective up to the date or until expiry of the period specified in the registration notice.
5. – A registration is valid despite an irregularity in the registration notice unless the irregularity is seriously misleading. The irregularity may be seriously misleading whether or not anyone is actually misled by it.

*Article 15*

1. – A chargee, seller or lessor wishing to have its registration of an international interest amended shall transmit or deliver to the registrar in conformity with the Rules:
  - (a) a notice in writing ("registration amendment notice"); and
  - (b) in the case of a security agreement, a copy of the chargor's written consent to the amendment, except where the amendment is covered by a prior written consent of which a copy has been transmitted or delivered to the registrar in conformity with the provisions of this or the preceding article.

2. – An amended registration shall take effect when recorded by the international registration system and remain effective up to the date or until expiry of the period specified in the registration amendment notice.

3. – The registration of an international interest shall be discharged on the transmission or delivery to the registrar, in conformity with the Rules, of a notice in writing ("registration discharge notice") signed by or on behalf of the chargee, seller or lessor.

#### *Article 16*

A certificate of registration which records on its face that it was issued by the registrar shall be *prima facie* evidence of the [ fact and time ] [ fact, time and order ] of registration without the need to prove the authenticity of the certificate.

#### *Article 17*

Articles 14 to 16 apply *mutatis mutandis* to a prospective international interest as they apply to an international interest.

#### *[ Article 18*

#### *Liability of International Registry ]*

### CHAPTER VI

### EFFECTS OF AN INTERNATIONAL INTEREST AS AGAINST THIRD PARTIES

#### *Article 19*

1. – A registered international interest has priority over a subsequently registered international interest except to the extent of any [ value added ] [ advances made ] by the holder of the previously registered interest without a pre-existing obligation to do so and at a time when it had actual knowledge of the subsequently registered interest.

2. – A registered international interest has priority over an unregistered international interest, even if the holder of the registered interest acquired it after the creation of the unregistered interest and with actual knowledge of it.

3. – A registered international interest has priority over any other interest acquired from the chargor, buyer or lessee at a time when the international interest was registered.

However, a registered international interest is subordinate to an interest which is not an international interest if the latter was acquired at a time when the international interest was unregistered, whether or not the person by whom it was acquired had actual knowledge of the international interest.

4. – (a) An international interest is valid against the trustee in bankruptcy and creditors of the chargor, buyer or lessee, including creditors who have obtained an attachment or execution, if prior to the bankruptcy, attachment or execution (as the case may be) the international interest has been registered in conformity with this Convention.

(b) For the purposes of this paragraph "trustee in bankruptcy" includes a liquidator, administrator or other person appointed to administer the estate of the chargor, buyer or lessee for the benefit of the general body of creditors.

5. – For the purposes of this article, where a registered prospective international interest becomes an international interest as the result of the chargor, seller or lessor acquiring rights in the object to which the interest relates, the international interest shall be treated as registered from the time of registration of the prospective international interest.

6. – Nothing in this article shall affect any special rules of insolvency law applicable to the insolvency of the chargor, buyer or lessee.

## [ CHAPTER VII

### TRANSFER OF AN INTERNATIONAL INTEREST]

## [ CHAPTER VIII

### SPECIAL PROVISIONS FOR AIRCRAFT AND AIRCRAFT ENGINES ]



## APPENDIX B

### AN EXTENDED ROLE FOR THE INTERNATIONAL REGISTRY

#### 1. Introduction

The Aviation Working Group<sup>1</sup> placed before the Study Group a Memorandum<sup>2</sup> containing recommendations relating to several aspects of the proposed Convention some of which relate to the scope of the international registry. The most significant of these recommendations are that the international registry include transfers of ownership and assignments of leases.

Recommendations 1.1 and 1.2 set out in the Memorandum are as follows:

1.1 The international registry established pursuant to the proposed Convention would contemplate the recordation of notices evidencing (not effectuating or constituting legally conclusive proof of) title/ownership transfers [contractual or by operation of law] of aircraft and aircraft engines (for this purpose which do not constitute "security interests" or "title reservation agreements" under the proposed Convention) by manufacturer's serial number. The failure to file any such notice would render such transfer voidable as against third parties (and, if sanctioned by domestic insolvency law, as against bankruptcy liquidators/trustees) who have made a subsequent Unidroit filing in respect of the relevant aircraft equipment, but not as between the parties.

1.2 All purchasers of aircraft (and their financiers) would acquire their interest in such aircraft equipment subject to all interests previously recorded in the registry with respect thereto.

Recommendation 4.1 set out in the Memorandum is as follows:

4.1 Security and absolute assignments of lease (and sub-lease) contracts shall be covered by the proposed Convention, and filings with the asset registry shall be made by manufacturer's serial number of the leased aircraft.

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<sup>1</sup> See text accompanying note 6 in main body of this report.

<sup>2</sup> See Unidroit, 1995, Study LXXII - Doc. 16, 1995. See also *Study Group for the preparation of uniform rules on international interests in mobile equipment: Sub-committee for the preparation of a first draft*, Unidroit 1995, Study LXXII-Doc. 21 (Summary report of third session, 11-13 October 1995), November 1995, paras. 10 and 38.

There can be no doubt that implementation of the recommendations set out in the Memorandum and replicated above would result in an international registry that is conceptually different and very much broader in scope than that described in the main body of this report. However, given the fact that the international registry would be one which would use specific item collateral descriptions (*e.g.* serial numbers of equipment) as the dominant registration-search criterion, implementation of the recommendations would appear to be feasible.

The Study Group will not only have to address the issue as to whether or not the international registry should provide for registration of transfers of ownership in aircraft equipment and assignments of aircraft leases and sub-leases, but also whether or not the extended scope of the proposed Convention and international registry should encompass the same types of transactions involving some or all of the other kinds of equipment to which the proposed Convention would apply.

Any decision to include registrations of ownership transfers and assignments of leases and sub-leases within the international registry would necessarily involve the preparation of additional priority rules to be included in the proposed Convention. The Aviation Working Group will present draft supplementary articles and associated materials relating to aircraft equipment to the April 1996 meeting of the Study Group. The following comments contain no explicit suggestions as to the form of these supplementary articles.

## **2. Conceptual differences**

Conceptually, the type of registry that is described in the main body of this report is one which is designed to protect third parties who acquire interests in equipment in the possession of persons falling into two categories: (i) persons who are not owners but who have a contractual right to possession of the equipment (buyers under title retention agreements and lessees); and (ii) owners in possession who have encumbered their ownership by giving security interests to credit grantors. Under this type of registry, the persons obligated to effect registrations in the international registry would be owners, in the case of category (i) and secured parties, in the case of category (ii). The persons who are the intended recipients of the protection afforded by registration requirements are principally<sup>3</sup> persons who acquire interests in the equipment in contractual dealings with the buyers, lessees or chargors (owners) in possession, as the case may be.

A transfer registry as proposed in the Memorandum would extend the system described in the main body of this report to protect persons from the misconduct of persons registered as transferees in the registry (registered transferees) who are not owners of the equipment because their ownership interests have been transferred away. The persons obligated to effect registrations in the registry would be persons who are transferees from registered transferees whether or not in

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<sup>3</sup> As noted in the main body of the report, the proposed Convention will address as well the priority position of unsecured creditors and liquidators/trustees. See text accompanying note 33.

possession of the equipment. The intended recipients of the protection afforded by registration would be persons who attempt to acquire *in rem* interests in equipment from registered transferees who, because they have transferred their ownership, do not have these rights to transfer.<sup>4</sup>

An assignment registry as proposed in the Memorandum would extend the system described in the main body of this report to protect persons from the misconduct of registered transferees who are owners or holders of *in rem* interests in the equipment or the misconduct of lessees who grant sub-leases. The perceived need for protection arises in situations in which registered transferees or lessees who grant sub-leases have assigned rights arising under their leases or sub-leases to assignees and who thereafter assign the same rights to other assignees.<sup>5</sup> The persons obligated to effect registration in the international registry would be the assignees of the leases or sub-leases.

### 3. Functional requirements

An international registry that provides for the registration of transfers and assignments along with the registration of security interests and the interests of lessors and sellers would be very similar in function to the registry described in the main body of this report. All registrations, of whatever nature, would be entered into the data base *seriatim*. There would be no need to maintain separate transfer and assignment registries; however, as noted below, it may be necessary to address some special concerns that arise in the context of registration of notices indicating transfers of ownership (transfer notices).

Since the registry would not be a title registry but merely a public record of purported transfers of ownership of equipment, the registrar would not be required to guarantee the existence or verify the validity of a contract of transfer between the putative transferor and putative transferee. However, it is very likely that there will have to be some mechanism to ensure that a person cannot easily claim to be a transferee (by registering a transfer notice indicating a transfer to it) when the property in the equipment has not been transferred to it. There are at least four ways to address the potential for fraud in this context.

One way is to require the person who tenders a transfer notice indicating a transfer to file with the notice a copy of the transfer agreement. The second is to require that the transferor provide separate written authorisation to the registrar to register the transfer notice. Both of these approaches present logistical problems. Since they require the person registering the transfer notice to submit along with the notice an additional document, remote, electronic registration of

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<sup>4</sup> Whether the protected persons include unsecured creditors and liquidators/trustees remains to be determined.

<sup>5</sup> While not recommended in the Memorandum, the same reasoning that calls for registration of assignments could be extended to situations in which a registered transferee who has leased equipment to one lessee leases the same equipment to a second lessee on terms that conflict with the first lease.

transfer notices would not be possible. If the decision is made to have satellite offices through which transfers must be registered, this concern could be addressed. The required copy of the transfer agreement or written consent of the transferor could be filed at the satellite office. When the administrator of the office is satisfied that this requirement has been met, he or she would authorise the electronic registration of a transfer notice in the international registry. It would be necessary to have uniform rules promulgated under the proposed Convention prescribing what must be filed at a satellite office and the procedures to be followed before an electronic registration of a transfer is effected by the satellite office administrator.

The third approach is an electronic variant of the second. Persons who are registered transferees of identified equipment could be issued by the international registry with a special identification number.<sup>6</sup> A transfer of ownership of that equipment would not be registered unless the transfer notice contained that number. The number could be changed frequently in order to reduce the chances that it might find its way into the hands of unauthorised persons.

The fourth approach (which could be employed in tandem with the third approach) is to require the register, upon registration of a transfer notice, to give notice of the registration (verification notice) to the putative transferor (whose name and address is recorded in the data base as a result of registration of a prior transfer notice indicating a transfer of ownership to it). The putative transferor would be given the legal right to have registration of the transfer removed simply by returning the notice to the registrar demanding the removal. The right to have a transfer notice indicating the transfer re-registered would thereafter be determined in litigation between the parties or in proceedings initiated by the putative transferee seeking an order requiring the registrar to re-register it.

The fourth approach eliminates the need to tender supplementary documentation along with a registry notice. However, since it operates *ex post facto* and not prophylactically, there will be a period of time between the date of registration of a transfer notice indicating an alleged transfer and the date when the putative transferor can respond to the verification notice during which the registry records will indicate that the transfer has taken place. Since third parties who acquire interests in the equipment from the putative transferee must be given the assurance that the information in the registry can be relied upon, it will be necessary to ensure that, during this period, any further registered transfer, security interest, lease or assignment of a lease between the putative transferee and such third parties be treated as having priority. In situations where the registry has direct electronic access to the putative transferor (whose name and address is recorded in the data base as a result of registration of a prior transfer notice indicating a transfer of ownership to it), delivery of and response to the verification notice should take very little time and the period of exposure to loss of interest to third parties would be very short.

In the main body of this report, it is suggested that persons effecting registrations in the international registry be allowed to specify the duration of the registration. This feature would not

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See text accompanying notes 25 and 26 in the main body of the report.

apply to registrations of transfers of ownership. All such transfers would remain permanently on the data base and be searchable at all times. The result would be that a person searching the registry would be in a position to determine the "chain of title" back to the first registered transfer of ownership.

