UNIDROIT 2003
C.G.E. Space Pr./1/W.P. 5
(Original: English)

INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW

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THE PRELIMINARY DRAFT PROTOCOL ON MATTERS SPECIFIC TO SPACE ASSETS: AN OVERVIEW OF ITS OBJECTIVES AND KEY PROVISIONS

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Rome, July 2003

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I. – PURPOSE OF THE CONVENTION

In November of 2001, the Convention on International Interests in Mobile Equipment (the "Convention") and a Protocol thereto on Matters specific to Aircraft Equipment (the "Aircraft Protocol") were adopted and opened to signature in Cape Town.[1] Sponsored by the International Institute for the Unification of Private Law ("UNIDROIT")[2] and the International Civil Aviation Organization (I.C.A.O.), these instruments are the first two elements of a uniform international system providing for the registration and enforcement of security interests and interests held by chargees, conditional sellers and lessors in a variety of high-value mobile equipment including airframes, aircraft engines, railway rolling stock and space assets. The Convention, Aircraft Protocol and contemplated rolling stock and space assets protocols will reduce certain risks associated with the financing and acquisition of these types of equipment by establishing clear, substantive and commercially oriented international rules to govern such transactions.

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[*] The Space Working Group ("S.W.G.") is an Organisation bringing together representatives of the various parties involved in the space industry, that is manufacturers, operators, financiers and insurers. It works closely with the various international Organisations active in the regulation of matters pertaining to Outer Space. It was set up by Mr Nesgos in 1997, at the request of the President of UNIDROIT, for the purpose of, first, preparing a preliminary draft Protocol to what was then still the preliminary draft UNIDROIT Convention on International Interests in Mobile Equipment on Matters specific to Space Assets capable of being submitted to the UNIDROIT Governing Council for consideration with a view to transmission to Governments and then organising representation of the space industry's interests in the subsequent intergovernmental consultation process. Its work is co-ordinated by Mr Nesgos, with the assistance of Mr Panahy. S.W.G. participants involved in the preparation of the Space Assets Protocol include Alcatel Space Industries, Alenia Spazio S.p.A., Arianespace, Assicurazioni Generali S.p.A., Astrium G.m.b.H., Astrium S.A.S., Baker & McKenzie, BNPParibas, Boeing Capital Corporation, Crédit Lyonnais Group, Deutsche Bank, EADS Germany G.m.b.H., Inmarsat, La Réunion Spatiale, Lockheed Martin Finance Corporation, Lockheed Martin Global Telecommunications, Milbank, Tweed, Hadley and McCloy LLP, Space Systems/Loral and Telespazio S.p.A.

[1] Both the Convention and the Aircraft Protocol have to date been signed by 26 States: Burundi (16 November 2001), Chile (16 November 2001), China (16 November 2001), Congo (16 November 2001), Cuba (16 November 2001), Ethiopia (16 November 2001), France (16 November 2001), Ghana (16 November 2001), Jamaica (16 November 2001), Jordan (16 November 2001), Kenya (16 November 2001), Lesotho (16 November 2001), Nigeria (16 November 2001), South Africa (16 November 2001), Sudan (16 November 2001), Switzerland (16 November 2001), Tonga (16 November 2001), Turkey (16 November 2001), United Kingdom (16 November 2001), United Republic of Tanzania (16 November 2001), Italy (6 December 2001), Senegal (2 April 2002), Panama (11 September 2002), Germany (17 September 2002), Saudi Arabia (12 March 2003) and the United States of America (9 May 2003). The Convention will enter into force three months after the date of deposit of the third instrument of ratification or accession as regards a category of objects to which a Protocol applies. The texts of the Convention and the Aircraft Protocol may be viewed at the UNIDROIT web site (www.unidroit.org).

[2] UNIDROIT is an independent intergovernmental Organisation established in 1926 as an auxiliary organ of the League of Nations and subsequently re-established in 1940 on the basis of a multilateral agreement, the UNIDROIT Statute. UNIDROIT is based in Rome, Italy and has 59 member States drawn from the six continents.

II. – BACKGROUND AND INTEREST IN THE SPACE ASSETS PROTOCOL

In parallel to the efforts undertaken in support of the Convention and Aircraft Protocol and at the invitation of the President of the UNIDROIT, the S.W.G. began working in July of 1997 on the preparation of a preliminary draft Protocol on Matters specific to Space Assets (the "Space Assets Protocol"). In February of 2002, the text established by the S.W.G. was reviewed by a Steering and Revisions Committee convened by the President of UNIDROIT to ensure the compatibility of the instrument with the text of the Convention. Subsequently, in May of 2003, the UNIDROIT Governing Council authorised convening the first session of a UNIDROIT Committee of governmental experts for initiation of the intergovernmental process and preparation of the draft Protocol to the Convention on International Interests in Mobile Equipment on Matters specific to Space Assets, to be held in Rome December 15-19, 2003.

A diverse range of parties in the space sector, including satellite manufacturers, launch services providers, satellite operators, financial institutions, insurance brokers and underwriters, and Governments encouraging privatisation and commercial activities have expressed interest and participated in the preparation of the Space Assets Protocol. Despite the recent doldrums experienced in the telecommunications sector, the global space and satellite industry has remained relatively stable as compared to other industry segments. Revenues for the commercial space and satellite industry exceeded US$ 100 billion in 2002. The most recent industry forecasts predict the launch of approximately 300 commercial satellites through 2012 (average of 23.5 geostationary and eight non geostationary satellites per year). It is expected that new demand for high-bandwidth satellite services such as High-Definition Television, increased demand for internet-via-satellite in rural areas and continued global take-up of direct-to-home services will grow industry revenues at an average annual rate of between 10-20% over the next decade.

Interestingly, the recent negative economic trends, including the convergence of overcapacity in the telecommunications market, including terrestrial and undersea cable systems, aversion to new technologies by a cautious banking community and international geopolitical events have further highlighted the need for a clear, substantive and commercially oriented international regimen to support asset-based financing of commercial space equipment and services. Lack of access to the high-yield and public equity markets has resulted in a growing trend for space-segment service providers and lenders to engage in financing transactions secured by relevant satellite assets (including, in certain cases, a pledge of revenues generated by the satellites) and procured launch services. Recent examples of asset-based financing in the space and satellite sector include a $1.25 billion secured credit facility for PanAmSat Corporation arranged by Credit Suisse First Boston and Deutsche Bank and a secured financing of the XM-3 satellite for XM Satellite Holdings provided by Boeing Capital Corporation.

III. – STRUCTURE OF THE CONVENTION AND ITS RELATIONSHIP WITH THE SPACE ASSETS PROTOCOL

In order to address adequately the unique aspects of each category of identifiable high-value mobile equipment, the Convention provides a general conceptual framework while contemplating the formulation of individual protocols to govern each category of mobile property. As a result, the Convention applies to any category of equipment covered by a protocol, only as among Contracting

States to that protocol, and subject to the terms of such protocol. This protocol structure permits flexibility in adapting the Convention principles to a unique class of assets and accommodates a deliberative process and consensus building. As the Convention is subject to the terms of each protocol, the two texts are to be read and interpreted as a single instrument with no distinction being made between the terms of the Convention and the protocols.

The approach of a framework Convention with controlling protocols may be considered unorthodox as protocols conventionally serve as subsequent amending instruments. Nevertheless, this approach has been contemplated by customary international law as evidenced by and codified in the Vienna Convention on the Law of Treaties,[3] which defines "treaty" to include "two or more related instruments".

IV. – OBJECTIVES OF THE SPACE ASSETS PROTOCOL

The Space Assets Protocol is particularly relevant to asset-based financing as the nature of and the jurisdictional issues involved with space assets are quite different and unique in many respects from other categories of mobile equipment. For example, space assets are not within the territory of any State once launched into space. Moreover, future applications of space technology are likely to result in space assets that are assembled or manufactured in space. Accordingly, the method by which an international interest in a space asset is recorded and enforced, along with special remedy provisions, will be detailed in the Space Assets Protocol.

A further *raison d'être* for the Convention and the corresponding Space Assets Protocol is that many legal systems do not adequately provide for the registration and perfection of a security interest in a space asset. In those jurisdictions that recognise non-possessory pledges of personal property and that have debtor-based systems of recording security interests, such as jurisdictions whose legal systems derive from British common law, a security interest in an orbiting satellite can be created in the same manner as ordinary earth-based collateral. For example, APT Satellite Company, a Hong Kong corporation, obtained financing for the manufacture, launch and operation of its APSTAR satellite, granting under Hong Kong law a first priority security interest in the satellite and its associated rights. However, in many common law jurisdictions, the rules governing perfection are those established by the jurisdiction in which the property is located. This creates special problems for space assets.

Many civil law countries, however, follow a different system. For instance, in a transaction involving the Indonesian satellite owner and operator, P.T. Asia Cellular Satellite (ACeS), the method chosen to assign as security an interest in the GARUDA satellite was by a fiduciary transfer agreement, governed by Indonesian law, whereby ACeS transferred title to the satellite and certain other personal property to a security agent acting in a fiduciary capacity. The grant of security in these assets is not well developed in Indonesia. Finally, in the United States, because orbiting satellites are neither within the jurisdiction of any State nor fit plainly into the category of "ordinary goods", "mobile goods" or "general intangibles", a creditor has no certainty that filing financing statements in any jurisdiction will perfect a security interest.

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3 23 May 1969, 1155 *United Nations Treaty Series* 331 (the "Vienna Convention").

While this gap in many States' legal regimes is not new, the nature of space and satellite financing has changed markedly in the last decade, thereby increasing the necessity for an appropriate legal regimen. Previously, commercial satellites were owned and transponders were leased almost exclusively by governmental agencies and well-capitalised, blue chip companies. Asset-based financing in the satellite area was therefore limited. Financiers were adequately comforted by the sovereign credit of the governmental agency or the strength of the balance sheet of the commercial borrower or by taking a security interest in other earth-based and more readily marketable assets of the debtor. Thus, if a debtor defaulted on a loan made to finance the manufacture and use of a satellite or to finance the lease of a satellite transponder, the financier could rely on the assets of the company as a whole. More recently, however, satellite owners and lessors include companies with limited capital, unproven or erratic credit-standing and a short history of operating success. Often the satellite or the transponder and its associated rights, such as contractual and licensing rights, including authorisations for use of radio-frequency spectrum and orbital slots, are the only significant assets of the company. Consequently, the ability to take a valid, perfected security interest in these assets may determine whether or not a satellite project can be successfully implemented.

V. – MAIN FEATURES OF THE CONVENTION AND THE SPACE ASSETS PROTOCOL

A. Defining space assets

The first and foremost task of the S.W.G. was to define "space assets". The present definition in the Space Assets Protocol contemplates: (i) any separately identifiable asset that is in space or that is intended to be launched in space or has been returned to space; (ii) any separately identifiable components forming a part of a space asset referred to in (i) or attached to or contained within such asset; (iii) any separately identifiable asset assembled or manufactured in space; and (iv) any launch vehicle that is expendable or can be reused to transport persons or goods to and from space.

Obtaining a security interest in an orbiting satellite clearly does not benefit a creditor if, upon default, the creditor is limited to physical or constructive possession of the satellite. Thus, the Space Assets Protocol also contemplates granting creditors recourse to certain "associated rights" related to the operation of a satellite[4]: (i) any permit, licence, authorisation or equivalent instrument that is granted or issued by a national or intergovernmental or other international body or authority to control, use or operate a space asset, relating to the use of orbital positions and the transmission, emission or reception of radio signals to and from a space asset, which may be transferred or assigned, to the extent permissible and assignable under the laws concerned [5]; (ii) all rights to payment or other performance due to a debtor by any person with respect to space assets; and (iii) all contractual rights held by the debtor that are secured by or associated with the space assets. There is great significance in intangible rights and "control" in the context of "associated rights" such as

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4 In recognition of potential conflicts with domestic laws, the Space Assets Protocol permits a Contracting State, in accordance with its laws, to restrict or attach conditions to the exercise of the remedies where such remedies would involve or require the transfer of controlled goods, technology or data, or would involve the transfer or assignment of "associated rights."

5 This reference to "the laws concerned" is intended to include obligations arising under the International Telecommunication Union and other communications treaty systems.

governmental authorisations, intellectual property required to control, use and operate equipment, and contractual rights such as warranties. Space assets, naturally, encompass a broader category of rights than is the case for other equipment or assets covered by the Convention.

B. Forms and constitution of international interests

The notion that lies at the conceptual centre of the Convention and the Space Assets Protocol (together, the "Texts") is that of an international interest, which means a proprietary interest in mobile equipment, created by virtue of the provisions of the Convention and its relevant protocol. The Convention sets out three transaction types that create international interests: (i) an interest granted under a security agreement; (ii) an interest vested in a conditional seller under a title reservation agreement; and (iii) an interest vested in a lessor under a leasing agreement. These three categories have been employed to respect the majority of legal systems that draw distinctions between security and title-type interests. The Convention points to the "applicable law" to determine the category to which an interest belongs. There are some substantive distinctions in the Texts regarding treatment of different categories of international interests, the most important among them being the separate default remedies.

An international interest is created where the agreement creating or providing for the interest satisfies four conditions specified in the Convention: (i) the agreement must be in writing; (ii) the agreement must relate to an object in respect of which the chargor, the conditional seller or lessor has power to enter into the agreement; (iii) the agreement must uniquely and sufficiently describe the object with reference to, among other things, the manufacturer's name, manufacturer's serial number and its model designation[6]; and (iv) in the case of a security agreement, the agreement must enable the secured obligations to be identified. The satisfaction of the foregoing conditions is both necessary as well as sufficient to constitute an international interest.

C. The international registration system

1. Generally

One of the most important features of the Convention is the establishment of an international registry for each category of mobile equipment under which creditors will have the ability to centrally register their international interests and search for competing interests. The international registration system is pivotal to the whole exercise of creating international interests in

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6 The Space Assets Protocol contemplates that it shall be necessary and sufficient to identify the relevant space assets if the description of such space asset: (i) provides the name of the debtor and the creditor; (ii) provides an address for the debtor and for the creditor; (iii) contains a general description of the space asset indicating the name of the manufacturer (or principal manufacturer, if more than one manufacturer exists), its manufacturer's serial number (if one exists) and its model designation (or comparable designation, if a model designation does not exist) and indicating its intended location; (iv) provides the date and location of launch; (v) in the case of a separately identifiable component forming a part of the space asset or attached to or contained within the space asset, provides a description of such separately identifiable component, the space asset of which it forms a part, to which it is attached or within which it is contained and each of the other identification criteria specified in Article VII with respect to such space asset; and (vi) such additional identification criteria as may be specified in the Protocol. Participants in the S.W.G. have agreed that inclusion of multiple search criteria would increase the reliability of searches in a computerised registration data base as contemplated for the International Registry.

mobile equipment. The International Registry shall have an international legal personality and capacity to exercise its functions, will not be subject to any particular national law and will also be entitled to immunity from legal process (unless immunity is waived by the Registry). In determining the priority of conflicting interests, the sequential ordering of registration ("first-to-file") shall be the sole criterion for all priority determinations not involving preferred non-consensual rights and interests.

A registered interest has priority over a subsequently registered interest and over an unregistered interest, whether or not the unregistered interest is eligible for registration. Thus, the first party to file wins even if the party was aware of the competing interest at the time of registration. Although this seems to be a severe rule, the arguments in favour of the "first-to-file" concept are based on the availability of relevant information upon reasonable search and hence the opportunity to protect one's interest by registration or withholding funds. As the international registration system contemplated under the Texts is intended to provide pragmatic, easily accessible information regarding potentially competing interests in a particular transaction to any interested party, the burden or allocation of risk to a subsequent-in-time registrant should be minimal and transparent.

2. Treatment of non-consensual and prospective interests

The Texts contain provisions relating to the treatment of non-consensual rights and interests. Such rights are included in the general priority scheme based on the reasoning that such inclusion will ultimately enhance the utility of the international registration system. A Contracting State has the option to set out categories of non-consensual rights and interests and, on the basis of such categorisation, such rights and interests will be registrable as international interests. If a Contracting State thinks that certain non-consensual rights and interests can be treated fairly by participating in a first-to-file regimen, it can indicate so in its ratification instrument.

The Convention and the relevant protocol also permit the registration of prospective interests. This serves two purposes: first, it puts others on notice of future interests, and secondly, it ensures the priority of the prospective interest for the registrant. Upon the fulfilment of the conditions and requirements prescribed by the relevant protocol, the prospective interest becomes an actual interest and the priority of that interest is determined with reference to the date of the filing of such prospective interest.

3. Modalities, liabilities and immunities of the International Registry

The Texts will set out the conditions and requirements necessary to give effect to registration. Registration becomes effective upon entry of required information into the registry data base so as to permit such registration to be easily searchable. A certificate will be issued by the International Registry to that effect, which shall be *prima facie* proof of the validity of the facts contained therein. Other regulations will address matters such as the medium of information transmission to the registry, the duration period for a registration and the requirements of conducting a search.

Once effective registration has taken place, the International Registry shall be liable to compensate for loss suffered by any person due to any error or system malfunction in the Registry. The courts of the State where the registrar of the International Registry is situated shall have jurisdiction to resolve any disputes arising out of the liability provision. These provisions are essential to build confidence in the international registration system, particularly during its infancy. Subject to the above provisions the International Registry, the Registrar and the staff of the International Registry shall, in the exercise of their functions, enjoy immunity from legal process. The assets, documents and archives of the International Registry shall also be inviolable and immune from seizure or legal process.[7]

D. Remedies available upon default

A core provision of the Texts is a default remedy provision that permits the holder of an international interest to take certain actions without regard to the location of the asset in which the international interest is registered. The Texts include the basic remedies available to the obligee upon default by the obligor. In the event of default in the performance of a secured obligation, the chargee may: (i) take possession or control of any object charged to it; (ii) sell or grant a lease of any such object; (iii) collect or receive any income or profits arising from the management or use of any such object; and (iv) apply for a court order authorising or directing any of the above acts. In the event of default by the conditional buyer under a title reservation agreement or by the lessee under a leasing agreement, the conditional seller or the lessor, as the case may be, may terminate the agreement and take possession or control of any object to which the agreement relates. The conditional seller or the lessor may also apply for a court order authorising or directing either of the foregoing remedies. In the event of default, the obligee may change or cause to be changed any access or command codes required to facilitate access to, and the command, control and operation of the space asset.

The most likely and effective remedy with respect to an orbiting satellite is the taking of constructive repossession (or control) through telemetry, tracking, and command (TT&C). The most expeditious means of taking control is by using the existing TT&C facility. As this may pose legal and practical difficulties, the obligee should be entitled to seek judicial relief in any country that would have "line of sight" of the satellite.

E. Expedited remedies

The time frame in which the above-stated remedies can be enforced is of paramount importance and may vary from one legal system to another. The effects of protracted justice and procedural delays are significant to obligees since equipment that requires immediate preservation necessitates speedy judicial relief. The Texts contain an optional provision entitling an obligee that adduces *prima facie* evidence of default by an obligor to "speedy judicial relief" in the form of a variety of court orders. A Contracting State that opts to apply expedited remedies shall ensure that an obligee that adduces *prima facie* evidence of default by the obligor may, pending final

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[7] The United Nations has been approached as one possible Supervisory Authority. The possibility of the United Nations serving as Supervisory Authority was considered by the Legal Subcommittee of U.N./COPUOS at its 42nd session. Other intergovernmental Organisations have also expressed an interest in serving as Supervisory Authority.

determination of its claim, obtain speedy judicial relief in the form of one or more of the following orders:

(a) preservation of the object and its value;

(b) possession, control, custody or management of the object;

(c) sale or lease of the object;

(d) application of the proceeds or income of the object; and

(e) immobilisation of the object.

These provisions will not restrict the right of transaction parties to simultaneously proceed with litigation on the merits of the case. These provisions are, in any case, not intended to be exhaustive and are in addition to interim judicial relief under the relevant "applicable law". In fact the provisions relating to speedy judicial relief contained in the Texts are *sui generis* and not dependent upon or derived from national injunctive relief rules. While the purpose of national injunctive rules is fairness, equity and prevention of irreparable damage, the purpose of speedy remedies under the Texts is commercial prudence in the light of an objective standard of *prima facie* proof of default. In the event Contracting States wish to retain national injunctive relief, they may make a declaration to this effect.

VI. – CONCLUSION

There are three principles that underlie asset-based financing. They are: (1) transparency in the priority principles under which proprietary interests are registered; (2) prompt enforcement of remedies; and (3) comfort that the priority principles and enforcement mechanisms will not be modified or qualified due to bankruptcy of the obligor. Some of the provisions embodying the above principles, as drafted in the Convention and Space Assets Protocol, may raise policy considerations for certain countries regarding insolvency rules, time-tables applicable to legal proceedings and the ability to take possession of assets without the need for judicial proceedings. The Texts contain provisions that specifically contemplate and permit declarations in respect of these crucial matters. While use of declarations to address policy issues is customary, their use as a basic feature of these treaty instruments is innovative. At the time of ratification, Contracting States will be given the opportunity to weigh their economic and non-economic interests and policies and decide whether to opt for these critically important provisions. While the elective nature of these provisions may have important financial implications, this structure permits the Convention and Space Assets Protocol to be tailored to address multiple economic, financial and political concerns.

Space and satellite finance is still in its formative stages when compared to other types of equipment finance. Aerospace manufacturers are still evolving from Government contractors to investors in space and satellite projects. Financial institutions are still learning about industry needs and the particular risks of space financing. The need for asset-based financing and leasing is now emerging in an environment driven by privatisation, deregulation, global demand, increased international trade and less predictable access to high-yield and public equity financing sources. The space and satellite sector, including satellite manufacturers, launch services providers, satellite operators, financial institutions, insurance brokers and underwriters, and Governments can benefit greatly from the uniform and predictable regimen governing security interests in space assets as provided for by the Convention and the Space Assets Protocol.