UNIDROIT COMMITTEE OF GOVERNMENTAL EXPERTS
FOR THE PREPARATION OF A DRAFT PROTOCOL TO
THE CONVENTION ON INTERNATIONAL INTERESTS IN
MOBILE EQUIPMENT ON MATTERS SPECIFIC TO
SPACE ASSETS
Third session
Rome, 7/11 December 2009

PRELIMINARY DRAFT PROTOCOL
TO THE CONVENTION ON INTERNATIONAL INTERESTS IN MOBILE EQUIPMENT ON MATTERS SPECIFIC TO SPACE ASSETS
(as revised by the Committee of governmental experts at its first session
(Rome, 15/19 December 2003))
and
ALTERNATIVE TEXT OF THE PRELIMINARY DRAFT PROTOCOL,
IMPLEMENTING POLICY ISSUES
REFERRED TO AND EXAMINED BY THE STEERING COMMITTEE
(prepared, at the request of the Steering Committee,
for presentation to the Committee of governmental experts,
by Professor Sir Roy Goode (United Kingdom) and Mr Michel Deschamps (Canada):

COMMENTS AND PROPOSALS

submitted by Governments, Organisations and the international commercial space, financial and insurance communities

INTRODUCTION

On 27 and 28 July 2009 the UNIDROIT Secretariat transmitted, under cover of invitations to Governments, Organisations and representatives of the international commercial space, financial and insurance communities to attend the third session of the UNIDROIT Committee of governmental experts for the preparation of a draft Protocol to the Convention on International Interests in Mobile Equipment on Matters specific to Space Assets (hereinafter referred to as the Committee), the text of the preliminary draft Protocol to the Convention on International Interests in Mobile Equipment on Matters specific to Space Assets as revised by the Committee during its first session, held in Rome from 15 to 19 December 2003 (hereinafter referred to as the preliminary draft Protocol), and an alternative text of the preliminary draft Protocol, implementing policy issues referred to and examined by the UNIDROIT Steering Committee (prepared, at the request of the Steering Committee, for presentation to the Committee, with an explanatory memorandum, by Professor Sir Roy Goode (United Kingdom) and Mr Michel Deschamps (Canada)) (hereinafter referred to as the alternative text), with an invitation to formulate comments thereon for consideration by the Committee at its third session.
As of 9 November 2009 the UNIDROIT Secretariat had received comments and proposals from the Government of Lebanon, Mr S. Kozuka (Sophia University, Tokyo), Ms P.L. Meredith (Co-Chair, Space Law Practice Group, Zuckert Scoutt & Rasenberger, L.L.P., Washington D.C.), on behalf of leading space insurance underwriters, and the SKY Perfect JSAT Corporation. These comments are reproduced hereunder.

**COMMENTS SUBMITTED BY GOVERNMENTS**

**Lebanon**

The Embassy of Lebanon in Italy has the honour to communicate [to UNIDROIT] an advisory opinion from the Legislation and Advisory Service of the Ministry of Justice of Lebanon concerning the preliminary draft Protocol.

After studying "the preliminary draft Protocol and its annexes", the Legislation Service, while confirming that the preliminary draft is not contrary to Lebanese public policy, would like to make certain comments and invite UNIDROIT to respond to the following questions: 1

(a) Article I(d) of the preliminary draft Protocol

This Article sets out the terms used in the preliminary draft. The definition given for "insolvency-related event" is unclear. Does this refer to a case of bankruptcy as defined by Lebanese law or does it mean something else?

(b) Article V(3) of the preliminary draft Protocol

This provision states that: "Registration of a contract of sale remains effective indefinitely. Registration of a prospective sale remains effective unless discharged or until expiry of the period, if any, specified in the registration".

This Article does not clarify the meaning of "registration": is it *ad solemnitatum*? In other words, does registration of a contract of sale have probative or constitutive value? Moreover, this provision does not indicate the place of registration: is a special Registry contemplated or is this a reference to the Land Registry?

(c) Article XI(5) (Alternative B) of the preliminary draft Protocol

This provision states that: "If the insolvency administrator or the debtor, as applicable, does not give notice in conformity with paragraph 2, or when it has declared that it will give the creditor the opportunity to take possession of or control and operation over the space asset but fails to do so, the court may permit the creditor to take possession of or control and operation over the space asset upon such terms as the court may order and may require the taking of any additional step or the provision of any additional guarantee”.

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1 UNIDROIT responded to the questions raised by the Legislation and Advisory Service of the Ministry of Justice of Lebanon, by Note Verbale addressed to the Embassy of Lebanon in Italy, on 20 October 2009.
This provision does not identify the “court” in question. The preliminary draft Protocol in no place sets out the jurisdictional competence of the court as regards place and competence as well as its seat (where does it sit?).

It would be helpful to spell out the competent court to avoid any conflict of jurisdiction in the application of the future Protocol.

COMMENTS SUBMITTED BY THE INTERNATIONAL COMMERICAL SPACE, FINANCIAL AND INSURANCE COMMUNITIES

Mr S. Kozuka (Sophia University, Tokyo)

The author supports the policy contained in the alternative text and the following comments are merely of a technical nature. As regards the definition of “space asset” (Article I(2)(k)), observations will be made in another note, with the suggestions about possible criteria for identifying space assets.

(a) Rights assignment

The rights assignment is a transaction to enable the creditor to benefit from the debtor’s rights by way of security or satisfaction of the associated right (Article I(2)(h) of the alternative text). It resembles the law of “subrogation” in some countries, which entitles the creditor under a secured transaction to the rights or claims of the debtor without any agreement. Does the preliminary draft Protocol exclude such an idea so that, unless the rights assignment is agreed, the creditor cannot benefit from the revenue arising from the rights or claims held by the debtor? If so, would it not make the point clearer if it is so stated in the preliminary draft Protocol?

Suggested new wording (for Article V of the alternative text):

“Unless a rights assignment is agreed by the parties, no subrogation by the creditor takes place.”

(b) Obligations secured by the rights assignment

Article VI(c) of the alternative text requires “the obligations secured by the agreement” to be determined in the rights assignment agreement. Having decided that a rights assignment can be recorded in the Registry only as part of the registration of an international interest, one wonders whether this requirement is still necessary. It might be sufficient if the assigned debtor’s rights secure the whole of the obligations secured by the international interest (i.e. associated right), as if the debtor’s rights constitute part of the space asset.

Suggestion: delete Article VI(c) of the alternative text.

(c) Priority of recorded rights assignment

The recorded rights assignment must prevail over any other assignment of the same debtor’s rights made afterwards. In case the debtor assigns its rights to a party other than the creditor under the agreement involving the international interest, the priority of the recorded rights assignment should not be doubted, even if the assignment complies with the requirement under the applicable domestic law.
In this regard, it should be noted that a rights assignment made separately from the space asset has no chance of being recorded in the Registry. This could give rise to an allegation that the assignee, having had no chance of recording the assignment, should not be disadvantaged against a recorded rights assignment “for reasons of equity.” A hypothetical case borne in mind here would be one where an unsecured creditor approaches the debtor and, after negotiations with the latter, makes the latter assign its rights (debtor’s rights) in satisfaction of the unsecured claim.

The first question to be asked in this regard is whether this allegation is clearly excluded in Article IX(1) of the alternative text. The issue may relate to the term “[any other] unrecorded rights assignment” at the end of the paragraph. It is noted that the term “rights assignment” is defined as “a contract by which the debtor confers on the creditor an interest … in or over the whole or part of existing or future debtor’s rights” (emphasis added) and “creditor”, in turn, is defined as “a chargee under a security agreement, a conditional seller under a title reservation agreement or a lessor under a leasing agreement” in the base Convention. The literal reading of these definitions could lead to the conclusion that the assignment of a debtor’s right to a third party does not fall under the “unrecorded rights assignment.” The problem might be properly solved by adjusting the definition of “rights assignment.”

Suggested wording (for Article I(2)(h) of the alternative text):

“rights assignment” means a contract by which the debtor confers on another party an interest (including an ownership interest) in or over the whole or part of existing or future debtor’s rights …” (emphasis added).

The second, related question is whether the priority rule of Article IX of the alternative text should hold in the case of an assignment made prior to the recording of a rights assignment as well. If the answer is in the affirmative, the debtor’s rights (e.g. a claim arising under a lease contract of the transponder) are deprived of the chance of being assigned effectively, as such an assignment can be prevailed over by the recorded rights assignment at any time. It should be remembered here that, as long as the assignment does not relate to the space asset, there is no chance of it being recorded or otherwise securing its priority. Perhaps in this case, the right assigned before the recording of a rights assignment must be considered as no longer belonging to the debtor (not constituting the “debtor’s rights”) at the time of recording.

Suggested wording (for new Article IX(3) of the alternative text):

“Nothing in this paragraph affects the validity of any rights assignment made before the first recorded rights assignment and completed all the requirements under the applicable law.”

(d) Duty of assignor as to licences

Article XII of the alternative text has introduced the obligation to take all the steps in procuring the transfer of licences, rather than providing for the transfer of the licence as in previous drafts. The question is whether the person on whom the duty is imposed is the “assignor under a rights assignment or rights reassignment” as it stands in the alternative text. As the concept of “rights assignment” no longer relates to the licences (“related rights” in the preliminary draft Protocol) but merely to the debtor’s rights, the phrase does not seem to fit the situation. Perhaps the “debtor” or “assignor of the international interest,” as the case may be, will be the more appropriate person to owe the duty.
Suggested wording (for Article XII of the alternative text):

“1. - The debtor shall at the request of the creditor take all steps within its power to procure the transfer of its licence to the creditor or any other party designated by the creditor or the termination of its licence and the grant of a new licence to the creditor or any other party designated by the creditor, and shall fully co-operate with the creditor to that end.

2. – When the creditor assigns its international interest in the space asset, the creditor shall at the request of the assignee of the international interest take all steps within its power to procure the transfer of its licence to the assignee or the termination of its licence and the grant of a new licence to the assignee, and shall fully co-operate with the assignee to that end.”

Ms P.L. Meredith (Co-Chair, Space Law Practice Group, Zuckert Scoutt & Rasenberger, L.L.P., Washington D.C.), on behalf of leading space insurance underwriters

Re: satellite insurers’ salvage interests: proposed additions to the preliminary draft Protocol and the alternative text

The preliminary draft Protocol and the alternative text as currently drafted do not accommodate a well established legal principle, namely, insurer salvage, as it applies to satellite insurance.

Salvage plays a unique and important role in satellite insurance. Once a satellite loss has been paid in full, the insurer is entitled to salvage by way of title to, or revenues or sales proceeds generated from the malfunctioning satellite. Salvage is particularly significant in satellite insurance because the satellite may have substantial life left (salvage value) even after it has been declared a Constructive Total Loss.

Salvage interests cannot be registered under the preliminary draft Protocol and the alternative text. In Sir Roy Goode’s words, “[t]his means that having paid out the claim in full and acquired salvage rights in the satellite the insurer has nothing it can register so as to protect itself against subsequent international interests . . .” Consequently, a subsequent buyer or creditor by registering an international interest would wipe out an insurer’s salvage interest, even when with knowledge of its existence.

To remedy this unintended consequence of the preliminary draft Protocol and the alternative text as currently drafted, major space insurance underwriters would ask UNIDROIT to add language to the preliminary draft Protocol to address this concern. Insurance plays a critical role in the very satellite financing the preliminary draft Protocol seeks to promote. Indeed, creditors, as a rule, demand that the satellite operator (debtor) take out insurance to protect the satellite asset.

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2 The leading space insurance underwriters in question are Munich Re, Swiss Re, SCOR, La Réunion Spatiale, Space Co-Groupe AGF, and Atrium.
(a) The meaning of salvage

In the context of commercial satellite insurance, salvage usually refers to the right of insurers, upon full payment of a satellite loss: (1) to take title to the degraded satellite (hereinafter referred to as **Title Salvage**) or (2) to receive a portion of the revenues generated from the operation of, or sales proceeds from that satellite (hereinafter referred to as **Revenue Salvage**).

Satellite insurance policies customarily provide for salvage. In the United States of America, insurers’ salvage interests may also arise by operation of equity.

(b) The significance of salvage in satellite insurance

Salvage plays a key role in satellite insurance that is different from other industries. The way satellite insurance policies are structured, even when the satellite is declared a Constructive Total Loss and insurers pay the full amount of the insurance, the satellite may have significant remaining life, albeit with partial or degrading functionality.

In other words, the satellite may have considerable value left even after it has been declared a Constructive Total Loss. Having paid the loss, insurers are entitled to that value as salvage. This salvage interest is not being accommodated by the preliminary draft Protocol and the alternative text.

(c) Salvage interests do not qualify for registration

The preliminary draft Protocol and the alternative text provide for an International Registry for the registration and protection of “international interests” and certain other interests in satellites and other space assets. Salvage interests do not qualify.

An international interest is defined as an “interest held by a creditor” that is: (1) granted under a security agreement; (2) vested in the conditional seller under a title reservation agreement; (3) vested in the lessor under a leasing agreement; or (4) vested in a buyer under a contract of sale.

3 Salvage is “the property saved or remaining after a fire or other loss, sometimes retained by an insurance company that has compensated the owner for the loss,” amongst other meanings. Black’s Law Dictionary 1367 (8th ed. 2004). See also John A. Appleman, Insurance Law & Practice (Matthew Bender 1st ed., 2007) § 3808 (“[T]he term ‘salvage’ may also be used . . . as designating that part of the property that survives the peril and is saved.”).


5 Preliminary draft Protocol, attached as W.P. 4 to UNIDROIT’s invitation of 28 July 2009 to participate in the third session of the UNIDROIT Committee of governmental experts for the preparation of a draft Protocol to the Convention on International Interests in Mobile Equipment on Matters specific to Space Assets (Rome, 7/11 December 2009), Ch. III; alternative text, attached as W.P. 5 to UNIDROIT’s same invitation, Ch. III; Convention on International Interests in Mobile Equipment, 2001 (hereinafter referred to as the Convention), Art. 17(2)(a).

6 Convention, Art. 16(1)(a) (non-consensual rights and interests); Art. 16(1)(b)-(e).

7 See preliminary draft Protocol, Art. I(2)(g)(i), (iv); alternative text, Art. I(2)(k) (defining “space assets” to include satellites and transponders, amongst other space assets).

8 Convention, Arts. 1(o), 2(2)(a)-(c). See preliminary draft Protocol, Art. III; alternative text, Art. III (applying the Convention to a contract of sale and treating the buyer as the creditor and the seller as the debtor); Convention, Art. 41 (providing that Protocols may specify that the Convention shall apply to sales and prospective sales).
A salvage interest is not an "international interest" or any other registrable interest. \(^9\) It does not meet the criteria listed in (1)-(4); \(^10\) it is also not "held by a creditor" as that term is defined. \(^11\)

(d) **The preliminary draft Protocol and the alternative text do not accommodate salvage**

As the preliminary draft Protocol and the alternative text are currently drafted, a subsequent buyer or creditor would wipe out insurers’ salvage interests (even after the insurers have paid the loss and acquired salvage) simply by registering the sale or security interest in the form of an international interest under the future Protocol.

A "registered interest has priority . . . over an unregistered interest," \(^12\) such as, insurers’ salvage interests, which cannot be registered. The priority applies even if the creditor has knowledge of the pre-existing salvage interest. \(^13\) These are some examples:

(i) **Buyer takes title free and clear of salvage, even with knowledge**

A subsequent buyer of a satellite under a registered sale "acquires its interest in that asset free from . . . an unregistered interest, even if the buyer has actual knowledge of the unregistered interest." \(^14\) In other words, the buyer acquires the satellite free of any salvage obligations to the insurer, even where he knows that the insurers have paid a loss and acquired salvage rights.

(ii) **Creditors may exercise default remedies at the expense of salvage, even with knowledge**

A subsequent creditor under a security agreement may exercise the following default remedies without regard for the insurers’ existing salvage, even with knowledge of the salvage interest:

\((α)\) take possession or control of the satellite;

\((β)\) sell or lease the satellite; or

\((γ)\) collect and receive any income or profits from the use of the satellite. \(^15\)
(e) Proposed language to be added to the preliminary draft Protocol and the alternative text

To remedy this situation, the insurers initially, in 2007, requested that they be allowed to register salvage interests, but have instead agreed to request that the following clauses be added to the preliminary draft Protocol and the alternative text for Title Salvage and Revenue Salvage, respectively:

"For the purposes of Article III of the Protocol, an interest in a space asset acquired by a satellite insurer as a salvage interest is deemed to have been acquired by way of sale. 16

For the purposes of Article 16(1)(c) of the Convention, when an insurer makes a payment of insurance proceeds for a covered loss of an insured space asset in which a creditor has an international interest, the insurer shall have the right of subrogation to the creditor's associated rights and related international interest and any recorded debtor's rights in the space asset to the extent of the insurer's salvage interest. This right of subrogation shall be in addition to and shall not affect any right of subrogation the insurer may have under national law or the insurance policy."

(f) The objective of the proposed clauses

The Title Salvage clause is intended to remedy the current situation where the acquisition of title (ownership) through salvage is not registrable. By treating the acquisition of Title Salvage as a sale, it may be registered. Sir Roy Goode proposed as follows:

"[S]ince the draft Space Protocol, like the Aircraft Protocol, extends the Convention to cover outright sales, a paragraph could be added that for the purpose of Article III an interest in a satellite acquired by a satellite insurer as a salvage interest is deemed to have been acquired by way of sale . . ."17

The Revenue Salvage clause is intended to allow for subrogation to the creditor's international interest by insurers that have paid proceeds for a satellite loss, thereby affording the insurer a means to protect its claim to salvage. Without the clause, "[t]he insurer has no right of subrogation to the creditor's international interest because this has been discharged by payment and there can be no right of subrogation against the debtor . . ."18 To remedy this consequence,

17 Explanatory memorandum, ¶ 19.
18 Id. ¶ 18. In the United States of America, as a general rule, payment of proceeds to a creditor extinguishes the insured's debt to the creditor, thus leaving no claim or security interest for the insurer to subrogate into. See, e.g., New York Jurisprudence: Ins. §2193 [2nd ed.] ("[P]ayment by the insurer to the mortgagee, to the extent of his or her interest, under a standard mortgage clause is ordinarily regarded as having been made on behalf of the mortgagor and extinguishes the mortgagor's debt . . .") (quoting Reed v. Federal Ins. Co., 510 N.Y.S.2d 618, 623 (N.Y. App. Div. 1987)). The rule does not apply if the insurer is not liable under the policy due to some fault of the insured; in that case the debt is not extinguished and the insurer has an equitable subrogation right. See, e.g., In re SPG of Schenectady, Inc., 833 F.2d 413, 418 (2nd Cir. 1987) ("[O]nly a showing of the mortgagor's culpable conduct would prevent the insurance proceeds from being applied to the mortgage debt and would trigger the insurer's subrogation rights . . ."); Merchants Nat'l Bank v. Southeastern Fire Ins. Co., 854 F.2d 100, 105 (5th Cir. 1988) (citing Tolar v. Bankers Trust Savings &
the proposed text allows insurers who have paid insurance proceeds and acquired salvage interests a limited right of subrogation, to the extent of their salvage interests.

**SKY Perfect JSAT Corporation**

**Re: public service exemption (See footnote 3 to Article XXVII(3) of the alternative text)**

(a) *The proposed menu of options*

The inclusion of a menu of options from which Contracting States could make a selection by declaration at the time of ratification or accession is being proposed. Seemingly the range of options are, however, so broad that it is not easy to understand the common concept behind these; for example, while the options as for who shall have the right to exercise a “step-in” right are substantial, the options relating to the arbitration of disputes concerning the maintenance of a public service might be procedural. Options for protection for the continuation of public services and those for protection for the exercise of default remedies appear together in the menu.

The wider choice is to be tabled in order to command the broad level of consensus, the vaguer the message about the direction where the international commercial space and financial communities should go might become.

In addition, we are concerned that Contracting States would not choose the options suited to their national laws, to the contrary, the inclusion in the future Protocol of a range of options might virtually encourage Contracting States to select the options less protecting the creditors’ rights and make the relating domestic legislation to limit creditor remedies as a result.

(b) *The recommendations by the United Nations Commission on International Trade Law (UNCITRAL)*

As indicated by the Secretariat in the Summary report on the meeting of the Sub-committee on public service held last May (Study LXXIIJ – Doc. 16), the recommendations including “step-in” rights of the Legislative Guide on Privately Financed Infrastructure Projects (hereinafter referred to as the *Legislative Guide*) and the Model Legislative Provisions on Privately Financed Infrastructure Projects (hereinafter referred to as the *Model Provisions*) prepared by UNCITRAL are suggestive of how to address the question of public service.

The recommendations in the Legislative Guide and the Model Provisions are desirably to be reflected in the Contracting States’ legislation and the agreements among related parties such as creditors, satellite operators and service providers.

Based upon our understanding of the nature of the Legislative Guide and the Model Provisions, the future Protocol is to be considered not a treaty on the same level as the Canterbury Loan Ass’n., 363 So.2d 732 (Miss. 1978)) (similar statement). This rule against subrogation against one’s own insured/mortgagor extends also to *contractual* subrogation, with limited exceptions. See, e.g., Lee L. Russ, *Couch on Insurance*, § 224.1 (3d ed. 2003) (citing AGIP Petroleum Co., Inc. v. Gulf Island Fabrication, Inc., 920 F. Supp. 1318 (S.D. Tex. 1996) and Vesta Ins. Co. v. Amoco Production Co., 986 F.2d 981 (5th Cir. 1993)) (reimbursement); Farr Mann & Co. v. M/V Rozita, 903 F.2d 871, 879 (1st Cir. 1990) (citing Great Lakes Transit Corp. v. Interstate S.S. Co., 301 U.S. 646, 654 (1937)) (insured caused own loss).
Treaty between France and the United Kingdom but a more general overarching framework. If necessary, a treaty like the Canterbury Treaty is to be executed among related States under the regime of the future Protocol.

(c) The possible creation of a new right

We are sharing the concern expressed in the course of the meeting of the Sub-committee on public service at the idea of giving Contracting States a right to limit the exercise of default remedies that did not exist before, as this might negatively affect the creditor’s right of ownership. As urged in the Sub-committee, special attention is to be paid to the effects that any proposed solutions to the issue of public service might have upon the relationships amongst a Contracting State, a provider of a public service, a debtor operating the relevant satellite and the creditors of that satellite.

It is understandable that the term “public service” should not be defined in the future Protocol to avoid the risk of creating an international duty. The same careful consideration should be given to the question to balance the need of Contracting States to guarantee the continuation of a public service with the rights of the creditors. We have to be careful to introduce premature international right and obligation.

The question as to how best to balance is to be left to the development of business practice in the coming years. Legislation-based solutions can also be alternatively realised by agreement-based contracts originating in intensive negotiations among the parties. It is significant to understand the dynamics of the commercial and financial communities and respect the agreements to be executed among the concerned parties, including Contracting States, likely reflecting the recommendations by UNCITRAL as a consolidation of the practice already obtaining in the resolution of the public service issue in the context of privately financed infrastructure projects.

(d) Conclusions

1. The concern at the idea of giving Contracting States a right to limit the exercise of default remedies is to be broadly shared.

2. The inclusion in the future Protocol of a range of options might virtually encourage Contracting States to select the options less protective of creditors’ rights, thus presumably amplifying the concern of creditors.

3. The recommendations in the Legislative Guide and the Model Provisions by UNCITRAL are to be reflected in the Contracting States' legislation and the agreements among the related parties.

4. The question as to how best to balance the need of Contracting States with the rights of creditors is to be left to the development of business practice with the understanding of significance to respect the agreements among the concerned parties.

5. The harmonisation and co-ordination of practices and laws in terms of public service exemptions among States should hopefully be pursued by not creating a new right and obligation but facilitating the gradual adoptions by States of appropriate uniform rules of law.