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# CONTENTS

**Introduction**  
*(vii)*

**PART I – BASIC CONFERENCE MATERIALS**

<table>
<thead>
<tr>
<th>Item</th>
<th>Document</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Provisional Agenda</td>
<td>CONF. 7/1</td>
<td>3</td>
</tr>
<tr>
<td>Draft Rules of Procedure</td>
<td>CONF. 7/2</td>
<td>4</td>
</tr>
<tr>
<td>Draft Convention on international financial leasing as adopted by</td>
<td>Study LIX - Doc. 48</td>
<td>22</td>
</tr>
<tr>
<td>a Unidroit committee of governmental experts on 30 April 1987 with</td>
<td></td>
<td></td>
</tr>
<tr>
<td>explanatory report prepared by the Unidroit Secretariat</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Draft Convention on international factoring as adopted by a</td>
<td>Study LVIII - Doc. 33</td>
<td>81</td>
</tr>
<tr>
<td>Unidroit committee of governmental experts on 24 April 1987 with</td>
<td></td>
<td></td>
</tr>
<tr>
<td>explanatory report prepared by the Unidroit Secretariat</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Draft final provisions capable of embodiment in the draft</td>
<td>Study LIX - Doc. 49</td>
<td>105</td>
</tr>
<tr>
<td>Convention on international financial leasing drawn up by a</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Unidroit committee of governmental experts with explanatory notes</td>
<td></td>
<td></td>
</tr>
<tr>
<td>drawn up by the Unidroit Secretariat</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Draft final provisions capable of embodiment in the draft</td>
<td>Study LVIII - Doc. 34</td>
<td>114</td>
</tr>
<tr>
<td>Convention on international factoring drawn up by a Unidroit</td>
<td></td>
<td></td>
</tr>
<tr>
<td>committee of governmental experts with explanatory notes drawn up</td>
<td></td>
<td></td>
</tr>
<tr>
<td>by the Unidroit Secretariat</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Working Group of Technical Experts on international financial</td>
<td>CONF. 7/5</td>
<td>123</td>
</tr>
<tr>
<td>leasing (Rome, 29 February 1988): Report by the Unidroit Secretariat</td>
<td></td>
<td></td>
</tr>
<tr>
<td>List of participants</td>
<td>CONF. 7/INF. 1</td>
<td>131</td>
</tr>
</tbody>
</table>
PART II – COMMITTEE OF THE WHOLE

Basic papers

Comments on the draft Unidroit Convention on international financial leasing by:

Governments (Japan, Pakistan, South Africa, Spain, Switzerland, United States of America)  
CONF. 7/3 and Add. 1-3  
151

CONF. 7/4 and Add. 1-3  
168

Comments on the draft Unidroit Convention on international factoring by:

Governments (Japan, South Africa, Spain, United States of America)  
CONF. 7/6 and Add. 1, 2  
186

International Organisations (Hague Conference on Private International Law)  
CONF. 7/7  
200

Working papers on the draft Unidroit Convention on international financial leasing submitted by:

United Kingdom  
CONF. 7/C.1/W.P. 1  
204

Sweden  
CONF. 7/C.1/W.P. 2  
204

Finland  
CONF. 7/C.1/W.P. 3  
205

United States of America  
CONF. 7/C.1/W.P. 4  
206

Comité Maritime International  
CONF. 7/C.1/W.P. 5  
207

People’s Republic of China  
CONF. 7/C.1/W.P. 6  
210

Finland  
CONF. 7/C.1/W.P. 7  
212

United States of America  
CONF. 7/C.1/W.P. 8  
213

Sweden  
CONF. 7/C.1/W.P. 9  
218

United Kingdom  
CONF. 7/C.1/W.P. 10  
218

and Add.  
219

United States of America  
CONF. 7/C.1/W.P. 11  
220

Australia  
CONF. 7/C.1/W.P. 12  
226

Sweden  
CONF. 7/C.1/W.P. 13  
226

United Kingdom  
CONF. 7/C.1/W.P. 14  
228

Sweden  
CONF. 7/C.1/W.P. 15  
229

Canada, United Kingdom and United States of America  
CONF. 7/C.1/W.P. 16  
230
<table>
<thead>
<tr>
<th>Document</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Federal Republic of Germany</td>
<td>CONF. 7/C.1/W.P. 17</td>
</tr>
<tr>
<td>The Chairman</td>
<td>CONF. 7/C.1/W.P. 18</td>
</tr>
<tr>
<td>Informal Working Group on the proposal by the Comité Maritime International regarding Article 5(3)(c) in relation to ships</td>
<td>CONF. 7/C.1/W.P. 19</td>
</tr>
<tr>
<td>Informal Working Group on Article 14</td>
<td>CONF. 7/C.1/W.P. 20</td>
</tr>
<tr>
<td>Colombia</td>
<td>CONF. 7/C.1/W.P. 21</td>
</tr>
<tr>
<td>Philippines</td>
<td>CONF. 7/C.1/W.P. 22</td>
</tr>
<tr>
<td>Colombia</td>
<td>CONF. 7/C.1/W.P. 23</td>
</tr>
<tr>
<td>Sweden</td>
<td>CONF. 7/C.1/W.P. 24</td>
</tr>
<tr>
<td>France and Mexico</td>
<td>CONF. 7/C.1/W.P. 25</td>
</tr>
<tr>
<td>Canada</td>
<td>CONF. 7/C.1/W.P. 26</td>
</tr>
<tr>
<td>Working Group on Article 7(2)</td>
<td>CONF. 7/C.1/W.P. 27</td>
</tr>
<tr>
<td>Sweden</td>
<td>CONF. 7/C.1/W.P. 28</td>
</tr>
<tr>
<td>Federal Republic of Germany</td>
<td>CONF. 7/C.1/W.P. 29</td>
</tr>
<tr>
<td>Canada</td>
<td>CONF. 7/C.1/W.P. 30</td>
</tr>
<tr>
<td>Sweden</td>
<td>CONF. 7/C.1/W.P. 31</td>
</tr>
<tr>
<td>The Chairman of the Drafting Committee</td>
<td>CONF. 7/C.1/W.P. 32</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>CONF. 7/C.1/W.P. 33</td>
</tr>
<tr>
<td>Federal Republic of Germany</td>
<td>CONF. 7/C.1/W.P. 34</td>
</tr>
</tbody>
</table>

*Working papers on the draft Unidroit Convention on international factoring submitted by:*

<table>
<thead>
<tr>
<th>Document</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cuba</td>
<td>CONF. 7/C.1/W.P. 35</td>
</tr>
<tr>
<td>Italy</td>
<td>CONF. 7/C.1/W.P. 36</td>
</tr>
<tr>
<td>Sweden</td>
<td>CONF. 7/C.1/W.P. 37</td>
</tr>
<tr>
<td>Finland</td>
<td>CONF. 7/C.1/W.P. 38</td>
</tr>
<tr>
<td>The Secretariat</td>
<td>CONF. 7/C.1/W.P. 39</td>
</tr>
<tr>
<td>Sweden</td>
<td>CONF. 7/C.1/W.P. 40</td>
</tr>
<tr>
<td>Federal Republic of Germany</td>
<td>CONF. 7/C.1/W.P. 41</td>
</tr>
<tr>
<td>Italy</td>
<td>CONF. 7/C.1/W.P. 42</td>
</tr>
<tr>
<td>France, Mexico and Philippines</td>
<td>CONF. 7/C.1/W.P. 43</td>
</tr>
<tr>
<td>Sweden</td>
<td>CONF. 7/C.1/W.P. 44</td>
</tr>
<tr>
<td>Czechoslovakia</td>
<td>CONF. 7/C.1/W.P. 45</td>
</tr>
<tr>
<td>Working Group on Article 1(1)(c) and (3)</td>
<td>CONF. 7/C.1/W.P. 46</td>
</tr>
<tr>
<td>Working Group on Article 5</td>
<td>CONF. 7/C.1/W.P. 47</td>
</tr>
<tr>
<td>The Chairman of the Drafting Committee</td>
<td>CONF. 7/C.1/W.P. 48</td>
</tr>
</tbody>
</table>
Texts submitted by the Drafting Committee on the draft Unidroit Convention on international financial leasing:

Text of the Preamble and Chapters I and II

CONF. 7/D.C./1 and Add.  255

Texts submitted by the Drafting Committee on the draft Unidroit Convention on international factoring:

Preliminary text of Chapters I and II

CONF. 7/D.C./W.P. 13  261

Preliminary text of the Preamble and Articles 6 and X

CONF. 7/D.C./W.P. 13 Add.  264

PART III – FINAL CLAUSES COMMITTEE

Basic papers

Comments on the draft final provisions capable of embodiment in the draft Convention on international financial leasing by Governments (Japan)

CONF. 7/3  269

Comments on the draft final provisions capable of embodiment in the draft Convention on international factoring by Governments (Japan)

CONF. 7/6  270

Working papers on the draft final provisions capable of embodiment in the draft Convention on international financial leasing submitted by:

Comité Maritime International

CONF. 7/C.2/W.P. 1  271

Netherlands

CONF. 7/C.2/W.P. 2  271

Final Clauses Committee

CONF. 7/C.2/W.P. 3  272

United Kingdom

CONF. 7/C.2/W.P. 4  276

United Kingdom

CONF. 7/C.2/W.P. 5  276

(iv)
**Texts submitted by the Drafting Committee**

on the draft final provisions capable of embodiment in the draft Convention on international financial leasing:

<table>
<thead>
<tr>
<th>Document</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Text of Chapter III</td>
<td>277</td>
</tr>
<tr>
<td>Text of Chapter III approved by the Drafting Committee on 23 May 1988</td>
<td>280</td>
</tr>
<tr>
<td>Text of Chapter III approved by the Drafting Committee on 24 May 1988</td>
<td>284</td>
</tr>
</tbody>
</table>

**Text submitted by the Drafting Committee**

on the draft final provisions capable of embodiment in the draft Convention on international factoring:

<table>
<thead>
<tr>
<th>Document</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Text of Chapter IV approved by the Drafting Committee on 24 May 1988</td>
<td>287</td>
</tr>
</tbody>
</table>

**PART IV – PLENUM**

**Working papers on the draft Unidroit Convention on international financial leasing submitted by:**

<table>
<thead>
<tr>
<th>Document</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>France, Mexico and Philippines</td>
<td>293</td>
</tr>
<tr>
<td>France, Mexico and Philippines</td>
<td>293</td>
</tr>
<tr>
<td>Canada</td>
<td>293</td>
</tr>
</tbody>
</table>

**Reports to Plenum**

<table>
<thead>
<tr>
<th>Document</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Report of the Committee of the Whole (on the draft Unidroit Convention on international financial leasing)</td>
<td>294</td>
</tr>
<tr>
<td>Second report of the Committee of the Whole (on the draft Unidroit Convention on international factoring)</td>
<td>300</td>
</tr>
<tr>
<td>Report of the Final Clauses Committee (on the draft final provisions capable of embodiment in the draft Convention on international financial leasing)</td>
<td>305</td>
</tr>
<tr>
<td></td>
<td></td>
</tr>
<tr>
<td>---------------------------------</td>
<td>----------------</td>
</tr>
<tr>
<td><strong>Second report of the Final Clauses Committee</strong></td>
<td><strong>Page</strong></td>
</tr>
<tr>
<td>(on the draft final provisions capable of embodiment in the draft Convention on international factoring)</td>
<td>CONF. 7/C.2/Doc. 2</td>
</tr>
<tr>
<td><strong>Report of the Credentials Committee</strong></td>
<td>CONF. 7/8 and Add.</td>
</tr>
<tr>
<td><strong>Draft Final Act submitted by the Drafting Committee</strong></td>
<td>CONF. 7/10</td>
</tr>
</tbody>
</table>

**PART V – TEXTS/INSTRUMENTS ADOPTED BY THE CONFERENCE**

| Texts adopted by the Conference at its fourth plenary session | CONF. 7/9 | 321 |
| Final Act of the Conference | CONF. 7/11 | 327 |
| Unidroit Convention on International Financial Leasing | CONF. 7/11 Appendix I | 331 |
| Unidroit Convention on International Factoring | CONF. 7/11 Appendix II | 340 |

(vi)
INTRODUCTION

At the invitation of the Government of Canada, a diplomatic Conference for the adoption of the draft Unidroit Conventions on international factoring and international financial leasing was held in Ottawa from 9 to 28 May 1988.

The draft Conventions submitted for adoption at the Conference had been drawn up by twin committees of governmental experts convened by the International Institute for the Unification of Private Law (Unidroit). The other basic working materials of the Conference were twin sets of draft final provisions prepared by the Unidroit Secretariat and comments on the two draft Conventions and sets of draft final provisions submitted by Governments and international Organisations.

59 Governments and ten international Organisations were represented at the Conference which elected Mr T.B. Smith (Canada), member of the Unidroit Governing Council, President. Messrs I. El-Kattan (Egypt), L. Réczei (Hungary), H. Ríos de Marimón (Chile), W. Rolland (Federal Republic of Germany) and Z. Yuan (China) were elected Vice-Presidents of the Conference. The first and second readings of the draft Convention on international financial leasing, including the draft Preamble thereto and Article F of the draft final provisions thereof, and of the draft Convention on international factoring, including the draft Preamble thereto and an Article X as well as Article F of the draft final provisions thereof, were assigned to a Committee of the Whole, the Chairman of which was Mr L. Sevón (Finland). The first and second readings of all but Article F of both sets of draft final provisions as well as the titles of both draft Conventions were assigned to a Final Clauses Committee, the Chairman of which was Mr G. Brennan (Australia). The Conference also set up a Drafting Committee, the Chairman of which was Mr R.M. Goode (United Kingdom), and a Credentials Committee, the Chairman of which was Mr W. Rolland.

The Conference completed its work on 26 May 1988 with the adoption of the Unidroit Convention on International Financial Leasing and the Unidroit Convention on International Factoring, which were opened to signature two days later, following the signature of the Final Act of the Conference, at the closing session of the Conference.

This volume constitutes Volume I of the Acts and Proceedings of the Conference and contains the following Conference papers:

(1) the basic Conference papers;
(2) papers submitted to the Committee of the Whole;
(3) papers submitted to the Final Clauses Committee;
(4) papers and reports submitted to the Plenum;
(5) the texts and instruments adopted by the Conference.

Volume II of the Acts and Proceedings of the Conference will contain summary records of all sessions of the Plenum and the Committee of the Whole as well as a complete list of all the papers issued in connection with the Conference.
PART I

BASIC CONFERENCE MATERIALS

<table>
<thead>
<tr>
<th>Provisional Agenda</th>
<th>3</th>
</tr>
</thead>
<tbody>
<tr>
<td>Draft Rules of Procedure</td>
<td>4</td>
</tr>
<tr>
<td>Draft Convention on international financial leasing as adopted by a Unidroit</td>
<td>22</td>
</tr>
<tr>
<td>committee of governmental experts on 30 April 1987 with explanatory report</td>
<td></td>
</tr>
<tr>
<td>prepared by the Unidroit Secretariat</td>
<td></td>
</tr>
<tr>
<td>Draft Convention on international factoring as adopted by a Unidroit committee of</td>
<td>81</td>
</tr>
<tr>
<td>governmental experts on 24 April 1987 with explanatory report prepared by the</td>
<td></td>
</tr>
<tr>
<td>Unidroit Secretariat</td>
<td></td>
</tr>
<tr>
<td>Draft final provisions capable of embodiment in the draft Convention on international financial leasing drawn up by a Unidroit committee of governmental experts with explanatory notes drawn up by the Unidroit Secretariat</td>
<td>105</td>
</tr>
<tr>
<td>Draft final provisions capable of embodiment in the draft Convention on international factoring drawn up by a Unidroit committee of governmental experts with explanatory notes drawn up by the Unidroit Secretariat</td>
<td>114</td>
</tr>
<tr>
<td>Working Group of Technical Experts on international financial leasing (Rome, 29</td>
<td>123</td>
</tr>
<tr>
<td>February 1988): Report by the Unidroit Secretariat</td>
<td></td>
</tr>
<tr>
<td>List of participants</td>
<td>131</td>
</tr>
</tbody>
</table>
PROVISIONAL AGENDA

Opening of the Conference

Election of the President of the Conference

1. – Adoption of the Agenda

2. – Adoption of the Rules of Procedure

3. – Election of the Vice-Presidents and other Officers of the Conference

4. – Appointment of the Credentials Committee

5. – Organisation of the work of the Conference, including the establishment of a Final Clauses Committee and other Committees, as necessary

6. – Consideration of the draft Unidroit Convention on international financial leasing (Committee of the Whole I)

7. – Consideration of the draft Unidroit Convention on international factoring (Committee of the Whole II)

8. – Examination of the Reports of:
   (a) the Committee of the Whole I
   (b) the Committee of the Whole II
   (c) the Final Clauses Committee
   (d) the Credentials Committee
   (e) other Committees

9. – Adoption of the Final Act of the Conference and of any instruments, recommendations and resolutions resulting from its work

10. – Signature of the Final Act and of any instruments adopted by the Conference
DRAFT RULES OF PROCEDURE FOR THE CONFERENCE

Table of contents

<table>
<thead>
<tr>
<th>Rule</th>
<th>Chapter and Description</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Composition of Delegations</td>
<td>8</td>
</tr>
<tr>
<td>2</td>
<td>Alternates or Advisers</td>
<td>8</td>
</tr>
<tr>
<td>3</td>
<td>Submission of Credentials</td>
<td>8</td>
</tr>
<tr>
<td>4</td>
<td>Credentials Committee</td>
<td>8</td>
</tr>
<tr>
<td>5</td>
<td>Provisional Participation in the Conference</td>
<td>9</td>
</tr>
<tr>
<td></td>
<td>CHAPTER II - PRESIDENT, VICE-PRESIDENTS, etc.</td>
<td></td>
</tr>
<tr>
<td>6</td>
<td>Election</td>
<td>9</td>
</tr>
<tr>
<td>7</td>
<td>President</td>
<td>9</td>
</tr>
<tr>
<td>8</td>
<td>Ditto</td>
<td>9</td>
</tr>
<tr>
<td>9</td>
<td>Acting President</td>
<td>9</td>
</tr>
<tr>
<td>10</td>
<td>Ditto</td>
<td>10</td>
</tr>
<tr>
<td>11</td>
<td>Replacement of the President</td>
<td>10</td>
</tr>
<tr>
<td>12</td>
<td>The President shall not vote</td>
<td>10</td>
</tr>
<tr>
<td>Rule</td>
<td></td>
<td></td>
</tr>
<tr>
<td>------</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>CHAPTER III - STEERING COMMITTEE</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>13 Composition</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td>14 Functions</td>
<td>10</td>
<td></td>
</tr>
<tr>
<td><strong>CHAPTER IV - SECRETARIAT</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>15 Duties of the Secretary-General and the Secretariat</td>
<td>11</td>
<td></td>
</tr>
<tr>
<td>16 Statements by the Secretariat</td>
<td>11</td>
<td></td>
</tr>
<tr>
<td><strong>CHAPTER V - CONDUCT OF BUSINESS</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>17 Quorum</td>
<td>11</td>
<td></td>
</tr>
<tr>
<td>18 Speeches</td>
<td>11</td>
<td></td>
</tr>
<tr>
<td>19 Precedence</td>
<td>12</td>
<td></td>
</tr>
<tr>
<td>20 Points of Order</td>
<td>12</td>
<td></td>
</tr>
<tr>
<td>21 Time-limit on Speeches</td>
<td>12</td>
<td></td>
</tr>
<tr>
<td>22 Closing of List of Speakers</td>
<td>12</td>
<td></td>
</tr>
<tr>
<td>23 Adjournment of Debate</td>
<td>12</td>
<td></td>
</tr>
<tr>
<td>24 Closure of the Debate</td>
<td>13</td>
<td></td>
</tr>
<tr>
<td>25 Suspension or Adjournment of the Meeting</td>
<td>13</td>
<td></td>
</tr>
<tr>
<td>26 Order of Procedural Motions</td>
<td>13</td>
<td></td>
</tr>
<tr>
<td>27 Basic Proposals</td>
<td>13</td>
<td></td>
</tr>
<tr>
<td>28 Other Proposals and Amendments</td>
<td>13</td>
<td></td>
</tr>
</tbody>
</table>
Chapter VI - Voting

33 Voting Rights
34 Required Majority
35 Meaning of the expression "Representatives present and voting"
36 Method of Voting
37 Conduct during Voting
38 Division of Proposals and Amendments
39 Voting on Amendments
40 Voting on Proposals
41 Elections
42 Ditto
43 Ditto
44 Ditto
45 Equally Divided Votes
<table>
<thead>
<tr>
<th>Rule</th>
<th>Chapter and Description</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>46</td>
<td>Committees of the Whole</td>
<td>18</td>
</tr>
<tr>
<td>47</td>
<td>Drafting Committee</td>
<td>18</td>
</tr>
<tr>
<td>48</td>
<td>Establishment of other Committees and subsidiary bodies</td>
<td>18</td>
</tr>
<tr>
<td>49</td>
<td>Representation on Committees and other subsidiary bodies</td>
<td>18</td>
</tr>
<tr>
<td>50</td>
<td>Co-ordination by the Steering Committee</td>
<td>18</td>
</tr>
<tr>
<td>51</td>
<td>Officers</td>
<td>19</td>
</tr>
<tr>
<td>52</td>
<td>Quorum</td>
<td>19</td>
</tr>
<tr>
<td>53</td>
<td>Conduct of business and voting in Committees and other subsidiary bodies</td>
<td>19</td>
</tr>
<tr>
<td>54</td>
<td>Official and Working Languages</td>
<td>19</td>
</tr>
<tr>
<td>55</td>
<td>Interpretation from official languages</td>
<td>20</td>
</tr>
<tr>
<td>56</td>
<td>Interpretation from other languages</td>
<td>20</td>
</tr>
<tr>
<td>57</td>
<td>Summary Records</td>
<td>20</td>
</tr>
<tr>
<td>58</td>
<td>Languages of Documents and Summary Records</td>
<td>20</td>
</tr>
<tr>
<td>59</td>
<td>Plenary Meetings and Meetings of Committees and subsidiary bodies</td>
<td>20</td>
</tr>
<tr>
<td>60</td>
<td>Communiqués to the Press</td>
<td>21</td>
</tr>
<tr>
<td>Rule</td>
<td>Rule Description</td>
<td>Page</td>
</tr>
<tr>
<td>------</td>
<td>-----------------</td>
<td>------</td>
</tr>
<tr>
<td>61</td>
<td>CHAPTER X - OBSERVERS FROM GOVERNMENTAL AND NON-GOVERNMENTAL ORGANISATIONS</td>
<td>21</td>
</tr>
<tr>
<td>62</td>
<td>CHAPTER XI - AMENDMENTS TO THE RULES OF PROCEDURE</td>
<td>21</td>
</tr>
<tr>
<td>63</td>
<td>CHAPTER XII - SIGNATURE OF INSTRUMENTS</td>
<td>21</td>
</tr>
</tbody>
</table>

CHAPTER I - REPRESENTATION AND CREDENTIALS

Composition of Delegations

Rule 1

The delegation of each State participating in the Conference shall consist of accredited representatives and such alternate representatives and advisers as may be required.

Alternates or Advisers

Rule 2

An alternate representative or an adviser may act as a representative upon designation by the head of the delegation.

Submission of Credentials

Rule 3

The credentials of representatives and the names of any alternate representatives and advisers shall be transmitted to the Secretary-General of the Conference not later than twenty-four hours after the opening of the Conference. The credentials shall be issued by the Head of State or Government, the Minister for Foreign Affairs, the Minister concerned or on behalf of any of them. Any later change in the composition of the delegation shall as soon as possible be submitted to the Secretary-General of the Conference.

Credentials Committee

Rule 4

A Credentials Committee shall be appointed at the beginning of the Conference. It shall consist of five members who shall be appointed by the Conference on the proposal of the President. It shall examine the credentials of representatives and report to the Conference without delay.
Provisional Participation in the Conference

Rule 5

Pending a decision of the Conference upon their credentials, representatives shall be entitled provisionally to participate in the Conference.

Any representative to whose admission a State participating in the Conference has made objection shall be seated provisionally with the same rights as other representatives until the Credentials Committee has reported and the Conference has given its decision.

CHAPTER II - PRESIDENT, VICE-PRESIDENTS, etc.

Election

Rule 6

The Conference shall elect a President, five Vice-Presidents, the Chairmen of the Committees of the Whole provided for in Rule 46 and the Chairman of the Drafting Committee established under Rule 47. The Conference may also elect such other officers as it deems necessary for the performance of its functions.

President

Rule 7

In addition to exercising the powers conferred upon him elsewhere by these rules, the President shall preside at the plenary meetings of the Conference, declare the opening and closing of each plenary meeting, direct the discussions at such meetings, accord the right to speak, put questions to the vote and announce decisions. He shall rule on points of order and, subject to these rules of procedure, have complete control of the proceedings and over the maintenance of order thereat. The President may propose to the Conference the limitation of time to be allowed to speakers, the limitation of the number of times each representative may speak on any question, the closure of the list of speakers, the adjournment or closure of the debate, and the suspension or the adjournment of the meeting.

Rule 8

The President, in the exercise of his functions, remains under the authority of the Conference.

Acting President

Rule 9

If the President is absent for a meeting or any part thereof, he shall appoint one of the Vice-Presidents to take his place.
Rule 10

A Vice-President acting as President shall have the same powers and duties as the President.

Replacement of the President

Rule 11

If at any time the President is unable to perform his functions for the remaining period of the Conference a new President shall be elected.

The President shall not vote

Rule 12

The President, or Vice-President acting as President, shall not vote but may, where necessary, appoint another member of his delegation to vote in his place.

CHAPTER III - STEERING COMMITTEE

Composition

Rule 13

There shall be a Steering Committee which shall comprise the President and Vice-Presidents of the Conference as well as the Chairmen of the Committees of the Whole. The President of the Conference or, in his absence, a Vice-President designated by him shall serve as Chairman of the Steering Committee. The Secretary-General of the Conference and the Chairman of the Drafting Committee may be invited by the President to participate, without the right to vote, in the work of the Steering Committee.

Functions

Rule 14

The Steering Committee shall assist the President in the general conduct of the business of the Conference and, subject to the decisions of the Conference, shall ensure the co-ordination of its work.
CHAPTER IV - SECRETARIAT

Duties of the Secretary-General and the Secretariat

Rule 15

The Secretary-General of the International Institute for the Unification of Private Law shall be the Secretary-General of the Conference.

The Secretary-General shall appoint an Executive Secretary and a Deputy Executive Secretary of the Conference and shall provide and direct the staff required by the Conference and its Committees.

The Secretariat shall receive, translate, produce and distribute documents, reports and resolutions of the Conference; interpret speeches made at the meetings, prepare and circulate records of the public meetings; arrange for the custody and preservation of the documents in accordance with the decisions of the Conference; publish reports of the public meetings; distribute all documents of the Conference to the participating Governments and, generally, perform all other work which the Conference may require.

Statements by the Secretariat

Rule 16

The Secretary-General, the Executive Secretary, the Deputy Executive Secretary and any member of the Conference staff designated for that purpose may, at any time, make oral or written statements concerning any question under consideration.

CHAPTER V - CONDUCT OF BUSINESS

Quorum

Rule 17

A quorum of the Conference shall be constituted by the representatives of a majority of the States participating in the Conference.

Speeches

Rule 18

No person may address the Conference without having previously obtained the permission of the President. Subject to Rules 19, 20, 24 and 26, the President shall call upon speakers in the order in which they signify their desire to speak. The President may call a speaker to order if his remarks are not relevant to the subject under discussion.
Precedence

Rule 19

The Chairman or Rapporteur of a committee, or the representative of a sub-committee or working group, may be accorded precedence for the purpose of explaining the conclusion arrived at by his committee, sub-committee or working group.

Points of Order

Rule 20

During the discussion of any matter a representative may rise to a point of order, and the point of order shall immediately be decided by the President in accordance with the rules of procedure. A representative may appeal against the ruling of the President. The appeal shall immediately be put to the vote and the President's ruling shall stand unless overruled by the majority of the representatives present and voting. A representative rising to a point of order may not speak on the substance of the matter under discussion.

Time-limit on Speeches

Rule 21

The Conference may on the proposal of the President limit the time to be allowed to each speaker on any particular subject under discussion. When the debate is limited and a representative has spoken for his allotted time, the President shall call him to order without delay.

Closing of List of Speakers

Rule 22

During the course of a debate the President may announce the list of speakers and, with the consent of the Conference, declare the list closed. He may, however, accord the right of reply to any representative if a speech delivered after he has declared the list closed makes this desirable.

Adjournment of Debate

Rule 23

During the discussion of any matter, a representative may move the adjournment of the debate on the question under discussion. In addition to the proposer of the motion, two representatives may speak in favour of, and two against, the motion, after which the motion shall immediately be put to the vote. The President may limit the time to be allowed to speakers under this rule.
Closure of the Debate

Rule 24

A representative may at any time move the closure of the debate on the question under discussion, whether or not any other representative has signified his wish to speak. Permission to speak on the closure of the debate shall be accorded only to two speakers opposing the closure, after which the motion shall be immediately put to the vote. If the Conference is in favour of the closure, the President shall declare the closure of the debate. The President may limit the time to be allowed to speakers under this rule.

Suspension or Adjournment of the Meeting

Rule 25

During the discussion of any matter, a representative may move the suspension or the adjournment of the meeting. Such motions shall not be debated, but shall be immediately put to the vote. The President may limit the time to be allowed to the speaker moving the suspension or adjournment.

Order of Procedural Motions

Rule 26

Subject to Rule 20, the following motions shall have precedence in the following order over all the other proposals or motions before the meeting:

(a) To suspend the meeting;
(b) To adjourn the meeting;
(c) To adjourn the debate on the question under discussion;
(d) For the closure of the debate on the question under discussion.

Basic Proposals

Rule 27

The draft Convention on international factoring and the draft Convention on international financial leasing, prepared by the International Institute for the Unification of Private Law, shall constitute the basic proposals for discussion by the Conference.

Other Proposals and Amendments

Rule 28

Other proposals and amendments thereto shall normally be introduced in writing and handed to the Executive Secretary of the Conference who shall circulate copies to the
delegations. As a general rule, no proposal or amendment shall be discussed or put to the vote at any meeting of the Conference unless copies of it have been circulated to all delegations not later than the day preceding the meeting. The President or Chairman of a Committee may, however, permit the discussion and consideration of amendments, even though these amendments and motions have not been circulated or have only been circulated the same day.

Decisions on Competence

Rule 29

Subject to Rule 20, any motion calling for a decision on the competence of the Conference to discuss any matter or to adopt a proposal or an amendment submitted to it shall be put to the vote before the matter is discussed or a vote is taken on the proposal or amendment in question.

Withdrawal of Motions

Rule 30

A motion may be withdrawn by its proposer at any time before voting on it has commenced, provided that the motion has not been amended or that an amendment to it is not under discussion. A motion which has thus been withdrawn may be reintroduced by any representative.

Reconsideration of Proposals

Rule 31

When a proposal has been adopted or rejected it may not be reconsidered unless the Conference, by a two-thirds majority of the representatives present and voting, so decides. Permission to speak on a motion to reconsider shall be accorded only to the mover and one other supporter and to two speakers opposing the motion, after which it shall be put immediately to the vote.

Invitation to Technical Advisers

Rule 32

The Conference may invite or admit to one or more of its meetings any person whose technical advice it may consider useful in its work.
CHAPTER VI - VOTING

Voting Rights

Rule 33

Each State represented at the Conference shall have one vote.

Required Majority

Rule 34

1. - Decisions of the Conference on all matters of substance shall be taken by a two-thirds majority of representatives present and voting, and decisions on matters of procedure shall be taken by a simple majority of representatives present and voting.

2. - If the question arises whether a matter is one of procedure or of substance, the President of the Conference shall rule on the question. An appeal against this ruling shall immediately be put to the vote and the President’s ruling shall stand unless overruled by a two-thirds majority of the representatives present and voting.

Meaning of the expression “Representatives present and voting”

Rule 35

For the purpose of these Rules the phrase “representatives present and voting” means representatives casting an affirmative or negative vote. Representatives abstaining from voting or casting an invalid vote shall be considered as not voting.

Method of Voting

Rule 36

The Conference shall normally vote by show of hands. However, any representative may request a roll-call vote which shall be taken in the English alphabetical order of the names of the States participating in the Conference, beginning with the delegation whose name is drawn by lot by the President. The vote of each representative participating in any roll-call vote shall be inserted in the summary record of the meeting concerned.

Conduct during Voting

Rule 37

After the President has announced the beginning of voting, no representative shall interrupt the voting except on a point of order in connection with the actual conduct of the voting. Except in the case of elections held by secret ballot, the President may permit representatives to explain their votes after the voting. The President may limit the time to be allowed for such explanations.
Division of Proposals and Amendments

Rule 38

1. - Parts of a proposal or amendment thereto shall be voted on separately if the President, with the consent of the proposer, so decides or if a representative requests that the proposal or amendment thereto be divided and the proposer raises no objection. If the proposer objects to a request for division, permission to speak on the request shall be given first to the representative making the request to divide the proposal or amendment, and then to the mover of the original proposal or amendment under discussion, after which the request to divide the proposal or amendment shall be put immediately to the vote.

2. - Where parts of a proposal or amendment thereto have been voted on separately, those parts of a proposal which have been approved shall then be put to the vote as a whole.

3. - If all the operative parts of the proposal or amendment have been rejected, the proposal or amendment shall be considered to have been rejected as a whole.

Voting on Amendments

Rule 39

1. - A motion is considered to be an amendment to a proposal if it merely adds to, deletes from or revises part of that proposal. An amendment shall be voted on before the proposal to which it relates is put to the vote.

2. - If two or more amendments are moved to a proposal, the Conference shall first vote on the amendment furthest removed in substance from the original proposal and then on the amendment next furthest removed therefrom and so on until all amendments have been put to the vote. Where, however, the adoption of one amendment necessarily implies the rejection of another amendment, the latter amendment shall not be put to the vote.

3. - The President shall, in all cases, determine which amendment is furthest removed in substance from a proposal or whether the adoption of an amendment necessarily implies the rejection of another amendment. An appeal against the President’s ruling shall immediately be put to the vote and the President’s ruling shall stand unless the appeal is approved by a majority of the representatives present and voting.

4. - If one or more amendments are adopted, the amended proposal shall then be voted upon.

Voting on Proposals

Rule 40

If two or more proposals relate to the same question, the Conference shall, unless it decides otherwise, vote on the proposals in the order in which they have been submitted.
Elections

Rule 41

All elections shall be held by secret ballot unless the Conference decides otherwise.

Rule 42

Before the commencement of a secret ballot two scrutineers shall be appointed by the Conference, on the proposal of the President, from the delegations present. The scrutineers shall scrutinise the votes cast and report the results to the President indicating the number of votes cast including invalid votes, if any.

Rule 43

1. - If, when one person or one delegation is to be elected, no candidate obtains on the first ballot a majority of the representatives present and voting, a second ballot restricted to the two candidates obtaining the largest numbers of votes shall be taken. If on the second ballot the votes are equally divided the President shall decide between the candidates by drawing lots.

2. - In the case of a tie on the first ballot among three or more candidates obtaining the largest numbers of votes, a second ballot shall be held. If on such a second ballot a tie results among more than two candidates, the number shall be reduced to two by lot and the balloting, restricted to those two, shall continue in accordance with the preceding paragraph of this Rule.

Rule 44

When two or more elective places are to be filled at one time under the same conditions, those candidates obtaining on the first ballot a majority of the representatives present and voting shall be elected. If the number of candidates obtaining such majority is less than the number of persons or delegations to be elected, there shall be additional ballots to fill the remaining places, the voting being restricted to the candidates obtaining the greatest numbers of votes in the previous ballot, to a number not more than twice the places remaining to be filled; provided that, after a third inconclusive ballot, votes may be cast for any eligible person or delegation. If three such unrestricted ballots are inconclusive, the next three ballots shall be restricted to the candidates who obtained the greatest numbers of votes on the third of the unrestricted ballots, to a number not more than twice the places remaining to be filled, and the following three ballots thereafter shall be unrestricted, and so on until the places have been filled.

Equally Divided Votes

Rule 45

If a vote is equally divided on matters other than elections, the proposal shall be regarded as rejected.
CHAPTER VII - COMMITTEES

Committees of the Whole

Rule 46

The Conference shall establish a Committee of the Whole to deal with the draft Convention on international factoring and a Committee of the Whole to deal with the draft Convention on international financial leasing.

Drafting Committee

Rule 47

A Drafting Committee, composed of not more than nine members, shall be appointed by the Conference on the proposal of the President. The Drafting Committee shall prepare drafts and give advice on drafting as requested by the Conference or by a Committee of the Whole. It shall also prepare the Final Act of the Conference. The Drafting Committee shall not alter the substance of texts submitted to it, but shall have the power to review and co-ordinate the drafting of all such texts. The Committee shall report as appropriate to the Conference or to a Committee of the Whole.

Establishment of other Committees and subsidiary bodies

Rule 48

The Conference may establish such other committees and subsidiary bodies as it deems necessary for the performance of its functions.

Representation on Committees and other subsidiary bodies

Rule 49

Each State participating in the Conference shall be represented by one person on each Committee of the Whole and on other subsidiary bodies to which that State may be appointed. It may assign to these committees or subsidiary bodies such alternate representatives and advisers as may be required.

Co-ordination by the Steering Committee

Rule 50

1. - The Steering Committee may meet from time to time to review the progress of the Conference and its Committees and other subsidiary bodies and to make recommendations for furthering such progress. It shall also meet at such other times as the Chairman deems necessary or upon the request of any other of its members.
2. - Questions affecting the co-ordination of their work may be referred by other Committees and subsidiary bodies to the Steering Committee, which may make such arrangements as it thinks fit, including the holding of joint meetings of Committees or sub-committees and the establishment of joint working groups. The Steering Committee shall appoint, or arrange for the appointment of, the Chairman of any such joint body.

Officers

Rule 51

Except in the cases of the Chairman of a Committee of the Whole and the Chairman of the Drafting Committee, each committee, sub-committee, or working group shall elect its own officers. A Committee of the Whole shall elect two Vice-Chairmen who shall be designated as first and second Vice-Chairman and take precedence in that order. A Committee of the Whole may elect a Rapporteur.

Quorum

Rule 52

A majority of the representatives on a committee or other subsidiary body shall constitute a quorum.

Conduct of business and voting in Committees and other subsidiary bodies

Rule 53

The rules relating to officers and conduct of business contained in Chapters II, IV, V, VI, VIII and X shall be applicable mutatis mutandis to the proceedings of committees and other subsidiary bodies, except that all decisions of committees or other subsidiary bodies shall be taken by a majority of the representatives present and voting. However, in the case of reconsideration of proposals or amendments in a committee or subsidiary body, the majority required shall be that established by Rule 31.

CHAPTER VIII - LANGUAGES AND RECORDS

Official and Working languages

Rule 54

1. - The official languages of the Conference shall be English and French.
2. - The official languages shall also be the working languages.
Interpretation from official languages

Rule 55

Speeches made at the Conference, its committees and other subsidiary bodies in one of the official languages shall be interpreted into the other.

Interpretation from other languages

Rule 56

Any representative may make a speech in a language other than an official language. In this case, that representative shall provide for interpretation into one of the official languages. Interpretation into the other official language by the Conference interpreters may be based on any such interpretation given in the first official language.

Summary Records

Rule 57

1. - The Secretariat shall prepare summary records of the plenary meetings and of the meetings of the Committees of the Whole. These summary records shall be distributed to the participants as soon as possible after the closing of the meeting to which they relate.

2. - The participants shall, within three days after the circulation of the summary record, inform the Secretariat in writing of any changes to their own statements that they wish to have made.

Languages of Documents and Summary Records

Rule 58

Conference documents and summary records shall be made available in the working languages.

CHAPTER IX - PUBLIC AND PRIVATE MEETINGS

Plenary meetings and meetings of Committees and subsidiary bodies

Rule 59

The plenary meetings of the Conference and meetings of Committees of the Whole shall be held in public unless the Conference decides otherwise. Meetings of other committees and other subsidiary bodies of the Conference shall be held in private unless the Conference decides otherwise.
Communiqués to the Press

Rule 60

At the close of any meeting a communiqué may be issued to the press through the Secretary-General of the Conference.

CHAPTER X - OBSERVERS FROM INTERGOVERNMENTAL AND NON-GOVERNMENTAL ORGANISATIONS

Rule 61

1. - Observers from intergovernmental and non-governmental Organisations invited to the Conference may participate, without the right to vote, in the deliberations of the Conference, its committees and other subsidiary bodies upon the invitation of the President or Chairman as the case may be.

2. - Technical advisers invited or admitted to any meeting of the Conference, its committees or other subsidiary bodies in accordance with Rule 32 may take part, without the right to vote, in the deliberations of the Conference, its committees or other subsidiary bodies upon the invitation of the President or Chairman as the case may be.

3. - Written statements submitted by invited intergovernmental and non-governmental Organisations and technical advisers may be distributed by the Secretariat to the delegations at the Conference.

4. - Observers from intergovernmental and non-governmental Organisations participating in the Conference shall register with the Secretariat.

CHAPTER XI - AMENDMENTS TO THE RULES OF PROCEDURE

Rule 62

These rules of procedure may be amended by a decision of the Conference taken by a majority of the representatives present and voting.

CHAPTER XII - SIGNATURE OF INSTRUMENTS

Rule 63

1. - The Final Act resulting from the deliberation of the Conference shall be submitted for signature by the delegations.

2. - Full Powers shall be required of each Representative or Alternate Representative who signs any convention or other international instrument which may be drawn up and opened for signature by the Conference.

3. - Full Powers shall be issued either by the Head of State or Head of Government, or by the Minister for Foreign Affairs.
DRAFT CONVENTION ON
INTERNATIONAL FINANCIAL LEASING

PREAMBLE

THE STATES PARTIES TO THIS CONVENTION,

RECOGNIZING the importance of removing certain legal impediments to the international financial leasing of equipment, while maintaining a fair balance of interests between the different parties to the transaction,

AWARE of the need to make international financial leasing more available to developing countries,

CONSCIOUS of the fact that the rules of law governing the traditional contract of hire need to be adapted to the distinctive triangular relationships created by the financial leasing transaction,

RECOGNIZING therefore the desirability of formulating certain uniform rules relating primarily to the civil and commercial law aspects of international financial leasing,

HAVE AGREED as follows:

CHAPTER I - SPHERE OF APPLICATION

Article 1

1. - This Convention governs a financial leasing transaction as defined in paragraph 2 of this article in which one party (the lessor)

(a) on the specifications of, and on terms approved by, another party (the lessee), enters into an agreement (the supply agreement) with a third party (the supplier) under which the lessor acquires plant, capital goods or other equipment (the equipment) and

(b) enters into an agreement (the leasing agreement) granting to the lessee the right to use the equipment in return for the payment of rentals.

2. - The financial leasing transaction referred to in the previous paragraph is a transaction which includes the following characteristics:

(a) the lessee specifies the equipment and selects the supplier without relying primarily on the skill and judgment of the lessor;

(1) Text adopted by the Unidroit committee of governmental experts for the preparation of a draft Convention on international financial leasing at its third session (Rome, 30 April 1987).
(b) the equipment is acquired by the lessor in connection with a leasing agreement which, to the knowledge of the supplier, either has been made or is to be made between the lessor and the lessee; and

(c) the rentals payable under the leasing agreement are calculated so as to take into account in particular the amortisation of the whole or a substantial part of the cost of the equipment.

3. - This Convention does not apply to a transaction in which the equipment is to be used primarily for the lessee's personal, family or household purposes.

Article 2

1. - This Convention applies when the lessor and the lessee have their places of business in different States and when:

(a) those States and the State in which the supplier has its place of business are Contracting States; or

(b) both the supply agreement and the leasing agreement are governed by the law of a Contracting State.

2. - For the purposes of this article, if a party to the supply agreement or the leasing agreement has more than one place of business, the place of business is that which has the closest relationship to that agreement and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that agreement.

Article 3

This Convention applies whether or not the lessee has or subsequently acquires the option to buy the equipment or to hold it on lease for a further period, and whether or not for a nominal price or rental.

CHAPTER II - RIGHTS AND DUTIES OF THE PARTIES

Article 4

The supply agreement may not be varied without the consent of the lessee.

Article 5

1. - The lessor's real rights in the equipment shall be valid against the lessee's trustee in bankruptcy and creditors, including creditors who have obtained an attachment or execution.

2. - Where by the applicable law the lessor's real rights in the equipment are valid against a person referred to in the previous paragraph only on compliance with rules as to public notice, those rights shall be valid against that person only where they are valid according to such rules.
3. - For the purposes of the previous paragraph the applicable law is:

(a) [in the case of ships, aircraft, vehicles or other equipment subject to registration pursuant to the law of a State, the law of the State of registration];\(^{(2)}\)

(b) in the case of all other [mobile] equipment [normally used in more than one State], the law of the State where the lessee has its principal place of business; and

(c) in the case of all other equipment, the law of the State where the equipment is situated at the time when the person referred to in paragraph 1 is entitled to invoke the rules referred to in paragraph 2.

4. - This article shall not affect the rights of any creditor having a lien on or a security interest in the equipment.

Article 6

Any question whether or not the equipment has become a fixture to or incorporated in land, and if so the effect on the rights inter se of the lessor and a person having real rights in the land shall be determined by the law of the State where the land is situated.

Article 7

1. - (a) Except as otherwise provided by this Convention or the leasing agreement, the lessor shall not incur any liability to the lessee in respect of the equipment save to the extent that it has intervened in the selection of the supplier or the specifications of the equipment.

(b) The lessor shall not, in its capacity of lessor, be liable to third parties for any personal injury or damage to property caused by the equipment.

(c) The above provisions shall not govern any liability of the lessor in any other capacity, for example as owner.

[Alternative I

2. - The lessor warrants that the lessee’s quiet possession will not be disturbed by a person who has a superior title or right, or who claims a superior title or right and acts under the authority of the court, where such title, right or claim is not derived from any act or omission of the lessee.]

[Alternative II

2. - The lessor warrants that the lessee’s quiet possession will not be disturbed by a person who has a superior title or right, or who claims a superior title or right and acts under the authority of the court, where such title, right or claim is derived from an act or omission of the lessor.

\(^{(2)}\) It was agreed by the committee of governmental experts that the provisions of Article 5(3)(a) should be examined in advance of the diplomatic Conference by a working group of technical experts to be convened by Unidroit in order to see whether the solution proposed by the committee would be workable in practice. Cf. report of this working group at p. 123 infra.
3. - The previous paragraph does not affect any broader warranty of quiet possession by the lessor under the applicable law.]

**Article 8**

1. - The lessee shall take proper care of the equipment, use it in a manner consistent with that of a normal user and keep it in the condition in which it was delivered, subject to fair wear and tear.

2. - When the leasing agreement comes to an end the lessee, unless exercising its right to buy the equipment or to hold the equipment on lease for a further period, shall return the equipment to the lessor in the condition specified in the previous paragraph.

**Article 9**

1. - The duties of the supplier under the supply agreement shall also be owed to the lessee as if it were a party to that agreement and as if the equipment were to be supplied directly to the lessee.

2. - Nothing in this article shall entitle the lessee to terminate or rescind the supply agreement.

**Article 10**

1. - The lessee shall have the right, as against the lessor, to reject the equipment:

   (a) if the equipment fails to conform to the terms of the supply agreement; or

   (b) if the supplier fails to tender delivery within a reasonable time after the delivery date stipulated in the leasing agreement or, if none, that stipulated in the supply agreement or, in the absence of any stipulation as to date, within a reasonable time after the making of the leasing agreement.

2. - The right to reject non-conforming equipment shall be exercised by notice to be given to the lessor within a reasonable time after the lessee has discovered the non-conformity or ought to have discovered it. Rejection for non-conformity of the equipment under the supply agreement shall not preclude a fresh tender of the same equipment or a tender of other equipment in conformity with that agreement if made within a reasonable time after notice to reject.

3. - The lessee shall lose its right to reject the equipment where, if the equipment had been supplied to it as buyer, it would have lost the right to reject.

4. - Where the lessee has rejected the equipment in accordance with this article and the supplier has failed to make a fresh tender of the same equipment or a tender of other equipment in accordance with paragraph 2 of this article, the lessee shall be entitled to terminate the leasing agreement, meanwhile having the right to withhold rentals payable thereunder, and to recover any rentals and other sums paid in advance. Nevertheless, the lessee shall be obliged to pay the lessor a reasonable sum for the benefit the lessee has derived from the equipment.
5. - The lessee shall have no other claim against the lessor for non-delivery, delay in delivery or delivery of non-conforming equipment except to the extent to which this results from the act or omission of the lessor.

Article 11

1. - In the event of default by the lessee, the lessor may recover accrued unpaid rentals, together with interest.

2. - Where the lessee’s default is substantial, then subject to paragraph 5 of this article the lessor may also terminate the leasing agreement and after such termination may:
   (a) recover possession of the equipment; and
   (b) recover such compensation as will place the lessor in the position in which it would have been had the lessee performed the leasing agreement in accordance with its terms, except in so far as the lessor has failed to take all reasonable steps to mitigate its loss.

3. - The leasing agreement may provide for the manner in which the compensation referred to in paragraph 2 (b) of this article is to be computed and such provision shall be enforceable between the parties unless such compensation is disproportionate to the compensation provided for under paragraph 2 (b).

4. - Where the lessor has terminated the leasing agreement it shall not be entitled to enforce a term of the leasing agreement accelerating payment of the rentals.

5. - The lessor shall only be entitled to terminate the leasing agreement or accelerate payment of the rentals if it has by notice given the lessee a reasonable opportunity of remedying the default so far as the same may be remedied.

Article 12

1. - The lessor may transfer or otherwise deal with all or any of its rights in the equipment or under the leasing agreement. Such a transfer shall not relieve the lessor of any of its duties under the leasing agreement or alter either the nature of the leasing agreement or its legal treatment as provided in this Convention.

2. - The lessee may transfer the right to the use of the equipment or any other rights under the leasing agreement only with the consent of the lessor and subject to the rights of third parties.

Article 13

1. - This Convention applies in relation to a financial sub-leasing transaction as if the sub-lessee were the lessee, the sub-lessee were the lessee and the supplier from whom the lessor acquired the equipment were the supplier.

2. - In the case of a series of transactions involving the same equipment which includes more than one financial leasing transaction, this Convention applies as if the last financial lessor were the lessor and as if the supplier from whom the first financial lessor acquired the equipment were the supplier.
CHAPTER III - GENERAL PROVISIONS

Article 14

[1. - This Convention shall not apply where it is excluded either by the terms of the supply agreement or by the terms of the leasing agreement.

2. - The parties may, in their relations with each other, derogate from or vary this Convention except for the provisions of Article[s 7(2), 11(3) and (4)].

Article 15

1. - In the interpretation of this Convention, regard is to be had to its object and purpose as set forth in the Preamble, to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.

2. - Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based and in conformity with the law applicable by virtue of the rules of private international law.

EXPLANATORY REPORT
on the
DRAFT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING
prepared by the Unidroit Secretariat

I

BACKGROUND TO THE DRAFT CONVENTION

1. - Unidroit’s work on this draft Convention goes back to February 1974 when the 53rd session of the Unidroit Governing Council was seized of a proposal from the Unidroit Secretariat recommending the preparation of a preliminary study looking into the desirability and feasibility of drawing up uniform rules on leasing. The Governing Council agreed to this proposal, giving the topic priority status on Unidroit’s work programme for the 1975-77 triennium and empowering the President of Unidroit to convene a working group to study an international unification of the applicable rules on the subject.

2. - The preliminary report prepared by the Unidroit Secretariat pursuant to this decision was considered by a small working group of the Governing Council (1) which met in Rome on

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(1) The members of this group, all members of the Unidroit Governing Council at the time, were: Mr Richard D. KEARNEY, Ambassador, Deputy Legal Adviser to the Department of State of the United States of America; Mr Tudor R. POPESCU, Professor of Law in the University of Bucharest; Mr Jean Georges SAUVEPLANNE, Professor of Law in the University of Utrecht and Mr Benjamin A. WORTLEY, Professor of Law in the University of Manchester.
21 April 1975 to examine the feasibility of drawing up uniform international rules on the leasing contract. This group made a number of policy recommendations: first, to exclude real estate leasing from the scope of the proposed exercise, because of what was seen as the limited incidence of such operations at the international level and the enormous difficulties that would obtrude in any attempt to unify principles of the law of real property and the law of personal property in the same text; secondly, to exclude the leasing of ships, because of the special nature of the contract involved, which was considered to have more in common with charters; thirdly, to exclude the leasing of aircraft, also because of the special characteristics of the contract involved and in view of the study then underway within the International Civil Aviation Organization (I.C.A.O.) of the problems arising out of the lease of aircraft in international operations; fourthly, not to limit the scope of the work proposed to the tripartite financial leasing transaction but, for the time being at least, to envisage also the bilateral operating lease; fifthly, not to attempt, in view of the enormous difficulties that would be involved, any uniformisation of the law pertaining to exclusively domestic leasing operations but rather to address specifically international leasing. The working group finally recommended the circulation of the Secretariat’s report amongst experts with a request for comments and the gathering of further information on the precise nature of international leasing transactions.

3. - Following the endorsement of these recommendations by the Governing Council at its 54th session in April 1975, the Secretariat sent out a questionnaire to leasing operators and experts the world over, designed both to clarify certain legal problems peculiar to leasing transactions in general and to throw light on cross-border leasing in particular. Replies came in from all four corners of the world and were analysed by the Secretariat in a paper submitted to the Governing Council at its 55th session in September 1976. One of the major facts to emerge from this inquiry, as has been indicated above, was that the successful mounting of truly cross-border leasing transactions, as opposed to indirect international leasing transactions concluded through subsidiaries of the lessor incorporated in the country into which the latter wished to lease or by means of joint ventures, was still a rare occurrence, even if the sums involved in the small number of transactions actually mounted successfully were enormous, and that this was in no small measure due to the varying legal treatment accorded leasing from one country to another. Interest among those responding to the questionnaire leaned accordingly more towards a uniform international regulation of the rules governing leasing transactions in general rather than rules cast with international leasing specifically in mind. The primary purpose of the drafting of uniform rules was therefore seen as the resolution of the legal vacuum affecting leasing at the domestic level with a view to facilitating and thereby extending the possibilities for the use of this means of financing international trade.

4. - Twin doubts nevertheless persisted in the minds of members of the Governing Council regarding the aptness of this subject for unification, as regards first the feasibility of disentangling the private law aspects of leasing from its fiscal aspects, given the generally agreed unsuitability of the latter for an attempt at unification, all the more so in the same text as its private law aspects, and, secondly, the desirability of dealing with leasing separately from the general body of security interests in movables, a subject then being studied by the United Nations Commission on International Trade Law (UNCITRAL). In order to clarify these
doubts the Governing Council set up a restricted exploratory working group (2) drawn from amongst its own membership but assisted by consultant experts from the world of leasing practice. The working group gave positive answers to both questions when it met in Rome from 16 to 18 March 1977. As regards the first problem, it was of the opinion that, notwithstanding the considerable importance of fiscal considerations in specifically international leasing transactions, there was a *sui generis* derivation of private law in tripartite financial leasing which merited the framing of special rules cast with its particular characteristics in mind and that it would be possible in the drafting of such rules to steer clear of those aspects of leasing which rather fell within the competence of the revenue authorities, the philosophies underlying revenue law and private law being quite distinct. As regards the second problem, the group felt that it was perfectly feasible to formulate a legal framework around the *sui generis* leasing transaction without such a definition bringing the transaction automatically under the scope of Article 9 of the Uniform Commercial Code of the United States of America and similarly inspired security interest legislation. In particular, security interests being closely tied to an underlying sale contract, the only potential security interest in the *sui generis* type of financial leasing would be the purchase money security interest relating to the sale contract between supplier and lessor. The relationship between lessor and lessee under the leasing agreement itself, on the other hand, did not establish a security interest so long as no transfer of title took place.

5. - The working group accordingly recommended to the Governing Council that a study group should be set up with the assignment of drafting international uniform rules on the *sui generis* type of leasing transaction. It was felt that international uniform rules would realise a dual advantage in making it possible to leave the choice of the final form which the rules would take until a later stage, leaving open both the possibility that they be used to clarify the situation at the domestic level and the possibility that they be addressed to specifically international situations. The group also made a preliminary examination of the ground to be covered in the uniform rules, concluding with a number of policy recommendations to the Governing Council, among which the following may be singled out as being worthy of special mention:

(i) Clear concepts should be employed in the uniform rules so as to avoid an *a posteriori* classification of a lease as contemplated by the uniform rules under some quite different schema.

(ii) The principal aim of the uniform rules should be to regulate the tripartite leasing transaction in view of its *sui generis* characteristics in relation to the existing schemata with one or other of which it had hitherto generally been assimilated. Bipartite leasing operations should only find a place in the uniform rules to the extent that such operations did not fit within the schema of a nominate contract.

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(2) The Chairman of this group was Mr László RÉCZEI, Ambassador, Professor of Law in the University of Budapest, member of the Unidroit Governing Council (Hungary). Its members were: Mr Jean Georges SAUVEPLANNE, Professor of Law in the University of Utrecht, member of the Unidroit Governing Council; Mr Detlev F. VAGTS, Professor of Law in the University of Harvard, Counsellor on International Law to the Department of State of the United States of America, representative of Mr Richard D. Kearney, member of the Unidroit Governing Council (see *supra*, footnote 1). Mr Fritz PETER, Honorary Chairman of Leaseurope, served as expert consultant to the group, which was moreover assisted by: Mr Paolo CLAROTTI, Head of the Banking Division at the Commission of the European Communities, and Mr Augusto PANTOZZI, Professor of Revenue Law in the University of Rome.
(iii) Leasing could be defined negatively for the purposes of the uniform rules as neither a credit transaction nor a sale nor a financing transaction, but rather a special form of rental providing for the use of goods. The definition of leasing to be devised in such uniform rules could be based either on an identification of those characteristics which differentiated leasing from the existing contractual schemata with which it had hitherto been bracketed or on an enumeration of the requirements to be fulfilled before a transaction could be considered a leasing transaction for the purposes of the uniform rules, in the manner of the definition of "bill of exchange" in the 1930 Geneva Convention on Bills of Exchange and Promissory Notes, or else on an amalgam of the two.

(iv) The scope of the uniform rules should be limited to capital goods, thus to the exclusion of consumer transactions.

(v) The parties to the transaction should be professional parties and the item leased should have been leased for professional purposes only.

(vi) There was a case for excluding the leasing of aircraft, ships and rolling stock from the scope of the uniform rules, on the basis of the arguments advanced in the previous small working group of the Governing Council.

(vii) The leasing agreement to be addressed in the uniform rules should cover the use of an item leased for a length of time corresponding to its economic working life.

(viii) The lessor should remain the owner of the item leased, whatever agreements might be made with regard to the termination of the leasing agreement.

(ix) The lessee should not be obliged to purchase the item leased at the expiry of the leasing agreement, whereas equally the parties should be left free to include an option to purchase the item leased in the leasing agreement.

(x) Unless the contract provided otherwise, the lessee should have a direct right of action against the supplier in the event of the item leased not proving to be in conformity with the specifications given by the lessee.

(xi) The lessee should bear the physical risks arising in connection with the item leased, in view of the special situation obtaining in tripartite financial leasing. The general rule of the law of products liability according to which a lessor would be liable qua owner for any damage caused to a third party by the item leased should not apply to the special situation of the lessor in tripartite financial leasing.

(xii) Some means of protection of third party creditors of the lessee should be found, be it only in the form of a minimum requirement laying down the principle of registration but leaving the modalities of registration to be established by each country.

6. - The working group’s recommendation that a study group should be set up was endorsed by the Governing Council at its 56th session in May 1977. This study group, manned by eminent experts from legal and economic systems as diverse as those of Belgium, Brazil, France, Hungary, Italy, the Netherlands, Nigeria, Switzerland, the United Kingdom, the United States of America and Yugoslavia, held four sessions in Rome, from 17 to 19 November 1977, on 1 and 2 February 1979, from 30 September to 2 October 1980 and from 27 to 30 March 1984. The Study Group elected Mr László Récezi, Professor of Law in the University of Budapest and
at that time a member of the Unidroit Governing Council, as its chairman. Mr Réczei chaired all four sessions of the Study Group.

7. - The first session of the Study Group was devoted to consideration of a list of questions drawn up by the Unidroit Secretariat and the definition of equipment leasing agreed upon after many years of debate by Leaseurope at its annual working meeting in Oslo that same year. The list of questions was designed to pinpoint the matters to be dealt with in the uniform rules. On the basis of the Leaseurope definition the Study Group was moreover able to draw up a provisional draft definition of the *sui generis* form of equipment leasing generally known as financial leasing, on which it had decided to concentrate its attention. Two other significant policy decisions were taken at this first session, to wit, first, that the Study Group should seek to provide rules for leasing operations in general rather than address specifically international leasing situations, given that there could be no solution to the problems bedevilling the development of international leasing so long as there remained no solution to the problems bedevilling leasing at the national level, and, secondly, that aircraft, ships and rolling stock should be included in the general scope of the uniform rules.

8. - The provisional draft definition agreed at the first session of the Study Group provided the starting point for the tentative draft uniform rules on the *sui generis* form of leasing

(3) The members of the Study Group, with the sessions they attended indicated in brackets, were: Mr Luiz Olavo BAPTISTA, President of the São Paulo Bar Association and Professor of International Commercial Law at the Getulio Vargas Foundation, São Paulo(3); Mr El Mokhtar BEY, Directeur juridique et du contentieux juridictionnel with the Locafrance Group, Paris(1)(2)(3)(4); the late Mr Peter F. COOGAN, of Counsel, Messrs Murphy, Weir and Butler, San Francisco(1)(3)(4); Mr Ronald M. DEKOVEN, Attorney, Messrs Shearman and Sterling, New York(3)(4); Mr Giorgio DE NOVA, Professor of Civil Law in the University of Pavia(4); Mr Christian GAVAELDA, Professor of Commercial and Banking Law and Director of the Business Law Research Centre in the University of Paris I, Panthéon-Sorbonne(1)(3); Mr Royston M. GOODE, Crowther Professor of Credit and Commercial Law and Director of the Centre for Commercial Law Studies in Queen Mary College, University of London(1)(2)(3)(4); Ms Tinuade OYEKUNLE, Director, International and Comparative Law Division, Federal Nigerian Ministry of Justice, Lagos(2)(3)(4) and Mr Fritz PETER, Chairman of the Board of Directors of Industrie-Leasing AG, Zurich and Honorary Chairman of the European Federation of Equipment Leasing Company Associations (Leaseurope)(1)(2)(3)(4), who also served as consultant expert to the Study Group. The following observers also attended one or more sessions of the Study Group: Mr Massimo ALDERIGHI, Attorney, Studio Legale Tributario A. Fantozzi-L. Biscozzi, Rome(3); Mr Sergio BIANCONI, Deputy Head of the Legal Service, Italian Banking Association, representing the Banking Federation of the European Community(3); Ms Caroline BILLILOUD DE NUZILLET, Attaché, Legal Secretariat, International Chamber of Commerce, Paris(2); Mr Jesús BLANCO CAMPANÁ, Legal Adviser to the Spanish Ministry of Justice and Professor of Law in the University of Madrid(1); Mr Franco CAVALLARI, Branch Deputy Director, Banca Nazionale del Lavoro, Direzione Generale, Ufficio Studi, Rome(3); Mr Renato CLARIZIA, Professor of Law in the University of Urbino and Secretary-General of the Italian Leasing Association (Assilea), Rome(3)(4); Ms Mireille DUSEAUX, Principal Administrator, Directorate-General XV (Financial Institutions and Fiscal Matters), Commission of the European Communities(1)(2)(3)(4); Mr Augusto FANTOZZI, Professor of Revenue Law in the University of Rome(1)(2); Mr Paolo FERRO LUZZI, Professor of Commercial Law in the University of Perugia(3); Mr Mario GIOVANOLI, representing the Bank for International Settlements(4); Mr Sanford G. HENRY, international leasing consultant, London(2)(3)(4); the late Mr Matthias H. van HOOGSTRATEN, then Secretary-General of the Hague Conference on Private International Law(1); Mr Salvatore MACCARONE, Legal Adviser to the Italian Banking Association, representing the Banking Federation of the European Community(3); Mr Michel PELICHET, Deputy Secretary-General of the Hague Conference on Private International Law(3)(4); Ms Jelena VILUS, Professor of International Commercial Law in the University of Novi Sad, Yugoslavia(2).
transaction that were drawn up subsequently by the Unidroit Secretariat in tandem with the Chairman of the Study Group. For the other articles of this tentative draft the drafters sought to follow the general lines of the answers given by the Study Group to the aforementioned list of questions which it had considered at its first session. The provisions on public notice were, on the other hand, modelled on the equivalent provisions of the Uniform Commercial Code and the similarly inspired Personal Property Security Act of Ontario of 1967.

9. - This tentative draft was considered by the Study Group at its second session. Various proposals were put forward for its amendment at that session, notably regarding what was considered to be too detailed a public notice requirement for an intended international instrument. These proposals provided the inspiration for the subsequent work of revision carried out by the Unidroit Secretariat.

10. - This revised text was then the subject of consultation both among the members of the Study Group and within a working group set up by Leaseurope. This process of consultation yielded alternative revised texts, on the one hand, from two members of the Study Group and, on the other hand, from the Leaseurope working group. A third alternative revised text was then drawn up by the Unidroit Secretariat in tandem with the Chairman of the Study Group in an effort to reconcile the different trends evidenced in these various alternatives. A preamble was added to the original draft in accordance with the wish expressed by the Study Group at its second session that it should be made clear that the uniform rules were only designed to deal with the private law aspects of leasing and did not presume to invade the specific competence normally reserved by the legislator in respect of the fiscal and accounting aspects of leasing.

11. - The alternative revised drafts were considered by the Study Group at its third session. At this session the Group was able, subject to some drafting improvements which it was agreed could be worked out between the different members of the Study Group, to adopt a set of preliminary draft uniform rules on the sui generis form of leasing transaction. While the title of the draft still referred to uniform rules, underlining the original intention of the drafters to approach the problem from the angle of seeking to remove the differences in legal treatment existing from one jurisdiction to another, seen as one of the major obstacles to international leasing’s realisation of its full potential, the preamble and the scope of application provisions were couched in the form of a draft international Convention and the uniform rules addressed specifically international leasing situations. This change of approach was prompted, on the one hand, by recognition of the reluctance of certain States to become parties to international instruments in respect of any other than international transactions and, on the other hand, by the desire to indicate the Study Group’s opinion that the uniform rules’ greatest chance of success lay with their embodiment in an international Convention, the feeling being that a model law would not greatly improve the present situation of considerable differences of legal treatment of leasing from one jurisdiction to another.

12. - The Study Group, in adopting the text of preliminary draft uniform rules, recommended that, instead of following the usual course of transmitting the text prepared by the Study Group directly to a committee of governmental experts for the hammering out of a final text for adoption at a diplomatic Conference, the Unidroit Governing Council should rather first give the uniform rules maximum exposure among the businessmen and legal practitioners familiar with the everyday realities of leasing, inter alia by the organisation of symposia in different parts of the world. The purpose of these symposia would be to enable the text to be
presented to and discussed by practitioners. The unripeness of the uniform rules for consideration by governmental experts pending such time as they had been given such exposure among practitioners was considered to flow principally from two, not wholly unrelated factors: first, the continuing sparseness of attempts at the domestic level to legislate in this field and, secondly, the continuing evolution of the leasing mechanism in view of its well proven flexibility to meet constantly newly appearing market needs. Since this continuing process of evolution was largely the work of the denizens of the financial and business worlds, it was considered desirable to sound first the opinion of those responsible for this ongoing evolutionary process, in order to ascertain whether and to what extent the solutions advanced by the preliminary draft uniform rules were consonant with the realities of leasing practice.

13. - The Unidroit Governing Council at its 60th session in April 1981 endorsed this recommendation of the Study Group for the holding of symposia designed to give exposure to the uniform rules and the first in what was envisaged as a programme of symposia was held in New York on 7 and 8 May 1981. This symposium was sponsored by the American Law Institute-American Bar Association Committee on Continuing Professional Education. The audience assembled in New York was essentially composed of bankers, businessmen and practising lawyers having expertise in international leasing, mostly from the United States but also including some who had journeyed from Europe. Invitational in character, the symposium was structured in such a way as to permit a panel of speakers, largely made up of members of the Study Group,\(^{4}\) to introduce the provisions of the preliminary draft uniform rules and the audience to raise questions and indicate any criticism.

14. - The second in the programme of symposia, sponsored by Industrie-Leasing AG, the leasing subsidiary of the Swiss Bank Corporation and held in Zürich on 23 and 24 November 1981,\(^{5}\) was addressed essentially to an audience of Western and Eastern European bankers, businessmen and practising lawyers, although some participants came from further afield, from Egypt for instance.

15. - Presentation of the uniform rules to, and discussion thereof among a numerous Far Eastern audience were also possible at the First World Leasing Convention, organised by Leasing Digest Conferences in conjunction with the Hong Kong Equipment Leasing Association in Hong Kong from 10 to 12 January 1983.\(^{6}\)

\(^{4}\) In New York the panel of speakers was made up as follows: Co-chairmen: Mr Peter F. COOGAN, member of the Study Group; Mr Ronald M. DEKOVEN, member of the Study Group; Members: Mr E. Allan FARNSWORTH, Professor of Law, Columbia University, New York, member of the Unidroit Governing Council; Mr Roy M. GOODE, member of the Study Group; Mr Kraig KLOSSON, Chairman, International Committee, American Association of Equipment Lessor; Mr Peter H. PFUND, Assistant Legal Adviser for Private International Law, Department of State of the United States of America; Mr László RÉCZEI, Chairman of the Study Group; Mr Martin J. STANFORD, Secretary to the Study Group; Mr Detlev F. VAGTS, member of the restricted working group of the Unidroit Governing Council on the leasing contract.

\(^{5}\) The panel of speakers in Zürich was made up as follows: Chairman: Mr Fritz PETER, consultant expert to the Study Group; Members: Mr El Mokhtar BEY, member of the Study Group; Mr Tom M. CLARK, then Chairman of Leasseurope; Mr Peter F. COOGAN (see supra); Mr Ronald M. DEKOVEN (see supra); Mr Roy M. GOODE (see supra); Mr Michel PELICHET, observer of the Study Group; Mr László RÉCZEI (see supra); Mr Peter SEIFFERT, lawyer with Deutsche Anlagen-Leasing GmbH, Mainz; Mr Martin J. STANFORD (see supra).

\(^{6}\) Presentation of the uniform rules in Hong Kong was in the hands of Mr Ronald M. DEKOVEN (see supra), with additional information being supplied by Mr Martin J. STANFORD (see supra).
16. - Further presentation and discussion of the uniform rules was also possible at the seminar on international equipment leasing organised for French-speaking African lawyers by the International Development Law Institute in Rome from 6 to 17 February 1984.\(^{(7)}\)

17. - The Unidroit Secretariat in the meantime employed its best offices to ensure that the uniform rules received the maximum exposure world wide by the publication of regular articles thereon in the annual editions of the World Leasing Yearbook from 1980 onwards and, where possible, in the press.\(^{(8)}\) Regular and close ties of co-operation have at all stages of Unidroit’s work on this subject been maintained with the national, supranational and regional associations and federations representative of the leasing industry, most notably Leaseurope,\(^{(9)}\) the Asian Leasing Association, the American Association of Equipment Lessors and the Federación Latino Americana de Leasing (Felalease). On 12 June 1984 the Italian Finance Houses Association (Associazione Tecnica delle Società Finanziarie di Leasing e di Factoring), in conjunction with the law journal “Nuovi Investimenti”, organised a one-day seminar on the Unidroit draft in Milan. The audience, made up of Italian leasing specialists, was thus able to hear presentation of the draft and make such criticism and comments as it saw fit.\(^{(10)}\)

18. - At its fourth session the Study Group considered the case for the amendments proposed during the course of the programme of symposia and gave especial attention to the improvement of the drafting of the text. It had before it a revised version of the text adopted in October 1980 which had been prepared in Budapest in December 1983 by the Unidroit Secretariat in tandem with the Chairman of the Study Group. The aim of this revision was to give effect to the proposals for the amendment of the uniform rules made during the programme of symposia and other meetings. The major decisions taken at the final session of the Study Group were, apart from that of rejecting a proposal made at the New York symposium for the widening of the scope of the uniform rules to embrace bilateral leasing arrangements, in particular operating leases, first, to reintroduce that provision which had maintained its place right through the Study Group’s work prior to the symposia and which sought to highlight the financial nature of the sui generis type of lease by indicating that the duration of the leasing agreement took account of the period of amortisation of the leased asset (Article 1 (2)(d) of the text adopted in October 1980); secondly, the deletion of Article 2 of the text adopted in October 1980,\(^{(11)}\) a provision that had aroused much criticism on the occasion of the symposia, mainly

\(^{(7)}\) Presentation of the uniform rules was this time in the hands of Mr Martin J. STANFORD (see \textit{supra}) as Technical Coordinator of, and Visiting Instructor at the seminar.


\(^{(9)}\) Unidroit was twice, in 1976 in Munich and in 1982 in Amsterdam, given the opportunity to address annual working meetings of Leaseurope on the subject of the uniform rules.

\(^{(10)}\) On this occasion presentation of the uniform rules was in the hands of Mr Riccardo MONACO, then Secretary-General of Unidroit; Mr Giorgio DE NOVA, member of the Study Group and Mr Martin J. STANFORD (see \textit{supra}).

\(^{(11)}\) The text of Article 2 as adopted by the Study Group in October 1980 with subsequent modifications incorporated, with the agreement of the members of the Study Group, in the text published in March 1981 read as follows:

"Where a transaction is regarded as being subject to this Convention according to (a) the law of the State in which the leasing agreement was concluded or (b) the proper law of that agreement as determined by the rules of private international law of the forum, such a transaction shall also be regarded as being subject to this Convention in any other Contracting State."
on account of what was considered to be its obscure drafting, but which sought to ensure that once a given transaction was regarded as subject to the uniform rules under the law of the State in which the leasing agreement was concluded or under the proper law of that agreement, then it was automatically subject to the uniform rules in any other Contracting State; thirdly, the deletion of Variant II of Article 4 of the text adopted in October 1980 (12) following much criticism of that variant during the symposia on the ground that it would put the risk of loss of title too heavily on the lessor; fourthly, the introduction of a clause requiring the lessor to elect between the exercise of the remedies given it under the then Article 12 (1) of the uniform rules and the benefit of a clause accelerating its entitlement to all or any of the lease rentals upon the lessee’s default; fifthly, the introduction of an article by now common in international commercial law Conventions designed to ensure, on the one hand, that the uniform rules were interpreted in accordance with their international uniform character and not on the basis of the legal principles and traditions of the legal system of the judge or arbitrator called upon to decide a given case and, on the other hand, the observance of good faith.

19. - The preliminary draft uniform rules on international financial leasing as adopted by the Study Group at its fourth session were then, in accordance with Unidroit tradition, submitted for approval to the Governing Council at its 63rd session held in May 1984. This approval was given and the Council accordingly authorised the convening of a committee of government experts to hammer out the text of a draft Convention suitable to be submitted for adoption to a diplomatic Conference.

20. - Three sessions of this committee were held in Rome from 15 to 19 April 1985, from 14 to 18 April 1986 and from 27 to 30 April 1987. 40 Unidroit member States, (13) five non-member States, (14) six intergovernmental organisations, (15) two international non-governmental organisations, (16) three international professional associations (17) and five national professional associations (18) were represented in the committee’s work. Mr László Réczei, the representative of Hungary, was again elected chairman. Mr Royston M. Goode, a representative of the United Kingdom, was elected deputy chairman and chairman of the drafting

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(12) The text of Article 4, Variant II as adopted in October 1980 read as follows:

"The lessor’s title to the equipment shall be enforceable against all third parties provided that the lessor has complied with such rules (if any) as to public notice as may be prescribed by the law of the State of the lessee’s principal place of business. [Where the lessor has not so complied or where there are no such rules, its title is not enforceable against a person acquiring an interest in the equipment, by attachment or otherwise, unless the lessor proves that this interest was acquired in bad faith.]"

(13) Argentina, Australia, Austria, Belgium, Bulgaria, Canada, Chile, People’s Republic of China, Colombia, Denmark, Egypt, Finland, France, Federal Republic of Germany, Greece, Holy See, Hungary, India, Iran, Ireland, Italy, Japan, Korea, Luxembourg, Mexico, Netherlands, Nigeria, Norway, Poland, Portugal, Romania, San Marino, South Africa, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States of America, Venezuela.

(14) Algeria, Brazil, Peru, Philippines, Senegal.


(16) Banking Federation of the European Community, International Chamber of Commerce.

(17) European Federation of Equipment Leasing Company Associations (Leaseurope), Federation of Latin American Leasing Companies (Felalease), World Leasing Council.

committee. A drafting committee was set up at the first session of the committee of governmental experts. At the first session this drafting committee was manned by the chairman of the committee of governmental experts and the representatives of France and the United Kingdom, whereas at the second and third sessions it was enlarged to take in also one representative each from the delegations of Belgium, China, Finland and the United States of America. The committee of governmental experts gave the text adopted by the Study Group three readings as a result of which, at its final sitting on 30 April 1987, it was able, subject to reservations regarding certain provisions which it was agreed should be placed in square brackets for decision at the diplomatic Conference, to adopt the text of the draft Convention on international financial leasing set out supra. This text, together with its sister draft Convention on international factoring, will now be laid before a diplomatic Conference to be hosted by the Government of Canada. This Conference will be held at the Government Conference Centre in Ottawa from 9 to 28 May 1988.

II

GENERAL CONSIDERATIONS

Growth of leasing

21. - Leasing, notwithstanding the comparatively recent emergence of the technique at present known by this term, in fact has a long history. Historical evidence suggests its widespread use by the ancient Sumerians circa 5000 B.C. Its modern development, though, as a generally acceptable alternative to the outright purchase of equipment, is rather to be traced back to the development of the railways in the middle of the 19th century. The United Kingdom wagon leasing companies of the late 1850's were among the very first registered limited liability companies to avail themselves of the new corporate form. Though their activity only spanned a relatively short period, the wagon leasing companies made a vital contribution to the rapid development of railway freight. A similar pattern occurred in the United States of America where railroad companies pushing ahead with new routes concentrated their financial resources on the provision of track and facilities and obtained their rolling stock on leases known initially as "car trusts" but which later became known as "equipment trusts". Certain manufacturers of specialized machinery, starting with the Bell Telephone Company in 1877, subsequently found another application of leasing as a means of protecting their monopoly or near-monopoly position by limiting the use of their products to lessees.

22. - It was in the post-World War II period, however, that the spectacular growth of leasing really got underway. This can be seen as one aspect of the more general phenomenon of the movement towards a credit economy and the acceptance of debt financing by the business community. The initial impetus to the growth of leasing in the wake of World War II was given by those businesses needing to replenish their equipment. The conventional means of responding to this need in the United States, the conditional sale, was simply not suitable, requiring almost invariably as it did a down-payment of 15-20%, a sum which many businesses did not then have. Until the 1960's the use of leasing was thus principally confined in the United States to capital-poor, high-risk companies, and the total annual volume of new equipment leases over that period in the United States probably did not exceed U.S.$ 1 billion. It was in the late 1950's and with the advent of the 1960's that leasing came of age with its acceptance by large industrial
corporations, utilities, national banks and Governments, as well as the establishment of the first independent leasing companies, playing a role analogous to that of banks and other financial institutions, from which they nevertheless differed in that they aimed to buy and then lease equipment to their clients, rather than simply loaning them the necessary money to buy it. The first such company was founded in 1952 in San Francisco: the United States Leasing Corporation. It was through the expansion into Europe and the Far East of the first American leasing companies, and notably U.S. Leasing, that the first non-American leasing companies were established: Mercantile Leasing in the United Kingdom in 1960, Deutsche Leasing in the Federal Republic of Germany in 1962 and Orient Leasing in Japan in 1962. Manufacturer links provided the early impetus for these operations but leasing companies, whether or not linked to domestic financial institutions, soon began cultivating direct links with equipment users and leasing an ever wider variety of equipment to them.

23. - The 1970's and the beginning of the 1980's are generally considered to mark the most rapid period of growth in leasing world-wide. Thus in the United States the amount of new equipment on lease rose from U.S.$ 15 billion in 1975, to U.S.$ 37 billion in 1980, to more than U.S.$ 61 billion in 1983, and to an estimated U.S.$ 100 billion in 1987. On the basis of these figures, the leasing industry’s contribution to total plant and equipment acquisition by commercial businesses in the United States now stands at 29%. As regards Western Europe, the more than 600 leasing companies represented in the European Federation of Equipment Leasing Company Associations (Leaseurope), a federation which covers about 80% of the financial leasing industry in Western Europe and encompasses 16 countries, in 1972 purchased equipment for leasing to their customers costing some ECU 2.1 billion; by 1980 the total value of new equipment leased in the member countries of Leaseurope had climbed to ECU 12.2 billion. By 1985 Leaseurope member companies leased equipment to the value of ECU 29.1 billion (U.S.$ 24.7 billion). The pioneer of leasing in Asia has been Japan. In 1970 Japan’s 31 largest leasing companies signed contracts worth a total of U.S.$ 726 million. By 1976 this figure had grown to U.S.$ 1,938 billion and by 1981 to U.S.$ 7.5 billion. During the 1983 fiscal year ending on 31 March 1984, the total value of new leasing contracts concluded by member companies of the Japan Leasing Association amounted to U.S.$ 12.6 billion. This figure had grown to U.S.$ 25 billion by the 1986 fiscal year. Leasing has achieved roughly a 10% to 20% annual rate of growth over the last few years in Japan. Leasing’s share of total private sector capital expenditure in Japan has grown from 3.03% in 1980 to 6.9% in 1986.

24. - Developments elsewhere in the world have mirrored this trend of rapid growth, albeit from more recent beginnings. The Far East has seen some of the most startling figures in this regard. The setting up of the first leasing company in the People’s Republic of China dates back only to 1981. By 1985 Chinese leasing companies were concluding business for a value of U.S.$ 800 million, the volume of their business having grown 65 times since 1981. The first leasing company in India was set up in 1973: by the end of 1986 there were probably more than 500 leasing companies operating in India. The business written by Indian leasing companies at the end of 1986 was estimated to be about U.S.$ 370 million, nearly 75% of which was written by the 30-40 leaders of the market. Where there were only five leasing companies in Indonesia in 1980, 65 such companies are now registered there. This expansion was reflected in the increase in the total value of new Indonesian leasing contracts on a purchase-cost basis from Rp. 0.7 billion in 1975 to Rp. 368.6 billion in 1985. Some of the most startling figures of all, however, are those for the Republic of Korea which show an increase in the total value of new leasing contracts on an acquisition-cost basis from U.S.$ 203 million in 1982 to U.S.$ 1,027 million in 1985. From the establishment of the first leasing company in Malaysia in 1973, the
Equipment Leasing Association of Malaysia by July 1986 counted 147 member companies. The value of assets leased by Malaysian leasing companies now stands at M$ 1 billion, representing probably over 20% of total annual capital expenditure on equipment in Malaysia.

25. - In South American markets too leasing has grown apace, particularly in the early 1980's. By the end of 1982 approximately U.S.$ 3.5 billion were invested in leasing in South America, more than two-thirds of this sum – U.S.$2.6 billion – being concentrated in Brazil. This rate of growth dipped in the years 1982 to 1984, in common with that in other sectors of the economy, but has now picked up again to such an extent that the Brazilian leasing industry had by 1986 once again caught up with its 1982 investment figure of U.S.$ 2.6 billion.

26. - The world leasing business is estimated to have grown from U.S.$ 53 billion in 1979 to U.S.$ 200 billion by 1986. The July 1984 News Bulletin of the American Association of Equipment Lessors (A.A.E.L.) reported the results of an informal survey carried out by the A.A.E.L. which showed that American lessors financed U.S.$ 8-10 billion of equipment outside the United States during 1983. Mr Tom M. Clark in his address to the September 1984 Copenhagen annual working meeting of Leaseurope, entitled "International leasing in practice", made the first attempt, on the basis of the A.A.E.L. survey, to estimate the extent of cross-border leasing activity. On his assumption that the international activities of leasing groups of other countries, principally the United Kingdom and France in Europe together with Japan and Australia elsewhere, were roughly comparable in overall size to those of American lessors, he concluded that, just as United States domestic leasing represented about 50% of the world market, so the total figure for new international leasing business in 1983 could be put at upwards of U.S.$ 15 billion, that is more than the total new domestic business of members of Leaseurope's 16 national associations in 1983.

The need for a uniform legal treatment of financial leasing

27. - The technique known as financial leasing was developed by the financial community to respond to newly perceived market needs for which the existing range of financing techniques had shown itself to be inadequate. In common with other techniques developed by the business community it has tended for its contractual documentation to draw quite heavily, albeit at times indiscriminately, on existing contractual models. It has thus borrowed features from the traditional bailment contract just as it has also taken over concepts commonly associated with the conditional sale or hire purchase transaction. However, in fusing these different characteristics financial leasing ultimately outgrew its relationship with its original contractual models and developed a separate, albeit hybrid legal personality of its own. For a long time the significance of this phenomenon seemed to be lost on the courts of the various countries which invariably sought to resolve legal problems arising in connection with the new technique by reference to the conceptual armoury of those classical contractual schemata to which it owed its origins.

28. - To take but one example, in the United States of America the argument for a long time ran that leases could be adequately dealt with either under the law of bailment (the "true" lease) or under the provisions of Article 9 of the Uniform Commercial Code governing security interests (the lease by way of security). Only the isolated voice was to be heard arguing for the
inappropriateness of the remedies provisions of Article 9 to those leases which did not closely approximate to transactions traditionally handled as security devices and in any event such voices were still not willing to recognise the existence of a category of lease that was amenable neither to classification within the category of bailment contracts nor to classification within the category of conditional sale/security interests. Admittedly this thinking has now undergone a radical transformation with the approval on 9 August 1985 of the Uniform Personal Property Leasing Act by the National Conference of Commissioners on Uniform State Laws.

29. - The nefarious consequences flowing from this longstanding failure to recognise the inadequacy of the legal treatment of leases resulting from the indiscriminate application to them of the conceptual framework of the classical contractual schemata were compounded by the piecemeal nature of the attempts made over the years by the legislator to grasp the nettle of the legal nature of leasing. At times the legislator addressed itself to the fiscal aspects of leasing, at others it regulated the accounting aspects of leasing, at other times again it established the necessary conditions for leasing companies to operate in certain countries, but only rarely did it get fully to grips with the legal nature of leasing.

30. - The international potential of financial leasing was certainly not enhanced by the conspicuous failure to adopt a consistent attitude to its legal treatment from one jurisdiction to another. What started life in the Anglo-Saxon world as a form of bailment lease was, for instance, absorbed into countries with a civilist tradition as something more in the nature of a conditional sale. This proved to be a source of legal uncertainty in cross-border transactions, ownership for example being differently attributed according to the jurisdiction seized.

31. - Unidroit’s thinking in embarking on the preparation of uniform rules on the leasing contract was at one and the same time to bestow on the atypical leasing transaction known as financial leasing a separate legal infrastructure of its own conceived with its particular characteristics in mind rather than on the pattern of the traditional contractual schemata and thereby to remove those elements of legal uncertainty bedevilling the realisation of anything like financial leasing’s full potential at the cross-border level.

Some general remarks about the draft Convention

32. - In distinguishing this atypical lease from those neighbouring legal concepts to which it had previously almost invariably been assimilated, the authors of the draft Convention singled out two factors as being of crucial importance: first, the dynamic, pivotal role played in the transaction by the lessee who selects the equipment and supplier on its own with a concomitant reduction in the role of the lessor whose ownership is stripped of virtually all the normal attributes of that quality and whose interest in the transaction is the purely financial one of recouping its capital investment; secondly, the leasing agreement between lessor and lessee is concluded for a term which takes the period of economic amortisation of the equipment into consideration, whence the essentially financial nature of the transaction for the lessor, in that the lessee’s payment of its rentals is not merely consideration for its right to use of the equipment, as would be the case with a typical bailment, but also guarantees the lessor the amortisation of its capital investment.

33. - It was around a core made up of these twin characteristics that the authors of the draft
Constitution set about building a distinct legal framework for the *sui generis* type of lease. Whilst it was true that in so far as the constituent elements of this novel transaction were a sale and a bailment the *basic* rules to be applied in regard to this transaction would be those of the law of sale and the law of bailment, it was equally true that to the extent that this novel institution had in fusing these two contracts into a complex new transaction to meet new market needs rendered certain concepts of the law of sale and the law of bailment inappropriate to, and inadequate for the resolution of legal issues arising in connection with this legal hybrid, these basic rules would have to be suitably adapted in fashioning this new legal framework. Reflecting the origins of the new institution in the creativity of the denizens of the financial world it was the opinion of the authors of the draft Convention that in shaping this legal framework it would be more profitable to have foremost in one’s mind the economic finality of the transaction, as reflected by the parties in their respective agreements, than simply slavishly to try to force the new transaction into the conceptual framework of the classical contractual schemata out of which it had evolved.

34. - The very circumstances which had called into being the new transaction, that is the inadequacy of the existing range of financial techniques to meet newly perceived market needs, moreover provided a clear signal to the authors of the draft Convention to be on their guard against in any way seeming to impose a legislative straitjacket on the object of their attentions. Its dynamic, hybrid nature, forever sprouting new varieties to respond to changing market conditions, made the authors of the draft Convention keenly aware of the need to safeguard its inherent creative potential by leaving the parties maximum freedom in their contractual relations with one another. Moreover, this convinced the authors of the draft Convention that their efforts would be better employed in clarifying a limited number of fundamental points, capable of bringing out the atypical nature of financial leasing, than in endeavouring to achieve a systematic unification of all legal aspects of the subject, all the more so as the more one went into detail the more likely was one to become embroiled in aspects of the law governing the traditional sale and bailment contracts and the greater the differences between the manner in which these aspects would be regulated from one legal system to another. Concentration on such a limited number of fundamental aspects of financial leasing could, moreover, for the same reason be reasonably expected to enhance the chances of the acceptance of the end-product of this exercise by a large number of Contracting Parties.

35. - One preliminary issue which fell to be resolved in delimiting the ambit of the draft Convention was whether to restrict one’s efforts to the tripartite lease commonly known as financial leasing or whether to broaden the area of inquiry also to encompass the type of leasing generally referred to as operating leasing. The major factor which determined the decision of the authors of the draft Convention in this respect has already been adverted to above, namely the idea that the draft Convention should confer a separate legal status on the atypical lease capable of distinguishing it once and for all from those neighbouring legal concepts with which it had previously been the tendency to confuse it. Whereas there is undoubtedly a good deal of operating leasing engaged in by lessors operating in exactly the same manner as they would in a full-pay-out financial lease, notably in container leasing, and whilst it is true that there are many cases where it is only possible to determine with certainty whether the type of lease being used is a financial lease or an operating lease depending on what finally happens to the 20% or 30% residual factored in by the lessor at the outset of the lease, the fact is that the operating lease does not typically present the hallmarks of atypicality, referred to above in §32,
commonly found in the financial lease, to wit the leading, dynamic role played by the lessee in the selection of the supplier and the equipment and the correspondingly subsidiary, purely financial role played by the lessor, on the one hand, and the link between the leasing term and the period of economic amortisation of the equipment, on the other. As such the operating lease does not present the same problems of awkwardness of fit in the classical contractual schemata and is indeed generally amenable to treatment as a bailment.

36. - In particular, the restriction of the ambit of the draft Convention to the tripartite financial lease was essential to the draft’s whole underlying philosophy, in that the reason for insulating the lessor in most cases from liability for the condition of the equipment was because its role was purely financial in character, a consideration which would not apply in the typical operating lease, particularly in that type of operating lease where the lessor produces the equipment itself. Likewise, one of the principal reasons for focussing on financial leasing was precisely to deal with those special legal problems that arise out of the complex, tripartite nature of financial leasing, in particular the absence of contractual nexus between the supplier and the lessee, problems which do not arise with the typically bipartite operating lease. There was not the same need for an international instrument, indeed for any legislation at all, where all the parties had to do was to write their own contract, as was the case with the typically bipartite operating lease.

37. - Recent developments in the leasing world have nevertheless contributed to blur considerably the lines of demarcation between financial leasing and operating leasing. Thus for economic reasons leases entered into with airlines in developing countries are now frequently termed “operating leases”, while seeming nevertheless in substance to remain within the contours of the draft Convention. The aircraft is purchased from the manufacturer by a financial intermediary who in turn leases it to a national airline. Furthermore, the Draft Operational Regulations adopted by the preparatory committee of the signatory States of the 1985 Convention Establishing the Multilateral Investment Guarantee Agency (M.I.G.A.) contained certain recommendations to M.I.G.A.’s Board the effect of which would be to allow for M.I.G.A. coverage of leasing arrangements on condition, inter alia, that the lease was an operating lease. However, this requirement should again be seen more as a question of terminology than of substance, the underlying intention being to distinguish an eligible investment from a transaction that is nothing more than an export credit substitute. Article 12 (a) of the M.I.G.A. Convention provides that “eligible investments shall include equity interests... and such forms of direct investment as may be determined by the Board” of M.I.G.A.

38. - While the draft Convention was originally conceived as uniform rules designed to clarify the situation with regard to the sui generis type of leasing in general, albeit in particular with a view to facilitating and promoting cross-border transactions, this idea soon had to be sacrificed in view of the well-known reluctance of certain States to become parties to international instruments the effect of which will be to impinge on their domestic law and for this reason the draft Convention’s application is limited to international financial leases. However, the authors of the draft Convention never lost sight of the fact that for the vast majority of States that have no legislative infrastructure specifically addressing the atypical leasing transaction the greatest usefulness of the body of uniform rules contained in the draft Convention may well prove to be as the basis of domestic law designed to fill this legislative vacuum.
39. - The provisions of the draft Convention have been divided up into three parts, although it is important at this stage to bear in mind the limited objective of the authors of the draft Convention in making this decision, namely to enable them better to situate the problem raised by the provisions of Article 14, to wit which provisions of the draft Convention should be amenable to derogation. A first series of articles (Chapter I: Articles 1-3) delimits the future Convention’s sphere of application, both substantive and geographic. This is followed by the main body of substantive uniform rules contained in the draft Convention (Chapter II: Articles 4-13) dealing with the rights and duties of the parties to the financial leasing transaction. These provisions can be further sub-divided into those dealing with the parties’ rights and duties inter se (Articles 4, 7, 8, 9, 10, 11) and those dealing with the rights and duties of the parties with regard to third parties or outsiders (Articles 5, 6, 7 (1)(b) and (c)). The other two articles at present contained within Chapter II (Articles 12 and 13) are in fact more concerned with the draft Convention’s sphere of application. The main purpose of Article 12 is to extend the application of the draft Convention to those financial leasing transactions, commonly known as leveraged leases, in which in return for putting up a large part of the investment represented by the transaction, one or more lenders will receive an assignment from the lessor of the stream of rentals provided for under the leasing agreement. Article 13, on the other hand, seeks to extend the application of the draft Convention to sub-leasing arrangements. The proper place for these provisions as such may accordingly finally be found to be in a revamped Chapter I encompassing, on the line of other recent international instruments adopted in the commercial law field, both “sphere of application and general provisions”, although this would probably not be appropriate for Article 12 (2), dealing with the lessee’s right of assignment. Such a revamped Chapter I would also be able to absorb the third group of provisions at present contained in the draft Convention (Chapter III: Articles 14 and 15), which are general provisions traditionally found in international instruments of this ilk.

III

COMMENTARY ON THE BODY OF THE DRAFT CONVENTION

Title

40. - In common with other texts emanating from Unidroit committees of governmental experts, this text is styled a draft Convention. Its title indicates that it is concerned essentially with that type of leasing commonly known as financial leasing and with only the international manifestations of that phenomenon. As we have already had occasion to note, the delimitation of the ambit of the draft Convention by reference to international transactions is in no way intended to prevent those States the primary concern of which would be for legislation to govern domestic financial leasing transactions so to extend the draft Convention’s application. Its delimitation by reference to financial leasing goes back to the same occasion, namely the fourth session of the Unidroit Study Group when it was decided that the previous denomination of the subject-matter of the draft Convention, as the sui generis type of leasing transaction, was less felicitous than the name by which it had generally become known. The idea also was that the qualification of a legal institution as sui generis was not normally something that one would expect to find in a statute, let alone an international instrument, being a matter more appropriate for debate among legal scholars. It nevertheless remains true that the inclusion of the words “sui generis” in the title, and indeed also in the preamble up until the first session of governmental
experts, had the advantage of alerting the reader straight away to the fundamental idea behind the draft Convention, namely to enshrine therein the recognition of a new legal category that should no longer be confused with those neighbouring legal concepts from which it traced its origins. This concern has once again become topical, as alluded to earlier in this report, in view of the increasing blurring of the distinction between financial and operating leases. The specific expression “financial leasing” employed in the title should, accordingly, not be read as anything more than a term of art to encompass that particular type of transaction which is subsequently defined in Article 1 (2).

41. - Differences of opinion emerged as to the most suitable French title for the draft Convention. The Unidroit Study Group had come up with the appellation “location financière”, drawing inspiration from the titles of legislation passed in several jurisdictions belonging to the Latin linguistic tradition (notably the Belgian 1967 legislation which spoke of “location-financement”, the Spanish legislation of 1977 which employed the term “arrendamiento financiero”, the Colombian legislation of 1979 which also spoke of “arrendamiento financiero”, the Portuguese legislation of 1979 which spoke of “locação financeira”, the Venezuelan legislation of 1982 which again employed the term “arrendamiento financiero”, not to mention all Italian legislation on this subject which speaks of “locazione finanziaria”). However, certain French-speaking representatives attending the first session of governmental experts took exception to this appellation in view of what they considered to be the primacy of the term “crédit-bail” to denote this activity in the French language, after its use in the French legislation of 1966 and subsequent hallowed usage in France, notably in an “arrêté” on the Frenchification of terminology imported into France from abroad.

Preamble

42. - Enshrined in the preamble, in particular in the second and fourth clauses thereof, is the basic philosophy underlying the draft Convention, namely that, in order to foster the wider use of financial leasing at a cross-border level, it is important to remove the impediments to such cross-border transactions deriving from legal factors, and pre-eminent among such legal impediments must be counted the inadequacy of the legal treatment at present generally meted out to such transactions. The inadequacy of this legal treatment, as we have already had occasion to note, consists essentially in financial leasing being generally forced this way or that into one or other of the traditional contractual schemata, most notably the contract of bailment, to which it owes its origins and within the comfortable logic of which it has hitherto therefore almost invariably been the tendency to try to accommodate it. The authors of the draft Convention adjudged that it was time that the distinctive set of triangular relationships created by the financial leasing transaction should receive an appropriate legal treatment of their own cast with their particular characteristics in mind.

43. - At the same time the authors of the draft Convention recognised the continuing relevance of the rules governing the traditional contract of bailment to the financial leasing transaction. Indeed in the fourth clause of the preamble they acknowledge that these rules had been the starting point, the foundation for the rules embodied in the draft Convention. The draft Convention had, in taking over many of the rules, concepts and terminology of the law of bailment, had to adapt this regulatory, conceptual and terminological framework so as adequately to reflect the novel economic reality of financial leasing.
44. - It did not escape the attention of the authors of the draft Convention that not only have some of the most outstanding recent growth figures for leasing been recorded in developing countries but also that financial leasing has undoubtedly proven its worth in meeting just those capital investment needs which are at present so sorely felt among developing countries. In the third clause of the preamble the draft Convention accordingly proclaims its authors' commitment to the need to make international financial leasing more available to developing countries. Clearly this idea follows on from and is intimately connected with those ideas expressed in the previous clause of the preamble, that is that in order to make international financial leasing more available to developing countries it is especially vital to remove those legal impediments at present standing in the way of greater cross-border leasing traffic with such developing countries, on the one hand, and to ensure that a fair balance is maintained between the interests of the different parties to the transaction, one of which may well be in a developing country, on the other.

45. - Striking an equitable balance between the interests of the different parties to the leasing transaction was an objective ever in the forefront of the minds of the authors of the draft Convention. This search was conducted both in the context of the two contracts making up the complex financial leasing transaction and in that of the mutual relations of the parties inter se. The structure of the draft Convention is cast in the image of the economic reality of the transaction. Whilst it accordingly reflects the central, dynamic role played by the lessee, it nevertheless also seeks to achieve an overall apportionment of the rights and duties of all parties to the transaction that mirrors their different roles and levels of responsibility in relation to the transaction. (19)

46. - From the very beginning the authors of the draft Convention, bearing in mind the different philosophies underlying the treatment of financial leases for accounting and revenue purposes, on the one hand, and for strictly private law purposes, on the other, intended that the ambit of the draft Convention should be delimited by reference to the private law aspects of financial leasing alone, judging that it would be both unrealistic and presumptuous to endeavour to address such divergent concerns in one and the same text. This is not to preclude the possibility of the provisions of the draft Convention impacting indirectly, albeit involuntarily, on such non-private law aspects of the subject as its accounting and revenue treatment. In expressing this idea in the fifth clause of the preamble, the authors of the draft Convention in the event found the term "civil and commercial law aspects" preferable to "private law aspects" in the interest of accommodating those legal systems, notably the Socialist legal systems, which do not recognise the existence of a category of private law relations.

47. - Another fundamental feature of the draft Convention proclaimed in the preamble has already been alluded to, namely the realisation by the authors of the draft Convention that its

(19) One writer has already commented on the equitable distribution made under the draft Convention of the liability for product defects under a financial leasing transaction. Cf. Amelia H. BOSS, Products Liability and International Leasing Transactions: The UNIDROIT Draft Convention, in Journal of Products Law 1982, 143 at 147, where she writes: "The Convention defines the tripartite transaction as consisting of both the leasing agreement between the lessor and lessee and the supply agreement between the lessor and supplier. This broad coverage allows the Convention to consider both relationships together in fashioning its rules to achieve symmetry and equity between the parties. For example, the liability of the lessor for defective products may be limited while the supplier's liability is expanded; the lessee is still allowed recovery for product defects but the liability is more equitably distributed between the parties."
chances of success could only be enhanced by its concentration on a limited number of basic points capable of bringing out the atypical nature of the financial leasing transaction rather than by its attempting to achieve a systematic unification of all legal aspects of the subject. This idea is intended to be conveyed in the fifth clause of the preamble by the employment of the word “certain” before the words “uniform rules”. The corollary of this idea is that whole areas of the law relating to financial leasing will be left outside the draft Convention. The authors of the draft Convention were therefore at the same time aware of the need to ensure that its avowedly limited scope did not jeopardise its basic underlying purpose, namely to ensure that the atypical leasing transaction which it addresses is henceforth treated separately from those neighbouring legal concepts to which it has hitherto tended to be assimilated. This concern is echoed in the provisions of Article 15 (2).

48. - Special importance attaches to the preamble by virtue of the incorporation in Article 15 (1) at the final session of governmental experts of a reference to the “object and purpose” of the draft Convention “as set forth in the Preamble”. It would thus be incumbent upon those called upon to interpret the future Convention to have special regard to the objectives of the Contracting Parties as proclaimed in the preamble.

Article 1

49. - The opening article of the draft Convention delimits its substantive sphere of application. The subject-matter of the draft Convention already having been generically defined in the title and the preamble as “international financial leasing”, this article sets out what may be regarded in substance as a definition of “financial leasing”, leaving Article 2 to set forth the conditions that have to be met for a given financial leasing transaction to be regarded as “international” for the purposes of the draft Convention.

50. - As has already been mentioned above, the definition adopted in Article 1 is closely modelled on the definition of “equipment leasing” adopted after protracted negotiations by Leaseurope in 1977. The fact that the reaching of agreement on this definition of the activities pursued by its members caused Leaseurope such difficulty is eloquent testimony of the often widely differing conceptions of leasing from one country to another, even within the relatively limited geographical confines of Western Europe.

51. - Whereas the provisions of Article 1 present many of the characteristic traits of a legal definition, this is deceptive. The contents of Article 1 are not so much a legal definition of “financial leasing” in the broad, loose sense in which that term is employed and understood in everyday parlance, for to embrace in one definition all the possible variations on the hybrid mechanism generically referred to as “financial leasing” would probably be not only to attempt the virtually impossible but also unnecessarily to restrict its future pattern of evolution, as a description in the first place of the mechanics of a financial leasing transaction and secondly of those ingredients of the financial leasing transaction that establish its atypical credentials in relation to those neighbouring legal concepts with which by virtue of its provenance it has so much in common and with which it has accordingly in the past all too often been bracketed.

52. - The combined effect of paragraphs 1 and 2 is prima facie to exclude various types of leasing transaction from the ambit of the draft Convention. Foremost among the types of leasing that are not intended to be covered by the draft Convention are operating leasing and
short-term leasing, sometimes known as renting. This exclusion is implicit in the provisions of Article 1 (2)(c) which make it a necessary ingredient of the type of lease governed by the draft Convention that there is a link between the rentals payable under the leasing agreement and the period of economic amortisation of the leased asset, a link which would not normally exist under an operating lease or a renting agreement. However, bearing in mind the increasing blurring of the distinction between “financial leases” and “operating leases” of late, the authors of the draft Convention took the view that it would not be appropriate to exclude its application merely by virtue of the fact that the transaction in question is denominated an “operating lease” rather than a “financial lease.” This intention is conveyed by their inclusion of the words “as defined in paragraph 2 of this article” featuring in the chapeau of Article 1 (1). The definitional ingredients listed in Article 1 (2) are accordingly not so much definitional ingredients of the financial leasing transaction as that term is understood at any given moment in time as definitional ingredients of the type of transaction singled out for treatment under the draft Convention.

53. - By virtue of the basically tripartite nature of the transaction addressed in the draft Convention bipartite leasing transactions are also excluded from its scope of application. It is moreover primarily the special financial role played by the lessor in the transaction addressed by the draft Convention that determines its atypicality. Where there are only two parties to the transaction, a supplier and a user, the case for a derogation from the traditional rules of the law of bailment becomes that much more difficult to justify.

54. - That type of financial lease, above all practised in the real estate field, known as “sale and lease-back” is excluded from the ambit of the draft Convention by virtue of its opening article’s reference to the fact that the equipment to be leased is acquired by the lessor from the supplier: in the typical sale and lease-back situation the acquisition of the item to be leased to the lessee is effected between lessee and lessor.

55. - Another prima facie exclusion from the draft Convention results from the type of property singled out for treatment thereunder. The delimitation of the substantive sphere of application of the draft Convention by reference to “plant, capital goods or other equipment” is meant to exclude real estate leasing and to restrict its application to personal property leasing. The reasons underlying the decision not to tackle real estate leasing were essentially two-fold: first, the limited incidence of real estate leasing at the cross-border level and, secondly, the enormous difficulties that would inevitably arise in any attempt to unify principles of the law of real property and the law of personal property in the same text.

56. - Article 1 (3) excludes another category of leasing from the draft Convention and this is consumer leasing. In view of the different philosophies generally applied to consumer transactions, on the one hand, and to non-consumer transactions, on the other, it was considered politic to limit the application of the draft Convention to the latter. This decision was clearly additionally justified by the decision to restrict its sphere of application to international transactions, consumer transactions not generally being international in character. The language employed for the purpose of achieving this exclusion was modelled on the corresponding provision (Article 2 (a)) of the 1980 United Nations Convention on Contracts for the

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(20) Cf. supra §37.
(21) Cf. also §63 infra.
International Sale of Goods (hereinafter referred to as "the Vienna Sale Convention"). The significance of the addition of the word "primarily" in Article 1 (3) of the draft Convention to the formula employed in Article 2 (a) of the Vienna Sale Convention lies in the fact that otherwise, the criterion for determining whether a given transaction is or is not to be considered a consumer transaction for the purposes of the draft Convention being not the nature of the equipment as such but rather the use to which it is intended to be put, namely "the lessee's personal, family or household purposes", there would be a risk that the future Convention might apply in certain cases to goods which ordinarily were not intended to be used for specifically business or professional purposes and could just as well be used by a consumer but which, by reason of the party making use of them, namely a business, would become subject to the draft Convention.

57. - Two types of leasing transaction that are intended to be within the purview of the draft Convention, on the other hand, are that species of financial lease known as a leveraged lease and financial sub-lease arrangements. The application of the draft Convention is specifically extended to these types of financial lease, to the former by the provisions of Article 12 (1) and to the latter by the provisions of Article 13.

58. - The first feature of the atypical financial lease to which we are introduced in Article 1 is that it is a complex, basically tripartite transaction embracing two agreements, a supply agreement between the supplier and the lessor and a leasing agreement between this same lessor and the lessee. One of the prime objectives of the authors of the draft Convention has all along been to ensure that the type of lease addressed in the draft Convention should no longer be treated as two separate contracts but rather as a single, complex transaction setting off the interaction of two mutually interdependent agreements. The factual connection between the two constituent agreements of this transaction is brought out in that provision of the draft Convention (Article 1 (1)(a)) which states that the supply agreement is concluded on terms approved by the lessee. The previous treatment of this transaction as two distinct agreements has proved to be the source of much distortion of the economic reality underlying the parties' intentions. The purely financial nature of the lessor's interest in the transaction and the case for its consequent insulation from that liability in contract and tort that would normally flow from its capacity of lessor would not, for example, emerge from the leasing agreement viewed in isolation: they only make sense when the motives of the parties to the two agreements are seen in the overall context of the single complex transaction that provides the link between the mutual rights and duties of the different parties.

59. - This formulation of the type of lease addressed in the draft Convention in terms of a complex, triangular relationship enables the draft Convention to bring out, and at once to focus on the fundamental element of its originality, that is that element which justifies the atypical legal regulation that follows: the essentially financial nature of the transaction. As one commentator on the draft Convention has noted, this means that "the lessor's role is that of lender, the lessee's role is that of borrower. Instead of lending money directly for the purchase of equipment and then securing repayment of the debt through the pledge of the equipment as collateral, the lessor purchases the equipment, takes title in its own name, and then grants the use of it to the lessee in return for a promise to pay rentals." (22)

60. - The other side of the coin, as it were, to the lessor's purely financial role in the transaction is the lessee's dynamic, pivotal role. This provides the other principal hallmark of the originality of the atypical leasing transaction spelled out in Article 1, namely that it is on the specifications of the lessee that the lessor acquires the equipment to be leased from the supplier. The reality of financial leasing is indeed that the technical specifications of the equipment, the terms of payment and delivery are worked out directly between the lessee and the supplier, with delivery being made direct by the supplier to the lessee. It is thus a relationship effectively beyond the contractual pale that underpins to a large extent the logical basis of the atypical chain of rights and duties generated by the financial leasing transaction, in the sense that the lessee and the supplier are never at any stage co-contractants but are essentially responsible through their dealings with one another for the selection, with a view to the subsequent use, of a particular item of equipment, the lessor's role being confined to the injection of the necessary capital for the acquisition of the equipment. It is this quasi-contractual relationship between lessee and supplier which was felt to merit not only the shifting in the draft Convention of many of the rights and duties normally associated under a lease with the lessor onto the lessee but more specifically the recognition, in Article 9 (1), of the lessee's right to sue the supplier directly for the latter's breach of the terms of the supply agreement. The recognition of this right apart, the only legal link between the lessee and the supplier in the context of the financial leasing transaction lies through the lessor. The lessor indeed is the contracting party common to both legal relationships underlying the complex financial leasing transaction, bound as it is both to the supplier under the supply agreement, providing for the acquisition of the asset to be leased, and to the lessee under the leasing agreement, granting the lessee the right to use the asset acquired under the supply agreement.

61. - Up until the first session of governmental experts the opening article of the draft Convention had specifically referred to the "triptite" nature of the transaction addressed by the draft Convention. This was, however, considered inaccurate in so far as, as has already been mentioned, the future Convention also encompasses that special type of financial lease known as a leveraged lease, in which there will be more than three parties. Moreover, the basic tripartite pattern of the transaction singled out for treatment under the draft Convention is already clear enough from its description in Article 1 (1).

62. - Originally, moreover, the authors of the draft Convention had sought to drive home the distinctiveness of the type of lease addressed therein by the employment of distinctive indicia to denote the three parties to the transaction. Thus, instead of the traditional appellations "manufacturer", "lessor" and "lessee" the Study Group had at one time preferred the terms "supplier", "financier" and "user" respectively. This choice of labels was designed to reflect the essential role played by each party in the transaction. The term "financier" was however considered to be dangerous as a label and, while maintaining the term "supplier", for the other two parties the authors of the draft Convention reverted to the traditional appellations of "lessor" and "lessee", preferring to distinguish these parties from the classical lessor and lessee by their description of their atypical functions in the context of the financial lease.

63. - The subject-matter of the draft Convention is further delimited by reference to the types of equipment which are subject to the draft Convention. For the reasons expounded above, (23) the authors of the draft Convention decided to leave real property outside the scope

(23) Cf. §55 supra.
of the future Convention and to concentrate their attention on what is generally known as equipment leasing. In defining the "equipment" covered by the draft Convention Article 1 (1)(a) adopts the definition employed in the aforementioned Leaseurope definition, to wit plant, capital goods or other equipment. This definition must clearly be interpreted in the light, first, of the additional delimitation of the substantive sphere of application of the draft Convention introduced in Article 1 (3), namely that the equipment must be of a type that will not be used primarily for the lessee's personal, family or household purposes, the intention here, as has already been explained, to exclude consumer movables, and, secondly, of the decision to exclude real estate leasing from the ambit of the draft Convention. While the authors of the draft Convention were clear in their own minds that the draft Convention was principally designed to cover the leasing of movables, they nevertheless rejected the idea of spelling this out more explicitly, on the ground that this would probably involve introducing terms like "movables" and "immovables" into the draft Convention with the considerably differing meanings attributed to these notions from one legal system to another. The principal source of difficulty on this score was the reference in the draft Convention to "plant". (24) While there was no doubt that plant leased as a chattel which subsequently became annexed to land would qualify as equipment and accordingly fell within the scope of the future Convention in Common law jurisdictions, the same was not necessarily felt to be true where the chattel leased began life as a fixture. The authors of the draft Convention were not in the end convinced of the desirability of adding the qualification "movable" before the word "plant", for the reason adduced earlier in this paragraph, and decided accordingly to leave the matter open. Thus, while the draft Convention was never specifically intended to apply to real estate, its accidental application thereto cannot be ruled out in those cases where this follows from the interpretation given to "plant" by the courts of a given country. The disadvantages inherent in this approach were considered by the authors of the draft Convention to outweigh the aforementioned advantages of not having to introduce the slippery notions of "movables" and "immovables" into the text of the draft Convention.

64. - As regards three particular classes of equipment, aircraft, ships and rolling stock, a change of thinking by the authors of the draft Convention means that, whereas there was originally, from 1975 to 1977, a feeling that it might be better to exclude the leasing of these special classes of equipment from the scope of the draft Convention, (25) in the generally accepted interest of ensuring the draft Convention as broad a scope of application as possible these items of equipment have since then definitely been intended to be covered by the future Convention, notwithstanding the undeniable difficulty of classifying aircraft, ships and rolling stock in the same category as the general body of capital goods. Their inclusion was never felt to require any specific mention in the text, as, failing their express exclusion, their inclusion would follow implicitly under the umbrella of the term "capital goods".

65. - Article 1 (2) sets out those essentialia, those characteristic traits of financial leases which must be present for a given financial leasing transaction to be subject to the draft Convention. However, it is important to bear in mind that the characteristics listed in this paragraph are merely intended as features illustrative of the type of lease singled out for

(24) "Plant" is defined in the Shorter Oxford English Dictionary as "the fixtures, implements, machinery, and apparatus used in carrying on any industrial process".

(25) Cf. §§2, 5 (vi) supra.
attention by the authors of the draft Convention, as indeed prefigured by the words "as defined in paragraph 2 of this article" in the chapeau to Article 1 (1), and are not therefore intended to be exhaustive definitional ingredients.\(^{(26)}\) The importance of this paragraph lies in its spelling out of those elements which determine the *sui generis* credentials of the type of lease addressed in the draft Convention and thus provide the logical premise from which the subsequent articles of the draft Convention can then draw the original consequences.

66. - These characteristics formerly numbered six. Of those that have been lost en route, one was relocated in Article 3. The reason for this relocation was that while the inclusion in the leasing agreement of an option to purchase was a *sine qua non* of a financial leasing transaction under certain legal systems, under others its inclusion would alter the nature of the transaction, changing it instead into a hire-purchase or conditional sale transaction. Another, providing that the lessor was owner of the leased asset throughout the term of the leasing agreement, was dropped because it would not necessarily correspond to all financial leasing transactions, some of which used sub-leasing arrangements. The other, specifying that the type of leasing transaction addressed by the draft Convention embodied "one or more agreements", was considered by some to be a pleonasm, in so far as it was true of any contract that it could be expressed in one or more contractual documents, and by others to be misleading in that the fact that many financial leasing transactions were laid down in one document did not alter the fact that it was still made up of at least two contracts, a supply agreement and a leasing agreement. The committee of governmental experts adjudged that the idea behind this clause was moreover already conveyed in Article 1 (1).

67. - The first of the surviving characteristics of the financial leasing transaction covered by the draft Convention is set out in Article 1 (2)(a). Especial importance within the scheme of the draft Convention, notably as the basis of the shifting of the normal disposition of so many of the rights and duties of the parties under a traditional bailment contract, attaches to this clause. The lessee it is that is responsible for specifying the equipment, in the light of and with a view to its own operational requirements, and selecting the supplier, with whom it will work out directly such matters as the conditions of, and the time to be allowed for delivery, alterations, improvements, the conditions of, and the time to be allowed for payment. The lessee may in making these choices rely on the advice of third party experts but will essentially conduct negotiations with the supplier on its own as a reasonably informed user of the type of equipment it requires. The lessor's interest in the transaction being purely financial, its technical involvement will normally be correspondingly nil. It follows from this that it would be morally indefensible for a lessee that has had ample opportunity to check on the technical suitability of the equipment required by it prior to delivery to be able to blame the lessor for its own bad choice when the equipment upon delivery proves to be unsuited to its requirements. This clause accordingly provides the logical premise for that general insulation of the lessor from that liability towards the lessee that would normally attach to its capacity as lessor of the equipment (Article 7 (1)). It also furnishes the justification for the lessee being made a third party beneficiary of the duties assumed by the supplier under the supply agreement (Article 9 (1)). The technical specifications regarding the equipment are, as we have just seen, worked out directly between lessee and supplier but this factual link is not reflected in any contractual nexus, the result of which, failing the provisions of Article 9 (1), would be to make it difficult

\(^{(26)}\) But cf. §52 supra.
for the lessee to seek adequate redress from the supplier for its failure to deliver, late delivery or delivery of equipment that failed to measure up to that stipulated.

68. - However, just as the authors of the draft Convention recognised that it would be morally indefensible to make the lessor responsible for the lessee’s bad choice, in Article 7 (1), so they also acknowledged that there would nevertheless be cases, notably in international financial leasing transactions, where the large sums of money involved might at times necessitate some abandonment of the lessor’s technical neutrality in relation to the equipment. For instance, in the construction of a tanker it would be common for the lessor and the lessee to agree to have a team of engineers on the spot to monitor the changes of design that would regularly be called for. The lessor as owner and as the party contracting with the supplier would clearly be anxious to have the necessary technical expertise at its disposal to enable it to gauge the impact of any important change on its financial commitment under the supply agreement as well as on its potential liability towards third parties (in respect of rules of safety). In accordance with the general intention of the authors of the draft Convention to ensure it as broad a sphere of application as possible, it was recognised that it would be undesirable to create an inference that, where and to the extent that the lessor intervened in the sphere of autonomy reserved to the lessee under Article 1 (2)(a), the nature of the transaction would change to such an extent as to make it no longer amenable to treatment under the draft Convention. Accordingly Articles 1 (2)(a) and 7 (1)(a) are intended to have the combined effect that, in cases where the lessor’s technical neutrality in relation to the equipment is less than absolute – the justification for the word “primarily” in Article 1 (2)(a) – the transaction will still fall within the scope of the draft Convention but the general immunity from liability conferred upon the lessor vis-à-vis the lessee is to be reduced by the extent to which the lessor has intervened in the selection of the supplier or the specifications of the equipment.

69. - The provisions of Article 1 (2)(b) underline the fact that the complex financial leasing transaction addressed by the draft Convention will ordinarily comprise two contracts and bring out once more the link between these two contracts, the lessor acquiring the equipment from a supplier in pursuance of the agreement it has made with the lessee. The somewhat vague wording “in connection with” is designed to indicate that the lessee’s selection of the equipment is neither necessarily contemporaneous with, nor necessarily subsequent to the making of the leasing agreement, but may in fact precede the conclusion of this agreement, further testimony of the flexibility the authors of the draft Convention sought to build into the text. The fact that this provision, in common with Article 1 (1)(a), speaks of the equipment being “acquired” rather than being “purchased”, as at an earlier stage, reflects the feeling of the authors of the draft Convention that to say that the equipment was “purchased” by the lessor would not be entirely accurate to describe the case, frequent in the leasing of plant, where the land on which the plant was to be built was indeed purchased by the lessor but where the plant was then constructed on this land by a third party builder. The words “to the knowledge of the supplier” are intended to ensure that the draft Convention should only apply where the supplier is aware that the equipment in question is to be held on lease. This is particularly important in view of the provision in Article 9 (1) extending the duties owed by the supplier to the lessor under the supply agreement also to the lessee.

70. - More than any other provision in the draft Convention, it is Article 1 (2)(c) which brings out the financial nature of the transaction addressed in the draft Convention. It does so by positing a necessary link between the duration of the leasing agreement and the period of
the useful working life of the leased asset. It is a hallmark of the type of lease addressed by the
draft Convention that the rentals payable under the leasing agreement are not calculated in
function of the use-value of the equipment, as with a traditional bailment, but in function of what
is necessary to amortise the lessor’s capital investment. The measure of the lessor’s capital
investment in this regard is expressed in Article 1 (2)(c) in terms of the whole or at least a
substantial part of the cost of the equipment. However, aware as they were of the incidence of
other factors in the calculation of the lessee’s rentals and with a view to ensuring the future
Convention as broad a sphere of application as possible, the authors of the draft Convention
introduced the qualificatory expression “in particular” into the equation between the notion of
the rentals payable by the lessee under the leasing agreement and the notion of the amortisation
of the whole or a substantial part of the cost of the equipment. The addition of these two words,
for instance, indicates that the calculation of the lessee’s rentals will also normally reflect the
cost of the transaction to the lessor. It would also facilitate the extension of the application of
the future Convention to those leasing arrangements at present under consideration for
coverage under M.I.G.A.: among the Draft Operational Regulations adopted by the preparatory
committee of the signatory States of the M.I.G.A. Convention in September 1986 was one
recommending the coverage under M.I.G.A. of leasing arrangements under which the rentals
payable are “substantially dependent on the production, revenues or profits from the investment
project”.

71. - Doubts nevertheless lingered in the minds of one or two delegations to the final
session of governmental experts as to the felicitousness of the formulation of this provision.
One suggestion was that a more accurate formulation would be to refer not only to the rentals
payable under the leasing agreement but also all other financial obligations for which the lessee
was liable under the leasing agreement as being calculated so as to take into account in
particular the amortisation of the whole of the cost of the equipment. What was had in mind by
the reference to other financial obligations incumbent upon the lessee under the leasing
agreement apart from its rentals was the price at which the lessee would be entitled to exercise
any purchase option that might be included in the leasing agreement. The aim of bringing this
price into the equation of the lessor’s amortisation of its capital investment in Article 1 (2)(c)
was, by enabling the text to refer to the lessor’s amortisation of the whole of the cost of the
equipment, to avoid those difficulties that were felt to be implicit in referring to a “substantial”
part of the cost of the equipment, notably any inference that a part of the cost of the equipment
did not have to be amortised under the draft Convention.

Article 2

72. - This article delimits the geographic sphere of application of the draft Convention. It
basically sets forth the conditions to be met before a given financial leasing transaction may be
regarded as “international” and subject to the regimen of the draft Convention. The reasons
behind the decision taken by the authors of the draft Convention to restrict its sphere of
application to international transactions have already been rehearsed above.\(^{(27)}\) In drawing up
this article the authors of the draft Convention followed closely the basic structure and
terminology of the corresponding provisions of the Vienna Sale Convention (Articles 1 (1) and
10 (a)) and the 1983 Unidroit Convention on Agency in the International Sale of Goods

\(^{(27)}\) Cf. §38 supra.
(hereinafter referred to as “the Geneva Agency Convention”) (Articles 2 (1) and 8 (a)).

73. - Once it had been decided to tie the draft Convention to specifically international transactions, it became necessary to decide which should be the criteria for determining whether a given financial leasing transaction is to be regarded as international for the purposes of the draft Convention. The criterion normally employed to determine the international character of a legal relationship in recent international commercial law Conventions is that of the place of business of each of the parties to the relationship in question. This criterion was basically followed in the draft Convention. However, the difficulty with applying this principle in the case of the draft Convention was that, whereas in most of the cases addressed by such Conventions the relationship covered is basically a two-party relationship, the transaction addressed by the draft Convention is basically tripartite. Of the three possible places of business the Study Group elected to take those of lessor and lessee and to exclude the impact of that of the supplier. The reasoning behind this decision was that the leasing agreement was the fundamental legal relationship contained within the complex financial leasing transaction and that it was undesirable unnecessarily to restrict the future Convention’s sphere of application. However, this decision was overturned by the committee of governmental experts which considered that the impact of certain of the provisions of the draft Convention on the supplier’s position, notably Article 9 (1), meant that some account had to be taken in the provisions determining the future Convention’s sphere of application of the supplier’s place of business. Otherwise there was a very real risk that the effectiveness of the lessee’s remedies against the supplier under Article 9 (1) might be jeopardised in those cases where the law applicable to the supply agreement was not that of a State Party to the future Convention, thus enabling the supplier to invoke in its defence the argument that there was no contract between it and the lessee and thus defeat the lessee’s exercise of its remedies under Article 9 (1). In Article 2 (1)(a) the draft Convention therefore, while still taking the fact that the places of business of the lessor and the lessee are in different States and that these States are Contracting States as the fundamental criterion for the application of the future Convention, also requires that the place of business of the supplier be in a Contracting State before the future Convention can apply. However, in recognition of the fact that the leasing agreement is undoubtedly the fundamental legal relationship in the complex financial leasing transaction, the place of business of the supplier, it should be noted, does not also need to be in a State different from those in which the lessor’s and lessee’s places of business are located: it simply has to be in a Contracting State.

74. - A traditional alternative connecting factor employed for the application of international commercial law Conventions is that the rules of private international law of the forum lead to the application of the law of a State which has adopted the future Convention. This additional ground for the application of the future Convention is founded on the premise that, once it has been adopted by a State, then its rules should govern all financial leasing transactions of an international character as defined in the chapeau of Article 2 (1) in preference to its domestic law which was conceived with only internal financial leasing transactions in mind.

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(28) Cf. for example Article 1 (1) of the Vienna Sale Convention and Article 2 (1) of the Geneva Agency Convention.
Thus, when by the operation of the rules of conflict the law of a Contracting State is found to be applicable by the judge seized of the case, then it is the future Convention which, by virtue of this principle, should apply to the transaction. The major difficulty in applying this principle to the financial leasing transaction arose, as with Article 2 (1)(a), from the fact that the relations governed by the draft Convention are not bipartite but tripartite. For the same reason as has been expounded in the previous paragraph in respect of the solution reached in Article 2 (1)(a), namely that, while the fundamental legal relationship in the complex financial leasing transaction is undoubtedly the leasing agreement, it is essential that account should also be taken in the sphere of application provisions of the future Convention of their impact on the supplier, the authors of the draft Convention in Article 2 (1)(b), whilst aware that such an additional criterion would necessarily restrict the cases in which the future Convention would be applicable, concluded that for the future Convention to be applicable by virtue of the operation of the rules of private international law it would have to be necessary not only for the leasing agreement to be governed by the law of a Contracting State but also for the supply agreement to be governed by the law of a Contracting State. It follows that it does not matter whether the law applicable to the leasing agreement is the same as, or differs from that applicable to the supply agreement: the only requirement is that these two laws should be the laws of one or more Contracting States. This alternative connecting factor for the application of the future Convention is, it should be noted, intended to include those cases where the parties themselves designate the law of a Contracting State to govern their respective contractual relations.

75. - In line with Article 95 of the Vienna Sale Convention and Article 28 of the Geneva Agency Convention, it should be noted that Article F of the draft final provisions capable of embodiment in the draft Convention drawn up by the Unidroit Secretariat,\(^{30}\) however, allows States to declare at the time of becoming Parties to the future Convention that they will not be bound by Article 2 (1)(b).

76. - The provisions of Article 2 (2) follow closely those of other recent international commercial law Conventions (notably Article 10 (a) of the Vienna Sale Convention and Article 8 (a) of the Geneva Agency Convention). They are designed to indicate the relevant place of business for the purpose of determining the applicability of the future Convention under Article 2 (1) where one or more of the parties to the transaction has more than one place of business. The relevant place of business is stated to be that which has the closest relationship to the agreement in question, that is the supply agreement or the leasing agreement, and its performance. In determining the closeness of this relationship the draft Convention invites those called upon to apply it to have regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of the agreement in question.

**Article 3**

77. - This article seeks to resolve the difficulties that arise out of the fact that, whereas the inclusion in the leasing agreement of an option to purchase the leased asset in favour of the lessee is in some jurisdictions, notably Civil law systems, an essential ingredient of the atypical

\(^{30}\) Cf. Study LIX - Doc. 49.
The leasing transaction addressed in the draft Convention,\(^{31}\) under other legal systems, notably Common law jurisdictions, the inclusion of such an option would prevent the agreement being qualified as a lease at all and would lead instead to its requalification as a hire-purchase or conditional sale transaction. The purpose of Article 3 is thus essentially to preserve the application of the draft Convention in those jurisdictions in which the inclusion of a purchase option would otherwise destroy the transaction’s characterisation as a lease. Equally in those jurisdictions which would normally regard the inclusion of such a purchase option as an essential ingredient of its domestic financial leases its effect is that such a jurisdiction would have to recognise that a transaction could still be a financial leasing transaction for the purposes of the draft Convention even in the absence of any purchase option in the leasing agreement.

78. - There was a time when those among the authors of the draft Convention who were more accustomed to a compulsory purchase option in the leasing agreement argued that this provision went to the essence of the transaction addressed by the draft Convention and as such should feature among the characteristic traits of the transaction set forth in Article 1 (2). However, given the width of the gulf separating the attitude of the different legal systems on this question of purchase options, it was acknowledged that to elevate the stipulation of such a purchase option to the status of a definitional ingredient of the type of transaction addressed by the draft Convention would be seriously to jeopardise the acceptability of the future Convention in those jurisdictions where the inclusion of such a purchase option would destroy the leasing agreement’s characterisation as a lease altogether. Likewise to attempt to introduce a clause in Article 1 (2) that would encompass the position taken by both groups of legal systems on this point would, it was felt, be to introduce an intolerable degree of legal uncertainty into the applicability of the future Convention. As it stands under Article 3, the inclusion of an option to purchase in the leasing agreement amounts to an optional ingredient of the type of leasing transaction addressed by the draft Convention. The future Convention is intended to apply whether or not a purchase option is included in the leasing agreement in question. The authors of the draft Convention concluded there was no good reason why the draft Convention should not apply regardless of the particular solution adopted on this subject in the individual country. The draft Convention is after all specifically addressed to international transactions and accordingly does not purport to impinge on the varied situation existing in this regard from one country to another regarding wholly domestic transactions.

79. - The words “has or subsequently acquires” are intended to indicate that this provision covers both the case where the purchase option is conferred under the leasing agreement itself – the word “has” is the appropriate word here – and those cases where it is either conferred under a separate agreement, reached say at the end of the lease term, or under a variation of the original leasing agreement – the appropriate words for these cases are “or subsequently acquires”. The question also came up during the drafting of this provision as to whether it would be appropriate to be more explicit as regards the time when the purchase option, where granted, should be exercisable. In practice such options are made exercisable either during or at the end of the lease term. However, it was adjudged better not to lay down any specific time for the exercising of purchase options in the draft Convention so as to leave the parties maximum flexibility in this

\(^{31}\) In these countries such a purchase option represents an important part of the financial bargain for both lessor and lessee, the pre-negotiated price at which the option is exercisable reflecting the amount paid by the lessee in rentals; cf. also §71 supra.
regard; the lessee is therefore free to acquire the asset at the moment in time most favourable to its interests.

80. - At one stage this provision referred to the lessee’s “right” to buy the leased asset. In the end, however, the term “option” was judged more opportune with a view to making it clear that this provision did not purport to cover the situation where the lessee’s right derived from an obligation to purchase the leased asset, since such an agreement would constitute a sale contract.

81. - Apart from the purchase option, where this is exercisable, there are of course two other possible courses of action open to the lessee at the end of the lease term. One of these is stated in this article, namely “to hold” the equipment “on lease for a further period”, usually at a much reduced and in some cases a peppercorn rental. It was not judged necessary to spell out the lessee’s other possible course of action in this provision, first because it is already stated elsewhere, in Article 8 (2), and secondly because it is not in the nature of a special right conferred on the lessee by the leasing agreement but is simply the lessee’s duty where it either has not exercised a purchase option, if exercisable, or has not taken the equipment on lease for a further period, to wit to return the leased asset to the lessor, who will then normally dispose of it on the second-hand market. When Article 3 speaks of the lessee deciding to hold the equipment on “lease” for a further period, this raised the question whether the second lease had necessarily to be a leasing agreement of the kind contemplated by the draft Convention or whether it would be sufficient for it to be a traditional bailment contract. Here again the authors of the draft Convention, anxious to leave the parties the maximum freedom of contract, agreed that both possibilities were intended to be encompassed.

82. - The words “and whether or not for a nominal price or rental” at the end of Article 3 were designed to deal with the controversy that rages in some jurisdictions over what constitutes a sale. An economic test is applied in these jurisdictions whereby if the option fee or renewed rental is purely nominal then the transaction is characterised as a sale, with the concomitant risk that in these jurisdictions the cases for the future Convention’s application might end up being substantially narrowed in respect of such transactions. These words accordingly serve two purposes. First, they indicate that the mere fact that the option fee or renewed rental is nominal does not take the transaction in question outside the future Convention. Secondly, they serve as an indication to those called upon to apply the future Convention that they should not apply general economic tests with a view to excluding from the future Convention what it was intended to cover, namely those transactions which whilst in form leases might in some jurisdictions be regarded as sales.

Article 4

83. - This article deals with the extent to which, once the financial leasing transaction has been concluded, the lessor and the supplier should be free to vary the supply agreement. The basic idea behind this article is that, while there can be no harm in the parties negotiating better terms for themselves, in order to safeguard the interests of the lessee, any attempt to vary the supply agreement once the leasing agreement has been made must be sanctioned by the lessee. Given that it is the lessee who is to use the equipment, it is vital that there should be no room for collusion between the supplier and the lessor to the detriment of the lessee.
84. - Up until the final session of governmental experts the authors of the draft Convention had considered it important that this rule should be balanced by another, making the lessor’s consent necessary for any variation, subsequent to the making of the supply agreement, in the specifications given by the lessee to the supplier. They had taken the view that, just as it is legitimate for the lessee to want to have access to the best equipment available for its particular needs, it is equally legitimate that the lessor should first be given an opportunity to declare its opinion on any consequential variation in the terms of the specifications given by the lessee to the supplier, for instance during the ongoing construction of the item to be leased, that might have the effect of increasing its responsibilities. However, the committee of governmental experts at its final session decided to delete this rule, basically on the ground that it was hard to conceive how the lessee could affect the terms of the supply agreement, once this had been made, in so far as it was not a party to that agreement but also because, in so far as the lessor was a party to the supply agreement, it was merely stating the obvious to require the lessor’s consent to any variation of the specifications given by the lessee to the supplier. The authors of the draft Convention accordingly concluded that the whole question of whether the lessee should have the right to vary the terms of the supply agreement should not be governed by the future Convention, but should rather be left to be settled by the terms of the parties’ own agreement and in accordance with the applicable law.

85. - As has been mentioned above, this article is in no way intended to interfere with the parties’ right to negotiate better terms for themselves, all the more so as the effect of the negotiation of better terms by supplier and lessor could well be to improve the terms of the leasing agreement for the lessee, principally in the shape of lower rental payments. Thus the lessor and the supplier might well agree to vary their original agreement by the terms of a buy-back arrangement, enhancing the lessor’s guarantee and enabling it to pass this onto the lessee in the form of lower rentals. Such private arrangements between the parties are to be expected, given that they will often be dealing with one another on a continuing basis over a number of years. On the other hand, whereas the rule contained in Article 4 is designed to prevent the variation of the supply agreement by the lessor and the supplier inasmuch as the result of such variation would be to worsen the situation of the lessee, it was not considered feasible or worthwhile to formulate a distinction between the positive and negative impact of individual variations on the position of the lessee.

Article 5

86. - One of the thorniest problems arising in connection with leases as indeed with all transactions involving the separation of ownership and possession in respect of property concerns how best to inform innocent third parties coming into contact with leased property, through their dealings with the lessee, that it is subject to a reservation of title, since failing such notification appearances, that is the fact of the lessee’s possession of the asset, would normally induce third parties, notably creditors of the lessee, to believe they were dealing with the owner, rather than the lessee, of the asset in question. This problem was particularly acute in the case of financial institutions contemplating lending to the lessee on the security of its assets, as a physical inspection of all the equipment of the potential debtor of the financial institution would simply not be feasible.

87. - Consideration was given within the Study Group to the use of a whole range of
systems of public notice, from the simple affixing of a plaque on the equipment, as required under the law of more than one country, to the highly sophisticated computerised system of registration against the lessor already in use in more than one jurisdiction. Experience has revealed the limitations of the affixing of plaques as the basis of a foolproof public notice system, such plaques being so relatively easy to remove. Balance-sheets were also considered but rejected as inadequate for this purpose, in view of the fact that they served a quite different function, that of a general public notice, from the function that was required here, namely a notice to a specific kind of third party. The vast majority of opinion within the Study Group recognised the ultimate desirability of a system of registration as the most effective means of giving notice of the lessor’s title to third parties. However, apart from the fact that in many countries registration was only considered feasible for large unit goods that were easily identifiable, such as ships, aircraft and motor vehicles, the greatest single difficulty recognised as obtruding with the embodiment of however minimal a public notice requirement in the future Convention was seen as the very limited number of jurisdictions that had such public notice systems in place at the present time. The organisational and financial implications of a public notice requirement based on registration were accordingly seen as making such a solution a non-starter.

88. - The Study Group was nevertheless anxious that the future Convention should give some expression of its conviction that a public notice system of some sort was the only real answer to this problem, and thus perhaps give some momentum to the future institution of such systems in the various countries. The solution with which the Study Group came up was a rule whereby, where there were rules as to public notice for financial leasing transactions of the type contemplated in the future Convention in the country where the lessee had its principal place of business, then the lessor’s title would only be good against third parties if the lessor had complied with such rules. The corollary of this rule was that, if there were no rules as to public notice for financial leasing transactions under the law of the country where the lessee had its principal place of business, the lessor’s title would automatically be good against third parties.

89. - This rule, while recognised as a key provision of the future Convention in so far as it set out to regulate conflicts over the leased asset which could not simply be regulated in the agreements of the parties, nevertheless attracted much criticism at the first session of governmental experts. This criticism essentially reflected the very different philosophies underlying the methods of resolving conflicts between the dispossessed owner of property and a third party who had acquired that property in good faith in, on the one hand, Common law jurisdictions and, on the other hand, Civil law jurisdictions. Whereas the former, under the nemo dat quod non habet rule, recognised the dispossessed owner’s general right to assert its title against third parties, application of the Civil law principle that en fait de meubles possession vaut titre meant that in Civil law jurisdictions an innocent third party would take free of the dispossessed owner’s title. Civil law jurisdictions proved unwilling to depart from such a fundamental principle of their legal systems for the sake of financial leasing transactions alone. The committee of governmental experts accordingly concluded that it would have to discontinue its efforts to regulate conflicts between the lessor, on the one hand, and both third parties acquiring the equipment from the lessee in good faith and the lessee’s ordinary creditors, on the other. The scope of its efforts was therefore narrowed down to the regulation of those conflicts that arise between the lessor and the ordinary creditors of a lessee that had been declared bankrupt. In any case, the committee was convinced that the incidence of cases
involving a dishonest lessee disposing of the leased asset to a third party would be extremely rare in practice and that the area where real difficulties would arise in this connection was precisely that where the lessee had been declared bankrupt, and that it would be more fruitful for the draft Convention to address this practical problem rather than becoming embroiled in the extremely delicate issue of third parties in good faith.

90. - Another area where the solution of the Study Group attracted considerable criticism from the committee of governmental experts was over the connecting factor to be employed for the purpose of determining the public notice requirement to be incorporated in the future Convention. The Study Group had made this the law of the State where the lessee had its principal place of business. However, concern was expressed in some quarters at the prospect of the lessor’s rights as against third parties being subordinated to a public notice requirement imposed by the law of a State other than that where the equipment was located. The task of third parties in seeking to comply with such a requirement could well, it was argued, be most arduous. They might well not know that the lessee was holding the equipment on lease, let alone that the lease in question was a cross-border lease governed by special international rules. The country where the lessee’s principal place of business was located might well, moreover, be a quite different country from that where the equipment was physically located, thus creating problems for the third parties in question in knowing which country’s public notice records to search. The reason why the Study Group had decided to depart from the generally accepted connecting factor for determining questions of title to property or proprietary rights, that is the *lex rei sitae*, was that an important category of leased assets, particularly in international leases, was mobile and by its very nature liable to move from one jurisdiction to another. As an example of the problems inherent in taking the *lex rei sitae* as the appropriate connecting factor for the public notice requirement in respect of this category of equipment, the committee considered the case of construction equipment on lease to a construction firm that regularly moved all round the world. It concluded that it would be unrealistic to expect such equipment to have to be registered in each of the countries where it happened to be used for a shorter or longer period of time.

91. - Only a small number of countries had passed legislation on this subject and it was accordingly felt that instruction might usefully be sought in the solutions proposed under these statutes. The French legislator in its 1972 decree on the public notice formalities to be complied with in respect of financial leasing transactions, for instance, had selected the place where the lessee had its principal place of business in preference to the place where the equipment was located as the appropriate place for registration. The reasons underlying this choice were as follows. First, given that this article was concerned more with possible conflicts between the lessor and third party creditors of a bankrupt lessee than with the unlikely case of a conflict between the lessor and innocent third parties to whom the lessee had fraudulently disposed of the leased asset, the lessee’s principal place of business was particularly appropriate as a connecting factor in so far as it would normally be in the country where the lessee had its principal place of business that its bankruptcy would be declared. Secondly, the law of the State where the lessee had its principal place of business had the advantage over the *lex rei sitae* that the places to which a third party would have to look would be concentrated in one country. Thirdly, in the case of the arrest of a leased ship or the attachment of a leased aircraft carried out in respect of a debt owed by the lessee’s principal place of business while the ship or the aircraft was abroad, provided that the State where the arrest or the attachment was carried out was a Party to the future Convention the advantage of having the lessee’s principal place of
business as the appropriate connecting factor would be that, once the lessee’s representative had informed the person carrying out the arrest or the attachment that the ship or the aircraft, as the case might be, was on lease, this person would simply have to check against the public registry of the place where the lessee had its principal place of business.

92. - Under Article 9 of the Uniform Commercial Code of the United States of America and under the Saskatchewan Personal Property Security Act, S.S. 1978-79 a distinction was drawn for registration purposes between equipment of a type likely to be used in more than one jurisdiction, that is equipment that is intrinsically mobile, and equipment that is likely to be used in only one jurisdiction. For the former category of equipment the law of registration was the law of the lessee’s place of business and for the latter it was the lex rei sitae.

93. - The foregoing considerations were reflected in the final solution with which the committee of governmental experts came up in Article 5. Their text only essays a solution to those conflicts between the lessor and third party creditors of the lessee arising in the limited context of the latter’s bankruptcy. It does not attempt to deal with conflicts between the lessor and those third parties acquiring the leased asset in good faith from the lessee. It should be noted that this article speaks not of the lessor’s title to the equipment but rather of the lessor’s real rights in the equipment, reflecting the decision of the authors of the draft Convention to encompass situations, such as sub-leasing arrangements, where the lessor will not necessarily be owner of the equipment. Under the terms of Article 5 (1) the lessor’s real rights in the equipment are stated to be valid against the lessee’s trustee in bankruptcy and unsecured creditors, including creditors who have obtained an attachment or execution. The reason why it was deemed appropriate to insert a special reference to creditors of the lessee who have obtained a judicial attachment or execution was that simply to make the lessor’s rights valid against unsecured creditors of the lessee would in itself achieve nothing in so far as an unsecured creditor will only seek to overreach the lessor’s rights at such time as it seeks to obtain the leased asset by some judicial process.

94. - The general rule enunciated in Article 5 (1) is, however, subject to a special rule set out in Article 5 (2). This covers the case where under the applicable law the lessor’s real rights against the lessee’s trustee in bankruptcy and unsecured creditors are only valid upon compliance with a public notice requirement. Where this is the case Article 5 (2) provides that the lessor’s real rights shall only be valid against the lessee’s trustee in bankruptcy and unsecured creditors under the future Convention where the lessor has complied with such a requirement. Where the lessor fails to comply with such a requirement of the applicable law, then the lessor’s real rights in the equipment are as a result no longer valid against the lessee’s trustee in bankruptcy and unsecured creditors under the draft Convention.

95. - In the light of the various problems alluded to above in respect of the choice of connecting factor for the determination of the public notice requirement laid down in Article 5 (2), the committee of governmental experts at its final session hit upon a new formula for establishing the relevant connecting factor. Article 5 (3) in fact establishes a three-tier system for this purpose, equipment being divided into three different categories. In respect of the generality of equipment the applicable law is, in line with the traditional conflicts rule in this field, the lex rei sitae (Article 5 (3)(c)). On the other hand, this law was not judged to be appropriate for that class of equipment which, by virtue of being mobile, would normally be used in more than one jurisdiction. Under Article 5 (3)(b) the applicable law for this class of
equipment is accordingly made the law of the State where the lessee has its principal place of business. Anxious to avoid creating any inference under Article 5 (2) of a double registration requirement for that special class of mobile equipment, such as ships and aircraft, already subject to registration – the term “registration” in this context being used not in the sense of registration of rights in, ownership of, or of a security interest in an asset but in the sense of registration of a particular type of asset – pursuant to the law of a State, the committee proposed in Article 5 (3)(a) that the applicable law for this special class of equipment should be the law of the State of registration. However, the committee of governmental experts was only too aware of its limited expertise in the specialist field of ship and aircraft registration and of the complexities inherent in the subject, notably the different purposes for which registration may be required, and therefore requested the Unidroit Secretariat to sound out technical experts in advance of the diplomatic Conference with a view to ascertaining whether the solution it had come up with in Article 5 (3)(a) would be workable in practice. This enquiry was underway at the time this report was being written. In the meantime Article 5 (3)(a) is presented in square brackets indicating that it is a matter that will have to be settled at the diplomatic Conference. It should be noted that two delegations to the final session of governmental experts took the view that a better solution to the problem which the draft Convention sought to deal with in Article 5 (3)(a) was to exclude ships and aircraft from the application of the provisions of Article 5 altogether.

96. - Square brackets were also inserted around the words “mobile” and “normally used in more than one State” in Article 5 (3)(b). The term “mobile” aroused much criticism within the committee of governmental experts, on the ground that virtually all equipment apart from fixtures could be considered to be mobile. As a result it was proposed either clarifying it by the addition of the words “normally used in more than one State” along the lines of the formula employed in Article 9 of the Uniform Commercial Code and similarly inspired Canadian legislation or replacing it by these words altogether. As it proved difficult to reach a decision on this point within the committee of governmental experts, it was felt wiser to forward both expressions to the diplomatic Conference for decision.

97. - Article 5 (4) is designed to indicate that all questions of priority as between the lessor and a lien creditor or secured creditor of the lessee are not intended to be dealt with in Article 5 and are accordingly left to be dealt with by the applicable law.

**Article 6**

98. - This article deals with the situation, frequent in practice, where the leased equipment becomes a fixture of real property. The text of this article as adopted by the Study Group sought to regulate eventual conflicts of interest arising in respect of the leased asset as between the equipment lessor and the real estate lessor or an encumbrancer of the realty. It was agreed that, as with the eventual conflicts of interest addressed in Article 5, these conflicts would in practice only arise where the lessee had gone bankrupt. The solution proposed by the Study Group was, along the lines of Article 9-313:5 of the Uniform Commercial Code and Section 36(4) of the Ontario Personal Property Security Act of 1967, to recognise the equipment lessor’s right to enter upon the property of the owner or encumbrancer of the realty to sever its equipment, subject only to it having priority under the *lex rei sitae* over the claim of any person having an interest in the realty concerned and to its duty to reimburse the owner or encumbrancer of the realty for any damage occasioned by the act of severance.
99. - This rule, however, proved unacceptable to the representative of a Civil law system attending the first session of governmental experts. He saw it as proposing a radical departure from what he considered to be a fundamental tenet of his legal system, namely that the owner of realty has priority over the owner of personality, and he could not see the case for making such an exception for the sake of financial leasing transactions alone. The drafting committee, unable to make any headway with the various compromise solutions put forward, accordingly proposed the deletion of Article 6 at the conclusion of the committee of governmental experts' first reading. However, on second reading, while there was agreement that it would be unwise to attempt to reinstate any substantive rule on this subject, support emerged for a limited restoration of this article designed to put parties to financial leasing transactions on notice that all conflicts arising as between the equipment lessor and the owner or encumbrancer of the realty to which the leased equipment has become a fixture are referred to the *lex rei sitae* and that the applicable rules may accordingly differ depending on the location of the equipment. This proposal was accepted by the committee of governmental experts and incorporated in the new Article 6. The conflicts of interest referred under this rule to the *lex rei sitae* are spelled out in this provision as, first, the whole question of whether the leased equipment has or has not become a fixture to, or incorporated in realty and, secondly, the question of the rights of the equipment lessor and the owner or encumbrancer of the realty *inter se* in relation to the equipment.

**Article 7**

100. - At first sight the provisions of Article 7 might appear to involve a fairly radical departure from the law of most countries. In fact, they do little more than reflect the situation existing in practice, in that financial leases invariably contain detailed provisions absolving the lessor from responsibility for defective or non-conforming equipment and requiring the lessee to indemnify the lessor against claims brought by third parties. It reflects the general philosophy underlying the draft Convention, that is the special nature of financial leasing, seen both in the lessor's role and in that of the lessee, in excluding the lessor's liability in contract or tort in most situations in which it would otherwise normally have been held liable in its capacity of lessor of the equipment. The finance lessor will in most cases have no technical expertise with regard to the equipment's specifications, will never take delivery of the equipment and normally will not even have any reason to see it. Its role is limited to supplying the capital needed for the acquisition of the equipment. It is the lessee, we have seen in Article 1 (2)(a)*supra*, who relies primarily on its own skill and judgment in selecting both equipment and supplier, and who typically conducts negotiations with the supplier on its own as a reasonably informed user. If there is any reliance on the knowledge and representations of another party in this context, indeed it is the lessee's reliance on the supplier's knowledge of the equipment and its representations in this regard, so much so indeed that it is the supplier rather than the lessor who in effect under the draft Convention is in many ways treated as the party who places the equipment into the stream of commerce. In Article 9, moreover, the draft Convention recognises that in most cases it is the supplier, rather than the lessor, who is the appropriate party from whom the lessee should seek redress where the equipment turns out to be defective or otherwise not in conformity with the terms of the supply agreement.

**Exceptions to the general principle of the lessor's immunity**

101. - Before analysing the extent of the immunity granted the lessor under this article, it
is important to be clear about what is not intended to be included in this immunity. It is an
exoneration that is confined to those liabilities that would flow as a matter of law from the
lessor's notional delivery of the equipment under the leasing agreement, from the lessor's being
treated as the legal supplier of the equipment in relation to the lessee under most jurisdictions.
It is not therefore intended to affect those liabilities that would be imposed by contract, whether
by express terms of the leasing agreement or by terms implied in fact. This restriction of the
lessor's immunity is spelled out in the opening words of Article 7 (1)(a) ("Except as otherwise
provided by ... the leasing agreement"). Equally the lessor's immunity in relation to the lessee
is clearly not intended to affect those liabilities imposed upon the lessor elsewhere in the draft
Convention. This is notably the case with the provisions of Article 10. This limitation on the
lessor's immunity is also spelled out in the opening words of Article 7 (1)(a) ("Except as
otherwise provided by this Convention"). Equally the general immunity conferred upon the
lessor under Article 7 is not intended to extend to breaches of statutory duty, in that it is
questionable whether States would be prepared to accept an exclusion of those special duties
imposed by statute over and above those imposed by the general law of tort.

102. - The fact that the immunity conferred under Article 7 (1)(a) is stated to be
commensurate with the lessor's non-intervention in the selection of the supplier or the
specifications of the equipment means, as a corollary, that where the lessor does so intervene,
then it will be liable to the lessee to the extent of its intervention. This follows from the logical
premise upon which the immunity conferred upon the lessor under Article 7 is founded, namely
the lessor's technical neutrality in relation to the equipment. We have already seen, in Article
1 (2)(a), that this technical neutrality of the lessor has been made a definitional ingredient of
the type of lease addressed by the draft Convention. The question of the degree of the lessor's
intervention in the sphere of autonomy normally reserved exclusively to the lessee under the
draft Convention needed to defeat the lessor's right to raise its immunity under Article 7 (1)(a)
was considered a matter best left to be resolved by the applicable national law.\(^{32}\)

103. - It follows from the fact that the immunity in tort conferred upon the lessor under
Article 7 (1)(b) is stated to extend only to that liability for personal injury or damage to property
casued by the equipment that would flow from its capacity of lessor that it is not the intention
of Article 7 (1) of the draft Convention to affect any liability that might be imposed on a finance
lessor in some other capacity, notably as owner of the leased asset. Whereas there are under
most jurisdictions relatively few liabilities that would in this context flow from ownership as
such, most liabilities being imposed on the lessor as legal supplier of the equipment, there is
special international legislation, notably the International Convention on Civil Liability for Oil
Pollution Damage adopted in Brussels in 1969 and amended in London in 1984, which would
have the effect of imposing liability on a finance lessor as owner. The authors of the draft
Convention were at all times conscious of the need to avoid the embodiment in the future
Convention of a rule that would run counter to such special international legislation to which
States that might otherwise have wished to become Parties to the future Convention might
already be Contracting Parties. Article 7 (1)(c) accordingly makes it clear that the immunity
from liability conferred upon the lessor under Article 7 (1)(a) and (b) is without prejudice to
any liability it might incur as owner of the equipment but that the question of such liability is
not governed by the draft Convention.

\(^{32}\) Regarding this provision cf. also §68 supra.
104. - The fact that the provisions of Article 7 (1)(c) speak not only of the lessor’s liability as owner but more generally of its liability in any capacity other than as lessor, including that of owner, indicates that the authors of the draft Convention contemplated that there might well be capacities other than that of owner in which the lessor’s immunity under Article 7 might be forfeited. This might, in particular, be the case with the 1985 E.E.C. Directive on the approximation of the laws, regulations and administrative provisions of the Member States concerning liability for defective products, Article 3 (2) of which provides that any person importing a product into a Community country with a view to leasing it is to be deemed a producer for the purposes of the Directive and is to be liable to the same extent as if it were a producer. The authors of the draft Convention, however, took the view that it was more practical and allowed for greater flexibility to refrain from seeking to enunciate an exhaustive list of all the capacities in which the lessor might be found liable, their primary objective being rather to ensure that the lessor would not henceforth be treated, simply by virtue of letting out the equipment, as the notional legal supplier of the equipment.

105. - The other exception to the lessor’s immunity under Article 7 proved rather more troublesome for the committee of governmental experts. This concerns the lessor’s duty to ensure the lessee’s quiet possession under the lease. The division of opinion that emerged within the committee of governmental experts as to the appropriate measure of the lessor’s liability for disturbances of the lessee’s quiet possession is reflected in the presentation of alternative solutions, Alternative I and Alternative II, to Article 7 (2). It also reflects the inherent contrast between, on the one hand, the idea expressed by certain delegations to the committee of governmental experts that it was appropriate to extend the notion that quiet possession goes to the essence of a lease to the atypical leasing transaction addressed by the draft Convention and, on the other, the reality that, in view of the lessor’s purely financial role in such transactions, the lessor’s warranty of quiet possession is invariably excluded in finance leases.

106. - Up until the second session of governmental experts this provision had attracted no controversy, the idea all along having been simply to ensure that the lessor remain liable for any disturbance of the lessee’s quiet possession resulting from the lawful act of a third party having a superior title or right not derived from any act or omission of the lessee, that is where the lessor did not have the right to dispose of the equipment or where its right to do so was qualified in some way and because of that a third party was entitled to claim possession by virtue of a paramount title, for example where its use was in breach of a patent or trademark. At the second session of governmental experts, however, a body of feeling emerged that favoured the extension of the lessor’s warranty of quiet possession under Article 7 (2) to cover a disturbance resulting from the lawful act of a third party not necessarily having a superior title or right but laying claim to such a superior title or right. The committee, however, was divided on the advisability of agreeing to such an extension and accordingly forwarded alternatives to the final session of governmental experts. At this session the committee, albeit still divided, accepted the principle that the lessor’s liability for any disturbance of the lessee’s quiet possession resulting from the lawful act of a third party having a superior title or right should be extended to cover any disturbance of the lessee’s quiet possession resulting from a third party laying claim to such a superior title or right. It was, however, the committee’s opinion that the lessor could not be made liable for all claims to a superior title or right made by third parties and that the category of claims for which the lessor could be held liable under Article 7 (2) would have to be narrowed down. The committee took the view that the lessor’s warranty of quiet
possession in relation to such claims would have to be limited to claims that were serious and therefore not merely vexatious. The criterion it adopted for ascertaining the seriousness or otherwise of such claims was to require that the person asserting such a claim was acting under the authority of the court, for instance under an interim order for the return of the property to the claimant. Where what in the event turned out to be an unsurmountable division of opinion emerged within the committee at this final session was over whether the lessor had to have been at fault in a third party being able to disturb the lessee’s quiet possession for it to be liable under this provision. On the one hand, there was a body of feeling that the lessor should incur liability under this provision regardless of whether or not it had been at fault in the third party being able to disturb the lessee’s quiet possession, the only circumstances in which it would be relieved from such liability being where the disturbance had been caused by the lessee’s own fault. This broader measure of the lessor’s liability is expressed in Alternative I. On the other hand, there was a body of feeling which maintained that the lessor had actually to have been at fault in the third party being able to disturb the lessee’s quiet possession for it to incur liability under Article 7 (2). This narrower measure of the lessor’s liability is expressed in Alternative II, which, it should be noted, includes an extra paragraph, Article 7 (3), the effect of which would be to preserve any broader warranty of quiet possession guaranteed under the applicable law. The division of opinion on this provision was so marked that, when the committee of governmental experts came to discuss which provisions of the future Convention should be made mandatory under Article 14, certain representatives, admittedly reflecting a minority opinion, again took the view that the lessor’s right to quiet possession was of the essence of a finance lease and that Article 7 (2) should therefore be made a mandatory provision of the future Convention. This was a matter on which, the committee being unable to reach agreement, it was therefore judged best to leave the making of a decision to the diplomatic Conference and hence the reference to Article 7 (2) as a mandatory provision of the draft Convention is presented in square brackets.

107. - Being clear in our minds about the cases not meant to be covered by the general immunity in contract and tort conferred upon the lessor under Article 7, we now have to address ourselves to the content of this immunity. This immunity is examined below, first, as regards its impact on the liability that would ordinarily attach to the lessor vis-à-vis the lessee and, secondly, in its impact on that liability in tort that might otherwise attach to the lessor vis-à-vis third parties.

Lessor’s liability to lessee

108. - Article 7 (1)(a) has the effect of excluding those contractual terms implied by law from the supply of equipment, notably the duty to ensure that the equipment supplied is of merchantable quality and fit for its known purpose. The need to exclude the lessor’s liability in respect of these duties arises, as we have seen, from the fact that most jurisdictions treat the lessor as the legal supplier in relation to the lessee, even though it does not physically deliver the equipment. Breach of these duties would usually entitle the lessee to damages as against the lessor and might give it a right to reject the equipment and withhold payment of its rentals or even terminate the leasing agreement completely. As such the immunity in contract conferred upon the lessor under this clause has, of course, to be read in conjunction with, and is correspondingly limited by the lessee’s right to reject the equipment, terminate the leasing agreement and in certain limited circumstances withhold the payment of its rentals under
Article 10.

109. - The provisions of Article 7 (1)(a) are also intended to exclude those liabilities in tort that the lessor would normally incur towards the lessee in its capacity of lessor. This would, for example, be the case with any liability in tort that the lessor might incur through the equipment proving not only to be defective but also unsafe and causing death or personal injury to the lessee, or damage to property of the lessee, although most jurisdictions would make such liability dependent in any event on proof of negligence on the part of the lessor. The immunity from liability in tort conferred upon the lessor under Article 7 (1)(a) would, however, probably have its greatest impact in those jurisdictions, in particular the United States of America, in which the lessor might in certain circumstances find itself exposed to a suit alleging strict liability on the ground that it was to be considered as having introduced the defective equipment into the stream of commerce. This immunity has, however, to be interpreted in conjunction with what has already been said (33) regarding any liability that the lessor might incur as a producer under the aforementioned 1985 E.E.C. Directive. The lessor’s general immunity in tort would, however, in principle preclude the lessee from claiming contribution or indemnity from the lessor in respect of liability incurred by the lessee to a third party as a result of a defect in the equipment.

110. - The basic reasons underlying the decision of the authors of the draft Convention to exclude the lessor’s liability in contract and tort towards the lessee in most situations have already been rehearsed above. (34) It suffices to recall here, by way of justification of the specific exclusion of the lessor’s liability towards the lessee in respect of the implied warranty of merchantable quality, that the lessor will not normally be a merchant as to the type of equipment leased: it will generally only be a merchant in the extension of credit. With regard to the exclusion of the lessor’s liability towards the lessee in respect of the implied warranty of the equipment’s fitness for its known purpose, on the other hand, it has to be remembered that the lessor will not normally have shown any skill or exercised any judgment upon which the lessee has relied in its selection of the equipment. The case for the lessor’s immunity from liability in tort towards the lessee is founded on its non-involvement in the selection of the supplier and the specifications of the equipment and on the fact that it will normally at no stage profess any technical expertise with regard to the equipment’s physical characteristics.

Lessor’s liability to third parties

111. - A finance lessor will not as a rule incur liability to third parties who sustain injury or damage to their person or property as a result of defects in the equipment. There being by definition no contractual nexus between the lessor and such third parties, such a claim would only lie in tort and most jurisdictions would require the third party to show that the lessor had been guilty of negligence, for instance in leasing equipment that it knew or ought to have known was unsafe. Given the finance lessor’s technical neutrality in most financial leases, the burden of proving such negligence on the part of a finance lessor is usually a heavy one. Moreover, in most Common law jurisdictions such liability would attach to the lessee as being the party in possession of the equipment. The major impact of the immunity from liability in tort vis-à-vis third parties conferred upon the lessor under Article 7 (1)(b) is therefore once again likely to

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(33) Cf. §104 supra.
(34) Cf. §100 supra.
be in those jurisdictions, such as the United States of America, with an ever expanding concept of strict products liability as a result of which the lessor might find itself being exposed to a suit alleging such strict liability merely by virtue of the fact that the lessor is to be treated as notionally delivering the equipment under the leasing agreement and therefore as notionally putting it into the stream of commerce. As we have already indicated in respect of the immunity in tort vis-à-vis the lessee conferred upon the lessor under Article 7 (1)(a), this immunity must, however, be interpreted in conjunction with what we have already said (35) regarding any liability that the lessor might incur as a producer under the aforementioned 1985 E.E.C. Directive.

Article 8

112. - This article spells out the lessee’s duty of care in relation to the equipment from the moment that it is delivered into the lessee’s hands up until the time that it has to be returned to the lessor at the end of the lease term. Paragraph 1 details the lessee’s duty of care during the lease term, while paragraph 2 specifies the condition in which the equipment must be returned to the lessor at the end of the lease term, in the event that it does not exercise any purchase option that it may have or decides not to seek a renewal of the lease.

113. - The duty of care imposed on the lessee under Article 8 (1) is that of a “normal user”. The standard of care that must be displayed by the lessee to this end is specified to be “proper care”. This standard of care is further clarified by the additional requirement that the lessee must keep the equipment in the same condition as it was in at the time of delivery, after allowance has been made for fair wear and tear. In effect this means that the lessee is under a duty to keep the equipment in good working order. This is made even more explicit by Article 8 (2) which specifies that when the lessee comes to return the equipment to the lessor at the end of the lease term, then the equipment must be in “the condition specified in the previous paragraph”, in other words still in a state of good working order. It is true that individual leasing agreements may regulate these matters differently. In some countries it may, for instance, be unusual for there to be an exception in the leasing agreement for fair wear and tear. However, whilst it is also true that leasing agreements invariably contain detailed provisions as to possession, care and use of the equipment, the authors of the draft Convention considered that the provisions of Article 8 could serve a useful purpose in those cases where the lease was silent on some or all of these matters, all the more so as this was par excellence a provision that they intended to be subject to the parties’ agreement.

114. - There was discussion within the Study Group of whether the draft Convention should cover the question of what should happen where the equipment was accidentally destroyed at some stage during the leasing agreement. While the value of the equipment would normally be covered by insurance, this still left the problems of how the insurance monies should be applied and what should be the effect of destruction of the equipment on the leasing agreement: if the insurance monies were to be applied in restoring the equipment, the question arose as to whether a new contract came into existence between the parties to the original leasing agreement or whether the original agreement should go on applying to the restored equipment. It was the opinion of the authors of the draft Convention that this was a matter best left to be settled by the parties in their contract.

(35) Cf. §104 supra.
Article 9

115. - The problem addressed by this article is that of the lessee’s remedies against the supplier where the latter has failed to tender delivery in conformity with the terms of the supply agreement. The wide terms of the immunity from liability vis-à-vis the lessee conferred upon the lessor under Article 7 (1) presuppose an alternative avenue of redress for the lessee for the deleterious consequences which it sustains through such a breach of the terms of the supply agreement by the supplier. The authors of the draft Convention took the view, as we have seen above, that since it is the lessee and the supplier who typically conduct negotiations on their own regarding the equipment’s specifications and since if the lessee relies on the knowledge and representations of another party in this context it is upon the supplier’s, the most appropriate party from whom the lessee should seek redress in the event of such a breach of the supply agreement by the supplier is the supplier itself. However, the conversion of this principle into an effective right of action exercisable directly by the lessee proved to be the source of some difficulty.

116. - In effect, unless some form of collateral contract can be deduced in the circumstances from the negotiations between lessee and supplier, there is no contractual nexus between these two parties. This has not surprisingly hitherto created problems for the lessee wishing to bring proceedings against the supplier. The techniques employed to get round this problem have varied. Some jurisdictions have treated the supply agreement as creating stipulations for the benefit of a third party, in this case the lessee. This technique was recently given the legislative stamp of approval when it was embodied in Section 2A-209 (“lessee under finance lease as beneficiary of supply contract”) of the proposed final draft (6 April 1987) of Article 2A (Leases) of the Uniform Commercial Code. The techniques generally employed have, however, rather involved the lessor agreeing either to assign its claims against the supplier under the supply agreement to the lessee or to enforce its own rights as buyer against the supplier for the lessee’s benefit, or else the lessor, when placing the order for the equipment, contracting as agent for the lessee as well as on its own behalf. Both these techniques were adjudged by the Study Group to be inadequate inasmuch as the claim pursued by or in the right of the lessor can only be for such loss as would have been recoverable by the lessor, whereas the lessee will naturally enough be wanting to recover its own measure of loss. This may well differ from the lessor’s. To take the example of equipment which upon delivery proves to be partially unfit for the purpose for which it was intended, the lessor will, under the hell and high water clause customarily included in financial leasing agreements, be entitled to recover its rentals come what may. The supplier could accordingly with reason assert in its defence to any claim brought by the lessor that the latter has not sustained any financial loss, save to the extent that the value of the equipment for re-leasing or re-sale purposes has depreciated in proportion to the extent to which it had proved to be partially unfit for the purpose for which it was intended. The lessee’s measure of loss will, on the other hand, be quite different from that of the lessor. Its loss will be essentially consequential in nature, in the shape of the loss of production and trading income that it will sustain through the equipment’s partial unfitness for its purpose, not to mention the negative impact that its loss of production will probably also have on its trading image.

117. - The lessee might, however, find itself entitled to nothing more than nominal damages if restricted to recover against the supplier only as the lessor’s assignee. It was to meet the foregoing problems, notably that posed by the lessee’s lack of privity of contract with
the supplier, that the Study Group proposed that the future Convention should create a new statutory direct right of action exercisable by the lessee against the supplier. This solution, however, proved to be the source of misgivings among some members of the committee of governmental experts at its first session. They feared lest their legal systems might be reluctant to accept the introduction of such a direct right of action when the same result could already be achieved under their legal systems by the lessor’s assignment of its rights under the supply agreement. These jurisdictions, it transpired, did not have the problem experienced by so many legal systems discussed above, namely that a lessee would be restricted as assignee to the measure of loss recoverable by its assignor. Under the principle of the Drittschaden-liquidation, in Austria and the Federal Republic of Germany, for example, it was possible for one party to recover in respect of the loss of another party who, while not a party to the contract in question, has a close connection thereto.

118. - The assignment solution nevertheless continued to pose many problems for the jurisdictions which did not have this possibility. Moreover, the measure of loss recoverable by the lessor against the supplier might be subject to qualification for some reason, for instance by virtue of a right of set-off in favour of the supplier, which would result in the lessee’s remedies under an assignment from the lessor being also correspondingly limited. Another problem with the assignment solution resided in what was seen as the impossibility for the lessor to have to assign all its rights under the supply agreement. Some of the lessor’s rights, it was argued, the lessor could not reasonably be expected to abandon. This was in particular the case with its right to terminate the supply agreement, since this would have the effect of revesting title to the equipment in the supplier, whereas for the lessor its title was an essential element of its security and under many jurisdictions the basis of its receiving those tax indemnification benefits which enabled it to offer the lessee more advantageous rental terms. This in turn raised the whole question of which of the rights of the lessor under the supply agreement would, under the assignment solution, have to be assigned to the lessee.

119. - Once it became clear that neither the assignment solution nor the direct right of action solution was going to prove acceptable, the committee looked at different compromise solutions. One of these proposed that, where the supplier knew the purpose for which the lessee required the equipment and the loss sustained by the lessee was therefore reasonably foreseeable by the supplier, the lessee should be entitled to require the lessor to bring legal proceedings to recover both its loss as well as any additional loss sustained by the lessor itself. This would, in particular, have met one of the objections raised to the direct right of action solution, namely that the supplier would face the likelihood of two different claims being brought by two different parties in respect of the same damage on two separate occasions. However, other compromise solutions, essentially based on the lessee being for the purposes of this provision treated as an additional party to the supply agreement, fared better.

120. - Indeed the solution which the committee of governmental experts finally hit upon in Article 9 (1) was to extend the benefit of the supplier’s duties under the supply agreement to the lessee as if the latter were a party to that agreement and as if the equipment were to be

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(36) This argument rested on the premise that the supplier would normally expect to find the lessor as its only interlocutor but this reasoning may be criticised as in practice the specifications regarding the equipment are negotiated directly between lessee and supplier and it is accordingly not unreasonable for the latter to expect to find the lessee as its adversary in the event of litigation.
supplied directly to the lessee. This solution, it should be noted, has much in common with that of paragraph 1 of the proposed new Section 2A-209 of the Uniform Commercial Code. (37) Originally the authors of the draft Convention proposed making the benefit of this provision available only where the supplier knew the purpose for which the lessee required the equipment, that is for the purpose of being held on lease, but subsequently they adjudged this specification to be superfluous in that it followed automatically from the terms in which the sphere of application provisions of the future Convention were drawn, in particular the words “to the knowledge of the supplier” incorporated in Article 1 (2)(b), that the future Convention would only apply where the supplier knew that the equipment was to be held on lease. Prior to the final session of governmental experts the words “for its professional or business purposes” featured at the end of Article 9 (1) but these too were finally adjudged to be superfluous in view of the fact that, by virtue of Article 1 (3), the future Convention was in any event only intended to apply to transactions in which equipment was to be used primarily for such business or professional purposes.

121. - As a rider to the rule set out in Article 9 (1), Article 9 (2) makes it clear, however, that, for the reasons expounded above, (38) the rights conferred upon the lessee vis-à-vis the supplier under Article 9 (1) do not include the right to terminate or rescind the supply agreement, rights which remain vested in the lessor alone. There was a proposal that the right to vary the supply agreement should also be specifically excluded under this provision from those rights conferred upon the lessee vis-à-vis the supplier under Article 9 (1). We have already had occasion to comment on the fate reserved to this proposal in the context of Article 4. (39)

122. - The authors of the draft Convention were at all times conscious of the need to avoid the supplier being exposed to liability in respect of the same loss or damage twice over, that is to both lessor and lessee. Indeed the Study Group essayed a solution to this problem the effect of which would have been to require both lessor and lessee to be joined as parties to any proceedings against the supplier for the latter’s breach of the terms of the supply agreement. This proposal had to be dropped because in the event it was feared lest it might unduly encroach on domestic procedural law. A similar proposal, for an additional paragraph to Article 9, was made within the forum of the committee of governmental experts. This proposal would have had the effect that, once the lessee had acquired rights of action as against the supplier under Article 9 (1), then these rights would no longer have been exercisable by the lessor against the supplier. However, this proposal was also found unacceptable, on the ground that the interests of the lessor and the lessee were quite distinct. Whilst in the event unable to agree on a provision on this matter, it was nevertheless the committee’s feeling that the draft Convention should be understood on the basis that the supplier could not be held liable to two parties for the same loss or damage.

(37) This provides as follows:
“(1) The benefit of the supplier’s promises to the lessor under the supply contract and of all warranties, whether express or implied, under the supply contract, extends to the lessee to the extent of the lessee’s leasehold interest under a finance lease related to the supply contract, but subject to the terms of the supply contract and all of the supplier’s defenses or claims arising therefrom.”
(38) Cf. §118 supra.
(39) Cf. §84 supra.
Article 10

123. - This article treats of the lessee's remedies against the lessor in the event of the supplier's failure to tender delivery in conformity with the terms of the supply agreement. It should be borne in mind that this is a matter normally exhaustively regulated in the leasing agreement and as such the provisions of this article are intended to be subject to the parties' agreement under Article 14.

124. - The first of the lessee's remedies against the lessor under this article is detailed in paragraphs 1 and 2. This is the right to reject the leased equipment. It is stated to arise either where the equipment upon delivery proves to be not in conformity with the terms of the supply agreement, which basically means that it is either wholly or partly defective (Article 10 (1)(a)) or where delivery is not tendered within a reasonable time of the date fixed for delivery or, where no delivery date was fixed, within a reasonable time of the making of the leasing agreement (Article 10 (1)(b)). The logic behind this provision is that it would be wrong to require the lessee to wait for delivery indefinitely or to have to make do with non-conforming equipment. It will be noted that in determining the relevant delivery date for the purpose of calculating the "reasonable" time to be allowed for delivery, Article 10 (1)(b) accords priority to the date set in the leasing agreement. Thus if a date for delivery is set in both the leasing agreement and the supply agreement, it is that fixed in the leasing agreement that provides the starting point for the running of the "reasonable" period of time allowed for delivery under Article 10 (1)(b). The due delivery date fixed in the supply agreement provides this starting point only where no such date is stipulated in the leasing agreement. The priority given to the date fixed in the leasing agreement reflects the fact that the remedy being granted to the lessee under these paragraphs is against the lessor. As has already been explained supra in the context of Article 9, (40) the reason why the authors of the draft Convention considered it appropriate to grant the lessee this remedy vis-à-vis the lessor and not vis-à-vis the supplier stems from the fact that the effect of granting the lessee the right to reject the equipment as against the supplier would have been to divest the lessor of its security in the transaction, namely its title to the equipment.

125. - Paragraph 2 of this article makes the lessee's right to reject vis-à-vis the lessor exercisable by notice. Such notice must be given to the lessor within a reasonable time after the lessee has discovered the non-conformity or ought to have discovered it. This language is clearly designed to cover the case of hidden defects which only emerge some time after delivery has been tendered. The lessor is given the right to cure the non-conformity by a fresh tender provided this is made within a reasonable time after the giving of notice to reject. The subject of the "fresh tender" is specified to be either a re-tender of the same piece of equipment as was tendered before, therefore suitably repaired, or else the tender of an alternative item of equipment, corresponding to that stipulated for under the supply agreement. A propos of the lessor's right to make a fresh tender, the view was expressed that it might be desirable to restrict this right to re-tender so as not to subject the lessee to the possibility of an endless series of non-conforming tenders, each made within a reasonable time after notice of rejection of the previous tender. It was feared that this might unfairly limit the lessee's chances of looking elsewhere for the equipment that it required. It was nevertheless explained that this provision sought merely

(40) Cf. §118 supra.
to give the lessor a parallel right to cure a non-conforming tender by making a fresh tender to the corresponding right given to a seller under the Vienna Sale Convention. Moreover, the language employed in Article 10 (2) speaks specifically of a fresh tender.

126. - There was some criticism of the expression “a reasonable time” as employed in this provision. The fear was expressed that it erred too much on the side of vagueness. However, it was explained that this was a notion, drawn from the Common law, that had been imported into other international Conventions in the commercial law sector, such as the Vienna Sale Convention. It afforded a measure of flexibility that was particularly desirable in international transactions in so far as it would be impossible to specify a single period apt for all transactions and all circumstances. Just one example of the way in which circumstances could change from one international transaction to another would be the distances involved. It was accordingly judged that this was a matter best left to be assessed by the judge in the light of the particular circumstances of the case. One factor that the judge might wish, for instance, to take into consideration in this context might, it was felt, be whether the lessor or the supplier had offered to have non-conforming equipment put right.

127. - Article 10 (3) deals with the problem, significant above all in the case of hidden defects in the equipment which the lessee only discovers some time after the equipment has been in operation, of the point in time at which the lessee should lose its right to reject the equipment under Article 10 (1). It is clear that there has to be some cut-off point beyond which the lessor can be sure that there is no longer any risk that the lessee can exercise the right to reject. There was an attempt by a number of representatives within the committee of governmental experts to fix this moment at the time when the lessee intimates acceptance of the equipment to the lessor or supplier. This solution would have had the advantage of corresponding with the practice current in financial leasing transactions for the lessor only to disburse the purchase price to the supplier at such time as it has been notified by the lessee that the equipment has been delivered and is in good working order. However, this solution was found to be unacceptable, principally on the ground that the remedies granted the lessee against the supplier under Article 9 would not by themselves give the lessee adequate redress in the event of hidden defects emerging only after the initial intimation of acceptance – for instance, the lessee’s remedies against the supplier under Article 9 would be considerably limited as a result of the prohibition contained in Article 9 (2) on the lessee terminating or rescinding the supply agreement - but also because of a reluctance to deprive the lessee of its right to reject equipment that it would ordinarily have been supplied with under a standard form of contract. In the event the solution reached by the committee was to equate the lessee with an ordinary buyer for this purpose: the lessee under Article 10 (3) will accordingly lose its right to reject where it would have lost this right if the equipment had been supplied to it as a buyer. It was felt that it was right that if, as a buyer, the lessee would have been treated as against the supplier as having decided to retain the equipment, it should also be so treated as against the lessor.

128. - Article 10 (4) gives the lessee a further remedy as against the lessor. This is the right to terminate the leasing agreement and to recover any rentals and other sums it may have paid in advance. This right is exercisable by the lessee once it has rejected the equipment under Article 10 (1) and the supplier has still failed to make a conforming tender even after the further reasonable time permitted under Article 10 (2). The reason why the lessee’s right to reject, on the one hand, and its right to terminate the leasing agreement and recover any rentals and other monies paid in advance, on the other hand, are set forth separately in Article 10 is that the authors
of the draft Convention basically adopted the line that it would not be right to allow the lessee, who had after all selected the supplier and given the specifications for the equipment, to terminate the leasing agreement and recover any rentals and other monies it may have paid in advance from the lessor, who had only gone into the transaction to finance the lessee’s acquisition of the use of an asset chosen by that same lessee without any technical role in relation to the equipment’s characteristics having been played by itself, so long as there was still an opportunity under Article 10 (1) and (2) for the making of a conforming tender.

129. - While the authors of the draft Convention were not prepared to give the lessee a general right to withhold the payment of its rentals in the event of a non-conforming tender, taking the view that the lessee basically had a straight choice, either to retain the equipment and assert its rights against the supplier for non-conformity under Article 9 (1) or to reject it and recover whatever rentals and other monies it may have paid to the lessor, they nevertheless did in the end recognise a temporary right – the temporary nature of this right being brought out in the text of Article 10 (4) by employment of the word “meanwhile” – for the lessee to withhold payment of its rentals, during that limited period of time necessary for it to make up its mind, following the tender of non-conforming equipment, whether to reject or not.

130. - However imperfect may be the use that the lessee may be able to make of such non-conforming equipment, admittedly probably at a lower capacity than that foreseen by the parties in their agreement, the authors of the draft Convention were of the opinion that the lessor should be entitled to reasonable compensation in respect of such beneficial use, if any, of the equipment as the lessee may have had. This right of the lessor is spelled out in the second sentence of Article 10 (4).

131. - Under Article 10 (5) the lessee’s right to reject the equipment, to terminate the leasing agreement and to recover any rentals and other monies that it may have paid in advance and temporarily to withhold payment of its rentals while deciding whether or not to reject a non-conforming tender are in effect stated to be the limit of the lessee’s remedies against the lessor in the event of the supplier’s failure to deliver the equipment in accordance with the terms of the supply agreement, save in one set of circumstances: this is where the non-delivery, late delivery or tender of non-conforming equipment is the lessor’s own fault, which would normally mean where the lessor had failed to settle the purchase price with the supplier. In such a case Article 10 (5) leaves open the possibility for the lessee to sue the lessor for any additional loss, over and above the compensation represented by its recovery of any rentals and other sums it may have paid in advance, that it may sustain through the supplier’s failure to deliver the equipment in accordance with the terms of the supply agreement.

Article 11

132. - This article deals with the consequences of a lessee’s default in the performance of its duties under the leasing agreement, notably detailing the range of remedies this opens up for the lessor. As such it may be considered as constituting those elements of a liquidated damages clause which local law should not cut down. It is in no way intended to limit the parties’ freedom to stipulate a liquidated damages clause of their own in the leasing agreement, and as such was, with the exception of paragraphs 3 and 4, intended to be open to derogation under Article 14.

133. - The lessor’s remedies are divided for the purposes of this article into two categories,
those that it may exercise in the event of any default by the lessee and those that it may only exercise where the lessee’s default is “substantial”. The former are treated in Article 11 (1) and the latter in Article 11 (2). The draft Convention did not essay a definition of either “default” or “substantial default” on the ground that, given the limited objectives of both this article and the draft Convention in general, namely the establishment of a basic rather than an exhaustive legal framework for the atypical leasing transaction, these were matters best left to the parties in their agreement, all the more so since consumer transactions were excluded from the ambit of the draft Convention by Article 1 (3) so that both parties to the type of leasing agreement envisaged here could safely be considered to be professionals. In the type of leasing done at the international level, moreover, the rule as regards what is to be considered as an event of default differs considerably from contract to contract. The essential factor behind this differentiation lies in the degree of creditworthiness of the individual lessee. Thus the better the lessee’s creditworthiness, the more the lessor will be prepared to restrict the circumstances deemed under the lease to constitute default, whereas the weaker the economic situation of the lessee the more the lessor is going to be inclined to press for a more extensive interpretation of the events constituting default. It should moreover be borne in mind that a lessor will not press for the enforcement of its contractual rights and remedies upon the mere first occurrence of an event deemed in the leasing agreement to constitute default: leasing agreements customarily provide for the lessor to give the lessee notice in such circumstances that an event has occurred which with the passage of time will nevertheless become a default justifying its invocation of the rights and remedies set forth in their agreement.

134. - The first remedy, set out in Article 11 (1), is for the lessor to recover accrued unpaid rentals, together with interest, in the event of a default by the lessee in the performance of its duties under the leasing agreement.

135. - In the event of a “substantial” default by the lessee, on the other hand, the lessor may also, according to Article 11 (2), terminate the leasing agreement. However, by virtue of Article 11 (5), this right to terminate is only exercisable following the giving of notice by the lessor to the lessee to remedy its default to the extent that the same may be remedied. Article 11 (5) provides that the lessee must be given a “reasonable” opportunity of remedying its default. This restriction on the lessor’s right to terminate the leasing agreement is clearly designed to meet just that concern alluded to in paragraph 133 supra, namely that the lessee’s mere failure, for instance, to pay one of its rentals right on time should not automatically bring down on it the full force of the sanctions laid down in the leasing agreement. Article 11 (5) recognises that there will, of course, be some cases where the lessee will be unable to remedy its default, in particular following its bankruptcy, and in such cases it may reasonably be inferred from the language of Article 11 (5) that the serving of notice on the lessee and the subsequent need to await a further reasonable period of time may be dispensed with. We have had occasion elsewhere to comment on the word “reasonable” as employed in the draft Convention.[41] It suffices to recall here that it was considered inappropriate to set specific time-limits in an instrument designed to be of international application.

136. - Once the lessor has terminated the leasing agreement, but not before, it also becomes entitled, under Article 11 (2)(a), to recover possession of the equipment and, under Article 11 (2)(b), to recover such compensation as may be necessary to place it in the position

[41] Cf. §126 supra.
in which it would have been had the lessee duly performed its part of the leasing agreement and not defaulted. The fact that the lessor’s right to repossess is made contingent on its first having terminated the leasing agreement again reflects the concern adverted to supra,\(^{(42)}\) namely that repossession should not be used by the lessor as a means of exerting pressure on the lessee to pay its rentals \(^{(43)}\) but should only be possible where the lessor has already terminated the leasing agreement. The right to repossess can be quite important for the lessor where the lessee is unwilling to part with possession and given the reluctance of Common law jurisdictions to entertain applications for specific performance. Where a lessee is in default, repossession may often represent for the lessor, notwithstanding the fact that it is not a merchant and does not ordinarily deal in such equipment, its best guarantee of salvaging some of its investment, as the straitened circumstances that will probably have determined the lessee’s default are just as likely to affect its ability to meet a claim in damages.

137. - The other remedy granted the lessor following its termination of the leasing agreement, to wit the recovery of such compensation as may be necessary to place it in the position in which it would have been had the lessee duly performed its duties under the leasing agreement, illustrates the basic attitude of the authors of the draft Convention regarding what should be considered as a reasonable computation of the lessor’s measure of loss in such circumstances. The lessor’s role in the transaction, as we have seen, is at all times a narrowly financial role. It is accordingly a very serious upset for the lessor’s financial calculations when, upon the lessee’s default, that is through no fault of its own, it finds itself from one minute to the next obliged to repossess at an unforeseen moment during the term of the leasing agreement. This upset will, moreover, be compounded by various other factors, responsibility for which cannot reasonably be attributed to the lessor. For instance, the equipment will frequently have been constructed specially to the lessee’s specifications, rendering the lessor’s task of finding someone willing to take it off its hands all the more difficult, particularly at a price that will bear some relation to its calculations when it embarked on the transaction. Moreover, once there has been a breach of the leasing agreement by the lessee constituting “substantial default” and thus entitling the lessor to repossess the leased asset, the lessee, in the absence of an additional agreement providing for the lessee’s safekeeping of the asset pending its collection by the lessor, would no longer be liable for any damage sustained by the equipment after such time. The aim of the authors of the draft Convention was to ensure that the net effect of the compensation to be paid under Article 11 (2)(b) would be to place the lessor in the position in which it would have been had it received the total number of rentals stipulated under the leasing agreement. They refrained from attempting to spell this out in greater detail, although their basic idea was that the lessor should be able to recover an amount equivalent to the discounted value of the lost future rentals, after giving credit against that sum for the sum it would have received from disposing of the repossessed asset in a commercially reasonable manner. Finally in connection with Article 11 (2)(b) it should be noted that the authors of the draft Convention considered it worthwhile to spell out that the compensation recoverable by the lessor under this clause is subject to its duty to take all reasonable steps to mitigate its loss.

\(^{(42)}\) Cf. §126 supra.

\(^{(43)}\) However, while such a concern might in some cases be justified in the context of a domestic leasing transaction, it would seem to be somewhat less likely in that of an international leasing transaction. Quaere whether a French lessor would go to the lengths of seeking to repossess equipment leased in Ecuador for a fortnight to exert such pressure.
138. - The law governing minimum payment clauses is in many countries considered a matter of public policy and in recent years legislation has been passed, both at the national and the supranational level, giving the courts a wide measure of discretion in revising the sums fixed by the parties in their agreement. Article 11 (3) is to be understood in this light. It in no way seeks to oust the manifest right of the courts to review the bargain struck between lessor and lessee: it merely states that, in recognition of the current practice of lessors in attempting to articulate their measure of damage in the form of such a liquidated damages clause, the court should, in the event of a dispute arising, have regard, in the first place at least, to the provisions agreed between the parties on the manner in which the compensation to be paid by the lessee upon default under Article 11 (2)(b) is to be computed, subject always to its finding that in the circumstances the compensation provided for is disproportionate. Clearly the factors involved in the court making such an evaluation will be complex. For instance, the economic conditions may well have changed by the time that the lessor comes to repossess its asset following the lessee’s default so that the lessee’s rental obligations as stipulated under the leasing agreement may be either higher or lower than the current market price for a similar period of time. The difficulties involved in proving the fairness of a given liquidated damages clause in the light of such imponderables were considered to strengthen the case for recognising the parties’ right to negotiate a remedy in anticipation of default. The fact that Article 11 (3) provides that the parties’ agreement on this matter is to be enforceable between them “unless such compensation is disproportionate” was designed to remind the parties, in particular a lessor in a powerful bargaining position, not to overreach in their negotiation of such a remedy. Given the difficulties alluded to above regarding the computation of fair compensation in the wake of default rather than in anticipation of the same, the court in finding as to the disproportionateness or otherwise of the individual liquidated damages clause stipulated by the parties was intended by the authors of the draft Convention to have regard to the situation obtaining at the time when the leasing agreement was entered into, rather than the situation as it had developed by the time of default.

139. - The effect of Article 11 (4) is to alter the range of remedies exercisable by a lessor upon the lessee’s default in those cases where the leasing agreement includes, as it often will, an acceleration clause entitling the lessor upon the lessee’s default to require immediate payment by the lessee of all the outstanding rentals due under that agreement. In recognition of the injustice that would be wrought by allowing the lessor both to benefit from such an acceleration clause and to terminate the leasing agreement – thus opening the way for it also to repossess the equipment, which it could then sell or re-lease – Article 11 (4) requires the lessor in such a case to elect between the exercise of one or the other of these remedies. Thus where the lessor elects to terminate the leasing agreement, it is thereby debarred from seeking to enforce such an acceleration clause. Moreover, it was the opinion of the authors of the draft Convention that, since the fact of suing for rentals presupposes that there is a current leasing agreement on foot, the fact that the leasing agreement has been terminated means that there is no longer any justification for the lessor to be able to sue for such rentals. Finally it should be noted that the same protection as that given the lessee in respect of the lessor’s termination of the leasing agreement referred to earlier (44) is also given to the lessee under Article 11 (5) in respect of the lessee’s enforcement of an acceleration clause. Accordingly, the lessor

(44) Cf. §135 supra.
can only enforce such a clause after it has given the lessee notice of its duty to remedy its default and allowed it a further reasonable time in which to do so. As with the provision relating to the lessor's termination of the leasing agreement, the lessor's duty to give the lessee notice of its duty to remedy its default and to allow it a further reasonable period of time in which to do so is made contingent on it being possible for the lessee in the circumstances to cure its default, the inference being that the lessor is otherwise dispensed of the need to give the lessee such notice and allow it such an additional period of time.

Article 12

140. - This article deals, in its first paragraph, with the question of the lessor's assignment of all or part of its real rights in the equipment or all or part of its contractual rights under the leasing agreement and, in its second paragraph, with that of the lessee's right to assign its right to use the equipment or any other rights it may possess under the leasing agreement. As such it seeks to facilitate matters for those jurisdictions that place legal restrictions on the transfer of rights.

141. - The question of the lessor's assignment of all or part of its rights is particularly critical in those jurisdictions where a particular species of financial lease, the leveraged lease, is common. In leveraged leases, whereas legal title to the equipment and hence entitlement to the tax indemnification benefits associated with ownership, vest in the lessor, the latter will, by reason of the huge amounts of money involved, put up only a part of the capital cost represented by the purchase of the equipment. For the remainder it will have recourse to one or more lenders who will assure their position by requiring an assignment to themselves of the stream of rentals provided for under the leasing agreement. It was feared lest, without a provision on the lines of Article 12 (1), there was a risk that such transactions might, by virtue of involving more than the three parties specified in Article 1 (1), fall outside the scope of the draft Convention, whereas for those countries for which leveraged leasing was important it was vital that such transactions should come under the draft Convention, all the more so given the high incidence of leveraged leasing transactions among those countries' international financial leasing operations.

142. - Such transfers by the lessor of its rights in the equipment or under the leasing agreement are accordingly permitted under Article 12 (1). The words "or otherwise deal with", coming after the word "transfer" in the first sentence of this provision, were added because of what was feared to be the inadequacy of the term "transfer" to cover the case of the Civil law "hypothece". Such a transfer by the lessor can clearly only affect its rights, and not also its duties under the leasing agreement, as is specified in the second sentence of this provision. This clause was also by extension intended to indicate that neither can such a transfer affect the lessee's rights under the leasing agreement.

143. - The lessor's transfer of its rights under Article 12 (1) is not, however, to be used as a means of circumventing the application of the future Convention: the second sentence of Article 12 (1) thus goes on to provide that such a transfer may alter neither the nature of the leasing agreement nor its legal treatment as provided in the draft Convention. Thus where, prior to the assignment, the draft Convention was already applicable, say, by virtue of the lessor and the lessee having their places of business in different States and both these States and the State

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(45) Cf. §135 supra.
where the supplier’s place of business was located being Contracting States (Article 2 (1)(a)), the draft Convention would not cease to be applicable merely because, subsequently to the assignment, both the lessor and the lessee found their places of business to be in the same State. This result reflected the considered opinion of the authors of the draft Convention that it was not possible to legislate for fraud at the international level. Likewise, a financial lease not subject to the draft Convention as originally concluded, that is a wholly domestic transaction, could not, merely by virtue of the lessor’s transfer of its rights under Article 13 to a party having its place of business in another State be transformed into an international transaction subject to the draft Convention. It should be noted that in those States, like France and Senegal, which require lessors to have the status of either a bank or a financial institution, the transferee from a lessor would have to have the same status as the transferor.

144. - The fundamental idea behind Article 12 all along having been to bring leveraged leases explicitly within the scope of the draft Convention, the authors of the draft Convention never considered the question of the lessor’s assignment of its duties under the leasing agreement. The fact that this question was not as a result addressed in the draft Convention should, however, in no way be seen as prohibiting such assignments: rather it is yet another example of a matter left to be settled by the parties in their agreement and the applicable law.

145. - Article 12 (2) balances the right of assignment given to the lessor under Article 12 (1) by recognition of the lessee’s right to assign its right to use the equipment or any other rights it may possess under the leasing agreement. Enshrinement in the draft Convention of this right of assignment for lessees is particularly important for those countries with planified economies. Circumstances might change during the currency of the leasing agreement as a result of which the original lessee might drop out of the picture. However, the person of the lessee is obviously a matter of primordial concern to the lessor and this is why Article 12 (2) makes the lessee’s right of assignment subject to the lessor’s consent. The lessee’s right of assignment is furthermore specified to be subject to the rights of third parties.

Article 13

146. - It had all along been the intention of the authors of the draft Convention that its application should extend to those sub-leasing arrangements so common in international financial leasing transactions. Evidence of this intention was to be found, for example, in the employment of the term “real rights” rather than “title” in Article 5 (1) and (2). At its final session the committee of governmental experts nevertheless judged it opportune to include a provision in the future Convention expressly extending its application to sub-leases. An alternative formula, involving an amendment to the sphere of application provisions of the draft Convention, was rejected as making those provisions over-cumbersome, although it was recognised that the rightful place of this provision might well finally be in the sphere of application provisions of the future Convention.

147. - The effect of paragraph 1 is that, in the case of a financial sub-leasing transaction, the sub-lessee is to be treated as the lessor for the purposes of the draft Convention, the sub-lessee as the relevant lessee and the supplier from whom the lessee acquired the equipment as the relevant supplier. Article 13 (2) deals with the situation where there is a series of transactions involving the same equipment including more than one financial leasing transaction. It
provides that in respect of such a series of transactions the last financial lessor is to be treated as the relevant lessor and the party who supplied the first financial lessor as the relevant supplier.

Article 14

148. - This article is a provision found in most international commercial law Conventions. It reflects the idea that Conventions in the commercial law field should not as a rule deprive the parties of their freedom to choose alternative rules to govern their transaction. While no decision was taken on which provisions, if any, of the future Convention should be mandatory, the committee of governmental experts made a preliminary examination of the issues involved. Some representatives felt that, given the commercial nature of all the parties to the transaction and the need to allow for further evolution of the leasing technique, the entire text should be amenable to exclusion. Others felt that the application of certain provisions at least needed to be guaranteed. It was the unanimous feeling of the committee, on the other hand, that the parties should not be free to contract out of the sphere of application provisions of the future Convention, even though it was not felt that this needed to be stated explicitly in Article 14. The authors of the draft Convention were at all times conscious of the risks inherent in the effect of these provisions being able to be changed at will, in particular in view of the delicate balance between the interests of the parties to the transaction established throughout the draft Convention as a whole.

149. - The committee of governmental experts accordingly drew up two rules, one (Article 14 (1)) permitting the total exclusion of the future Convention and the other (Article 14 (2)) guaranteeing the application of certain of its provisions. That allowing for total exclusion was placed in square brackets to indicate that this was a matter which the committee of governmental experts judged involved a policy decision, which was better left to be taken at the diplomatic Conference. In Article 14 (2) the committee, on the other hand, made an attempt to identify those provisions which it felt should be made mandatory. The effect of this provision would be, subject to some uncertainty as to the precise status of Article 7 (2) in this regard, to leave the parties free, in their relations with each other, to derogate from or vary all provisions of the future Convention save Article 11 (3) and (4), that is the provision dealing with the enforceability of minimum payment clauses, a question considered to be a matter of public policy in certain jurisdictions, and that precluding the lessor from both terminating the leasing agreement and enforcing an acceleration clause. There was also, as we have had occasion to note elsewhere, a certain body of feeling within the committee of governmental experts that the lessor's warranty of quiet possession was of the essence of a finance lease and that Article 7 (2) should accordingly also be made mandatory. This point of view did not, however, command more than minority support, the point being made that it was invariably the practice in financial leasing transactions for the lessor's warranty of quiet possession to be excluded. It was eventually judged wise to leave the decision on this question to be taken at the diplomatic Conference, a reference to Article 7 (2) accordingly being inserted in Article 14 (2) in square brackets. Finally a propos of Article 14 (2) it should be noted that it only proposes to give the parties the right to contract out of those provisions which concern their relations with one another and that as a result the provisions of Articles 5, 6, 14 and 15 are also clearly not intended to be subject to the parties' agreement.

(46) Cf. §106 supra.
Article 15

150. - This is another provision which has now become a common feature of international Conventions in the commercial law field. It is addressed principally to those called upon to decide cases involving the interpretation of the future Convention, that is judges and arbitrators. If the objectives of the authors of the draft Convention in seeking to establish an international uniform legal infrastructure for financial leasing transactions are not to be thwarted by those called upon to interpret its provisions, it is clearly essential, as proclaimed in Article 15 (1), that they have regard to the international character of the draft Convention and to the need to promote uniformity in its application, in other words that they avoid seizing the first opportunity to interpret it in the light of the principles and traditions of their own legal system. The provisions of Article 15 (1) furthermore exhort those called upon to interpret the future Convention to have regard to the need to ensure the observance of good faith in international trade. “International trade” in the sense which the authors of the draft Convention wished to give it in this provision is to be read as including international investment.

151. - The other factor to which those called upon to interpret the future Convention are exhorted to have regard under the terms of Article 15 (1) is its object and purpose as set forth in the Preamble. This reference to the Preamble in the provisions on interpretation clearly underscores the draft Convention’s commitment to maintaining a fair balance of interests between the different parties to international financial leasing transactions.

152. - Article 15 (2) seeks to ensure that the special distinct status conferred on the particular type of leasing transaction addressed by the draft Convention will not be jeopardised as regards all those many issues which have not, both consciously and unconsciously, been specifically dealt with in the draft Convention. It would again be undesirable if the objectives of the authors of the draft Convention were to be thwarted by judges and arbitrators filling in these gaps on the basis of the solutions of their domestic law, all the more so given that it was precisely the inadequacy and inappropriateness of these solutions which provided the starting point for Unidroit’s initiative on this subject. Article 15 (2) accordingly provides that matters not expressly settled in the draft Convention but which are nevertheless governed by the same are to be settled in conformity with the general principles on which it is based and the law applicable by virtue of the rules of private international law. It will be noted that, unlike the Vienna Sale Convention (Article 7) and the Geneva Agency Convention (Article 6), which provide that the applicable law is only to be referred to for the settlement of a given matter where it proves impossible in respect of that matter to glean any general principles on which the Convention in question is based, in the case of the draft Convention such general principles and the applicable law are put on an equal footing. The basic reason underlying this departure was, on the one hand, what was feared might prove to be the difficulty of gleaning general principles from the draft Convention and, on the other, the important role that rules of conflict play in determining the sphere of application of the draft Convention.
DRAFT CONVENTION ON
INTERNATIONAL FACTORING (1)

PREAMBLE

THE STATES PARTIES TO THIS CONVENTION,

CONSCIOUS of the importance of providing a legal framework that will facilitate international factoring, while maintaining a fair balance of interests between the different parties involved in factoring transactions,

AWARE of the need to make international factoring more available to developing countries,

RECOGNIZING therefore that the adoption of uniform rules which govern certain aspects of international factoring and take into account the different social, economic and legal systems would contribute to the removal of legal barriers in international trade and promote the development of international trade,

HAVE AGREED as follows:

Article 1

1. - For the purpose of this Convention, “factoring contract” means a contract concluded between one party (the supplier) and another party (the factor) pursuant to which:

(a) the supplier may or will assign to the factor receivables arising from contracts of sale of goods made between the supplier and his customers (debtors) other than those for the sale of goods bought for their personal, family or household use;

(b) the factor is to perform at least two of the following functions:

- finance for the supplier, including loans and advance payments;
- maintenance of accounts (ledging);
- collection of receivables;
- protection against default in payment by debtors;

(c) notice of the assignment of the receivables is to be given in writing to debtors.

2. - In this Convention references to “goods” and “sale of goods” shall include services and the supply of services.

(1) Text adopted by the Unidroit committee of governmental experts for the preparation of a draft Convention on certain aspects of international factoring at its third session (Rome, 24 April 1987).
3. - In this Convention "writing" includes any form of writing, whether or not signed.

Article 2

1. - This Convention applies whenever the receivables assigned pursuant to a factoring contract arise from a contract of sale of goods between a supplier and a debtor whose places of business are in different States:

(a) when the supplier, the debtor and the factor have their places of business in Contracting States; or

(b) when both the contract of sale of goods and the factoring contract are governed by the law of a Contracting State.

2. - For the purpose of this Convention, if a party to the contract of sale of goods or the factoring contract has more than one place of business, the place of business is that which has the closest relationship to the contract and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that contract.

Article 3

1. - The parties to the factoring contract may exclude the application of this Convention.

2. - The parties to the contract of sale of goods may exclude the application of this Convention only in respect of receivables arising at or after the time when the factor has received notice in writing of such exclusion.

3. - Where the application of this Convention is excluded in accordance with the preceding paragraphs of this article, such exclusion may be made only as regards the Convention as a whole.

Article 4

As between the parties to the factoring contract:

(a) a contractual provision for the assignment of existing or future receivables shall not be rendered invalid by the fact that the contract does not specify them individually, if at the time of conclusion of the contract or when they come into existence they can be identified to the contract;

(b) a provision in the factoring contract by which future receivables are assigned operates to transfer the receivables to the factor when they come into existence without the need for any new act of transfer.

Article 5

1. - The assignment of a receivable by the supplier to the factor shall be effective notwithstanding any agreement between the supplier and the debtor prohibiting such assignment.

2. - However, such an assignment shall not be effective against the debtor when he has his
place of business in a Contracting State which has made a declaration under Article X of this Convention.

Article 6

A factoring contract may validly provide as between the parties thereto for the transfer, with or without a new act of transfer, of all or any of the supplier’s rights deriving from the sale of goods, including the benefit of any provision in the contract of sale of goods reserving to the supplier title to the goods or creating any security interest.

Article 7

1. - The debtor is under a duty to pay the factor if, and only if, the debtor does not have knowledge of any other person’s superior right to payment and notice of the assignment:

(a) is given to the debtor in writing by the supplier or by the factor with the supplier’s authority;

(b) reasonably identifies the receivables which have been assigned and the factor to whom or for whose account the debtor is required to make payment; and

(c) relates to receivables arising under a contract of sale of goods made at or before the time the notice is given.

2. - Irrespective of any other ground on which payment by the debtor to the factor discharges the debtor from liability, payment shall be effective to discharge his liability pro tanto if made in accordance with paragraph 1 of this article.

Article 8

1. - In a claim by the factor against the debtor for payment of a receivable arising under a contract of sale of goods the debtor may set up against the factor all defences of which the debtor could have availed himself under that contract if such claim had been made by the supplier.

2. - The debtor may also assert against the factor any other defences, including any right of set-off, in respect of claims existing against the supplier in whose favour the receivable arose, and available to the debtor at the time the debtor received a notice of assignment conforming to Article 7 of this Convention.

Article 9

1. - Without prejudice to the debtor’s rights under Article 8 of this Convention, non-performance or defective or late performance of the contract of sale of goods by the supplier shall not alone entitle the debtor to recover money paid by the debtor to the factor if the debtor has a claim against the supplier for recovery of the price.

2. - The debtor who has such a claim against the supplier shall nevertheless be entitled to recover money paid to the factor:

(a) to the extent that the factor has not paid the purchase price of the receivable to the
supplier; or

(b) where at the time the factor paid such purchase price he knew of the supplier’s non-performance as regards the goods to which the debtor’s payment relates.

**Article 10**

1. - Where a receivable is assigned by a supplier to a factor pursuant to a factoring contract governed by this Convention:

   (a) the rules set out in Articles 3 to 9 of this Convention shall, subject to paragraph (b) of this article, apply to any subsequent assignment of the receivable by the factor or by a subsequent assignee;

   (b) the provisions of Articles 7 and 8 of this Convention shall apply as if the subsequent assignee were the factor.

2. - Notice to the debtor of the subsequent assignment may also constitute notice of the assignment to the factor.

3. - This Convention shall not apply to an assignment which is prohibited by the terms of the factoring contract.

**Article 11**

1. - In the interpretation of this Convention, regard is to be had to its object and purpose as set forth in the Preamble, to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.

2. - Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based and in conformity with the law applicable by virtue of the rules of private international law.

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**Article X**

A Contracting State may at any time make a declaration in accordance with Article 5, paragraph 2 of this Convention that an assignment under Article 5, paragraph 1 shall not be effective against the debtor when he has his place of business in that State.
EXPLANATORY REPORT

on the

DRAFT CONVENTION ON INTERNATIONAL FACTORING

prepared by the Unidroit Secretariat

I

BACKGROUND TO THE DRAFT CONVENTION

1. - The origins of the work on this draft Convention date back to a decision taken on the basis of a Secretariat memorandum by the Unidroit Governing Council at its 53rd session, held in Rome in February 1974, to include in the Work Programme for the triennial period 1975 to 1977 the subject of the assignment of debts in general and more particularly that of factoring contracts. The Council also requested the Secretariat to prepare a preliminary study on such contracts which would permit the Council to take a decision on the order of priority to be accorded to the item with a view to the elaboration of uniform rules.\(^{(1)}\)

2. - The Governing Council was seized of a preliminary report submitted by the Secretariat at its 55th session, held in Rome in September 1976, on which occasion it authorised a wider distribution of the report and accompanying questionnaire, especially to practitioners; at its 56th session it decided to set up a restricted group of members of the Governing Council, assisted by one or more experts on factoring, to examine an analysis of the replies to the questionnaire. The detailed conclusions of the group\(^{(2)}\) were brought to the attention of the Governing Council at its 57th session, held in Rome in April 1978, and in accordance with the powers conferred upon him by the Council the President of Unidroit constituted a study group for the preparation of uniform rules on the factoring contract. The study group held three sessions in Rome, the first on 5 and 6 February 1979, the second from 27 to 29 April 1981 and the third from 19 to 21 April 1982.\(^{(3)}\) At the conclusion of that session the study group adopted the preliminary draft uniform rules on certain aspects of international factoring.

3. - At its 62nd session, held in Rome in May 1983,\(^{(4)}\) the Governing Council approved the draft rules and decided to communicate the text of the preliminary draft, together with an explanatory report prepared by the Secretariat,\(^{(5)}\) to the Governments of the member States of Unidroit, with a request for observations. In the light of the observations received, the Governing Council decided at its 63rd session in May 1984 to set up a committee of governmental experts for the preparation of draft uniform rules on certain aspects of international factoring\(^{(6)}\) (hereinafter referred to as “the committee”).

4. - The text of the preliminary draft uniform rules was considered and revised at three

\(^{(2)}\) For the report on the session of the restricted group, see Study LVIII - Doc. 4.
\(^{(3)}\) The reports on the three sessions are contained in Study LVIII - Doc. 7, Study LVIII - Doc. 10 and Study LVIII - Doc. 13 respectively.
\(^{(5)}\) Study LVIII - Doc. 16.
sessions of the committee, held in Rome from 22 to 25 April 1985, from 21 to 23 April 1986 and from 22 to 24 April 1987 respectively. At its second and third sessions the committee also considered a set of draft final provisions prepared by the Secretariat. Mr Royston M. Goode chaired the committee throughout, as also the drafting committee which met on the occasion of each session to take account of the amendments made in plenary. In all, 33 member States of Unidroit, four non-member States, three intergovernmental organisations and two non-governmental international organisations, as well as three international and three national professional associations took part in the work of the committee.

5. - At the close of its third session, the committee completed its work with the adoption of the text of a draft Convention on international factoring which was now ready for submission to a diplomatic Conference for adoption. At the closing session of the third and final session of the Unidroit committee of governmental experts for the preparation of a draft Convention on international financial leasing, which was held immediately after the session of the committee of governmental experts for the preparation of a draft Convention on certain aspects of international factoring, the Canadian representative announced that his Government would host a diplomatic Conference for the adoption of the two draft Conventions. The Conference will be held in Ottawa from 9 to 28 May 1988.

II

GENERAL CONSIDERATIONS

6. - Although the origins of factoring are to be found in antiquity, and the institution underwent a new development in the nineteenth century in the relations between Great Britain and the United States of America, it was only after the First World War that its characteristics became clear, first in Common law countries, then in other Western countries and finally in the world at large. Since the nineteen-sixties, its considerable and uninterrupted growth, including its expansion into ever more diversified fields of activity and an increasing number of countries, bear witness to the adaptation of this means of financing to meet the needs of contemporary commercial activity. A brief explanation of the economic role of factoring and of the legal mechanisms adopted to regulate it at national level will permit a better understanding of the reasons which influenced the choices made by the authors of the draft Convention in their

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(7) The Secretariat prepared a commentary on the text of the preliminary draft Convention drawn up by the committee at its first session (Study LVIII - Doc. 20), as well as a revised commentary on the text of the preliminary draft Convention drawn up by the committee at its second session (Study LVIII - Doc. 25) and a summary report on the third session of the committee (Study LVIII - Doc. 32).
(8) For the revised version of the draft final provisions, see Study LVIII - Doc. 34.
(9) Argentina, Australia, Austria, Belgium, Canada, Chile, People's Republic of China, Czechoslovakia, Egypt, France, Federal Republic of Germany, Greece, Holy See, Hungary, India, Ireland, Italy, Korea, Luxembourg, Mexico, Netherlands, Nigeria, Norway, Poland, San Marino, South Africa, Spain, Sweden, Switzerland, Turkey, United Kingdom, United States of America, Venezuela.
(10) Algeria, Peru, Philippines, Senegal.
(12) Banking Federation of the European Community, International Chamber of Commerce.
(14) This note concerns the French version only.
attempt to provide a suitable legal framework at international level for a device forged and employed with success by the commercial and financial worlds.

7. - Recourse to factoring by a small or medium-sized manufacturer or supplier of services who sells on credit terms to his professional or commercial customers is the result of a decision to rationalise his business: it frees him from a certain number of concerns of a financial character which are assumed by a professional who offers a wide range of services characterised by the efficiency and low cost permitted by specialisation. The services offered by the factor may be summarised as four: in the first place he may assume the risk of the insolvency of the supplier’s debtors; after enquiring into the creditworthiness of each debtor, the factor will, when he judges it appropriate, establish a credit limit calculated principally by reference to the turnover in respect of the debtor and to the average term for payment, and he will assume the risk of non-payment resulting from the debtor’s insolvency up to the limit of the credit granted. According to whether or not this service is provided, the factoring transaction will be designated “recourse” or “non-recourse” factoring. Moreover, factoring may serve the purpose of financing debts (receivables), the factor advancing to the supplier an amount proportional to the value of the receivables, payment of which by the debtor will only be made later at the time stipulated. The two other services traditionally offered by factors are, on the one hand, the handling of the supplier’s accounts with his debtors, which implies their maintenance, the conduct of correspondence and the soliciting of payment by debtors, with the aid of the most advanced technical methods of management, and on the other the recovery of receivables from debtors, the latter making payment directly to the factor who pays over the sums in question to the supplier in accordance with the arrangements they have agreed upon. When the factor is authorised to accept payment of the receivables, he will also take the necessary steps for their recovery. The supplier may agree with the factor, on the basis of both commercial and legal considerations, whether or not to give notice to the debtor that he is bound by a factoring contract. In particular, when the recovery of receivables is included among the services for which provision is made, the debtor is by such notice informed that he can obtain discharge only by paying the factor.

8. - The factor obtains payment for his services in the form of the commission he receives from the supplier, which may amount to up to two percent of the value of each receivable, calculated in accordance with the services provided and their cost in each case. Whenever he agrees to make advance payments against the receivables the factor takes the benefit of the corresponding interest. It will readily be appreciated that factoring transactions can only be based on a continuing relationship between the supplier and the debtors in question and this on account both of the nature of the services which characterise factoring and of the primordial importance for the factor to amortise his investment. It is precisely for these reasons that the factor will require the supplier to grant him the exclusive right to factor the receivables or certain categories of receivables which arise out of the supplier’s commercial dealings with his customers.

9. - It is apparent from this brief description of factoring that it presents many economic advantages. As has been seen, it provides financial liquidity, the certainty of payment and the handling and recovery of receivables, the choice of the combination of the services being left to the parties. In each system, legal means have been sought to ensure the development of this relatively recent technique of financing in the most satisfactory manner possible, in terms not only of facilitation and flexibility, but also of certainty and cost, and this explains the fact that
while in most countries it is the assignment of receivables which provides the underlying legal basis for factoring transactions, the procedures whereby such assignments are effected and the rules which govern the different aspects of them differ considerably. In consequence, when the supplier has commercial dealings with foreign buyers, the problem of distance and the difficulties facing the former in obtaining information as to the financial position of the latter, language barriers and frequently ignorance of the applicable foreign law make the services offered by factors all the more attractive. It is nevertheless true that the divergencies in national law and the frequent uncertainty as to the law applicable to a given transaction or to one or another aspect of it create problems which the factoring industry must constantly face and which it seeks to overcome by passing on to suppliers the increased cost of its services.

10. - It is in these circumstances that the Unidroit committee of governmental experts, endorsing the conclusions of the study group, recognized that trade would be encouraged by facilitating factoring and that it would therefore be desirable to draw up uniform rules in this connection. It also agreed however to limit the attempt at unification to international factoring, considering that such a restriction would be conducive to the acceptance of the uniform rules by a greater number of States for while it might be desirable in theory to contemplate the preparation of uniform rules on factoring at national as well as international level, there could well be a strong reluctance on the part of many States to accept changes to well-established principles of law which are of much more general application than simply to factoring transactions. While the committee opted, as regards the form of the future instrument, in favour of a Convention, it emphasized on a number of occasions in the course of its work that this choice would leave it open to those States which wished to do so to draw on the international rules when preparing national legislation directed to domestic transactions. As to the general approach followed in the elaboration of the draft Convention, the committee decided to limit the scope of its work of unification to what may be considered the keystone of factoring transactions, namely the specific question of assignments, and to lay down basic minimum principles concerning a restricted number of aspects raising particular problems. Furthermore, it should be pointed out that the rules governing the mechanics of assignments are limited to the relations between the three parties directly interested – the assignor, the assignee and the debtor – to the exclusion of situations involving third parties, and this is one of the reasons for the deletion of a provision which had initially been included concerning the liability of the factor towards third parties for damage caused by goods of which he has become owner as a result of the transfer of the benefit of a reservation of title clause. As regards the other hand the problems relating to priorities between the rights of the factor and those of third parties in the receivables, it is on account of their extreme complexity that the committee decided not to deal with them, by way either of a substantive rule of law or of a conflicts rule, and this notwithstanding the widely expressed regret that the Convention failed to regulate an aspect of the question which created very great difficulties at international level.

11. - Before embarking on a commentary on each of the provisions of the draft Convention, reference should be made to the committee’s concern to take account as far as possible of the 1980 United Nations Convention on contracts for the international sale of goods (hereinafter referred to as “the Vienna Convention”), since the transactions governed by the future Convention on international factoring most often follow an international sale transaction which may therefore be subject to the Vienna Convention. This concern is evidenced in a number of ways: firstly in the general structure of the draft (in particular the order of the articles), sometimes in the provisions of a given article and finally, whenever possible and desirable, in
the terminology employed with a view to seeking harmonisation of the concepts to be found in various recent international instruments dealing with related matters. Although the committee did not consider the possibility of grouping the articles together under general chapter headings, as is the case with other international trade law Conventions, several parts may be identified as follows. The first concerns the scope of application, both substantive and territorial, and the possibility for the parties to exclude the application of the Convention (Articles 1 to 3); one could also include within this chapter Article 10, which broadens the scope of application of the Convention by applying the principles set out in it to assignments made subsequent to those effected under a factoring contract governed by the Convention. The second would contain the rules removing certain obstacles which may exist under national law to the validity of the assignment of receivables or of the transfer of rights accessory to the receivables between the parties to the factoring contract (Articles 4 and 6). A third part would be that concerned with certain effects of the assignment on the debtor (Articles 7 to 9), whereas Article 5 concerns both the question of the validity of the assignment *inter partes* and that of its effects on the debtor. Finally, Article 11 contains general provisions relating to the interpretation of the rules of the Convention.

III

COMMENTARY ON THE PROVISIONS OF THE DRAFT CONVENTION

Title

12. - The title of the draft Convention was slightly modified in the course of the committee’s work, originally reading “Preliminary draft Convention on certain aspects of international factoring” so as to indicate from the outset the limited scope of the work in hand. The committee preferred however to simplify the title of the future Convention by stating its purpose in general terms, although it was agreed to maintain in the preamble an express reference to the fact that only certain aspects of the matter are dealt with.

Preamble

13. - The second and third paragraphs, the source of which is to be found in the provisions proposed for inclusion in the preamble to the Unidroit preliminary draft Convention on international financial leasing, set out the aims of the instrument, namely the provision of a legal framework that will facilitate international factoring while maintaining a fair balance of interests between the different parties involved in such transactions and making international factoring more available to developing countries. The last two paragraphs take over almost word for word the corresponding provisions of the preamble to the Vienna Convention and lay stress on the development of international trade while respecting the differences between social, economic and legal systems.

Article 1

14. - As indicated above in the general considerations, and as is apparent from the provisions of the preamble itself, the aim which guided the work on the draft Convention was
that of facilitating factoring as a means of assisting the development of international commercial exchanges. Given the variety of forms which factoring has assumed in practice and the legal frameworks within which it has been accommodated or to which it has been adapted in different countries, as broad a definition as possible has been sought in the Convention so as not to hinder the expansion of activities which already are, or may be, assimilated to this technique of financing in certain countries. Thus the possibility of limiting the application of the rules to recourse factoring or of fixing a maximum timelimit for the credit granted to the buyer under the sale contract to which the receivables relate was ultimately rejected. An important derogation from this principle is constituted by the decision to restrict the scope of application to transactions in which debtors are to be given written notice of the assignment. The definition in Article 1 seeks therefore to identify what may be considered to be the lowest common denominator in notification factoring and, after indicating the parties to the factoring contract, namely the supplier on the one hand and the factor on the other, paragraph 1 sets out the respective duties of the parties in their contractual relations.

15. - Sub-paragraph (a) defines the supplier's obligation to the factor, namely the assignment of receivables arising from a contract: this is the legal basis for factoring as a financing technique. The language agreed by the committee: "the supplier may or will assign ..." reflects factoring practice in the sense of the supplier's undertaking to assign receivables which will arise thereafter, although it may also constitute the act under which existing receivables are assigned; finally, the supplier may in many cases be free to assign, or not to assign, certain kinds of receivables, in accordance with agreements concluded with the factor. It should be noted that the provision is silent as to the procedures for the assignment for while at an earlier stage of the work it was required that it should be made "on a continuing basis" and "by way of sale or security", the committee considered as to the first point that the continuing relationship between the parties to the factoring contract was implicit in the functions performed by the factor and in the wording of Article 1, and was more generally of the opinion that a strict interpretation of those expressions in the light of the concepts and characterisations of national law could run the risk of excluding the application of the Convention in certain cases.

16. - Sub-paragraph (a) also lays down a number of conditions regarding the contracts which give rise to the receivables assigned. In the first place, they must be contracts for the sale of goods or for the supply of services (Article 1, paragraph 2), and they must moreover be concluded between the supplier and his customers in the course of their business, the intention being essentially to exclude consumer transactions on account of the special regime governing such transactions under the law of a number of countries. The language finally adopted is that of the negatively framed definition contained in Article 2(a) of the Vienna Convention, which excludes contracts between the supplier and his customers "for the sale of goods bought for their personal, family or household use". It should also be stressed that the assignment of receivables arising out of contracts concluded with public bodies or enterprises of a non-profit making character will be subject to the provisions of the Convention on international factoring, as also will be the assignment of receivables relating to other categories of sales excluded from the application of the Vienna Convention under Article 2(b) to (f) thereof. As to the question of whether the prospective Convention should apply to the assignment of receivables arising from sale contracts concluded orally, the committee agreed that this was a matter which should be left to be decided by the law applicable to the contract as there was no intention here of imposing any condition as to the form of the contract of sale.
17. - Sub-paragraph (a) having set out the supplier's duty to the factor, sub-paragraph (b) of Article 1, paragraph 1 deals with the obligations of the factor. In practice, factors perform a series of widely differing functions; it seemed however that only four of those most frequently found in factoring transactions needed to be mentioned, namely: finance, which usually assumes the form of a loan or advance payment; the maintenance of accounts (ledging); the collection of receivables and protection against default in payment by debtors, this latter expression referring to the factor's assumption of the risk of the insolvency of the supplier's customers and not to the case of the debtor's refusal to make payment as a consequence of his disputing his obligation to pay. For a contract of assignment to be considered as a factoring contract for the purposes of the future Convention, the factor must agree thereunder to perform at least two of these functions for indeed since none of them when taken alone is characteristic of factoring, each of them may be absent from a factoring contract. It should also be underlined that the requirement in sub-paragraph (b) and the conditions set out in sub-paragraphs (a) and (c) are cumulative, with the consequence that if the contract provides that the receivables are to be assigned by the supplier to the factor and that the debtor must receive notice of the assignment, then even if the two functions performed by the factor are the collection of receivables and the maintenance of accounts the contract will be a factoring contract for the purposes of the Convention.

18. - The last element which, under sub-paragraph (c), characterises as a factoring contract one meeting the conditions set out in sub-paragraphs (a) and (b) is that it provides that notice of assignment of the receivables will be given to debtors (in writing). This important restriction, which derogates from the declared principle of embracing the most diverse forms of factoring, has from the very outset been retained as a criterion for the definition of the factoring contract for the purposes of the Convention. Among the considerations which led to this decision was a concern that the inclusion of non-notification factoring could result in the Convention applying to a large number of transactions, in particular international banking operations where the receivable is used as security, transactions which might moreover assume forms of factoring unknown to some legal systems, and the fact that in any event the problems raised by assignments were totally different in respect of the rights of debtors according to whether the assignment was or was not notified to them. It should be noted that when the parties to the factoring contract choose the form of notification factoring (which will necessarily be the case if the future Convention is to apply) the function of recovery of the receivables will almost always be performed by the factor: in that event, the requirement of notice in Article 1, paragraph 1 (c) is completed by the conditions set out in Article 7, paragraph 1 concerning in particular the manner of the notification, which gives rise to the debtor's duty to pay the factor.

19. - The other two paragraphs of Article 1 contain definitions. While paragraph 2 provides that "... references to "goods" and "sale of goods" shall include services and the supply of services", in accordance with the decision of the committee concerning the contracts which may give rise to receivables assigned under a factoring contract, paragraph 3 is intended to clarify what is meant by "writing", a term which concerns the form of the notice referred to in Article 3, paragraph 2 as well as notice to the debtor. In the latter case the committee was of the belief that it was important for the parties to know with certainty whether a stamp or sticker affixed on an invoice issued to the debtor would be deemed to be a "written" communication in the absence of any signature. The provision reads: "In this Convention "writing" includes any form of writing, whether or not signed"; the committee was however at the conclusion of
its work conscious of the unsatisfactory nature of this wording which failed to mention modern means of communication, and it requested the Unidroit Secretariat to prepare for the Conference another formulation which could be based on definitions contained in other international texts, some of them still at the drafting stage, or in national law.

20. **Article 2**

Paragraph 1, whose structure is based on that of Article 1, paragraph 1 of the Vienna Convention, contains two kinds of provisions. The first determine the substantive scope of application which Article 1 has limited to factoring contracts, restricting it to the factoring of international receivables. This approach was decided on by the committee as it facilitates the application of the rules of the future Convention to domestic transactions for those States which wish to do so. Paragraph 1 establishes on the other hand the territorial scope of application of the Convention by indicating the connecting factors leading to its application.

21. **The introductory language** of paragraph 1 provides that: "This Convention applies whenever the receivables assigned pursuant to a factoring contract arise from a contract of sale of goods between a supplier and a debtor whose places of business are in different States." Whereas Article 1 gives the definition of "factoring" for the purposes of the Convention, this provision of Article 2 defines "international" factoring. Since the principal aim of the proposed Convention is to facilitate factoring as an instrument for the promotion of international trade, it is easy to understand that the international character of factoring transactions should be determined by the international character of the contract of sale. This is moreover the one and only relevant factor as attempts to identify an independent international character of factoring contracts have shown that it would be undesirable for a receivable arising from a domestic sale relationship to be submitted to a different legal regime according to whether it is assigned to a factor in the same country or abroad, or yet again successively to two different regimes, the first of which might be internal law and the other the international Convention. The criterion selected for the purpose of qualifying the contract of sale of goods as international is that traditionally employed in recent international trade law conventions and in particular the Vienna Convention, Article 1, paragraph 1 of which provides that the parties to the contract must have their places of business in different States. In consequence, the place of business of the factor has no bearing on the question. It should finally be noted that the introductory language of paragraph 1 is intended to make it quite clear that, when a factoring contract makes provision for the assignment of both national and international receivables, only transactions relating to the latter will be subject to the regime established by the Convention.

22. The determination of the territorial scope of application of the future Convention proved to be an extremely complex matter, principally on account of the two "layers" of contractual relations present in the transaction under consideration. In effect, as stated in the preceding paragraph, the "foreign" aspect of the factoring contract, which is itself most often purely national in character, is to be found in the contract of sale; furthermore, the draft Convention contains provisions governing certain effects of the sale contract on the factor and others which relate to the effects of the assignment on the debtor. Moreover, the committee was concerned that while the Convention should have as extensive a scope of application as possible so as to cover a wide range of transactions, this should not cause any prejudice to the legitimate interests of the parties involved. These various considerations finally led the committee to adopt
the solution contained in the two sub-paragraphs of paragraph 1 of Article 2. Sub-paragraph (a) provides that the Convention will apply to the assignment of international receivables “when the supplier, the debtor and the factor have their places of business in Contracting States”. The committee considered that it was particularly desirable that the Convention should have an autonomous scope of application based on objective connecting factors which would provide the certainty and speed indispensable for international factoring transactions and this solution seemed to be the one which best guaranteed the protection of the interests of each of the parties concerned, in particular those of the debtor who, although not a party to the factoring contract, might find his position altered by the assignment and who must in consequence know which law will be applicable. Sub-paragraph (b) on the other hand provides an alternative ground for the application of the Convention based on conflicts rules: thus even when the conditions laid down in sub-paragraph (a) are not met, the Convention will nevertheless apply “when both the contract of sale of goods and the factoring contract are governed by the law of a Contracting State”, this formula being intended to cover those cases where the rules of private international law lead to the application of the law of a Contracting State to each of the two contracts, including those where the parties have chosen the law of a Contracting State to govern their respective contractual relationships. The reasons which led to the two contracts being taken into consideration were the same as those which dictated the choice of the places of business of the three parties in sub-paragraph (a). It should moreover be noted that the two contracts may both be governed by the law of the same Contracting State or each by the law of a different Contracting State. There was, however, some criticism within the committee of the introduction of a connecting factor based on conflicts rules in this Convention on the ground that it would cause serious difficulties in its practical application as the parties would, notwithstanding the large number of transactions and the speed with which they must be handled, have to undertake complicated and costly enquiries to ascertain whether the conditions laid down in Article 2(1) (b) had been satisfied. With a view to giving the future instrument a wide scope of application and so as to avoid departing from a solution contained in many recent international trade law conventions, the committee ultimately decided to maintain the rule, although it should be recalled that Article F of the draft final provisions (13) permits States to make a declaration that they will not be bound by Article 2, paragraph 1 (b).

23. - Since, as in other modern international trade law conventions, it is the place of business of the parties which serves to determine the international character of the contract of sale of goods and therefore of the factoring contract as well as the conditions for the application of the Convention under paragraph 1 (a), a factor which is moreover decisive for the application of Article 5, paragraph 1, it was essential to include a provision indicating the relevant place of business when one or more of the three parties involved has more than one place of business. The committee took over, subject to the adaptations which were necessary having regard to the two contractual relationships relevant to factoring transactions, the formulation of the corresponding provision of the Vienna Convention (Article 10 (a)). Article 2, paragraph 2 reads as follows: “For the purpose of this Convention, if a party to the contract of sale of goods or the factoring contract has more than one place of business, the place of business is that which has the closest relationship to the contract and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that contract”. The word “contract” in the third line of this provision should be understood

(13) See page 114 infra.
as that corresponding to the legal relationship contemplated.

Article 3

24. - Article 3 determines the extent to which the parties involved in factoring transactions may exclude the application of the prospective Convention and the circumstances in which such exclusions are operative. It should be recalled that in the course of the committee’s work a view was expressed by some participants to the effect that the whole of the Convention could be of mandatory application, principally for the reason that it would be unlikely that the factor would wish to exclude rules which were designed to facilitate international factoring and that this aim would be frustrated if the parties to the contract of sale were to be free to choose another law to govern the assignment. A majority however declared itself to be firmly attached to the principle of party autonomy, all the more so as the subject fell within the domain of international trade law, and stressed the fact that the choice of a mandatory regime could be detrimental to the success of the prospective Convention whereas many States would on the other hand be prepared to accept an instrument from whose provisions the parties could derogate.

25. - The principle which originally guided the thinking of the committee was that the parties might, in their relations with each other, exclude the application of the Convention. It seemed that the supplier and the factor could have a legitimate interest in submitting their relations to a law other than the Convention and that such freedom should be accorded to them, the debtor in any case not being a party to such an agreement. The rule is thus laid down in Article 3, paragraph 1 that: “The parties to the factoring contract may exclude the application of this Convention”.

26. - Paragraph 2 is concerned with those situations where it is the supplier and the debtor who stipulate in the contract of sale or in a separate instrument that the Convention on international factoring shall not apply in the event of the assignment of the receivables arising under that contract. Notwithstanding some doubts as to the desirability of allowing the parties to another contract (in this case the sale contract) to determine indirectly the law applicable to the contract governed by the future Convention (namely the factoring contract), the prevailing view was that the legitimate interests of the debtor, whose position was to a certain extent affected by the assignment, to exclude the application of the prospective rules should also be recognized. With a view however to protecting the factor who, on account of the need for certainty and speed in conducting the transactions with which he deals, must be able to proceed on the assumption that the Convention will govern the assignment, the committee agreed that he must be given notice, and not simply by means of the contract of sale, of the decision of the parties to that contract that the Convention shall not apply to assignments of receivables arising after the giving of such notice to the factor. In consequence, paragraph 2 provides that: “The parties to the contract of sale of goods may exclude the application of this Convention only in respect of receivables arising at or after the time when the factor has received notice in writing of such exclusion”. It should be noted that the term “writing” is to be understood in the light of the definition contained in Article 1, paragraph 3 of the future Convention.

27. - Finally, paragraph 3 of Article 3 provides that: “Where the application of this Convention is excluded in accordance with the preceding paragraphs of this article, such exclusion may be made only as regards the Convention as a whole”. Although special agreements may sometimes be concluded between the debtor and the factor, in particular in
connection with the rights dealt with in Article 8, the general view within the committee was that the future instrument should be seen as a whole which could not be split up or modified without disturbing the balance which it was sought to achieve between the rights and obligations of the parties involved in factoring transactions.

Article 4

28. - It has been seen from the commentary thereon that Article 1 contains a number of elements permitting a characterisation of a "factoring contract", one of which is that the supplier undertakes to assign or directly assigns receivables to the factor. Article 4 for its part provides a sound legal basis for the factoring contract effectively to assign the supplier’s receivables to the factor, certain legal systems in effect not recognizing the global assignment of receivables, in particular future receivables. After affirming the validity as between the parties to the factoring contract of a clause in that contract under which existing or future receivables are to be assigned (subject to sufficient identification of them), it indicates the time at which the transfer of the future receivables takes place.

29. - The introductory language limits the scope of the rules which follow to relations between "the parties to the factoring contract". This formulation was preferred to an express designation of the parties so as to avoid any ambiguity as regards the scope of the article in those legal systems where the term "supplier" might be understood as possibly including a trustee in bankruptcy carrying on the supplier’s business, an interpretation which would run counter to the committee’s decision not to deal with the problem of the effectiveness of the assignment against third parties (including the trustee in bankruptcy or any other creditor of the supplier), certain effects of the assignment on the debtor being dealt with in Articles 7 to 9 of the Convention. Sub-paragraph (a) seeks to overcome the difficulties existing in some legal systems caused by the fact that an agreement to assign receivables may not be valid on account of the absence of any precise indication of the subject-matter of the assignment. It should be noted that it was not the committee’s intention to establish a general rule governing the validity of the contract independently of other grounds of invalidity recognized by the applicable national law, a consideration which led it to clarify the English text as follows: "a contractual provision ... shall not be rendered invalid by the fact that ...", a refinement absent from the French text ("une clause du contrat ... est valable, même si ...") as in the opinion of the French-speaking representatives its wording could be open to no other interpretation than that intended by the committee. The only condition imposed by sub-paragraph (a) as regards the rule of limited validity enunciated by it is that the receivables must be described in such terms by the factoring contract that those subject to the assignment can be determined without difficulty, the time at which a given receivable may be identified to the contract being the conclusion of that contract as regards receivables already in existence and, in respect of future receivables, the time when they come into existence. Although the committee preferred not to lay down criteria governing the identifiability of receivables so as to leave a wide measure of appreciation to the judge, considerations which may be relevant are, for example, the designation by the contract of the line of goods or services contemplated, the countries from which the supplier’s customers come or, possibly, a list of regular customers agreed by the parties to the factoring contract.

30. - Following the statement of principle as to the validity of global assignments, sub-paragraph (b) of Article 4 deals with the recognition of the effects of such a clause, namely the
effective transfer not only of existing receivables, which goes without saying, but also of future receivables, the assignment being operative in such cases at the very moment at which the receivable arises. While this rule reflects the law of a certain number of States, even though the parties sometimes choose to make a new assignment purely for evidentiary purposes so as to avoid the need for the whole factoring contract to be exhibited in court, in other legal systems an act of assignment relating to specifically designated receivables distinct from the factoring contract itself is necessary for an effective assignment of the receivables to the factor. It was for those legal systems which do not recognize the global assignment of future receivables that the committee considered that it would be desirable to clarify the moment at which the transfer becomes operative so as to permit the determination, always independently of the question of priorities, of the time as from which the factor will become entitled to certain rights.

Article 5

31. - Article 5 attempts to settle a particularly thorny problem in the field of international factoring caused by the radically different solutions to be found in national law concerning the question of the validity of assignments to the factor when the supplier has acted in breach of an undertaking to his customer not to factor the receivables arising from their contract. The main interest of the debtor is to guard himself against a change in his creditor and to be certain that he will obtain discharge by making payment to the supplier, thus being free from any concern as to third party claims. As regards the supplier however, the factoring of receivables subject to a prohibition on assignment may sometimes be a source of financing necessary for the conduct of his business. Independently of priority questions involving third parties, the factor will, according to whether or not national law gives effect to the prohibition on assignment, either enjoy no rights in the receivable or acquire rights over it in accordance with the terms of the assignment stipulated by the parties to the factoring contract, a problem which is particularly acute in the event of the insolvency of the supplier.

32. - From the outset of the work on the draft, there was a feeling that such an important matter could not be left aside without seriously compromising the value of the future Convention as a whole. The underlying aim of facilitating international factoring would seem to lead to upholding the validity of the transfer, an approach initially followed in the draft rules. Some members of the committee supported this solution, which they saw as providing a degree of security in international factoring transactions, either because it reflected the position in their national law or, even though it constituted a departure from that law, was nevertheless acceptable in the context of international transactions; other representatives however were firmly opposed to a provision which ran counter to the fundamental principle of the respect of party autonomy. The question was the subject of lengthy and detailed debate at various sessions of the committee, at which the supporters and the opponents of the original rule adduced a number of arguments which need not be repeated here. The committee considered compromise solutions, none of which however, after careful examination, provided full satisfaction. The possibility was then studied of combining a provision dealing with the validity of an assignment effected in violation of a prohibition thereon stipulated between the parties to the contract of sale with a reservation clause which, while it would not offer a uniform solution to this

(16) See Study LVIII - Doc. 26, p. 13 et seq.
controversial question, would at least have the merit of opening the way to a certain measure of harmonisation.

33. - The first attempt to settle the problem by way of the proposed new approach consisted in the affirmation of a basic principle ("[t]he assignment ... shall be effective"), combined with a rule displacing the principle ("[t]he provisions of the preceding paragraph shall not apply ...") when the debtor has his place of business in a Contracting State which has made a declaration to that effect. This solution was based on a similar approach adopted in the Vienna Convention (Articles 11, 12 and 96) and was intended, whenever the condition concerning the debtor’s place of business was satisfied, to give free play to the rules of private international law to determine the applicable law for the purpose of resolving the question of the validity of the assignment. Serious objections were however raised in relation to this formula, the actual effects of which did not seem to be clear, and which was also criticised on the ground that it could in effect lead to the same result as that which some were seeking to avoid, all the more so as it was probable that the law applicable to the assignment would most often be that of the seller’s place of business, and in consequence that of the factor, a solution which would hold out scant prospects of protection to the debtor.

34 - Moreover, on the basis of an earlier decision to limit the principle of the validity of the assignment of the receivable to the right to payment (following the model of the Uniform Customs and Practices for Documentary Credits), with the consequence that the debtor could never, unlike the case of other rights over the receivable, contest such a transfer, the committee came to the conclusion that it must distinguish the validity inter partes of the assignment from the question of its effectiveness against the debtor. Given the agreement reached within the committee on this important point, it decided to accept the principle of a reservation of a substantive character which would in any event have the merit of guaranteeing certainty. The rule finally adopted may be set out as follows: the general principle to be found in paragraph 1 that “[t]he assignment of a receivable by the supplier to the factor shall be effective notwithstanding any agreement between the supplier and the debtor prohibiting such agreement” means on the one hand that the prohibition on assignment agreed by the parties to the contract of sale has no effect on the validity of the assignment of the receivable as between the parties to the factoring contract (17) and on the other that it does not prevent such an assignment having effects on the debtor. The exception to this rule, which applies by virtue of paragraph 2 when the debtor has his place of business in a State which avails itself of the declaration for which provision will be made in the final clauses (see at present Article X of the text of the draft), will have no incidence on the validity of the assignments as between the parties to the factoring contract but will on the other hand protect the debtor from any effects of the assignment on him when he has stipulated a prohibition on assignment with the supplier. It follows that the factor cannot, in cases contemplated by Article 5, paragraph 2, rely on the provisions of the future Convention dealing with the position of the debtor subsequent to the assignment, namely Articles 7 to 9.

(17) Attention should be drawn to the fact that, like Article 4, Article 5, paragraph 1 does not seek to establish a general rule on validity but is intended only to remove the obstacle which could be created by the prohibition on the assignment.
Article 6

35. - Article 6 performs a similar function to Article 4 in that after providing in its introductory language that the only relations dealt with are those between the parties to the factoring contract, it affirms the validity and effectiveness of a clause in a factoring contract providing for the transfer to the factor not only of the receivables but also of the rights of the supplier in the receivables assigned: what is intended here is to ensure that rights deriving from future sales may be transferred, thereby removing an obstacle existing in some legal systems, although it is to be understood that this article also applies to the transfer of rights already in existence.

36. - Apart from establishing the principle of the validity of the transfer of rights, Article 6 indicates the method of transfer: the parties may agree that the assignment of the receivable will automatically carry with it any corresponding securities or alternatively that the rights in question can only be transferred by a special instrument to that effect. When the parties are silent on this point the matter will fall to be decided by the applicable national law, but it is in any event clear that whatever the choice of the parties as regards the method of transfer, it remains subject to the rules as to form or public notice of the applicable law to the extent that they seek to make the transfer effective against third parties.

37. - It should finally be mentioned in connection with the words “the supplier’s rights deriving from the sale of goods” that the committee intended to cover securities (to be understood in the broadest sense so as to embrace the different forms existing under national law) which guarantee the assigned receivables in particular or, more generally, the performance of the contract of sale as a whole; moreover, both contractual and legal securities are contemplated. The committee considered it useful to cite by way of example the reservation of title. It need scarcely be added that this provision in no way affects questions concerning the validity and possible recognition abroad of such guarantees.

Article 7

38. - After laying down a number of rules relating to the validity of the assignment between the parties to the factoring contract, the draft Convention contemplates in Articles 7 to 9 the position of the debtor subsequent to the assignment (subject naturally to the provisions of Article 5, paragraph 2). It should be recalled that the committee chose from the outset of its work to dissociate the two aspects - validity inter partes and effects of the assignment on the debtor - so as to avoid placing the latter under a duty to make enquiries, possibly difficult ones, which could entail the most serious consequences for him.

39 - Whenever the factoring contract provides that the factor shall recover the receivables (or in the converse case, if the factor has good reason to require payment directly by the debtor), the debtor is under a duty in accordance with paragraph 1 of Article 7 to make payment to the factor, an obligation which derives from the notice given in the manner prescribed in subparagraphs (a) to (c). Moreover, a condition additional to that of notice is one that the debtor did not have knowledge of any other person’s superior right to payment of the receivable. This requirement, which the committee saw as being bound up with the concept of good faith, seems however to place a certain burden on the debtor, for although he has no obligation to conduct research into the possible existence of creditors other than the factor, on the other hand
whenever the debtor has knowledge of another person's claim to payment of the receivable, the present language of the provision may be taken as obliging him to make enquiries as to the merits of the claim and, if it does exist, as to whether it constitutes a superior right to payment. It should in conclusion be made clear that the two conditions (absence of knowledge of a superior right and notice given in accordance with sub-paragraphs (a), (b) and (c)) are both necessary and sufficient to create the debtor's obligation to pay the factor, which cannot therefore arise, in the context of a factoring transaction governed by the prospective Convention, from any rules of the applicable national law, whether more or less strict.

40. *Sub-paragraph (a)* recalls in the first instance the requirement already referred to in Article 1, paragraph 1 (c) that notice must be given in writing, a notion to be understood in the light of the definition to be found in Article 1, paragraph 3. On the other hand this provision indicates the person who must give notice: this may first of all be the supplier on the ground that he is the original creditor who has concluded a contract with the debtor. The factor has however a legitimate interest in the debtor's receiving notice of the assignment as it is to him that payment must be made and, in those legal systems where priority among creditors is determined by the order in which notice is given, he will in most cases be more diligent than the supplier. Consequently, the committee considered that the factor should himself be capable of giving notice of the assignment, on condition however that he acts with the supplier's authority, this formula simply indicating that the debtor must have reasonable grounds for believing in the existence of the factor's authority, if appropriate by making enquiries of the supplier, although questions regarding the form of the authority and the possibility for notice to be given by other persons acting in the name of the supplier or of the factor are left to the applicable law.

41. *Sub-paragraph (b)* provides that the notice must reasonably identify the beneficiary under the assignment to whom the debtor must make payment: this may be the factor himself and the committee agreed that the notice need not necessarily indicate that the assignee was indeed a factor, or a bank receiving payment on behalf of a factor. The notice must moreover reasonably identify the receivables so that the debtor may be informed of the precise subject-matter of the assignment while, under *sub-paragraph (c)*, it must relate only to receivables arising under a contract made at or before the time the notice is given. In consequence, although a clause in the factoring contract effectively transfers all future receivables from the supplier to the factor pursuant to Article 4 of the draft Convention, notice of the assignment of a future receivable will only place the debtor under an obligation to pay if the contract under which the receivable arose was made at or before the time notice was given.

42. *Paragraph 2* of Article 7 provides in the first instance that payment by the debtor to the factor discharges the debtor's liability *pro tanto* if made in accordance with the provisions of paragraph 1. On the other hand, while the committee agreed that the debtor's obligation to make payment under the future Convention could only arise in cases where the conditions set out in paragraph 1 were met, it was nevertheless of the opinion that the debtor should be entitled to make payment and thereby to discharge his liability when such payment would have that effect under the applicable national law. Given the committee's unwillingness to refer to the applicable law without indicating how it should be determined, and its preference not to lay down a connecting factor in an instrument establishing uniform rules of substantive law, the paragraph provides that payment by the debtor in accordance with paragraph 1 shall discharge him from liability "irrespective of any other ground on which payment by the debtor to the
factor discharges the debtor from liability”.

Article 8

43. - This article is concerned with the extent to which the debtor may set up certain defences against the factor at the time of payment. Paragraph 1 deals with defences relating to the receivable assigned and provides that the debtor may set up against the factor all defences of which the debtor could have availed himself under the same contract if such claim had been made by the supplier. Paragraph 2 relates to defences available to the debtor against the supplier not connected with the receivable. The rule which has been adopted, and which is moreover to be found in many legal systems, is that the rights and claims on which the debtor may rely against the other party to the contract at the time he received notice of the assignment may be asserted against the factor. This solution is to be explained by a concern to protect the factor’s position in respect of contracts concluded between the supplier and the debtor which subsequently give rise to rights of set-off of which the factor had no knowledge.

44. - It may be noted that Article 8 limits itself to laying down two fundamental principles concerning the debtor’s rights as against the factor, many aspects of the question thus being left to national law, especially those falling under the complicated law of set-off. In particular the committee deemed it preferable not to indicate whether the rights “available to the debtor” are those due for payment or simply those in existence at the time notice is received. Furthermore, while the provision confirms the debtor’s right of set-off in relation to rights or claims “existing against the supplier in whose favour the receivable arose”, it leaves open the question of the effectiveness of rights of set-off arising out of any earlier dealings between the debtor and the factor, or of dealings with other suppliers of the debtor who assign their receivables to the same factor. Likewise, Article 8, paragraph 2 provides that the notice which serves to limit the defences is that given in accordance with Article 7 of the Convention. It is in consequence to be understood that the effects of different forms of notice which will not therefore be effective under the future Convention will be determined by the applicable national law. Finally, some legal systems provide that in certain cases the debtor will lose the benefit of defences, in particular his right of set-off (in some systems when the debtor accepts the assignment), and the committee recalled that in conformity with Article 11, paragraph 2 the absence of any rule on this matter in the Convention would in any event mean that the question would be determined by the applicable national law.

Article 9

45. - The case contemplated by Article 9 is that where the debtor has already fulfilled his obligation to make payment but has not received consideration in that the supplier has failed to perform his obligations under their contract. The special feature of this situation following the assignment of the receivable is that, when looked at from the debtor’s point of view, there is a dissociation of the person who receives payment from the one who supplies the goods or services. In the case of a continuing relationship the debtor may certainly, in accordance with Article 8, paragraph 2, subsequently set-off against the factor his rights against the supplier (recourse by the factor against the supplier being dealt with in the factoring contract); however the problem here is that of deciding whether the factor is obliged to return to the debtor money received from him.
46. - A certain number of arguments were adduced in the committee in favour either of denying the debtor’s right to recover money paid to the factor or of leaving the problem to be decided by the applicable law. The committee as a whole was however in agreement as regards the general approach which would determine the solution to be adopted, namely that the debtor’s position should be neither improved nor worsened as a result of the assignment. In particular there was thus no reason, in the event for instance of the supplier’s bankruptcy, for the debtor to recover a sum from the factor when he might not have been able to do so had no factoring contract been concluded. On the other hand, in those legal systems where the debtor loses his right to claim recovery of the price from the supplier because it is the factor who has received payment, it did not seem fair to deprive the debtor of the possibility of recovery from the factor. Paragraph 1 reflects a concern not substantially to alter the debtor’s existing situation, by providing that the supplier’s failure to perform shall not alone entitle the debtor to recover money paid to the factor (any other grounds of recovery which may exist under national law therefore being unaffected). The application of this rule is however restricted by the last part of the provision to those cases where, under the applicable national law, the debtor has not been deprived by the assignment of his claim against the supplier for recovery of the price.

47. - The committee considered it desirable to state in paragraph 2 two exceptions to the general rule intended to protect the factor (exceptions applicable on condition that the debtor has a claim against the supplier for recovery of the price), which are, independently of the position of the debtor, justified by the financial role of the factor in the transaction. Sub-paragraph (a) provides that the debtor may recover money paid to the factor to the extent that the latter has not paid the purchase price of the receivable to the supplier, the situation contemplated being that of the unjust enrichment of the factor when the sum paid by the debtor has remained in the hands of the factor, either because the latter ought already to have paid the supplier or because he has not yet done so. For its part, sub-paragraph (b) is concerned with the case where the factor has already paid the supplier the purchase price of the receivable although he knew at the time of such payment that the supplier had not yet performed his own obligations towards the debtor. The committee considered that in such circumstances it was the factor and not the debtor who should subsequently assume the financial risk deriving from non-performance or defective or late performance by the supplier, all the more so as it is customary for factors to include in the factoring contract guarantees as to performance and to retain part of the advance with a view to securing their position against the supplier.

Article 10

48. - In conformity with Article 1, the articles of the draft Convention preceding Article 10 have been concerned with the situation where it is one and the same factor to whom the supplier assigns the receivable and to whom payment is made by the debtor. Although this system is well known in international factoring, it is more often the case that, for reasons of practicality, a second factor enters on the scene: the supplier assigns the receivable pursuant to a factoring contract concluded with a factor who is usually located in the same country and the latter in his turn assigns the receivable to another factor who acts as his correspondent in the debtor’s State, the two factors being respectively designated by practice as “the export factor” and “the import factor”. It is evident that from the outset of the work it was understood that this kind of factoring should fall within the rules to be contained in the future instrument, the
position of the subsequent factor to whom the assignment is made being assimilated, *mutatis mutandis*, to that of the other party to the factoring contract concluded by the supplier, not only as regards the provisions concerning the validity of the assignment of the receivable but also the conditions under which the assignment may be effective against the debtor. While the committee entertained no doubts as to the usefulness of applying the Convention to assignments as between factors, on the other hand the drafting of this article caused a number of difficulties\(^{(18)}\) arising principally from the fact that although the relations between the parties to the contract for the subsequent assignment may be assimilated to those between the parties to the factoring contract, the underlying sale relationship retains its relevance in a number of respects. The present wording of Article 10, paragraph 1 is a combination of two approaches to the transposition to subsequent assignments of the rules of the Convention previously examined by the committee. At its final session however it considered that the drafting called for improvement, in particular in the light of a detailed examination of the way in which the transposition mechanism would operate in connection with each of the provisions of the future Convention.

49. - Article 10 contains provisions relating to the future Convention’s scope of application as well as substantive rules of law. The introductory language of paragraph 1 determines the connecting factor according to which the Convention will apply to subsequent assignments of the receivable by the factor or by a subsequent assignee. The committee rejected a number of criteria such as the particular characteristics of the contract for the subsequent assignment of the receivables or the character of the parties to that contract; nor did it consider it desirable to establish a connecting factor based on the subsequent assignee’s place of business or on an alternative conflicts rule modelled on Article 2, paragraph 1 (b), principally because the subsequent assignee is most often in practice a factor with his place of business in the same State as the debtor. The only condition required for the rules of the Convention to apply – in accordance with sub-paragraphs (a) and (b) – to a subsequent assignment of a receivable is that the latter has previously been “*assigned by a supplier to a factor pursuant to a factoring contract governed by this Convention*”.

50. - The two sub-paragraphs of paragraph 1 contain the very principle on which the extension of the scope of application of the Convention rests. *Sub-paragraph (a)* provides that the rules laid down in Articles 3 to 9 (with the exception of Articles 7 and 8 which are dealt with in sub-paragraph (b)) apply to any subsequent assignment of the receivable by the factor or by a subsequent assignee. The term “subsequent assignment” is to be understood as referring to the transfer of the receivable by the person to whom it has been assigned and not, of course, to a second fraudulent assignment by the same assignor. In this connection it may be recalled that a proposal was made at the second session of the committee for the inclusion of a separate article laying down a limited priorities rule which would apply in such cases; given however the difficulty of reaching agreement on a criterion acceptable to all legal systems and of the restricted scope which such a rule would enjoy in practice, this proposal was rejected by the committee. Moreover, if a series of transactions takes place following the first assignment, all of those assignments will be governed by the Convention provided that that assignment was itself governed by the rules of the Convention and, as indicated above, this will be the case

\(^{(18)}\) See Study LVIII - Doc. 23, p. 5 *et seq.*, which also sets out the drafting proposals made by the Secretariat.
whatever the form or the characteristics of the subsequent assignment or assignments and the status or places of business of the subsequent assignees. The committee considered that the flexible formulation of the rule contained in sub-paragraph (a) would permit those called upon to interpret it to apply to any subsequent assignment of the receivable the principles governing an assignment made pursuant to a factoring contract. Those principles may briefly be recalled here, in the context of subsequent assignments, in respect of each of the articles in question. In the first place Article 3, which permits the parties to exclude the application of the Convention, has been included among those referred to by Article 10 as a consequence of the changes in the order and numbering of its provisions; in the event of it being decided to allow the parties to a subsequent assignment to exclude the application of the Convention to their transaction, it would be preferable to indicate in detail the operation and effects of such a rule, in particular in regard to its implications for the debtor. By virtue of the combination of Articles 10 and 4, a subsequent assignor may validly make a global assignment of future receivables and may also transfer rights deriving from the sale of goods (Article 6). In conformity with Article 5, a prohibition on assignment agreed upon by a supplier and a debtor who has his place of business in a Contracting State which has made the declaration for which provision is made in the corresponding article (at present Article X), will not prevent a subsequent assignment of the receivable which has already been validly assigned pursuant to a factoring contract, although the debtor will continue to be protected from the effects of such assignments. Finally, the circumstances set out in Article 9 in which the debtor may recover payments made to a factor may without difficulty be transposed so as to apply to a subsequent assignment as it is obvious that the debtor will only pay once, either to the assignee of the supplier when there is only one factor, or to the last assignee in the event of successive assignments, especially when the factoring transaction is performed by two factors.

51. - As regards Articles 7 and 8, the committee considered it useful to reconsider at its final session the fiction contained in sub-paragraph (b) of Article 10, paragraph 1 whereby the subsequent assignee is, as regards the debtor, placed in the position of the factor. For the same reasons as those set out in relation to Article 9, the debtor is, in the case of a subsequent assignment, required to pay only the subsequent assignee, subject to the requirements of Article 7, paragraph 1 being met, and is discharged from liability in accordance with paragraph 2 of that article. Similarly, the debtor may set up against the subsequent assignee any of the defences under the contract of sale and rights of set-off existing against the supplier referred to in Article 8. It may therefore be noted that in these circumstances the draft Convention is silent as to the rights of set-off available to the debtor against the last assignee arising out of his relations with the factor or any earlier assignee, a matter which will in consequence fall to be determined by the applicable national law.

52. - When notice of the subsequent assignment is not given to the debtor, the latter is informed only of the first assignment made pursuant to the factoring contract and thus in such cases the rules contained in Articles 4 to 6 will govern the corresponding aspects of the validity of both the first and the second assignments, although the provisions of Articles 7 to 9 will be of relevance only to the first assignment. As a general rule however, in international factoring transactions, the supplier gives notice to the debtor that he must make payment to a person who is in fact the subsequent assignee, no notice having been given of the first assignment. Since only notification factoring is dealt with by the future instrument pursuant to Article 1, paragraph 1 (c), it was important to ensure that the absence of notice regarding the first assignment would
not have the effect of excluding it (and in consequence all subsequent assignments) from the application of the Convention and for this reason it was decided to include a provision such as paragraph 2 of Article 10 by virtue of which "[n]otice to the debtor of the subsequent assignment may also constitute notice of the assignment to the factor".

53. - Paragraph 3, which provides that: "This Convention shall not apply to an assignment which is prohibited by the terms of the factoring contract" was introduced at the request of one delegation which recalled that its law did not allow a receivable which had already been assigned to be assigned a second time and that factoring contracts contained a clause whereby the factor undertook not to reassign the receivable. In the context of international transactions the supplier directly assigned the receivables to an import factor in the same State as that in which the debtor had his place of business. It may however be noted that doubts were expressed within the committee as to the need for such a provision. In any event it did not seem that the possible application of the Convention to a subsequent assignment made in violation of a prohibition contained in the factoring contract would validate such an assignment (Articles 4 to 6 in effect doing no more than laying down rules of limited validity), this question being determined by the applicable national law, which is indeed the result to which paragraph 3 leads. Furthermore, as regards the effects on the debtor, he would not, unless the supplier himself had given notice to the debtor of the subsequent assignment made in contravention of his own obligation in the factoring contract, be under a duty to pay the subsequent assignee pursuant to Article 7 since the latter would have no authority from the supplier to give notice of the assignment.

Article 11

54. - Article 11 concerns the rules of interpretation to be applied in respect of the future Convention. The language of paragraph 1 is based on that of the corresponding provision of the Vienna Convention, namely Article 7, which has been incorporated in a number of international trade law conventions and lays stress on the promotion of uniformity in the application of the Convention, having regard to its international character, so as to avoid the attempt at harmonisation at legislative level being defeated by different or piecemeal approaches at the stage of implementation by judges or arbitrators: the paragraph also refers to the observance of good faith in international trade. Furthermore, a new consideration, not to be found in the precedents for the wording of this article, has been added to those designed to aid in the interpretation of the Convention, namely its object and purpose as set forth in the preamble, so as to ensure that the Convention will be applied in accordance with the intention of its authors and with the declared objectives of States when they become Parties to it. Finally, paragraph 2 supplements the first part of paragraph 1 in that it is directed not to the interpretation of the provisions of the Convention but to the principles to be applied to matters governed by the Convention which are not settled by it. For such cases, mention is made of the general principles on which the Convention itself is based and, moreover, of the law applicable by virtue of the rules of private international law. It should be noted that unlike the Vienna Convention (Article 7) and the Geneva Agency Convention (Article 6) which contemplate reference to the applicable law only in the absence of general principles on which the Convention is based, such principles and the applicable law are here placed on the same footing.
DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING DRAWN UP
BY A UNIDROIT COMMITTEE OF GOVERNMENTAL EXPERTS,
WITH EXPLANATORY NOTES
(drawn up by the Unidroit Secretariat)

I. INTRODUCTION

1. - In accordance with a request made by the Unidroit committee of governmental experts for the preparation of a draft Convention on international financial leasing (hereinafter referred to as “the committee”) at its first session, held in Rome from 15 to 19 April 1985 (1), the Unidroit Secretariat drew up a set of draft final provisions designed to be capable of embodiment in the text of the future Convention on international financial leasing.

2. - These draft final provisions were to a large extent modelled on the corresponding provisions of the 1983 Geneva Convention on Agency in the International Sale of Goods (hereinafter the “Geneva Agency Convention”), the most recent example of an international Convention to be adopted at a diplomatic Conference convened under the auspices of Unidroit. It should however be borne in mind that the close relationship between the subject-matter of that Convention and that of the 1980 United Nations Convention on Contracts for the International Sale of Goods (hereinafter the “Vienna Sale Convention”) led to the adoption in Geneva of a number of solutions designed to ensure exact concordance between the two Conventions (cf. Article B, infra), which might not however necessarily be considered appropriate for other Conventions, notably the one under preparation on international financial leasing.

3. - Inspiration in the drawing up of these draft final provisions was accordingly also, where appropriate, sought in other recent models, notably the Protocol of 1984 to amend the International Convention on Civil Liability for Oil Pollution Damage, 1969 (hereinafter the “1984 Protocol”) (cf. Articles J and K, infra) and the 1985 Hague Convention on the Law Applicable to Contracts for the International Sale of Goods (hereinafter the “1985 Hague Convention”) (cf. Article D, infra).

4. - In the event the committee did not find time to consider these draft final provisions, moreover taking the view that such deliberations were normally reserved exclusively for the diplomatic Conference, (2) The Unidroit Secretariat, in drawing up this revised set of draft final

(2) Cf. Study LIX - Doc. 46, § 5.
provisions, has however taken account of the comments and suggestions made by representatives attending the Unidroit committee of governmental experts for the preparation of a draft Convention on certain aspects of international factoring (hereinafter “the factoring committee”) (3) with regard to the draft final provisions submitted to that committee by the Unidroit Secretariat. (4) The decision by the Canadian Government to host the diplomatic Conference for the adoption of the Unidroit draft Conventions on international factoring and international financial leasing in Ottawa in May 1988 has also enabled the Unidroit Secretariat to complete certain clauses of the draft final provisions, notably Articles A(1) and K(1) and the chapeau of Article K(2), as well as the drafting of the authentic text and witness clause.

5. - Bearing in mind that the committee (5) expected the present contents of Chapter III of the draft Convention on international financial leasing to be moved forward at the diplomatic Conference to an enlarged Chapter I entitled “Sphere of application and general provisions”, these draft final provisions would probably then become the subject of a new Chapter III entitled “Final provisions”.

II. SECRETARIAT PROPOSALS FOR THE FINAL PROVISIONS TO BE EMBODY IN THE PROPOSE CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Article A

1. - This Convention is open for signature at the concluding meeting of the Diplomatic Conference for the adoption of the Unidroit draft Conventions on international factoring and international financial leasing and will remain open for signature by all States at Ottawa until ......

2. - This Convention is subject to ratification, acceptance or approval by States which have signed it.

3. - This Convention is open for accession by all States which are not signatory States as from the date it is open for signature.

4. - Ratification, acceptance, approval or accession is effected by the deposit of a formal instrument to that effect with the depositary.

Commentary

The provisions of this article are essentially based on those of Article 22 of the Geneva Agency Convention, which were themselves based on precedents to be found in recent United Nations Conventions, such as the Vienna Sale Convention. In view of what is considered to be the desirability of incorporating an article on the functions of the depositary of the future Convention, on the lines of Article 17 of the 1984 Protocol (cf. Article K, infra), the drafting

(3) Cf. Study LVIII - Doc. 32, §§ 30-32.
(4) Cf. Study LVIII - Doc. 21.

106
of paragraph 4 departs from that of the Geneva Agency Convention in favour of that of the corresponding provision, Article 12(3), of the 1984 Protocol.

Article B

1. - This Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the third instrument of ratification, acceptance, approval or accession.

2. - For each State that ratifies, accepts, approves, or accedes to this Convention after the deposit of the third instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.

Commentary

This article is essentially modelled on Article 33 of the Geneva Agency Convention. In line with Article 99 of the Vienna Sale Convention, this requires the deposit of ten instruments of ratification, acceptance, approval or accession for the entry into force of the Convention and furthermore stipulates that such entry into force should only take effect twelve months after the date of deposit of the tenth such instrument.

Article B as originally drafted by the Secretariat, on the other hand, proposed a return to previous Unidroit practice as exemplified by the 1973 Washington Convention providing a Uniform Law on the Form of an International Will, Article XI of which provided for the entry into force of that Convention six months after the date of deposit of the fifth instrument of ratification or accession.

The factoring committee, however, forwarded a recommendation to the diplomatic Conference that the number of instruments be reduced still further, to three. This recommendation was felt to be justified by the limited, technical nature of the subject-matter of the prospective Convention. As this is an argument that would seem to be equally valid for the future Convention on international financial leasing, effect has also been given to it in the present draft final provisions.

[Article C

This Convention does not prevail over any international agreement which has already been or may be entered into and which contains provisions concerning matters governed by this Convention, provided that the supplier, the lessor and the lessee have their places of business in States parties to such agreement.]

Commentary

The effect of this provision, based on Article 90 of the Vienna Sale Convention and Article 23 of the Geneva Agency Convention, would be, in certain cases, to displace the application of the prospective Convention, entirely or in part, in favour of existing or future international
agreements, whether universal or regional in character, containing provisions concerning matters governed by it. This might, for example, be the case, as regards Article 5, with the 1948 Geneva Convention on the International Recognition of Rights in Aircraft.

This provision would also cover the case of any future Convention that might supersede that now under preparation unless, that is, it were to be deemed opportune to include in the present final clauses provisions establishing a revision procedure.

To the extent that one effect of Article C would be to weaken, to a certain extent, the universal character of the future Convention and thus to create a potential element of uncertainty for the parties, it is proposed that Article C would only apply when all three parties have their places of business in States parties to the other agreement containing provisions concerning matters governed by the prospective Convention.

There was a call for the deletion of the proviso to the corresponding clause of the draft final provisions drawn up for potential inclusion in the draft Convention on international factoring during discussion thereof by the factoring committee. This proviso was considered to represent an intolerable degree of interference in the autonomous sphere of application provisions of other quite distinct international agreements, in so far as its effect could be, for instance, to displace the application of such an international agreement for the sole reason that one of the parties to the factoring transaction did not happen to have its place of business in a State party to that other agreement\(^{(6)}\)

A case was even made out for the wholesale deletion of Article C at the last session of the factoring committee. This was founded on the argument that the prospective Unidroit Convention differed from other international instruments like the Vienna Sale Convention in so far as its terms of reference were drawn far more narrowly: the subject-matter of the future Convention was a very particular type of transaction, moreover only a limited number of aspects of which had been singled out for coverage therein. Another argument adduced in favour of the deletion of Article C was that it would avoid the danger of the “negative conflict of Conventions”, meaning the situation where two or more international instruments contain provisions yielding precedence to another instrument.

There was nevertheless reluctance on the part of a number of representatives to agree to the deletion of Article C without first giving the matter further thought. Just as the factoring committee accordingly came to the conclusion that the most appropriate solution in the circumstances was to place the provision in square brackets for decision at the diplomatic Conference, so this corresponding provision in the draft final provisions for the prospective Convention on international financial leasing is also submitted in square brackets.

**Article D**

1. - If a Contracting State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may amend its declaration by submitting another declaration at any time.

\(^{(6)}\) Cf. Study LVIII - Doc. 32, § 31 and Study LVIII - Doc. 34.
2. - These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. - If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

4. - If a Contracting State makes no declaration under paragraph 1 of this article, the Convention is to extend to all territorial units of that State.

Commentary

In recent years a number of formulae have been employed in international private law Conventions to meet the difficulties sometimes experienced by States with federal systems of government involving a constitutionally guaranteed division of powers among the constituent units of the federation.

The drafting of Article D follows that of Article 24 of the Geneva Agency Convention and also corresponds closely to the most recent expression of the inclination of States in this regard, namely Article 26 of the 1985 Hague Convention.

Article E

1. - Two or more Contracting States which have the same or closely related legal rules on matters governed by this Convention may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States. Such declarations may be made jointly or by reciprocal unilateral declarations.

2. - A Contracting State which has the same or closely related legal rules on matters governed by this Convention as one or more non-Contracting States may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States.

3. - If a State which is the object of a declaration under the previous paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which the Convention enters into force in respect of the new Contracting State, have the effect of a declaration made under paragraph 1 of this article, provided that the new Contracting State joins in such declaration or makes a reciprocal unilateral declaration.

Commentary

With minor adaptations, this article is based on Article 26 of the Geneva Agency Convention which was itself heavily influenced by the drafting of Article 94 of the Vienna Sale Convention. As with Article C supra, the opportunity that this article, which in effect amounts to a reservation clause, opens up for Contracting States to restrict the application of the prospective Convention could prove to be a source of uncertainty for the parties to international
financial leasing transactions as to which law would be applicable in a given case, and it is for this reason proposed that paragraphs 1 and 2 of Article E should only operate when all three parties, supplier, lessor and lessee, have their places of business in States concerned by the declaration or declarations.

**Article F**

A Contracting State may declare at the time of signature, ratification, acceptance, approval or accession that it will not be bound by Article 2(1)(b).

**Commentary**

Both the Vienna Sale Convention (Article 1(1)(b)) and the Geneva Agency Convention (Article 2(1)(b)) make provision for the application of the Convention not only when the specific objective connecting factors have been satisfied but also when the rules of private international law lead to the application of the law of a Contracting State. These models have been followed, albeit in amended form so as to take account of the tripartite nature and pluricontractual basis of the financial leasing transaction, in Article 2(1)(b) of the uniform rules which provides for the application of the prospective Convention when “both the supply agreement and the leasing agreement are governed by the law of a Contracting State”.

At both the Vienna and Geneva diplomatic Conferences, however, a number of States, especially Socialist States which have special legislation regulating foreign trade relations, called for the possibility to enter a reservation in respect of the application of the two Conventions in accordance with the rules of private international law in cases where they would not otherwise be applicable. The drafting of Article F is based on that of the reservation clauses contained in Article 95 of the Vienna Sale Convention and Article 28 of the Geneva Agency Convention.

**Article G**

1. - Declarations made under this Convention at the time of signature are subject to confirmation upon ratification, acceptance or approval.

2. - Declarations and confirmations of declarations are to be in writing and to be formally notified to the depositary.

3. - A declaration takes effect simultaneously with the entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral declarations under Article E take effect on the first day of the month following the expiration of six months after the receipt of the latest declaration by the depositary.

4. - Any State which makes a declaration under this Convention may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal is to take effect on the first day of the month following the expiration of six months after the date of the receipt of the notification by the depositary.
5. - A withdrawal of a declaration made under Article E renders inoperative, as from the date on which the withdrawal takes effect, any reciprocal declaration made by another State under that article.

Commentary

Precedents for the provisions of Article G are to be found in many international Conventions, the drafting of this article itself reproducing word for word Article 31 of the Geneva Agency Convention.

Article H

No reservations are permitted except those expressly authorised in this Convention.

Commentary

The wording of Article H follows that of Article 32 of the Geneva Agency Convention and is intended to prevent States making reservations other than those presently contemplated by Articles D, E and F or any other reservations which may be permitted under the prospective Convention.

Article I

This Convention applies when the leasing agreement and the supply agreement are both concluded on or after the date on which the Convention enters into force in respect of all the Contracting States referred to in Article 2(1)(a), or of the Contracting State referred to in paragraph 1(b) of that article.

Commentary

One of the most difficult problems to be solved in the context of private law Conventions involving tripartite relations is that of determining the time starting from which transactions will be subject to the provisions of the Convention once the requirements for its entry into force have been met. The position is complicated in this instance by the fact that Article 2 provides that the Convention will, subject to the introductory wording of the article, apply either when the supplier, the lessor and the lessee have their places of business in Contracting States (Article 2(1)(a)) or when both the supply agreement and the leasing agreement are governed by the law of a Contracting State (Article 2(1)(b)).

However, even when one or other of these requirements has been satisfied, it will still be necessary to ascertain at which point the application of the Convention will be triggered off in respect of a given transaction. Neither the corresponding provision of the Vienna Sale Convention (Article 100) nor that of the Geneva Agency Convention (Article 34) are, alas, of more than indirect persuasiveness in this context, the former being concerned with a bipartite transaction and the connecting factor for the application of the latter being that only one of the three parties, that is the agent, should have its place of business in a Contracting State.

Whereas the fundamental legal relationship contained within the tripartite financial leasing transaction was recognised by the authors of the draft Convention to be the leasing
agreement (7), they at the same time acknowledged the need to take due account in the provisions determining the application of the future Convention of the impact of certain of its provisions on the position of the supplier and on the supply agreement. Hence the original draft final provisions drawn up by the Unidroit Secretariat proposed alternative solutions to this problem. One of these proposed taking the fact that the leasing agreement was concluded on or after the date when the Convention entered into force as the trigger for the application of the future Convention. The other required both leasing agreement and supply agreement to have been concluded on or after the date of the Convention’s entry into force. Prior to the second session of governmental experts Governments were asked for their opinion on these alternatives. Only one reply in fact materialised, from the Austrian Government, and this favoured the second alternative.

In view of the importance the authors of the draft Convention attached to ensuring that sufficient account be taken of the role of the supplier and the supply agreement in the provisions determining the application of the future Convention, the Unidroit Secretariat, in laying these draft final provisions before Governments for the diplomatic Conference, has followed the suggestion of the Austrian Government in this regard and accordingly eliminated the first alternative, thus proposing that the Convention’s application should be triggered in respect of a given international financial leasing transaction only where both the leasing agreement and the supply agreement have been concluded on or after the date of the Convention’s entry into force. This proposal would moreover appear to acquire additional force from the specifically pluricontractual basis of the type of leasing transaction addressed by the draft Convention: it has to be remembered that one of the principal objectives of the draft Convention has all along been to move away from the unsatisfactory situation in which the type of leasing transaction addressed therein has been treated as two separate contracts and towards recognition of a new single, complex, atypical transaction involving the interaction of these two contracts.

Article J

1. - This Convention may be denounced by any Contracting State at any time after the date on which it enters into force for that State.

2. - Denunciation is effected by the deposit of an instrument to that effect with the depositary.

3. - A denunciation takes effect on the first day of the month following the expiration of twelve months after the deposit of the instrument of denunciation with the depositary. Where a longer period for the denunciation to take effect is specified in the instrument of denunciation it takes effect upon the expiration of such longer period after its deposit with the depositary.

Commentary

The provisions of Article J are essentially based on Article 16 of the 1984 Protocol, although in the wording of paragraph 3 inspiration was also sought in the corresponding provision of the Geneva Agency Convention (Article 35(2)).

(7) Cf. also El Mokhtar BEY and Christian GAVELDA, Problématique juridique du leasing international in Gazette du Palais 1979, 1st sem., 143 at 144.
Article K

1. - This Convention shall be deposited with the Government of Canada.

2. - The Government of Canada shall:

(a) inform all States which have signed or acceded to this Convention and the President of the International Institute for the Unification of Private Law (Unidroit) of:

(i) each new signature or deposit of an instrument of ratification, acceptance, approval or accession, together with the date thereof;

(ii) each declaration made under Articles D, E, F;

(iii) the withdrawal of any declaration made under Article G (4);

(iv) the date of entry into force of this Convention;

(v) the deposit of an instrument of denunciation of this Convention together with the date of its deposit and the date on which it takes effect;

(b) transmit certified true copies of this Convention to all signatory States, to all States acceding to the Convention and to the President of the International Institute for the Unification of Private Law (Unidroit).

Commentary

The functions of depositary of Unidroit Conventions are traditionally exercised by the Government of the State on the territory of which the diplomatic Conference for the adoption of the Convention in question is held. Unlike earlier Unidroit Conventions, the Geneva Agency Convention followed the Vienna Sale Convention in containing no specific article setting out the functions of the depositary. The Unidroit Secretariat however believes that such an article would be useful and has taken as a model for Article K the corresponding provisions of Article 17 of the 1984 Protocol.

Authentic text and witness clause

IN WITNESS WHEREOF the undersigned plenipotentiaries, being duly authorised by their respective Governments, have signed this Convention.

DONE at Ottawa, this .......... day of May, one thousand nine hundred and eighty-eight, in a single original, of which the English and French texts are equally authentic.

Commentary

The general language of this provision follows many precedents, in particular the Geneva Agency Convention. The reference to English and French as the authentic texts of the future Convention reflects the fact that the working languages of Unidroit are English and French and that the authentic texts of Unidroit Conventions have accordingly hitherto traditionally been drawn up in these two languages.
DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION
ON INTERNATIONAL FACTORING DRAWN UP
BY A UNIDROIT COMMITTEE OF GOVERNMENTAL EXPERTS,
WITH EXPLANATORY NOTES
(drawn up by the Unidroit Secretariat)

I. INTRODUCTION

1. - In accordance with a request made by the committee of governmental experts for the
preparation of a draft Convention on certain aspects of international factoring (hereafter
referred to as "the committee") at its first session held in Rome from 22 to 25 April 1985 (Study
LVIII - Doc. 19, paragraph 4), the Unidroit Secretariat prepared a set of draft final provisions
to accompany the draft articles of the Convention as revised by the committee at the afore-
mentioned session which were contained in Study LVIII - Doc. 21. These provisions were to
a large extent based on the corresponding provisions of the 1983 Convention on Agency in the
International Sale of Goods (hereafter referred to as the "Geneva Agency Convention"), the
most recent international Convention to be adopted at a diplomatic Conference under the
auspices of Unidroit. It should however be added that the close relationship between that
of Goods (hereafter referred to as the "Vienna Sale Convention") resulted in certain solutions
being adopted at Geneva with a view to ensuring exact correspondence between the two
Conventions (see Article B, below), which might not necessarily be appropriate for other
Conventions concluded on the basis of Unidroit drafts. The Secretariat has also taken account
of more recent models and in particular the Protocol of 1984 to amend the 1969 International
Convention on Civil Liability for Oil Pollution Damage (hereafter referred to as "the 1984
Protocol").

2. - In conformity with the tradition that the final provisions of Unidroit Conventions are
not the subject of lengthy discussion by the committees of governmental experts responsible
for the preparation of those Conventions, the committee for the most part restricted its
observations to those articles which were in one way or another related to the substantive
provisions of the draft Convention. The text of the final provisions reproduced hereafter takes
account of the observations and suggestions made by members of the committee at its second
and above all its third session.

3. - The announcement by the Canadian Government of its decision to host the diplomatic
Conference for the adoption of the draft Conventions on international factoring and on
international financial leasing in Ottawa in May 1988 has permitted the Secretariat to complete
some of the provisions of Articles A and K and of the Authentic text and witness clause.
II. DRAFT FINAL PROVISIONS CAPABLE OF EMBODIMENT IN THE PROPOSED CONVENTION ON INTERNATIONAL FACTORING

Article A

1. This Convention is open for signature at the concluding meeting of the Diplomatic Conference for the adoption of the Unidroit draft Conventions on international factoring and international financial leasing and will remain open for signature by all States at Ottawa until ......

2. This Convention is subject to ratification, acceptance or approval by States which have signed it.

3. This Convention is open for accession by all States which are not signatory States as from the date it is open for signature.

4. Ratification, acceptance, approval or accession is effected by the deposit of a formal instrument to that effect with the depositary.

Commentary

The provisions of this article are based largely on those of Article 22 of the Geneva Agency Convention which were themselves based on precedents to be found in United Nations Conventions, such as the Vienna Sale Convention, although the language of paragraph 4 departs from that of the Geneva Agency Convention in favour of that of Article 12, paragraph 3 of the 1984 Protocol in view of the introduction of Article K, which is itself based on Article 17 of the 1984 Protocol.

Article B

1. This Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the third instrument of ratification, acceptance, approval or accession.

2. For each State that ratifies, accepts, approves, or accedes to this Convention after the deposit of the third instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.

Commentary

Following Article 99 of the Vienna Sale Convention, Article 33 of the Geneva Agency Convention requires the deposit of ten instruments of ratification, acceptance, approval or accession for its entry into force and furthermore stipulates that such entry into force shall take effect twelve months after the date of deposit of the tenth such instrument.

Article B as originally drafted by the Secretariat involved a return to previous Unidroit practice as exemplified by the 1973 Convention providing a Uniform Law on the Form of an
International Will, Article XI of which provides for the entry into force of that Convention six months after the date of deposit of the fifth instrument of ratification or accession. At the third session of the committee it was however decided to propose to the diplomatic Conference that the number of instruments necessary for the entry into force of the Convention should be further reduced to three, given the limited and technical nature of its contents when compared with such instruments as those dealing with international contracts of sale and related matters.

[Article C]

This Convention does not prevail over any international agreement which has already been or may be entered into and which contains provisions concerning matters governed by this Convention, provided that the supplier, the factor and the debtor have their places of business in States parties to such agreement.]

Commentary

Based on Article 90 of the Vienna Sale Convention and Article 23 of the Geneva Agency Convention, this provision displaces, in certain cases, the application of the prospective Convention in favour of existing or future international agreements containing provisions concerning matters governed by it, for example agreements concluded by States on a regional basis. It would also cover any future Convention intended to supersede that now under preparation unless it were to be decided to include in the present final clauses provisions establishing a revision procedure.

One effect of Article C is to a certain extent to weaken the universal character of the future Convention and it could create an element of uncertainty for the parties. For this reason, it was proposed that Article C would only apply when all three parties have their places of business in States parties to another agreement concerning matters governed by the Convention itself.

On the occasion of both the second and the third sessions of the committee, criticism was levelled against the wording of this article on the ground that the proviso contained in the last three lines could have the effect of displacing the application of another international agreement for the sole reason that one of the parties to the factoring transaction, for example the debtor, did not have his place of business in a State party to that other agreement, a fact which might have been totally irrelevant to the question of the applicability of that instrument in accordance with the provisions governing its scope of application. It was therefore proposed that the last part of the article, beginning with the words “provided that”, should be deleted or at the very least that the place of business of the factor alone should be relevant.

A more radical proposal was directed to the deletion of Article C as a whole. It was in particular argued that unlike other Conventions, such as the Vienna Sale Convention and the 1980 Rome Convention on the Law Applicable to Contractual Obligations whose subject-matter was very broad, the prospective Convention on international factoring sought to regulate certain aspects of highly specific transactions, the application of the provisions of which Convention, it should be recalled, may be excluded by the parties. In these circumstances it was suggested that the lex specialis should prevail, while a further argument in favour of deleting the article was that it would avoid the danger of the so-called “negative conflict of Conventions”, that is to say the situation where two or more international instruments contain pro-
visions yielding precedence to another instrument.\footnote{As regards conventions dealing with conflicts of law, such as the 1980 Rome Convention on the Law Applicable to Contractual Obligations, Article 21 of which provides that: "This Convention shall not prejudice the application of international Conventions to which a Contracting Party is, or becomes a party", the difficulty might be overcome by following the precedent of Article 23 of the Geneva Agency Convention and adding the words "of substantive law" after the word "provisions" in line 2 of Article C.} A number of representatives were however reluctant to accept the proposal for the deletion of Article C without giving the matter further consideration and it was accordingly agreed to submit the provision to the diplomatic Conference in square brackets.

\textit{Article D}

1. - If a Contracting State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may amend its declaration by submitting another declaration at any time.

2. - These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. - If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

4. - If a Contracting State makes no declaration under paragraph 1 of this article, the Convention is to extend to all territorial units of that State.

\textit{Commentary}

In recent years a number of formulae have been employed in international private law Conventions to meet the difficulties sometimes experienced by States with a federal system of government involving a constitutionally guaranteed division of powers among the constituent units of the federation.

The text of Article D follows that of Article 24 of the Geneva Agency Convention and moreover corresponds closely also to the most recent expression of the will of States in this connection, namely Article 26 of the 1985 Hague Convention on the Law Applicable to Contracts for the International Sale of Goods.

\textit{Article E}

1. - Two or more Contracting States which have the same or closely related legal rules on matters governed by this Convention may at any time declare that the Convention is not to apply where the supplier, the factor and the debtor have their places of business in those States. Such declarations may be made jointly or by reciprocal unilateral declarations.
2. - A Contracting State which has the same or closely related legal rules on matters governed by this Convention as one or more non-Contracting States may at any time declare that the Convention is not to apply where the supplier, the factor and the debtor have their places of business in those States.

3. - If a State which is the object of a declaration under the previous paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which the Convention enters into force in respect of the new Contracting State, have the effect of a declaration made under paragraph 1 of this article, provided that the new Contracting State joins in such declaration or makes a reciprocal unilateral declaration.

Commentary

With minor adaptations, this article is based on Article 26 of the Geneva Agency Convention which was itself heavily influenced by the drafting of Article 94 of the Vienna Sale Convention. As with Article C supra, this possibility for Contracting States to restrict the application of the future Convention, which amounts in effect to a reservation clause, could create uncertainty for the parties as to which law would be applicable in a given case, and for this reason it is proposed that paragraphs 1 and 2 of Article E should only operate when all three parties, supplier, factor and debtor, have their places of business in States concerned by the declaration or declarations.

Article F

A Contracting State may declare at the time of signature, ratification, acceptance, approval or accession that it will not be bound by Article 2, paragraph 1(b).

Commentary

Both the Vienna Sale Convention (Article 1(1)(b)) and the Geneva Agency Convention (Article 2(1)(b)) make provision for the application of the Convention not only when the specific objective connecting factors have been satisfied but also when the rules of private international law lead to the application of the law of a Contracting State. These models have been followed in Article 2(1)(b) of the present draft Convention which provides for its application "where both the contract of sale of goods and the factoring contract are governed by the law of a Contracting State".

At both the Vienna and Geneva Conferences however a number of States, especially Socialist States which have enacted special legislation regulating foreign trade relations, called for the possibility to take a reservation in respect of the application of the two Conventions in accordance with the rules of private international law in cases where they would not otherwise be applicable. The text of Article F is based on that of the reservation clauses contained in Article 95 of the Vienna Sale Convention and Article 28 of the Geneva Agency Convention.

Article G

1. - Declarations made under this Convention at the time of signature are subject to confirmation upon ratification, acceptance or approval.
2. - Declarations and confirmations of declarations are to be in writing and to be formally notified to the depositary.

3. - A declaration takes effect simultaneously with the entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral declarations under Article E take effect on the first day of the month following the expiration of six months after the receipt of the latest declaration by the depositary.

4. - Any State which makes a declaration under this Convention may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal is to take effect on the first day of the month following the expiration of six months after the date of the receipt of the notification by the depositary.

5. - A withdrawal of a declaration made under Article E renders inoperative, as from the date on which the withdrawal takes effect, any reciprocal declaration made by another State under that article.

Commentary

Precedents for the provisions of Article G are to be found in many international Conventions, the text of the article itself following word for word Article 31 of the Geneva Agency Convention.

Article H

No reservations are permitted except those expressly authorised in this Convention.

Commentary

The wording of Article H follows that of Article 32 of the Geneva Agency Convention and is intended to prevent States making reservations other than those presently contemplated by Articles D, E and F or any other reservations which may be permitted, for example Article X.

Article I

This Convention applies when receivables assigned pursuant to a factoring contract arise from a contract of sale of goods concluded on or after the date on which the Convention enters into force in respect of the Contracting States referred to in Article 2, paragraph (1)(a), or the Contracting State or States referred to in paragraph 1(b) of that article, provided that:

(a) the factoring contract is concluded on or after that date; or

(b) the parties to the factoring contract have agreed that the Convention shall apply.
Commentary

One of the most difficult problems to be solved in the context of private law Conventions involving tripartite relations is that of determining which transactions will be subject to the provisions of the Convention once the requirements for its entry into force have been met. The position is complicated in this instance by the fact that Article 2, paragraph 1 provides that the Convention will, subject to the introductory wording of the article, apply (a) when the supplier, the debtor and the factor have their places of business in Contracting States or (b) when both the contract of sale of goods and the factoring contract are governed by the law of a Contracting State.

Assuming however that the requirements laid down by Article 2, paragraph 1(a) or (b) have been satisfied, it would still be necessary to determine at which point the "trigger" mechanism operates in respect of a given transaction. Is it for example sufficient if the receivables assigned under an existing factoring contract come into existence on or after the date of the entry into force of the Convention in respect of the State or States concerned, or should the sale contract under which the receivables arise have been concluded on or after the date of such entry into force, or again ought it to be necessary for the factoring contract itself to be concluded on or after that date.

Alternative texts reflecting all three solutions were prepared by the Secretariat and at its third session the committee opted in favour of a combination of the requirements that both the factoring contract pursuant to which the receivables are assigned and the contract of sale of goods which gives rise to those receivables should have been concluded on or after the date on which the Convention enters into force for the State or States referred to in Article 2, paragraph 1. Although the representatives of the factoring associations considered this solution to be generally speaking both equitable and practicable, some disquiet was expressed as to the need for the parties to a factoring contract to have to conclude a new contract subsequent to the entry into force of the Convention so as to render it applicable; it was therefore thought sufficient for them to make an appropriate amendment to an existing contract.

With a view to meeting this concern, the Secretariat has prepared a text for Article I, sub-paragraph (b) of the proviso to which would render the Convention applicable, always provided that the sale contract from which the receivables arise was concluded after the entry into force of the Convention for the State or States referred to in Article 2, paragraph 1, not only when the factoring contract has been concluded on or after that date, but also when the parties to the factoring contract have agreed that the Convention shall apply. While on the one hand the effect of this language is restrictive, in that the Convention would not become applicable simply because for example a minor term of the factoring contract had been amended after the entry into force of the Convention, it would on the other permit its application after that date not only in cases where an amendment to that effect is made to the factoring contract after the entry into force of the Convention, but also if such an amendment were made prior to that date so as to ensure the application of the Convention from the earliest possible time. If such an application were thought to be too extensive, then the language of Article I could be altered so as to restrict it to those cases where the agreement of the parties to the factoring contract that the Convention shall be applicable is stipulated after the entry into force of the Convention.
Article J

1. This Convention may be denounced by any Contracting State at any time after the date on which it enters into force for that State.

2. Denunciation is effected by the deposit of an instrument to that effect with the depositary.

3. A denunciation takes effect on the first day of the month following the expiration of twelve months after the deposit of the instrument of denunciation with the depositary. Where a longer period for the denunciation to take effect is specified in the instrument of denunciation it takes effect upon the expiration of such longer period after its deposit with the depositary.

Commentary

The provisions of Article J are based on Article 16 of the 1984 Protocol and on Article 35, paragraph 2 of the Geneva Agency Convention.

Article K

1. This Convention shall be deposited with the Government of Canada.

2. The Government of Canada shall:

   (a) inform all States which have signed or acceded to this Convention and the President of the International Institute for the Unification of Private Law (Unidroit) of:

      (i) each new signature or deposit of an instrument of ratification, acceptance, approval or accession, together with the date thereof;

      (ii) each declaration made under Articles D, E, F and X;

      (iii) the withdrawal of any declaration made under Article G, paragraph 4;

      (iv) the date of entry into force of this Convention;

      (v) the deposit of an instrument of denunciation of this Convention together with the date of its deposit and the date on which it takes effect;

   (b) transmit certified true copies of this Convention to all signatory States, to all States acceding to the Convention and to the President of the International Institute for the Unification of Private Law (Unidroit).

Commentary

The functions of depositary of Unidroit Conventions are traditionally exercised by the Government of the State on whose territory the diplomatic Conference for the adoption of the Convention in question is held. Unlike earlier Unidroit Conventions, the Geneva Agency Convention followed the Vienna Sale Convention in that it contained no specific article setting out the functions of the depositary. The Secretariat believes however that such an article would
be useful and has taken as a model for Article K the corresponding provisions of Article 17 of the 1984 Protocol.

*Authentic text and witness clause*

IN WITNESS WHEREOF the undersigned plenipotentiaries, being duly authorised by their respective Governments, have signed this Convention.

DONE at Ottawa, this .......... day of May one thousand nine hundred and eighty-eight in a single original, of which the English and French texts are equally authentic.

*Commentary*

The general language of the provision follows many precedents, in particular that of the Geneva Agency Convention. The reference to English and French as the authentic texts of the future Convention reflects the fact that those are the working languages of Unidroit and that the authentic texts of Unidroit Conventions have accordingly hitherto traditionally been drawn up in these two languages.
WORKING GROUP OF TECHNICAL EXPERTS
ON INTERNATIONAL FINANCIAL LEASING
(ROME, 29 FEBRUARY 1988):

REPORT
BY THE UNIDROIT SECRETARIAT

1. - A working group of technical experts on international financial leasing met at the seat of Unidroit in Rome on 29 February 1988. The meeting was opened by Mr R. Monaco, President of Unidroit. Following the adoption of the agenda, Mr R.M. Goode, representing the United Kingdom Government, was elected chairman of the working group on a proposal by Mr A.H.E. Popp, representing the Canadian Government. Mr Goode had been deputy chairman of the Unidroit committee of governmental experts that had drawn up the draft Convention on international financial leasing that was to be reviewed at the diplomatic Conference being hosted by the Canadian Authorities in Ottawa in May 1988. The meeting was attended by the representatives of three Unidroit member Governments,\(^1\) two intergovernmental organisations\(^2\) and five special invitees.\(^3\)

2. - The working group was seized of the following materials:

- Draft Convention on international financial leasing as adopted by a Unidroit committee of governmental experts on 30 April 1987 with explanatory report prepared by the Unidroit Secretariat (Study LIX - Doc. 48);

- Note by the Unidroit Secretariat (WP1);

- Comments by the Government of the Federal Republic of Germany (WP2);

- Comments by Mr Ronald C.C. Cuming, Professor of Law in the University of Saskatchewan (WP3);

- Comments by Dr M. Milde, Director, Legal Bureau, International Civil Aviation Organization (I.C.A.O.) (WP4);

- Report of an international working group set up by the Executive Council of the Comité Maritime International (WP5).

3. - A preliminary point clarified by the working group concerned the reference at page 3 of the aforementioned Note by the Unidroit Secretariat to “a redraft of Article 5(2), (3) and (4) [essayed by] representatives of the I.M.O. Secretariat and of the Unidroit Secretariat”. Any inference of I.M.O. co-authorship of this redraft that might be drawn from this statement was

\(^1\) Canada, France, United Kingdom.
\(^3\) Representing the International Law Association, the Italian Ministry of Transport and Alitalia - Linee Aeree Italiane S.p.A.
based on a misunderstanding. All that had in fact happened was that in the course of preparing this redraft a representative of the Unidroit Secretariat had had occasion to hold an informal discussion with a representative of the I.M.O. Secretariat during the third session of the Joint U.N.C.T.A.D./I.M.O. Intergovernmental Group of Experts on Maritime Liens and Mortgages and Related Subjects held in Geneva in November/December 1987 during which certain ideas were put forward. However, there was no formal I.M.O. input as such into the shaping of the redraft, the views put forward by the representative of the I.M.O. Secretariat on that occasion having been proffered in a purely personal capacity, and responsibility for the redraft remained entirely that of the Unidroit Secretariat.

4. - The Chairman prefaced discussion of the specific technical question referred to the working group by the Unidroit committee of governmental experts for the preparation of a draft Convention on international financial leasing at its final session, held in Rome in April 1987, to wit the viability of the solution proposed by that committee in Article 5(3)(a) of the draft Convention as adopted at that session, by setting this question in the general context of Article 5 of the draft. The prospective Convention was designed to facilitate cross-border financial leasing in a number of ways one of which was to establish that the lessor’s real rights in the leased equipment would be upheld as against the lessee’s trustee in bankruptcy and unsecured creditors of the lessee, including creditors who under some judicial process levied attachment or execution against the leased equipment, for example where they had an unsatisfied judgment debt against the lessee (Article 5 (1)). This limited priority rule apart, Article 5 did not seek to regulate the whole complex question of priorities as between competing real rights. This was brought out by Article 5 (4) indicating that all questions of priority as between the lessor and a lien creditor or secured creditor of the lessee are left outside the ambit of Article 5, to be regulated in accordance with the applicable law. Specific aspects of the question of priorities between a lessor and certain classes of secured creditor were already regulated by other international agreements, in particular those Conventions, both in existence and under preparation, dealing with liens and mortgages in ships and aircraft. Article 5(4) was thus in particular designed to indicate that Article 5 was in no way intended to interfere with the operation of such other international agreements.

5. - The technical question that had been referred to the working group arose out of the application of the rule contained in Article 5(2). In recognition of the fact that there were some States, albeit only a small number, with public notice systems already in place for the type of leasing transaction addressed in the draft Convention, this provision added a rider to the general rule stating the enforceability of the lessor’s real rights in the equipment contained in Article 5 (1). It provided that where under the applicable law the enforceability of the lessor’s real rights as against the lessee’s trustee in bankruptcy and that class of unsecured creditor of the lessee specified in Article 5(1) was subject to the lessor’s compliance with rules as to public notice, then those rights should only be valid against the aforementioned parties under the prospective Convention where the lessor had complied with such a public notice requirement. It was when the Unidroit governmental experts came to defining the applicable law for the purposes of this provision that its problems really began. The diversity of the equipment covered by the draft Convention meant that no one connecting factor would be adequate for this purpose. There was no problem in identifying the law to be looked to for equipment of a kind normally used in only one State: for this class of equipment it was sufficient to follow the conflicts of law rule traditionally employed in matters of title and proprietary rights, that is to apply the lex rei sitae
(Article 5(3)(c)). The obvious shortcomings of this rule from the point of view of legal certainty for equipment without a fixed situs, that is of a kind normally moving from one State to another in the course of its use, led the governmental experts to prefer the lessee's principal place of business as the appropriate connecting factor for this class of equipment (Article 5(3)(b)).

6. - The Unidroit governmental experts were nevertheless anxious to avoid creating any inference of a double or additional registration requirement under this rule for that special class of "equipment" covered by the draft Convention, such as ships and aircraft, which tend to be subject to registration by their very nature and independently of being supplied under a leasing transaction, whether under the terms of an international agreement or under national law. For this class of equipment the most appropriate law to look to for the purposes of Article 5(2) in the view of the Unidroit governmental experts was the law of the State where the leased asset was registered. This view was reflected in Article 5(3)(a). This law particularly commended itself to the governmental experts as being, in much the same way as the law of the flag, the type of law that tended to be resorted to in international agreements for needs of this ilk. In proposing this solution the committee was, however, only too aware of its limited technical expertise in matters of registration and of the complexities inherent in the subject, in particular the widely differing purposes for which registration may be required and the correspondingly wide range of registration systems in place. Not being sure whether the solution it had come up with in Article 5(3)(a) would be viable in practice, the governmental experts accordingly recommended that the Unidroit Secretariat should seek the advice of technical experts in this field and convene a meeting of such experts in advance of the diplomatic Conference to examine this question.

7. - In addition to the specific issue of the viability of Article 5(3)(a), the Unidroit Secretariat's consultations with technical experts in advance of the meeting of the working group had revealed a number of related points clearly requiring clarification. The first of these concerned the precise nature of the registration had in mind in Article 5(3)(a). There was agreement within the working group that this was not registration of an individual transaction but rather registration against a particular item, identified by a serial number, name or other identifying mark, typically a nationality registration.

8. - Another point which it was agreed, required clarification concerned the precise relationship between the type of equipment envisaged in Article 5(3)(a) and that contemplated by Article 5(3)(b). In particular, the language of Article 5(3)(b) needed tightening up in order to explain more clearly what was meant by equipment that was "mobile" and "normally used in more than one State" but was not caught by the terms of Article 5(3)(a). The working group was agreed that when Article 5(3)(b) spoke of equipment that was "mobile" and was "normally used in more than one State" it was not concerned with whether the item of equipment in question actually moved from one State to another but whether it was of a class of equipment that normally moved from State to State.

9. - Another shortcoming in the drafting of Article 5 that had come to light during the Unidroit Secretariat's sounding of technical experts concerned Article 5(4) of the text adopted in April 1987. It was felt that this provision had not been drafted in sufficiently comprehensive terms to encompass all the various types of maritime and air claim that would need to be safeguarded. The working group agreed that it needed to be expanded so as to make it clear that it covered not just rights in the nature of liens or security interests but rather the general range of real rights in ships and aircraft, for example rights of arrest, and that the limited priority
accorded the lessor under Article 5(1) was intended to be consistent with, and was accordingly subordinate to the provisions of any other international agreement governing real rights in aircraft and ships, for instance the 1948 Geneva Convention on the International Recognition of Rights in Aircraft.

10. - In essence the technical question referred to the working group was seen as having two limbs:

(1) Was the law of the State of registration capable of a clear meaning as the applicable law for “ships, aircraft, vehicles or other equipment subject to registration pursuant to the law of a State” under Article 5(3)(a)? In particular, was there only one such State at any given time or was there a possibility that the leased asset might be registered in more than one State simultaneously? Article 5(3)(a) worked on the assumption that there was only one State of registration at any one time. Clearly if this basic assumption were fallacious, defining the applicable law as the law of the State of registration would create uncertainty.

(2) Was the State of registration easily ascertainable by third parties? The lessee’s creditors had to be able to know where to make a search in order to find out whether equipment in the lessee’s possession was owned by a lessor or was subject to a proprietary interest in favour of a lessor.

11. - The working group tackled this question in two stages, dealing first with ships and secondly with aircraft, vehicles or other equipment subject to registration. It found the reference in Article 5(3)(a) to the State of registration inadequate for ships in that it was possible for a ship that had been bare-boat chartered (bare-boat charters sometimes involved a financial lease) to be registered in two States at the same time and either for both registrations to be operative at the same time or where the original registration had become dormant upon the vessel being registered in the State of the charterer for it still to be considered as being registered in the original State of registration as well. In relation to the problem of ships in the context of Article 5(3)(a) the working group came to the conclusion that the most appropriate solution at a technical level would in the circumstances be to refer to the law of the flag State. The law of the flag State had a certain appeal in an international instrument given its use in the Law of the Sea Convention and in other texts. While such a solution presented some of the same drawbacks that had been inherent in the “law of the State of registration” solution, namely the fact that the flag State might not necessarily have any direct connection with the financial leasing arrangement and therefore with the place where third parties could normally be expected to make a search regarding title to, or proprietary interests in the ship, it was nevertheless a fact that there could only be one flag State at any given time which at least had the merit of certainty. Moreover, the fact that the law of the particular flag State on the question of public notice for ships might in some cases prove to be minimal was not seen as necessarily constituting a drawback to this solution as the aim in Article 5(3)(a) was simply to identify, admittedly in a rather arbitrary fashion, a single jurisdiction whose public notice requirements, if any, were to apply so that the question of whether that jurisdiction did in fact have any public notice rules governing financial leasing was not in itself of importance for this purpose.

12. - While the working group’s technical solution to the problem raised by ships in the context of Article 5(3)(a) was therefore to refer to the law of the flag State, there was also some expression by individual members of the group of the view that there might be something to be said for looking at certain other possible options as a solution. Those canvassed were
essentially three in number. First, one member of the working group felt that there might be a case for not defining the applicable law in relation to ships in Article 5(3) so that, in the event of a dispute, the matter would fall to be resolved in accordance with the law applicable under the rules of private international law of the forum, although it was recognised that this would encourage forum shopping. Secondly, another member of the group canvassed the idea that the application of Article 5(2) should be excluded in relation to ships. This would, however, have the effect of overriding any public notice rules that might otherwise have been applicable and give the lessor priority against the parties specified in Article 5(1) without its having to comply with such public notice rules. The other possibility canvassed consisted in excluding Article 5 altogether in relation to ships, which would leave any dispute arising in respect of such leased assets between a lessor and unsecured creditors of the lessee to be resolved in accordance with the law applicable under the rules of private international law of the forum.

13. - The factors which had led the working group to conclude as to the unsuitability of the law of the State of registration as the applicable law for ships in the context of Article 5(3) did not appear to have the same force in relation to aircraft. In particular, under the 1944 Chicago Convention on International Civil Aviation there was no possibility of an aircraft being registered in more than one State at any one time. Moreover, the law of the State of registration particularly commended itself for aircraft in that the 1948 Geneva Convention on the International Recognition of Rights in Aircraft provided that rights in aircraft should be recorded on the register of the State of registration. On the other hand, the absence of any necessary direct connection between the State of registration and the financial leasing arrangement already noted in the context of ships was also apparent in the case of aircraft, particularly when the aircraft was sub-leased and its registration changed. However, set against this disadvantage was the fact that the State of registration of an aircraft was a quantity that was both known and certain, as well as being probably the place where any third party making a search regarding title to, or proprietary rights in the aircraft could be expected to look.

14. - In one paper laid before the working group (WP3) the author, Mr Ronald C.C. Cuming, Professor of Law in the University of Saskatchewan, had voiced his concern at referring to the State of registration for the purpose of defining the applicable law in relation to aircraft in Article 5(3) on the ground that the aircraft nationality register in Canada was not a public document and as such was not open to public inspection. The working group specified that Article 5(3) was not concerned with the public character or otherwise of the relevant nationality registration system. Its sole purpose in looking to a given aircraft nationality register was to identify the State whose public notice requirements, if any, had to be complied with by the lessor. If by recourse to this system the applicable law, that is the law of the State where the particular aircraft was registered, turned out to be the law of a State which had public notice requirements, then the aircraft register of that State was by definition open to public inspection.

15. - A subsidiary question which exercised the working group concerned how to classify an aircraft engine for the purposes of the definition of the applicable law in Article 5(3), that is whether it should be treated as an integral part of the aircraft - and as such subject to Article 5(3)(a) of the April 1987 text - or as an example of "all other [mobile] equipment [normally used in more than one State]" - and as such subject to Article 5(3)(b). The point was made that aircraft engines were often the subject of separate leasing transactions. It was the opinion of the working group that the word "aircraft" in the sense given to it in Article 5(3)(a) was intended to cover the complete aircraft, that is the aircraft complete with its engines and other component parts
for the time being attached to the aircraft, whereas an aircraft engine, in the same way as other components of an aircraft, when at the time not attached to the aircraft were to be treated as "all other [mobile] equipment [normally used in more than one State]", in relation to which the applicable law would accordingly be the law of the State where the lessee had its principal place of business. Since the essential purpose of Article 5 was to deal with disputes arising in respect of the leased asset as between the lessor and the lessee’s unsecured creditors, including an execution creditor, it would accordingly be necessary in each case to determine whether the conflict related to the engine as an integral part of the aircraft for the time being attached thereto or to the engine as a component part of the aircraft for the time being not attached thereto. There was agreement within the working group that this was a matter that could be adequately handled in the explanatory report on the prospective Convention.

16. - Following the working group’s deliberations, a small drafting group, made up of elements of the delegations of Canada, France and the United Kingdom, met to give effect to the conclusions reached by the working group. The results of their redrafting exercise are set out in the Appendix to this report.

17. - The only amendment effected in paragraph 1 of Article 5 was essentially of a drafting nature. Spelling out what was contemplated by the term “trustee in bankruptcy”, hitherto employed in this provision in a generic sense, was felt to enhance the precision of the ambit of this provision.

18. - One minor drafting amendment to paragraph 2 concerned only the English text. So as to bring the English text more into line with the French text and to make its meaning more clear, the final words of this provision were changed from “only where they are valid according to such rules” to “only if there has been compliance with such rules”.

19. - So as to give effect to the different conclusions reached by the working group as to the technical viability of the solution adopted in Article 5(3) (a) in April 1987 for ships, on the one hand, and for aircraft, vehicles and other equipment subject to what would typically be a nationality registration, on the other hand, the drafting group split up sub-paragraph (a) of paragraph 3 into two sub-paragraphs, (a) and (b). Sub-paragraph (a) reflects the technical solution found by the working group to the technical problem which was the subject of its remit as regards ships, in making the law of the flag State the applicable law for this class of leased asset. Sub-paragraph (b) constitutes the rump of sub-paragraph (a) as adopted in April 1987, making the law of the State of registration the applicable law for those leased assets other than ships encompassed therein. It also reflects the working group’s conclusion as to the desirability of specifying the nature of the registration contemplated in this provision, namely registration “by serial number, name or other identifying mark”. The only amendment proposed to what became sub-paragraph (c) was likewise designed to give effect to the working group’s conclusion as to the desirability of clarifying the fact that the type of equipment encompassed by this provision was not necessarily an item of equipment that normally moved in actual fact from State to State but was of a kind that would normally move from one State to another. The new sub-paragraph (d) did not contain any change.

20. - It proved impossible in the time available to agree on totally parallel English and French texts of paragraph 3. The source of this difficulty lay in the attempt to find a French equivalent of the expression “at the relevant time” employed in the chapeau of the English version of paragraph 3 and defined for the purposes of this paragraph in a second sentence.
thereof. This attempt having proven forlorn and the alternative, to wit to repeat the words “at
the time when the person referred to in paragraph 1 becomes entitled to invoke the rules referred
to in paragraph 2” in each of the four sub-paragraphs of the English version of paragraph 3,
having been adjudged to involve unacceptably inelegant drafting, it was finally agreed to
formulate the two versions differently for the time being. Thus in the English version of
paragraph 3 the expression “at the relevant time” is employed once only, in the chapeau
governing each of the sub-paragraphs of paragraph 3, and is then defined for the purposes of
each of these sub-paragraphs in a new second sentence added onto paragraph 3, whereas in the
French text the relevant time is spelled out at length in identical language in each of the four
sub-paragraphs of paragraph 3. The understanding was that this could be looked at again in
Ottawa on the occasion of the diplomatic Conference.

21. - The new paragraph 4 is designed to preserve the efficacy and therefore the priority (4)
of any other international agreement under which the lessor’s real rights in the equipment
are required to be recognised. The particular international agreement had in mind here is the
1948 Geneva Convention on the International Recognition of Rights in Aircraft. Thus if in a
given case an aircraft lessor might effectively find itself faced with a dual registration
requirement, under the Geneva Convention on the one hand and under Article 5(2) of the
prospective Unidroit Convention on the other, the lessor’s rights under the Geneva Convention
will be preserved even if the lessor has failed to comply with the public notice requirements of
Article 5(2).

22. - The new paragraph 5 represents the drafting group’s efforts to give effect to the
desire expressed by the working group that the contents of paragraph 4 of the 1987 draft should
be expanded so as to make it clear that the class of real rights that needed to be safeguarded under
that paragraph was not limited only to rights in the nature of a lien or a security interest but was
intended to cover the general range of real rights specifically conferred by law, whether national
or international, in relation to ships and aircraft, for example rights of arrest, maritime liens and
mortgages and such special rights as that given under the law of certain States permitting the
detention of an aircraft for non-payment of navigation service charges to the Authorities of the
State where it is detained.

APPENDIX

Article 5

of the draft Convention on international financial leasing
in the redraft proposed to give effect to the conclusions
reached by the working group of technical experts

Article 5

1. - The lessor’s real rights in the equipment shall be valid against the lessee’s trustee in
bankruptcy and creditors, including creditors who have obtained an attachment or execution.

(4) However, cf. also Article C of the draft final provisions (Study LIX - Doc. 49).
"Trustee in bankruptcy" includes a liquidator, administrator or other person appointed to
administer the lessee's estate for the benefit of the general body of creditors.

2. - Where by the applicable law the lessor's real rights in the equipment are valid against
a person referred to in the previous paragraph only on compliance with rules as to public notice,
those rights shall be valid against that person only if there has been compliance with such rules.

3. - For the purposes of the previous paragraph the applicable law is the law of the State
which is at the relevant time:

(a) in the case of a ship, the flag State;

(b) in the case of an aircraft, vehicle or other equipment registered by serial number,
name or other identifying mark pursuant to the law of a State, the State of registration;

(c) in the case of other equipment of a kind normally moving from one State to
another, the State where the lessee has its principal place of business;

(d) in the case of all other equipment, the State where the equipment is situated.

For the purposes of this paragraph the "relevant time" is the time when the person referred
to in paragraph 1 becomes entitled to invoke the rules referred to in paragraph 2.

4. - Paragraph 2 shall not affect the provisions of any other international agreement under
which the lessor's real rights in the equipment are required to be recognised.

5. - This Article shall not affect the rights of any creditor having:

(a) any lien on or security interest in the equipment or any right of arrest to enforce
such lien or security interest;

(b) any other right of arrest, detention or disposition conferred by law specifically in
relation to ships or aircraft.
LIST OF STATES AND ORGANISATIONS REPRESENTED AT 
THE DIPLOMATIC CONFERENCE FOR THE ADOPTION 
OF THE DRAFT UNIDROIT CONVENTIONS 
ON INTERNATIONAL FACTORING AND 
INTERNATIONAL FINANCIAL LEASING 
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PART II

COMMITTEE OF THE WHOLE

Basic papers

Comments on the draft Unidroit Convention on international financial leasing by:

Governments (Japan, Pakistan, South Africa, Spain, Switzerland, United States of America) .................................................................................. 151


Comments on the draft Unidroit Convention on international factoring by:

Governments (Japan, South Africa, Spain, United States of America) ............................................................................................................ 186

International Organisations (Hague Conference on Private International Law) ......................................................................................... 200

Working papers on the draft Unidroit Convention on international financial leasing submitted by:

United Kingdom .................................................................................. 204
Sweden ............................................................................................... 204
Finland ............................................................................................... 205
United States of America .................................................................... 206
Comité Maritime International ............................................................... 207
People’s Republic of China ................................................................. 210
Finland ............................................................................................... 212
United States of America .................................................................... 213
Sweden ............................................................................................... 218
United Kingdom .................................................................................. 218
United States of America .................................................................... 220
Australia ............................................................................................. 226
Sweden ............................................................................................... 226
United Kingdom .................................................................................. 228
Sweden ............................................................................................... 229

147
<table>
<thead>
<tr>
<th>Country/Group</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canada, United Kingdom and United States of America</td>
<td>230</td>
</tr>
<tr>
<td>Federal Republic of Germany</td>
<td>231</td>
</tr>
<tr>
<td>The Chairman</td>
<td>231</td>
</tr>
<tr>
<td>Informal Working Group on the proposal by the Comité Maritime International</td>
<td>232</td>
</tr>
<tr>
<td>Article 5(3)(c) in relation to ships</td>
<td></td>
</tr>
<tr>
<td>Informal Working Group on Article 14</td>
<td>233</td>
</tr>
<tr>
<td>Colombia</td>
<td>234</td>
</tr>
<tr>
<td>Philippines</td>
<td>234</td>
</tr>
<tr>
<td>Colombia</td>
<td>235</td>
</tr>
<tr>
<td>Sweden</td>
<td>236</td>
</tr>
<tr>
<td>France and Mexico</td>
<td>237</td>
</tr>
<tr>
<td>Canada</td>
<td>237</td>
</tr>
<tr>
<td>Working Group on Article 7(2)</td>
<td>238</td>
</tr>
<tr>
<td>Sweden</td>
<td>239</td>
</tr>
<tr>
<td>Federal Republic of Germany</td>
<td>240</td>
</tr>
<tr>
<td>Canada</td>
<td>240</td>
</tr>
<tr>
<td>Sweden</td>
<td>241</td>
</tr>
<tr>
<td>The Chairman of the Drafting Committee</td>
<td>243</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>244</td>
</tr>
<tr>
<td>Federal Republic of Germany</td>
<td>245</td>
</tr>
</tbody>
</table>

*Working papers on the draft Unidroit Convention on international factoring submitted by:*

<table>
<thead>
<tr>
<th>Country/Group</th>
<th>Page</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cuba</td>
<td>245</td>
</tr>
<tr>
<td>Italy</td>
<td>247</td>
</tr>
<tr>
<td>Sweden</td>
<td>247</td>
</tr>
<tr>
<td>Finland</td>
<td>248</td>
</tr>
<tr>
<td>The Secretariat</td>
<td>249</td>
</tr>
<tr>
<td>Sweden</td>
<td>249</td>
</tr>
<tr>
<td>Federal Republic of Germany</td>
<td>250</td>
</tr>
<tr>
<td>Italy</td>
<td>250</td>
</tr>
<tr>
<td>France, Mexico and Philippines</td>
<td>251</td>
</tr>
<tr>
<td>Sweden</td>
<td>251</td>
</tr>
<tr>
<td>Czechoslovakia</td>
<td>252</td>
</tr>
<tr>
<td>Working Group on Article 1(1)(c) and (3)</td>
<td>253</td>
</tr>
<tr>
<td>Working Group on Article 5</td>
<td>253</td>
</tr>
<tr>
<td>The Chairman of the Drafting Committee</td>
<td>254</td>
</tr>
</tbody>
</table>
Texts submitted by the Drafting Committee on the
draft Unidroit Convention on international
financial leasing:

Text of the Preamble and Chapters I and II ........................................ 255

Texts submitted by the Drafting Committee on the
draft Unidroit Convention on international
factoring:

Preliminary text of Chapters I and II ........................................ 261
Preliminary text of the Preamble and
Articles 6 and X ................................................................. 264
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Comments on the draft Convention by Governments
(Japan, Spain and the United States of America)

I. - GENERAL OBSERVATIONS

United States of America

The current draft (hereinafter referred to as the “1987 Draft”) Convention on international financial leasing (UNIDROIT Study LIX - Doc. 48) has been reviewed and considered by various interested parties in the United States under the auspices of the Department of State. We are optimistic that a Convention will be adopted that will be acceptable to many countries and contribute to the growth of international trade and the development of private international law.

We are concerned about the substance of three provisions contained in the 1987 Draft. These provisions are discussed below. Each is in square brackets, reflecting the failure of the committee of governmental experts (hereinafter referred to as “the committee”) to reach a consensus view at its final meeting.

We remain concerned about several less fundamental aspects of the 1987 Draft that are not discussed below. Many of these concerns are explained in our Observations and Proposals (UNIDROIT Study LIX - Doc. 36) submitted at the committee’s final meeting.

We may wish to submit separately some important proposed drafting changes to the 1987 Draft. Unlike the provisions discussed below, however, such proposals will not make material changes in substance.

II. - COMMENTS ON THE BODY OF THE DRAFT CONVENTION
(STUDY LIX - DOC. 48)

Re Articles 1 (1)(a) and 4

Japan

Because of the ambiguity of the phrase “on terms approved by, another party (the lessee)” in sub-paragraph (a) of paragraph 1, the sphere of application of this Convention is ambiguous. In other words, a question arises as to whether the lessee’s approval is required with respect to all terms of the supply agreement in order that a financial leasing transaction be covered by this Convention. In financial leasing transactions the lessor does not request the lessee to approve the terms for payment in the supply agreement since the lessee has no interest in them. Therefore, if the lessee’s approval should be required for all terms, including for payment, of
the supply agreement, the sphere of application of this Convention would become extremely limited.

On the other hand, if the lessee's approval is not necessarily required for all terms of the supply agreement, the following questions have to be answered:

(1) Are there any essential terms of the supply agreement which should be approved by the lessee without exception? If so, which terms are they?

(2) Is Article 4 applicable to a case where one or more terms of the supply agreement not approved by the lessee are modified? That is, is the lessee's consent necessary for a modification of terms?

Re Article 1 (3)

Spain

Proposed text:

"This Convention applies solely to transactions in which the equipment is to be used by the lessee primarily for business or professional purposes."

The aim of this proposed change is to adopt a positive criterion for the purpose of dealing with this question, which would moreover be in line with the definition traditionally given of the term "business or professional".

Re Article 2 (1)

Spain

The introductory words of this provision, that is the words coming immediately before sub-paragraphs (a) and (b) need to be clarified.

In the form in which the opening words of this provision are drafted in the English text, it is unclear whether the requirement for the application of the prospective Convention laid down therein must be completed by one of the other requirements specified in sub-paragraphs (a) and (b) or whether it suffices by itself where neither of the other two requirements for the application of the Convention is met.

The best way of removing this uncertainty might be to lay down the rule in three paragraphs, subject to the introductory words of this provision sufficing by themselves to bring about the application of the Convention without either of the requirements set forth in sub-paragraphs (a) and (b) of paragraph 1 being met.

Re Article 3

Spain

This article could be relocated and re-numbered Article 2 rather than Article 3 in order to improve the coherence of the definition of financial leasing. The purchase option customarily incorporated in this type of transaction is an optional ingredient of the definition. Accordingly, a provision relating to the purchase option should come after those provisions relating to the
definition of the transaction instead of being separated therefrom by the rule concerning the geographic sphere of application of the Convention contained in Article 2.

Re Article 5 (3)(a)

Spain

The criterion adopted would not make much sense, in particular in the case of ships flying a flag of convenience which might lead to the application of rules unknown to the lessor, the lessee and the supplier.

The Spanish Government would propose that the connecting factor in this provision should be “the law of the State where the lessor has its principal place of business”, the lessor being the holder of the real rights in the equipment which may be enforced against the lessee’s creditors and which are protected under the Convention in accordance with the provisions of Article 5 (1).

It is clearly with its own law that the lessor, who is entitled to the separatio ex iure domini, is going to be most familiar. Alternatively, one might consider employing the criterion of the “law of the State where the lessee has its principal place of business.”

Re Article 5 (3)(b)

Spain

The adjective “mobile” at present inside square brackets should be deleted.

The square brackets around the words “normally used in more than one State” should be deleted. Our comments regarding Article 5 (3)(a) also hold good for the connecting factor selected in this sub-paragraph.

Re Article 5 (3)(b) and (c)

Japan

While under paragraph 3 of Article 5 equipment is divided into three different categories for the purpose of determining the applicable law referred to in paragraph 2 of this article, the concept of “[mobile] equipment” is not yet established. As a result, a line of demarcation between the second category of equipment referred to in paragraph 3(b) of this article and the third category of equipment referred to in paragraph 3(c) of this article is obscure and may lead to confusion in the application of paragraph 3 of this article.

Re Article 7 (1)(a) and (b)

Japan

As regards the words “[e]xcept as otherwise provided by this Convention” in paragraph 1(a) of Article 7, reference should be made to specific provisions (paragraph 2 of this article and Article 10) in order to avoid ambiguities in interpretation of those words.
As regards the words "[e]xcept as otherwise provided ... by the leasing agreement" in paragraph 1(a) of Article 7, it is obvious under paragraph 2 of Article 14 that parties to the leasing agreement may derogate from paragraph 1(a) of Article 7. It is not necessary, therefore, to retain the above-mentioned words in paragraph 1(a) of Article 7. Consequently, the words "or the leasing agreement" should be deleted from paragraph 1(a) of Article 7.

While sub-paragraphs (a) and (b) of paragraph 1 of Article 7 were redrafted by the committee at its third session, paragraph 24 of the summary report of that session explains that the above modification is not intended to alter its substance. In order to avoid substantive change, however, the provision after the words "in respect of the equipment", which corresponds to the former sub-paragraph (b), should also have been added in the present sub-paragraph (b), not only in the present sub-paragraph (a).

Therefore, the provision after the words "in respect of the equipment" should be deleted from the present sub-paragraph (a) and, as a new sub-paragraph (c), the following provision, the meaning of which is similar to the former sub-paragraph (b), should be added (the present sub-paragraph (c) would be moved to a new sub-paragraph (d)):

"The above provisions shall not apply to the extent that the lessor has intervened in the selection of the supplier or the specifications of the equipment."

Incidentally, this new sub-paragraph (c) has the advantage of making clear that the question as to under what conditions the lessor will be liable in the event of intervention in the selection of the supplier or the specifications of the equipment is left to be resolved by the applicable law.

Re Article 7 (2) and (3)

Japan

As regards paragraph 2 of Article 7, Alternative I would impose upon the lessor an excessive liability - for example, the lessor would be liable for a disturbance of the lessee’s quiet possession even when caused by Government activities such as expropriation or by force majeure. It would be incompatible with the lessor’s position in financial leasing transactions and furthermore be contrary to the purpose of this Convention as set forth in the Preamble. (The fourth clause thereof states that the rules of law governing the traditional contract of hire need to be adapted to the distinctive triangular relationships created by the financial leasing transaction.) Therefore, Alternative II should be adopted.

Spain

Of the two alternatives proposed, the Spanish Government would prefer Alternative II, in view of its greater clarity and its formulation in the positive.

It is the lessor alone under this provision who warrants, or more correctly is under a duty to ensure the lessee’s quiet possession of the equipment leased. This provision contains no express reference to the supplier whose acts or behaviour may, however, interfere with the lessee’s rights. We accordingly propose that the supplier should also be under a duty under the prospective Convention to ensure the lessee’s quiet possession under this provision, in particular in view of the fact that the supplier is expressly referred to in Article 1 (2)(a) and (b)
of the draft Convention and is selected by the lessee, not that the possibility of the lessor exercising some influence over this choice is totally excluded (cf. the adverb "primarily" in Article 1 (2)(a)). At the end of Article 7 (2) we would therefore propose adding the words "or supplier".

Paragraph 3 of Article 7 should be retained and the square brackets around it accordingly removed. The amendment proposed to Article 7 (2), namely the addition of the words "or supplier", should also be made in this paragraph.

**United States of America**

Alternative I of Article 7 (2) is unacceptable to us and is likely to be unacceptable to many other countries as well. It states a rule which is unfair and wholly inconsistent with prevailing practice and custom in financial leasing transactions. We explained this point in some detail in our Observations and Proposals (UNIDROIT Study LIX - Doc. 36) submitted at the committee’s final meeting.

Alternative I requires the lessor to bear responsibility for all disturbances of the lessee’s quiet possession, saving only disturbances "derived from any act or omission of the lessee." This means, for example, that the lessor would be liable to the lessee for a disturbance arising out of a defect in title conveyed by the supplier. Yet it is the lessee who selects the supplier and who provides the specifications for the equipment. Indeed, were the lessee to rely "primarily on the skill and judgment of the lessor" with respect to these matters the transaction would be outside of the scope of the Convention (Article 1, paragraph 2(b)). If the lessor does intervene "in the selection of the supplier or the specifications of the equipment," then the lessor may be exposed to liability to the lessee to that extent (Article 7, paragraph 1(a)). The rule embodied by Alternative I, then, imposes risks on the lessor that the lessor cannot protect against except by refusing to enter into a transaction or by charging an additional fee to the lessee. In effect, Alternative I dictates that the lessor be an insurer of title for the lessee’s benefit.

The costs associated with imposing additional risks on finance lessors, pursuant to Alternative I, in all likelihood would be passed on to finance lessees. Our investigation indicates that lessees (in both developing countries and industrialised countries) do not desire to pay lessors to bear risks of disturbances of quiet possession caused by suppliers selected by lessees. Therefore, in financial leasing transactions the universal practice has developed whereby the parties agree that lessors will be responsible only for disturbances caused by lessor acts and omissions. This is the rule provided by paragraph 2 of Alternative II. Financial lessors and lessees have recognised that both parties are investing in the equipment and that the principal function of financial lessors is to provide funds for the purchase of the equipment from suppliers. The lessee invests in the right to use the equipment during the lease term and the lessor invests in the residual value of the equipment. Lessees do not seek out financial lessors in order to obtain surety bonds against disturbances in quiet possession. When a prospective user of equipment borrows money in order to purchase the equipment, it will not be relieved of its repayment obligation if there is a defect in title to the equipment. The result should be no different in the case of financial lessors. That is precisely why Article 9, paragraph 1 provides that the supplier’s duties under the supply contract also run to the lessee. The application of Alternative I would force lessees to buy unwanted protection from lessors. There is no reason to suspect that lessees are less able to protect themselves against risks in financial leasing.
transactions than in typical sales transactions.

Even if the parties would be free to derogate from any quiet possession rule imposed by the Convention, as we urge below, we would continue to maintain that Alternative I is unacceptable. It would send false and destructive signals to the courts which might be called upon to construe it as well as other provisions of the Convention. Surely the parties to financial leasing transactions will continue to agree to limit the responsibility of financial lessors for disruptions of quiet possession. It would be unfortunate indeed if the Convention, by adopting Alternative I, were to indicate that customary practice is inconsistent with its rules. Experience with financial leasing has shown that many courts have found it difficult to shed their traditional conceptions about the relationship between a lessor and a lessee. Therefore, many conventional aspects of financial leasing have appeared to such courts as unfair or one-sided. It is important that the Convention demonstrate that typical provisions of financial leasing transactions are fair, reasonable and merely reflect the very special division of rights and responsibilities peculiar to these transactions.

Some participants at the committee's final meeting expressed the view that the obligations imposed on lessors by Alternative I derive from the lessor's position as the "owner" of the equipment. While this view may be well-intentioned, we submit that the effect of applying Alternative I would be inconsistent with the spirit and letter of the Preamble. The Preamble recognises "the importance of removing certain legal impediments to the international financial leasing of equipment." It recognises that existing law needs "to be adapted to the distinctive triangular relationships created by the financial leasing transaction." The traditional rules concerning responsibilities of a lessor for a lessee's quiet possession represent precisely the sort of impediment which the Convention should remove. We do not understand how imposing a rule contrary to the practice and custom of financial leasing would adapt the law to financial leasing or remove existing impediments.

Alternative II is the better choice. Paragraph 3 of Alternative II was added at the committee's final meeting as a possible compromise. While we could support paragraph 3 if it were essential to the success of the Convention, we would do so reluctantly. Paragraph 3 also is inconsistent with the Preamble. Most of the proponents of Alternative I argued that the same or a similar rule now obtains in their respective States under existing law. If that is the case, then paragraph 3 would leave that law as it is. In our view the Convention should not attempt to restate or codify all aspects of the law relating to leasing transactions. Rather, it should address only those aspects which require a special rule for financial leasing transactions. Therefore, we submit a third alternative. If the diplomatic Conference favours the imposition of a rule which is contrary to existing practice and custom (Alternative I), and does not favour paragraph 2 of Alternative II, standing alone without paragraph 3, then we believe that the Convention should state no rule at all with respect to quiet possession. Presumably, the proponents of Alternative I would be satisfied to rely on existing law which, they have argued, is substantially similar to Alternative I.

Re Article 10 (1)(b)

Japan

Paragraph 1 of Article 10 provides that the lessor shall have the right, as against the lessee,
to reject the equipment in the cases specified in sub-paras (a) and (b). The provisions of paragraphs 2 to 4 of Article 10, however, only cover the case specified in sub-para (a), on a strict interpretation of such provisions. This means that there are no provisions governing the method and effect of exercising the right to reject the equipment in the case specified in sub-para (b); therefore, it is necessary to add a provision to fill this gap in Article 10.

Re Article 10 (3)

Japan

Paragraph 3 of Article 10 may prevent the spread of financial leasing transactions since the time is not clearly defined when the lessee shall lose its right to reject the equipment. It is further pointed out that paragraph 3 of Article 10 is in contradiction with the business practice in which once the lessee has delivered a “Lease Supplement (Acceptance Certificate)” to the lessor, the lessee cannot claim any longer that the equipment fails to conform to the terms of the supply agreement. Paragraph 3 of Article 10 should be, therefore, amended as follows:

“The lessee shall lose its right to reject the equipment when the lessee has informed the lessor of its acceptance.”

Re Article 10 (4)

Spain

A provision should be added to the last sentence making it clear that the lessee’s duty laid down there only arises if it has derived benefit from the equipment rejected and not in every case. Such a provision might read as follows:

“, if it has actually derived benefit therefrom.”

Re Article 11

Japan

Article 11 needs to be reviewed as a whole because of the following problems:

*Paragraph 1 of Article 11 seems to be misleading; there is a possibility that in accordance with this paragraph it might be misunderstood that claims for damages other than those for rentals and interest may not be admitted - in other words, there is a possibility of misunderstanding that this paragraph would provide all the remedies for the lessor in the event of default by the lessee. The reason for this is that although it is only natural in the leasing agreement for the lessor to demand payment of rentals from the lessee (see paragraph 1(b) of Article 1), this paragraph takes the trouble to provide this self-evident clause.

The relationship between the clause which begins with “except” in paragraph 2(b) of Article 11 and the clause which begins with “unless” in paragraph 3 of this Article is not clear. If, pursuant to paragraph 2 of Article 14, the parties to the leasing agreement agree with each other that the lessor has no duty to mitigate loss in their relations, is such an agreement taken into consideration when determining whether the agreed sum as compensation (liquidated damages) is disproportionate to the compensation provided for under paragraph 2(b) of Article 11?
Paragraph 3 of Article 11 provides that a provision concerning the sum agreed as compensation shall not be enforceable if the sum agreed is disproportionate to the compensation provided for under paragraph 2(b) of this article; in reality, however, the former is rarely equal to the latter. As a result, it would not make much sense to provide an agreed sum. Accordingly it seems at least necessary that the word “substantially” should be added before the word “disproportionate” following the example of Article 8 of UNCITRAL’s Uniform Rules on Contract Clauses for an Agreed Sum due upon Failure of Performance.

While paragraph 2 of Article 11 provides that the right to terminate the leasing agreement may be exercised only when the lessee’s default is substantial, paragraph 5 of the same article prescribes that a term of the leasing agreement to accelerate payment of the rentals may be enforceable even when the lessee’s default is not substantial. However, it is questionable to make such a distinction between both remedies.

Re Article 11 (2)

Spain

The qualification of the lessee’s default by the word “substantial”, at least in the English version, is not very clear and may well give rise to divergent interpretations by national courts.

One way of avoiding this result might be to quantify the default, at least by reference to a time factor. To achieve this purpose the words “[w]here the lessee’s default is substantial,” could be replaced by the words “[i]n the event of the lessee’s default in the payment of two (or three) rentals” or else by the words “[i]n the event of the lessee’s default in the payment of a sum equivalent to one quarter of the annual rentals due over a period of twelve consecutive months”.

Re Article 12 (1)

Spain

In the case referred to under this provision it should be clarified whether an assignment by the lessor to a third party of its rights in the leased equipment modifies the conditions of the lessee’s duty to pay rentals and of its duty to return the equipment at the end of the leasing agreement.

A second sub-paragraph could be added to this paragraph for this purpose. It might read as follows:

“However, where such a transfer entails changes in the conditions for the lessee’s performance of its duties, the lessor must give the lessee notice of these changes in writing”.

Re Article 13

Japan

As regards Article 13, which was newly introduced by the committee at its third session, it is not clear what difference there is between the sphere of application of paragraph 1 and that
of paragraph 2. Taking the example of a series of transactions involving the same equipment which consist of a financial main leasing transaction and a financial sub-leasing transaction, it seems that the sphere of application of paragraph 1 and that of paragraph 2 overlap one another in some part, because both paragraphs are applicable to the financial sub-leasing. In other words, it is not clear whether paragraph 2 is provided in order only to confirm the intent of paragraph 1 in the case of a series of financial sub-leasing transactions or to cover transactions other than a series of financial sub-leasing transactions. It may be pointed out that if the former is intended, paragraph 1 should be deleted; on the other hand, if the latter is intended, paragraph 2 should be more clearly reworded so as to clarify what kind of transactions it is applied to.

Re Article 14 (1)

**Japan**

Paragraph 1 of Article 14 should be retained, i.e. the square brackets should be removed.

**Spain**

Article 14 (1) should be retained in the form in which it is drafted at present. The square brackets around it should therefore be removed.

**United States of America**

Paragraph 1 should be retained and the square brackets in the 1987 Draft should be removed. Paragraph 1 is consistent with the approach taken in Article 6 of the 1980 United Nations Convention on Contracts for the International Sale of Goods (hereinafter referred to as “the Vienna Sale Convention”).

Re Article 14 (2)

**Japan**

Paragraph 2 of Article 14 provides that paragraph 2 of Article 7 and paragraphs 3 and 4 of Article 11 are not subject to the parties’ agreement. Such provisions, however, are not said to have such nature as to demand the exclusion of party autonomy on the ground of their close connection with the public interest. Taking into consideration the commercial character of this Convention – that is, consumer transactions are excluded from the sphere of application of this Convention – and the possible future development of financial leasing transactions, all provisions of this Convention should be subject to the parties’ agreement. It is, therefore, necessary to delete the words “except for the provisions of Article[s 7 (2),] 11 (3) and (4)” from paragraph 2 of Article 14.

**Spain**

Article 14 (2) should be retained in the form in which it is drafted at present. The square brackets should therefore be removed.

**United States of America**

The reference to Article 7(2), presently in square brackets, is unacceptable. For reasons
stated above in support of Alternative II of Article 7(2), if Alternative I were adopted it would be essential for parties to vary its terms in virtually every transaction. Even if Alternative II is adopted, the parties should remain free to negotiate and agree as to how the responsibilities should be allocated. There is no reason why warranties of quiet possession should receive any special treatment.

CONF. 7/3 Add 1
7 April 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Comments on the draft Convention by Governments (Switzerland)

Order in which the provisions of the draft Convention appear

The order in which the provisions of the draft Convention appear could be improved upon: the first sentence of Article 12(1) and Article 13, which regulate the sphere of application of the Convention, could be included in Chapter I. Articles 14 and 15 ("General provisions") could also be moved forward to Chapter I, so as to bring them into line with the order in which they appear in the draft Convention on international factoring.

Re Article 9

This provision does not state expressly that the lessee is entitled to sue the supplier for a reduction in the price of the equipment. We nevertheless feel that this possibility is meant to be covered under the draft Convention, so that the lessee would be entitled, without having to seek the lessor’s agreement, to bring an action against the supplier for a reduction in the price of the equipment and to receive directly from the supplier that part of the purchase price that the latter would be obliged to return. This could, however, be clarified in the explanatory report on the Convention.

Re Article 10

1. - Under paragraph 4 of this article, where, after the lessee has rejected the equipment, the supplier fails to make a fresh tender of the same equipment or a tender of other equipment, the lessee may terminate the leasing agreement, recover any rentals and other sums paid in advance and “meanwhile” has the right to withhold payment of its rentals.

The word "meanwhile" does not refer to the time that elapses between the rejection of the equipment and the termination of the leasing agreement but to the period of time necessary for the lessee to make up its mind, following the tender of non-conforming equipment, whether or not to exercise its right of rejection (cf. Study LIX - Doc. 48, § 129).
This is not made clear in the text. Paragraph 4, moreover, would not appear to be the most appropriate provision in which to deal with this problem.

2. - For this reason one might consider inserting a new paragraph 4\textsuperscript{bis}, drafted along the following lines:

\textquote{4\textsuperscript{bis} - Where the lessee is entitled to reject the equipment [in accordance with paragraph 1 of this article], it may withhold the rentals payable under the leasing agreement until such time as it is able to exercise this right.}

In this case, a consequential amendment would have to be made to paragraph 4, to wit the deletion of the words "meanwhile having the right to withhold rentals payable thereunder" ("4.-...the lessee shall be entitled to terminate the leasing agreement and to recover any rentals and other sums paid in advance. Nevertheless, ...").

Re Article 11

1. - In the event of the lessee's default, this Article gives the lessor two possibilities:

(a) he may recover accrued unpaid rentals, together with interest, regardless of the seriousness of the lessee's default (cf. Article 11 (1));

(b) he may also terminate the leasing agreement, if the lessee's default is substantial (cf. Article 11 (2)).

This article also acknowledges the possibility for the lessor to accelerate payment of the rentals (cf. Article 11(4) and (5)). However, this possibility is not conferred upon the lessor by the Convention itself; it would have to be given by the terms of the leasing agreement. This is brought out clearly by Article 11(4) but is not stated explicitly in Article 11(5). Failing correction of this divergency in the formulation of the two paragraphs, one might imagine that the draft Convention also gives the lessor, in the event of the lessee's substantial default, the possibility to accelerate payment of the rentals.

So as to avoid such an erroneous interpretation, Article 11(5) could be redrafted as follows:

\textquote{5. - The lessor shall only be entitled to terminate the leasing agreement or enforce a term of the leasing agreement accelerating payment of the rentals if it has by notice given the lessee a reasonable opportunity of remedying the default so far as the same may be remedied}.

As this condition applies equally well to the case where the lessor terminates the leasing agreement as to that where it accelerates payment of the rentals, this problem could also be resolved by reordering paragraphs 2 to 5 of Article 11:

\textquote{2. - Where the lessee's default is substantial, the lessor may also terminate the leasing agreement or enforce a term of the leasing agreement accelerating payment of the rentals, provided that it has by notice given the lessee a reasonable opportunity of remedying the default so far as the same may be remedied.}

3. - Where the lessor has terminated the leasing agreement, it may after such termination:
(a) recover possession of the equipment; and

(b) recover such compensation as will place the lessor in the position in which it would have been had the lessee performed the leasing agreement in accordance with its terms, except in so far as the lessor has failed to take all reasonable steps to mitigate its loss.

4. - The leasing agreement may provide for the manner in which the compensation referred to in paragraph 3(b) of this article is to be computed and such provision shall be enforceable between the parties unless such compensation is disproportionate to the compensation provided for under paragraph 3(b).

5. - Where the lessor has terminated the leasing agreement it shall not be entitled to enforce a term of the leasing agreement accelerating payment of the rentals."

2. - Where the lessor enforces a term of the leasing agreement accelerating payment of the rentals and actually receives these rentals earlier than the dates stipulated in the leasing agreement, it can then invest these sums and derive financial advantage therefrom. It is the current practice under leasing agreements for the lessor to give credit to the lessee for any such advantage. Article 11 does not regulate this question and thus leaves a gap which should be filled by a new paragraph 6, which could be drafted along the following lines:

"6. - Where the lessor has enforced a term of the leasing agreement accelerating payment of the rentals, it shall give credit to the lessee for the fact that it has received the rentals earlier than the dates on which they fell due under the leasing agreement."

3. - Should the preceding suggestions be accepted, Article 11 would run as follows (the amendments to the text of the draft Convention being indicated by the use of italics):

"1. - In the event of default by the lessee, the lessor may recover accrued unpaid rentals, together with interest.

2. - Where the lessee’s default is substantial, the lessor may also terminate the leasing agreement or enforce a term of the leasing agreement accelerating payment of the rentals, provided that it has by notice given the lessee a reasonable opportunity of remedying the default so far as the same may be remedied.

3. - Where the lessor has terminated the leasing agreement, it may after such termination:

(a) recover possession of the equipment; and

(b) recover such compensation as will place the lessor in the position in which it would have been had the lessee performed the leasing agreement in accordance with its terms, except in so far as the lessor has failed to take all reasonable steps to mitigate its loss.

4. - The leasing agreement may provide for the manner in which the compensation referred to in paragraph 3(b) of this article is to be computed and such provision shall be enforceable between the parties unless such compensation is disproportionate to the compensation provided for under paragraph 3(b).

5. - Where the lessor has terminated the leasing agreement it shall not be entitled to enforce a term of the leasing agreement accelerating payment of the rentals."
6. - Where the lessor has enforced a term of the leasing agreement accelerating payment of the rentals, it shall give credit to the lessee for the fact that it has received the rentals earlier than the dates on which they fell due under the leasing agreement."

Re Article 12

1. - Paragraph 1 of Article 12 permits the lessor to assign the benefit of the stream of rentals to a third party, which would appear to be perfectly justified.

We interpret this provision as giving the lessee the right to invoke as against the assignee any defences and objections which it may have had in relation to the lessor, in particular the right temporarily to withhold payment of its rentals in accordance with Article 10(4).

If this interpretation is incorrect, this provision should be amended so as to provide for this logical consequence, which is moreover spelled out expressly in Article 8(1) of the draft Convention on international factoring.

2. - Paragraph 2 of Article 12 provides that the lessee may assign "the right to the use of the equipment" and "any other rights" it may have under the leasing agreement, provided that the lessor has agreed to the assignment (and subject to the rights of third parties).

As a corollary to the fact that this provision only refers to the assignment of the lessee's rights under the leasing agreement, it follows that such an assignment may in no case have any negative consequences for the lessor: the lessee's duties in relation to the lessor will in fact remain unaffected and the lessor could, in particular, continue to require payment of the rentals by the lessee as if no assignment had ever taken place. This being the case, it would seem inappropriate to make the validity of the assignment subject to the lessor's consent. This provision should accordingly either be deleted - the parties would thus be left free to regulate this matter in the leasing agreement - or - better still - replaced by a rule, along the lines of Article 12 (1), giving the lessee the right to assign its rights under the leasing agreement. This rule might be worded as follows:

"2. - Subject to the rights of third parties, the lessee may transfer the right to the use of the equipment or any other rights under the leasing agreement. [Such a transfer shall not relieve the lessee of any of its duties under the leasing agreement or alter either the nature of the leasing agreement or its legal treatment as provided in this Convention.]

Re Article 14

1. - Paragraph 1 of Article 14 provides that the Convention shall not apply where it is excluded either by the terms of the supply agreement or by the terms of the leasing agreement.

The draft Convention here gives priority to the bilateral agreements and hence appears to ignore the fact that the leasing transaction addressed by the Convention is tripartite. We question the wisdom of deviating to this extent from the basic concept which underlies the draft Convention and is what determines its whole originality. These misgivings are only reinforced by the fact that the balance established by the Convention is a balance between the rights and duties of the three parties involved in the leasing transaction and therefore a balance which should only be jeopardised by the three parties acting in concert. It has to be added that the
requirement laid down by this provision can only be met if one of the three parties behaves contradictorily, that is when it makes one of the agreements subject to the Convention and not the other.

For that reason, paragraph 1 should be amended in such a way as to provide that the Convention shall not apply where it is excluded by both the terms of the supply agreement and the terms of the leasing agreement.

2. - Paragraph 2 of Article 14, as at present drafted, could result in the intended balance between the rights and duties of the three parties to the financial leasing transaction being seriously jeopardised. In particular, it would permit the parties to derogate from or vary Articles 9 and 10 which are the essential counterpart of the relief from liability accorded the lessor in Article 7.

Should it prove impossible to reach a consensus for making the Convention mandatory, Article 14 would have to be redrafted in a way that would guarantee the balance intended by the Convention.

3. - For these reasons, we would propose the following redraft of Article 14:

"Article 14

1. - This Convention shall not apply where it is excluded both by the terms of the supply agreement and by the terms of the leasing agreement.

2. - The parties may, in their relations with each other, derogate from or vary this Convention except for the provisions of Article[s 7 (2),] 11(3) and (4). Such a derogation or variation shall not alter either the fundamental balance between the interests of the parties or the legal treatment as provided in this Convention."

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22 April 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Comments on the draft Convention by Governments (Pakistan)

Re Article 1 (1)(a)

The article does not provide for the situation where:

(1) the Lessee has already entered into a contract of purchase with the supplier before entering into a lease agreement with the Lessor. In such circumstances the purchase agreement will be transferred to the Lessor;

(2) the Lessee has purchased and paid for the equipment and then approaches the Lessor
for sale and lease-back of the equipment. In such a case the Lessee, along with selling the equipment to the Lessor, will transfer all the warranties etc., given by the supplier to the Lessor.

Re Article 2 (2)

It is desirable to make provision in the article to determine/specify the place of business of parties concerned for the purposes of either the supply agreement or the leasing agreement.

Re Article 4

The obtaining of the consent of the Lessee to vary the supply agreement should be restricted to such matters as affect the rights and interests of the Lessee only.

Re Article 5

The Lessor's real rights are assumed to be those of ownership. If this is so, the words to describe these rights may be reconsidered and substituted to describe these rights in unambiguous terms.

Re Article 7

The Lessee in a financial leasing arrangement approaches the Lessor for a financial package and therefore the Lessee should not, and does not, expect any guidance from the Lessor in the choice of equipment. It therefore follows that the Lessor cannot be expected to be responsible for any defect in the equipment.

We further suggest that the Lessor be protected from any claim from third parties arising out of the ownership of the equipment. The following amendment is proposed in Article 7 (1)(b):

Add "use, operation or possession of" before the word EQUIPMENT at the end of the article.

The warranty of Lessor ensuring quiet possession of the assets should cover circumstances caused by acts or omissions of the Lessor only. All other events that may cause disturbance in Lessee's quiet possession will not be the responsibility of the Lessor. We therefore recommend adoption of alternative II.

Re Article 8 (2)

The article should further provide that the Lessee shall bear the cost of returning the equipment to the Lessor.

Re Article 9

The warranty given by the supplier to the Lessee shall be transferred to the Lessor if the period of the warranty is longer than the initial lease period and the Lessee does not purchase or take a second lease of the equipment.
Re Article 10

The article is one-sided against the Lessor. As defined in Article 1(1)(a), the Lessor does not play any role in the selection of equipment or the selection of the supplier of the equipment, or the terms of supply, as he merely follows the instructions of the Lessee. Further, the Lessee has direct recourse on the supplier under Article 9, to enforce the terms of the supply agreement.

We feel, therefore, that the Lessee should not have a right against the Lessor to reject the equipment (Article 10 (1) (a) and (b)) or to terminate the lease agreement (Article 10 (4)) on account of rejection of equipment. If the equipment is rejected and the supplier fails to supply the same equipment in rectified form or different equipment acceptable to the Lessee, the lease agreement may be terminated with following benefit to the Lessor:

(a) full payment of purchase price paid by the Lessor to the supplier and any other cost that the Lessor may have incurred in connection with the supply agreement or the lease agreement;

(b) compensation for investment of Lessor’s funds at the interest rate implied in the rentals agreed in the lease agreement, and for the period the funds are disbursed by the Lessor until they are paid back;

(c) compensation for the premature termination of the lease as agreed in the lease agreement.

Re Article 11

Article 11 (1) may be amended to provide that the Lessor shall have the right to recover interest on unpaid rentals.

In Article 11 (2) the meaning of substantial default may cause a lot of dispute. We feel that it should be defined and quantified. Similarly under Article 11(2)(b) the reference to all reasonable steps places a heavy burden on the Lessor. The word “all” should therefore be deleted.

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22 April 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Comments on the draft Convention by Governments (South Africa)

Re Article 3

Article 3 has been amended by the substitution for the expression “right” of the expression “option”.

This amendment is explained (paragraph 80, page 44, UNIDROIT 1987, Study LIX - Doc. 48) as follows:
“(The) term ‘option’ was judged more opportune with a view to making it clear that this provision did not purport to cover the situation where the lessee’s right derived from an obligation to purchase the leased asset, since such an agreement would constitute a sale contract.”

The objection to the previous formulation is therefore that a reference purely to a right to buy may be interpreted also to include an obligation to buy.

It is submitted that this amendment, however, causes other problems. An option is not the only right (without an obligation) that may be granted in favour of a lessee to purchase the leased equipment in future (for example, under South African and German law a “vorvertag” or right of first refusal).

It is, therefore, suggested that “the right to buy” is the appropriate expression to be used in Article 3 and to avoid the problem of the obligation to purchase the following sub-article may be inserted in Article 3 while the existing article be renumbered as sub-article 1:

“For the purposes of this article a right to purchase does not include an obligation to purchase.”

Acceptance of this suggestion would also be in line with the wording of Article 8 (2) which still refers to “the lessee’s...right to buy the equipment”.

Re Article 10

Non-conforming equipment

According to Article 10 (1)(a) the lessee shall have the right to reject the equipment if the equipment fails to conform to the terms of the supply agreement. No mention is made in Article 10 of the degree of defectiveness (non-conformity) with the result that the impression is created that the remedies mentioned in the article are available even in instances where the equipment is only in minor respects non-conforming. It is submitted for consideration that Article 10 should possibly be amended in such a way that mention is made of some degree of non-conformity.

Late delivery

Article 10 does not purport to deal with all aspects of late delivery. It is merely an attempt to regulate the lessee’s right to reject the equipment (cf. Article 10 (1)(b)) and/or his right to rescind the leasing agreement under certain circumstances (cf. Article 10 (4)). All other aspects of late delivery will be governed by the applicable law.

However, the logic of Article 10 (1)(b) is difficult to understand. How is it possible for a lessee to reject equipment not yet delivered to him? The only effect Article 10 (1)(b) may possibly have is that it gives the lessee the right to refuse a late delivery of the equipment. Such a refusal is tantamount to recission of the leasing agreement.

Article 10 (4) appears to be applicable only in the case of non-conforming equipment and not in the case of late delivery.

It is submitted that from a drafting point of view it seems to be desirable to deal with non-conforming equipment and late delivery in separate articles.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Comments on the draft Convention by international Organisations (Asian Leasing Association (Asialease))

MEMORANDUM OF COMMENTS

Re Article 1 (1)(a)

This does not provide for the situation where at the time of negotiating a lease the lessee has already entered into a contract of sale and purchase for the equipment with the relevant supplier and accordingly at the outset the supply contract is not entered into directly by the lessor with the supplier. It is therefore necessary to require the original supply contract entered into between the lessee and the supplier to be novated over to the lessor.

(1) Extract from the World Leasing Yearbook 1987, 29:
"Almost all the countries in Eastern Asia are represented in Asialease, with members coming from Hong Kong, India, Indonesia, Japan, Korea, Malaysia, Pakistan, the Philippines, Singapore, Sri Lanka, Taiwan (ROC) and Thailand. The Association also numbers among its members leasing firms from Australia, Iran, Switzerland and the United States. Being a young organisation, membership is expected to grow rapidly in the next few years.

There are four types of membership. They are: Institutional Member, which comprises any organisation or association of lessors in Asia; Individual Member, which includes individual corporations or companies engaged in leasing in Asia; International Member, which are individual corporate lessors or associations of lessors based outside Asia; and Associate Member, which groups professional bodies and business entities with an interest in leasing but which do not fall in any of the other three mentioned categories of members."

(2) The Honorary Secretary to the Hong Kong Equipment Leasing Association in his letter of 26 November 1987 communicating the comments of the Asian Leasing Association (Asialease) on the Draft Convention on international financial leasing set out hereafter stated:
"From the enclosed Memorandum you will note that we are most concerned at a number of important aspects of the draft Convention which we believe require further in-depth discussion with a view to appropriate drafting changes being made to the text of the Convention. Although the general nature of our comments might be seen to be partisan from the lessor's stand this is not intended to be the case. What we do intend to try to do is to ensure that the Convention properly reflects the true nature of a financial leasing arrangement. This is that the financier/lessor is brought into the transaction merely to provide for the financing to enable the lessee to obtain the use of the equipment it has selected at a particular price and on other terms it has agreed with a supplier of its choice. The financier comes to the transaction for this limited purpose and not with any intention to become involved in the supply contract for the relevant goods other than to obtain title to them so as to be able to enter into the relevant lease agreement. The lessor requires its liability in the transaction to be restricted to its ability to recover rental payments from the lessee and is not prepared to assume any liabilities in respect of the goods subject to the lease unless these are forced upon it by statute or otherwise by law as a result of it being the legal owner of the goods. Even in these circumstances the lessor will wish to seek indemnification from the lessee and probably moreover will wish to require the lessee to insure it against the relevant risk. At the moment in
Re Article 1 (3)

We note the provisions of this new article which we assume is intended to restrict the operation of the Convention to finance leases concluded in the course of a business. However the reference to "family" use seems a strange way of doing this.

Re Article 4

This should be amended to permit such things as an amendment to the payment terms and other matters not detrimental to the lessee without the consent of the lessee.

Re Article 5

We do not understand the reference to "real rights" in this Article but can only assume this means to refer to the lessor's proprietary interests as owner in the equipment under the leasing arrangement. We do not however believe this is a term of art generally recognised internationally and would suggest therefore that these words be re-examined with a view to adopting a new phrase more commonly understood in a wider number of jurisdictions.

Re Article 7

This Article contains one of our main areas of concern in the Convention where it is sought to involve the lessor in the supplier's liability for defective equipment. The fact of the matter is that in a true financial lease a lessor does not get involved at any stage in the selection of the equipment nor indeed in the choice of the supplier and merely gets involved in the contractual relationship with the supplier to acquire title to the equipment so as to be able to on lease it under the financial leasing arrangements to the lessee.

Article 7 addresses two separate issues. First the general condition of the equipment and secondly the lessor's right and title to the equipment and accordingly its ability to lease the same to the lessee and the lessee's ability to enjoy quiet possession of the equipment during the currency of the lease. These issues are in our view separate and distinct and should be treated quite differently. On the one hand we do not consider that the lessor in a financial lease should incur liability in respect of defective equipment but on the other hand we accept that the lessor must have the clear right and title to lease the equipment to the lessee. As a result of this we recommend the following changes to this Article:

(a) the deletion of the words "save to the extent that it has intervened in the selection of the supplier or the specifications of the equipment" at the end of Article 7 (1)(a). There are a number of reasons for this suggested change the principal two of which are as follows:

a number of places referred to in our Memorandum the Convention largely seems to ignore the realities of a finance lease and the role of the lessor in such a transaction. If the Convention is to be a success and to be adopted as widely as possible it must be acceptable to the business community to which it is directed; otherwise it will simply be ignored and contracted out of, thus rendering it redundant. This would no doubt be a great disappointment to all those involved in dedicating many years of time in the creation of the Convention. Although we are aware that the drafting of the Convention has already been in hand for a considerable period of time, we would not wish this to pre-empt due and careful consideration of the points we have made in the enclosed Memorandum which we believe call for attention."
(i) the wording in itself at the moment is vague and unclear and not open to
definite interpretation;

(ii) as the Convention has now been amended by the introduction of the new
Article 1 (3) providing effectively that it only regulates financial leases for business purposes
between business persons any concept of consumer protectionism to protect the unwary
individual consumer from the worldly lessor financier seems inappropriate. In the case of a
financial lease between business persons the lessee party will be the only party with the relevant
knowledge necessary to enable it to determine what equipment it requires for the particular
purpose and who is the correct supplier from which to obtain this equipment. Its only role
therefore in approaching the lessor is to obtain an appropriate financing package to acquire the
use of the equipment during the currency of the lease period. It does not look to or indeed expect
the financier to undertake any liability as to the quality of the equipment;

(b) we would suggest the inclusion of the words “use, operation or possession of the”
before the word “equipment” at the end of Article 7(1)(b) to distinguish this from any liability
of the owner (lessor) in respect of the equipment;

(c) we would request the deletion of Alternative I and the adoption of Alternative II
for Article 7(2). This restricts the lessor’s warranty as to the lessee’s ability to have quiet
possession of the equipment during the currency of the lease to any impediments in the lessor’s
(but no one else’s) right and title to lease the same to the lessee. Moreover an excessive liability
would be imposed upon the lessor if provision were made for extending the lessor’s warranty
liability to cover cases where unavoidable factors relating to force majeure (such as government
expropriation, labour disputes, etc.) could intervene, through no fault of the lessor’s, to disturb
the lessee’s quiet possession of the equipment.

Re Article 8

Article 8(2) should be amended to provide that the lessee should pay for the return of the
equipment to the lessor.

Re Article 9

We note the provisions of this Article which effectively confer the right on the lessee
directly to have recourse against the supplier of the equipment if it proves to be defective. This
is a further reason in our view for removing any liability on the part of the lessor for defective
equipment.

Re Article 10

The general concern expressed by us with regard to Article 7 applies equally well here in
this Article. Generally we are uncomfortable and unhappy with the effective operation of this
Article for the following reasons:

(a) as mentioned above in a financial lease we do not believe the lessor should become
involved in the obligations of the supplier with respect to the condition and fitness for purpose,
merchantability and otherwise of the equipment. This is particularly so when we note that the
Convention now by virtue of Article 1(3) provides that it will only apply to financial leases for business purposes between business or professional persons;

(b) by virtue of the operation of Article 9 the supplier is deemed to have a direct relationship with the lessee and accordingly the lessee will be able to claim on the supplier for any defects in the equipment;

(c) Article 10 simply does not appear properly to envisage the effects on the operation of the lease agreement of a rejection of the equipment by the lessee. It seems to anticipate that the supplier will have an opportunity during a period of time to deliver alternative equipment (we assume of the same type and specification as that originally contracted to be supplied) for adoption under the lease in place of the old defective equipment. However, during the period prior to delivery of the substitute equipment or indeed the failure of the supplier to deliver any substitute equipment what happens to the lease agreement? Is the lessee under an obligation to continue to pay rental at the original rates to the lessor or what? This is particularly relevant from the lessor’s perspective who will in fact be the only party who is out-of-pocket under the arrangements as having expended the full purchase price of the equipment to the supplier and incurred all the expenses and costs of putting the lease finance arrangements into place at the request of and for the sole benefit of the lessee. Where is the lessor’s right of recompense as against the lessee in these circumstances?

(d) why should the lessee in a commercial leasing arrangement negotiated between commercial entities at arms length have both the right to reject the goods as against the supplier, and the ability to obtain damages from the supplier for the defects (the effects of Article 9) and at the same time the right to terminate the lease with the lessor. If in these circumstances the lessee is to be given the right to terminate the lease against the lessor but is at the same time to have the right to proceed against the supplier in respect of claims for defects in the equipment then the lessee must have an obligation to repay the lessor the full purchase price of the relevant equipment together with any of its costs and expenses incurred in entering into the supply contract with the supplier for the equipment and entering into the lease agreement with the lessee. To do otherwise will have the effect of ensuring that any lessor engaged with an international financial lease will deliberately exclude the provisions of this Convention and accordingly make it redundant from the outset. We assume this must not be the intention of the parties in drafting and preparing this Convention which one would hope to have adopted by as many lessors in as many different countries as possible;

(e) the effects of the provisions of Article 10(3) are unclear to us and appear to be uncertain in their whole operation. They may however make more sense if the words “it has intimated acceptance to the lessor or the supplier or where” were inserted after “where” in the first line of this Article;

(f) the provisions of Article 10(4) are quite unacceptable for a number of the reasons referred to above. Moreover if any party is to have the opportunity to terminate the lease agreement upon the lessee rejecting the equipment as against the supplier it should surely be the lessor who should in addition be conferred with the right to claim on the lessee for the payment of the full principal amount due under the lease, any interest accrued to the date of termination and any costs and expenses relating to the entering into of the lease agreement and the supply contract.

171
Re Article 11

Article 11(1) should provide that upon a default by the lessee the lessor should not only have the right to recover accrued unpaid rentals together with interest (we assume to the date of payment and not merely to the date of termination of the lease agreement) but also an amount of interest for the remaining unexpired period of the primary lease period and the overriding right to repossess the equipment.

What is the meaning in Article 11(2) of a “substantial default”? This is not defined.

We would suggest the deletion of the word “all” in the last line of Article 11(2)(b) which if retained will impose an unacceptable burden on the lessor.

We do not understand the provisions of Article 11(4). Usually under a lease agreement upon a default by the lessee the lessor shall be entitled to terminate the leasing of the equipment thereunder and to claim for all arrears outstanding and to accelerate full payment of all remaining amounts of rental due thereunder less a discount in respect of the interest factor in the computation of the rentals for the period from the date of termination to the anticipated date of expiry of the primary lease period. The leasing agreement itself should not come to an end upon a default of the lessee which would only leave the lessor with a right to claim damages for breach of contract against the lessee. The amount of damages might or might not be the same as any sum able to be claimed under any predetermined termination payment formula set out in the lease agreement itself as referred to above.

The provisions of Article 11(5) seem to be in conflict with those in Article 11(4). In Article 11(4) it is provided that the lessor shall not be entitled to accelerate payment of rental under a lease agreement which is terminated. Article 11(5) however seems to anticipate that the lessor may have the ability to accelerate the payment of rentals if the lease has terminated by virtue of a breach by the lessee which though capable of remedy has not been remedied after the lessee has been given a reasonable opportunity to remedy the same. How do these two Articles interact with each other? Moreover what constitutes a reasonable opportunity for the lessee to remedy a breach capable of remedy?

There are aspects to this Article which we believe may be striving to deal with the difference which exists in certain common law jurisdictions (as indeed it does in a number of jurisdictions in which members of our Association reside) between a breach of a leasing agreement which may entitle the lessor to terminate the leasing of the equipment thereunder and only to claim for amounts owing up to the date of termination of the agreement and a breach of such a nature as to entitle the lessor to treat the agreement as having been repudiated and to claim for all amounts owing under the leasing agreement both for the period up to the date of termination and thereafter less, possibly, a discount in respect of the financial charge element in the calculation of rentals for the remaining unexpired period of the lease term. This however is a fairly complicated concept subject to a variety of different interpretations by the courts in the relevant common law jurisdictions which may indeed not have similar applicability in other countries around the world. We question here therefore the whole basis of treatment of these issues and the distinction between them and the way in which they are dealt with under this Article and indeed the desirability of this at all. This should be open to further critical review and discussion.
Re Article 14

We endorse the provisions of Article 14 as presently drawn as there must be the ability for any party wishing to adopt the Convention either to adopt it in part or to adopt it in whole or in fact specifically to exclude any agreement from its operation entirely. However, reference to Article 7(2) should be deleted from the provisions of Article 14(2).

CONF. 7/4 Add. 1
29 February 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Comments on the draft Convention by international Organisations (World Leasing Council) (1)

MEMORANDUM OF COMMENTS

I. - Introduction

The consideration by a diplomatic Conference in Ottawa from 9 to 28 May 1988 of the above-mentioned draft may be considered as a final stage in the elaboration of a Convention on international leasing.

Leasing experts belonging to various national leasing associations and leasing federations have co-operated with governmental and inter-governmental experts in the conception of this draft.

Several national leasing associations and international leasing federations have had the opportunity to express their comments on the successive drafts.

The Explanatory Report added to the Draft and being part of the Unidroit document LIX-Doc. 48 has clarified several obscure issues and so reduced the contentious subjects. It, therefore, seems very important that when implementing the Convention reference should be made to this Explanatory Report.

Below the World Leasing Council submits its position on those articles of the draft Convention which in its view seem capable of improvement.

(1) In his letter of 10 February 1988 communicating the comments of the World Leasing Council set out hereunder, Mr Florent J. de Cuyper, Secretary to the World Leasing Council, stated that the World Leasing Council is "an informal umbrella organisation grouping at present the regional leasing company federations of five continents, i.e. North America, Latin America, Europe, Asia and Australia, so that in fact it represents the leasing industry on a world wide basis."
II. - Comments on the draft Convention (Study LIX - Doc. 48)

Re Article 7

The Council believes that this Article contains one of its main areas of concern in the Convention where it is sought to involve the lessor in the supplier's liability for defective equipment. The fact of the matter is that in a true financial lease a lessor does not get involved at any stage in the selection of the equipment nor indeed in the choice of the supplier and merely gets involved in the contractual relationship with the supplier to acquire title to the equipment so as to be able to on lease it under the financial leasing arrangements.

The Explanatory Report (last sentence of item 110) confirms this view where it says:

"The case for the lessor's immunity from liability in tort towards the lessee is founded on its non-involvement in the selection of the supplier and the specifications of the equipment and on the fact that it will normally at no stage profess any technical expertise with regard to the equipment's physical characteristics."

As a result of this the Council recommends the following changes to this Article:

Article 7 (1)(a)

The deletion of the words "save to the extent that it has intervened in the selection of the supplier or the specifications of the equipment" at the end of Article 7 (1)(a).

There are a number of reasons for this suggested change, the principal two of which are as follows:

(i) the wording in itself at the moment is vague and unclear and not open to definite interpretation;

(ii) as the Convention has now been amended by the introduction of the new Article 1 (3) providing effectively that it only regulates financial leases for business purposes between business persons, any concept of consumer protection to protect the unwary individual consumer from the lessor financier seems inappropriate. In the case of a financial lease between business persons the lessee party will be the only party with the relevant knowledge necessary to enable it to determine what equipment it requires for the particular purpose and who is the correct supplier from which to obtain the equipment. Its only role therefore in approaching the lessor is to obtain an appropriate financing package to acquire the use of the equipment during the currency of the lease period. It does not look to or indeed expect the financier to undertake any liability as to the quality of the equipment.

Article 7 (1)(b)

The Council would suggest the inclusion of the words "use, operation or possession of the" before the word "equipment" at the end of Article 7 (1)(b) to distinguish from any liability of the owner (lessor) in respect of the equipment.
Article 7 (2)

The Council believes that the Convention should include Alternative II, which contains paragraphs 2 and 3 which state the correct view of a financial lessor’s warranty of quiet possession to a lessee, leaving any broader such warranties to other applicable law. The Council believes that Alternative I does not reflect economic reality or longstanding practice in the leasing business.

Re Article 8

Article 8 (2)

The Council believes that Article 8 (2) should be amended to provide that the lessee should pay for the return of the equipment to the lessor.

Re Article 9

The Council notes the provisions of this Article which effectively confer the right on the lessee directly to have recourse against the supplier of the equipment if it proves to be defective. This is a further reason in its view for removing any liability on the part of the lessor for defective equipment.

Re Article 10

The general concern expressed by the Council with regard to Article 7 applies equally well here in this Article. Generally the Council feels uncomfortable and unhappy with the effective operation of this Article for the following reasons:

(a) As mentioned above in a financial lease, the Council does not believe the lessor should become involved in the obligations of the supplier with respect to the condition and fitness for purpose, merchantability and otherwise of the equipment. This is particularly so when one notes that the Convention now by virtue of Article 1(3) provides that it will only apply to financial leases for business purposes between business or professional persons;

(b) By virtue of the operation of Article 9, the supplier is deemed to have a direct relationship with the lessee and accordingly the lessee will be able to claim on the supplier for any defects in the equipment;

(c) Article 10 simply does not appear properly to envisage the effects on the operation of the lease agreement of a rejection of the equipment by the lessee. It seems to anticipate that the supplier will have an opportunity during a period of time to deliver alternative equipment (the Council assumes, of the same type and specifications as that originally contracted to be supplied) for adoption under the lease in place of the old defective equipment. However during the period prior to delivery of the substitute equipment or indeed the failure of the supplier to deliver any substitute equipment, what happens to the lease agreement? Is the lessee under an obligation to continue to pay rentals at the original rates to the lessor or what? This is particularly relevant from the lessor’s perspective who will in fact be the only party who is out-of-pocket under the arrangements as having expended the full purchase price of the equipment to the supplier and incurred all the expenses and costs of putting the lease finance arrangements into
place at the request of and for the sole benefit of the lessee. Where is the lessor's right of recompense as against the lessee in these circumstances?

(d) Why should the lessee in a commercial leasing arrangement negotiated between commercial entities at arms length have both the right to reject the goods as against the supplier, and the ability to obtain damages from the supplier for the defects (the effects of Article 9) and at the same time the right to terminate the lease with the lessor? If in these circumstances the lessee is to be given the right to terminate the lease against the lessor but is at the same time to have the right to proceed against the supplier in respect of claims for defects in the equipment then the lessee must have an obligation to repay the lessor the full purchase price of the relevant equipment together with any of its costs and expenses incurred in entering into the lease agreement with the lessee. To do otherwise will have the effect of ensuring that any lessor engaged with an international financial lease will deliberately exclude the provisions of this Convention and accordingly make it redundant from the outset. The Council assumes this must not be the intention of the parties in drafting and preparing this Convention which one would hope to have adopted by as many lessors in as many different countries as possible.

Article 10 (3)

The Council believes that the effects of the provisions of Article 10 (3) are unclear and appear to be uncertain in their whole operation. They may however make more sense if the words “it has intimated acceptance to the lessor or the supplier or where” were inserted after “where” in the first line of this Article.

Article 10 (4)

The Council believes that the provisions of Article 10 (4) are quite unacceptable for a number of reasons referred to above. Moreover, if any party is to have the opportunity to terminate the lease agreement upon the lessee rejecting the equipment as against the supplier it should surely be the lessor who should in addition be conferred with the right to claim on the lessee for the payment of the full principal amount due under the lease, any interest accrued to the date of termination and any costs and expenses relating to the entering into of the lease agreement and the supply contract.

Re Article 11

Article 11 (1)

The Council believes that Article 11 (1) should provide that upon a default by the lessee the lessor should not only have the right to recover accrued unpaid rentals together with interest (it assumes to the date of payment and not merely to the date of termination of the lease agreement) but also an amount of interest for the remaining unexpired period of the primary lease period and the overriding right to repossess the equipment.

Article 11 (2)(b)

The Council would suggest the deletion of the word “all” in the last line of Article 11 (2)(b) which if retained will impose an unacceptable burden on the lessor.
Re Article 14

Article 14 (1)

The Council recommends that Paragraph 1 of Article 14 be included in the final Convention, as the parties to either the supply agreement or the leasing agreement should be able to freely contract whether or not the Convention applies.

Article 14 (2)

The Council further recommends that the reference to Article 7 (2) must be deleted from Article 14 (2), so that the parties will be free to contract whatever they wish with respect to warranties of quiet possession. A failure to delete such reference would make the Convention unacceptable.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Comments on the draft Convention by international Organisations
(Hague Conference on Private International Law)

With a view to the diplomatic Conference for the adoption of the draft Unidroit Conventions on international factoring and international financial leasing, to be held in Ottawa (Canada) from 9 to 28 May 1988 and pursuant to the President of Unidroit's letter of 14 December 1987 to the Secretary-General of the Hague Conference on Private International Law, the Permanent Bureau of the latter Organisation hereunder submits comments relating to two problems arising in both the draft Convention on international factoring and the draft Convention on international financial leasing, problems which have not apparently been sufficiently examined during the various sessions of the two Unidroit committees of governmental experts. One problem concerns the reservation to the geographical sphere of application of the two draft Conventions, the other whether or not the parties to the contract should be able to derogate, wholly or partly, from the provisions of the future Conventions.

Re Article F

Reservation to the geographical sphere of application

In both sets of draft final provisions drawn up by the Unidroit Secretariat is to be found an Article F which would authorise any Contracting State to declare that it will not be bound by Article 2 (1)(b).

In the supporting notes to this Article F, the Unidroit Secretariat simply recalls that an
identical reservation clause is to be found in the Vienna Convention on the International Sale of Goods (Article 95) and in the Geneva Convention on Agency in the International Sale of Goods (Article 28), without providing any reason for adopting a similar reservation in the prospective Conventions on international factoring and international financial leasing. In effect, this reservation problem was never discussed in any depth at the sessions of the Unidroit committees of governmental experts and it would indeed appear that this reservation is included in these draft final provisions solely to ensure that these texts are aligned on the Vienna and Geneva Conventions.

While there can be no gainsaying the desirability of two or more international instruments, dealing with relatively identical subject-matters (in the case in point, what is identical is the contractual nature of the relationships addressed), being harmonised from the point of view of their textual presentation and in particular employing similar concepts and definitions, one should be on one’s guard not to sacrifice the coherence of a text, and in particular the sphere of application of a Convention, for the mere sake of one text being absolutely aligned on another; in other words, to be specific it would be regrettable were the fact of seeking to align the reservation to the geographical sphere of application of the future Conventions on the Vienna and Geneva Conventions adversely to affect the balance and structure of the future Conventions. In this regard it is the opinion of the Permanent Bureau of the Hague Conference that purely and simply to repeat the reservation permitted under the Vienna and Geneva Conventions in the two draft Conventions could well have unexpected consequences which might jeopardise widespread application of the future Conventions and create delicate problems in practice, above all for leasing and factoring companies.

It should first of all be borne in mind that the reservation contained in Article 95 was adopted in the Vienna Convention at the request of certain delegations that did not want the judges of their countries to be obliged to apply the Vienna Convention where their conflict rules would lead to their own law being found to be applicable to a given sale contract. Thus the effect of Article 95 of the Vienna Convention for a State having availed itself of this reservation would be simply that where the conflicts rule of the judge of this State leads to the application of this judge’s own substantive law, then “he will not be bound” by Article 1 (1) (b) of the Convention. On this interpretation (an interpretation which is not shared by everybody), the reservation contained in Article 95 of the Vienna Convention (and the same of course is true for Article 28 of the Geneva Convention) has an application that is limited to the State availing itself of this reservation and moreover does not affect the normal operation of the conditions for the application of the Convention (Article 1) in other States.

The same is, however, not true for the draft Conventions on international factoring and international financial leasing, chiefly by virtue of the tripartite legal relationship covered by each of these two drafts. Two examples will help to bring out the difficulties which the adoption of Article F in the two Conventions would cause:

Let us take the case of the lessor’s place of business being located in State A, a Party to the future Convention, the lessee’s place of business in State B, also a Party to the future Convention and the supplier’s place of business in State C, which is not a Party to the Convention. In this case the future Convention on international financial leasing would not be applicable by virtue of Article 2 (1)(a), because the three parties to the legal relationship do not all have their place of business in a Contracting State. Let us now take the following cases:
Case I

The leasing agreement is subject either to the law of A or to the law of B, both States Parties to the Convention. The supply agreement is subject to the law of A, either because the parties to the agreement have so decided (freedom of contract) or because the objective conflict rules of State A lead to the application of the law of this State. State A has availed itself of the reservation permitted under Article F. Is it reasonable in this case for the judges of State A, or indeed for that matter for the judges of State B to be authorised not to apply the Convention, whereas the main agreement in the triangular relationship, the leasing agreement, was concluded between two parties whose places of business are both located in Contracting States, which is the fundamental requirement for the geographical application of the Convention, in so far as it is set forth in the opening words (the chapeau) of Article 2 (1) and whereas the parties to the supply agreement have expressly chosen the law of State A as the law to apply to their agreement so as to fall in line with the requirements of Article 2(1)(b)?

Case II

The leasing agreement is still subject either to the law of State A or to the law of State B but the supply agreement is subject to the law of State D (this could, for instance, be the State in which the leased equipment is to be used); State D is a Party to the Convention but has availed itself of the reservation permitted under Article F:

(a) Will the judges of State A be precluded from applying the Convention to the leasing agreement on the pretext that State D has availed itself of the reservation permitted under Article F?

(b) Is it again reasonable for the judges of State D to be allowed not to apply the Convention to relations between the lessor and the lessee, whereas that is what the parties expect and whereas, moreover, State D has introduced the rules embodied in the Convention on international financial leasing into its legal system?

These two examples (however, one could well imagine others) show that the reservation permitted under Article F in both draft Conventions has consequences which go well beyond those found in the Vienna Convention. In particular, Article F would have the effect of enabling one State to paralyse the operation of the Convention for the whole triangular relationship, even when the main agreement, the leasing agreement, is concluded between two parties whose places of business are situated in States which have not availed themselves of the reservation; this extraterritorial effect of a reservation has an element of exorbitance which would seem difficult to reconcile with the general principles of the law of treaties.

The Permanent Bureau feels that the inclusion of Article F in the two draft Conventions is all the more regrettable in so far as the geographical sphere of application of both Conventions is already extremely narrow, since it requires either that the places of business of all three parties to the triangular relationship be situated in Contracting States or that the leasing (or factoring) agreement and the supply (or sale) agreement be governed by the law of a Contracting State. To narrow still further this already narrow sphere of application by giving one of the States Parties to the Convention unilaterally the possibility to make a declaration leads one to doubt the usefulness of the attempt at unification undertaken by Unidroit in the field of international
financial leasing and in that of international factoring. The Permanent Bureau would suggest that Article F be deleted or, at the very least, if there is a State that truly cannot manage without such a reservation, that its effects be strictly limited to within the State that avails itself of the reservation.

**Re Article 14 of the draft Convention on international financial leasing/Article 3 of the draft Convention on international factoring**

*Option for the parties to exclude the Convention as a whole or in part*

Article 14 of the draft Convention on international financial leasing and Article 3 of the draft Convention on international factoring each give the parties to the contract the opportunity to exclude the application of the Convention in a manner which is truly paradoxical.

Article 14 of the leasing draft seems in effect to leave open to the parties the option either to exclude the application of the Convention as a whole or to vary, depending on their needs, certain provisions of the Convention, although in this case with the exception of certain key articles from which the parties may not derogate. Article 3 of the factoring draft offers the same alternative, albeit formulated in a different way.

This approach is unusual and would not appear to be satisfactory. Of the two possibilities:

- either the parties should be authorised to exclude the Convention as a whole or to derogate from any of its provisions whatsoever (this is the system adopted in Article 6 of the Vienna Convention on the International Sale of Goods);

- or the parties should be either wholly or partly prohibited from derogating from the provisions of a Convention, which then implies that they should not be allowed to exclude the Convention as a whole (this is the system generally employed in international transport Conventions).

However, to adopt in a Convention an Article which would give the parties both possibilities is illogical and results in an impasse: what attitude should judges take if the parties to the contract decide, at first, to exclude the Convention as a whole and then, subsequently, to include the provisions of the Convention in their contract, while varying the key provisions of the Convention, that is those provisions from which the parties are not entitled to derogate?

To be sure, the problem in both draft Conventions derives from the fact that they both address a triangular relationship: in fact it would appear difficult to accept that two parties to the contract may vary provisions of the Convention concerning a third party or the articles affecting the rights of third parties. In view of the fact that we are in a contractual situation and that accordingly the parties’ freedom of contract should be respected, it is suggested that Article 14 of the leasing draft and Article 3 of the factoring draft should be redrafted along the following lines:

"In their relations with each other [alone], the lessor (the supplier) and the lessee (the factor), on the one hand, and the lessor (the supplier) and the supplier (the debtor), on the other, may exclude the application of this Convention or derogate from or vary the effect of any of its provisions."
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Comments on the draft Convention by international Organisations
(World Bank/International Finance Corporation)

MEMORANDUM

Leases with Variable Rentals

1. - At the third session of governmental experts, the observer from the World Bank introduced the concept of leases in which the rentals are related to the returns generated by the lessee’s use of the equipment. While government experts felt unable to include an explicit reference to this concept without previous consideration, “there was, nevertheless, a general feeling that the matter merited careful consideration by governments with a view to the preparation of their position at the diplomatic conference” (see summary report of that session). Also, the term “calculated” in Article 1(2)(c) of the draft Convention on International Financial Leasing (the Convention) was substituted for the previous term “fixed” to extend the ambit of the Convention to such types of leases; and reference to arrangements under which the rentals payable are “substantially dependent on the production, revenues or profits from the investment project” is made in Sections 37, 52 and 70 of the explanatory report on the Convention, dated October 1987.

2. - On April 12, 1988 the Convention Establishing the Multilateral Investment Guarantee Agency (M.I.G.A.) entered into force. M.I.G.A. will guarantee foreign investments in its developing member countries against non-commercial risks (see attached handout on M.I.G.A.). Draft Operational Regulations for M.I.G.A. that were unanimously approved by a preparatory committee of signatory countries extend eligibility for coverage to leases “with terms of at least three years where the lessor leases capital goods to a lessee and where rental payments are substantially dependent on the production, revenues or profits of the Investment Project.” This extension of coverage was introduced as a means of overcoming creditworthiness problems of highly indebted countries where neither export credit financing or insurance is available, nor lessors are willing to assume the transfer risk on their own account.

3. - It should also be noted that the concept of leases with performance related rentals serves purposes similar to those of build-operated-and transfer-arrangements where in essence the price for a plant delivered is paid out of revenues from the operation of the plant. Such transactions have recently been included in the coverage of some national export credit insurance agencies, such as the German Hermes.

4. - It appears that relating rentals to the revenues from the use of leased equipment could facilitate the financing of exports to highly indebted countries – by making possible coverage by M.I.G.A., by encouraging national agencies to extend their coverage, and/or by enabling leasing companies or commercial banks to underwrite the transaction. It is therefore suggested
to ensure the application of the Convention to such arrangements. An explicit reference to them in the Convention could further stimulate their consideration and thus the adaptation of leasing transactions to developing countries' needs. The Conference might wish to consider including the following provision in the Convention:

"This Convention applies to international financial leasing transactions in which the rentals are dependent on the returns generated by the lessee's use of the equipment, subject to such modifications as the parties to such transactions may agree upon in view of the particular characteristics of such transactions."

Attachment

MULTILATERAL INVESTMENT GUARANTEE AGENCY (M.I.G.A.)

by

Jürgen Voss

On April 12, 1988 the Convention Establishing the Multilateral Investment Guarantee Agency ("the Convention") entered into force, establishing M.I.G.A. as a new member of the World Bank Group. M.I.G.A.'s Council of Governors, i.e. the representatives of M.I.G.A.'s member countries, will have its inaugural meeting on June 8, 1988 and elect M.I.G.A.'s Board of Directors. Before the end of June, the latter will elect M.I.G.A.'s President who in turn will appoint the staff. M.I.G.A. is expected to commence operations in the Fall.

As of April 15, 1988, thirty countries have ratified the Convention; together they will subscribe to some 53.5 per cent of M.I.G.A.'s authorised capital, i.e., some U.S. $575 million. Since a total of 63 countries signed the Convention and others are actively considering doing so, M.I.G.A.'s membership is expected to increase rapidly.

Objective

M.I.G.A.'s objective will be "to encourage the flow of investments for productive purposes among member countries, and in particular to its developing countries."(1) It is designed to complement the activities of other international development institutions with a particular focus on enhancing mutual understanding and confidence between host governments and foreign investors; heightening the awareness of investment opportunities; increasing information, knowledge and expertise related to the investment process; promoting equity-type forms of project financing responsive to developing countries's needs; as well as assisting developing countries in arresting and reversing capital flight.

To serve these purposes, M.I.G.A. will guarantee eligible investments against losses from non-commercial risks and provide a broad range of research, promotional, technical assistance and consultative services. It is directed to "give particular attention ... to the importance of increasing the flow of investments among developing member countries."

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(1) All citations are taken from the Convention Establishing Multilateral Investment Guarantee Agency ("the Convention").
Salient features

Guarantee Program

The scope of M.I.G.A.'s guarantee program is delineated in terms of covered categories of risk as well as types of investment, investors and host countries eligible for coverage. With respect to each of these features, the Convention avoids rigid definitions and thus enables M.I.G.A. to flexibly develop its program in response to emerging market forces.

M.I.G.A. will provide coverage against the risks of restrictions on the repatriation of investment proceeds in freely usable currency (transfer and inconvertibility risk), expropriation and similar measures, breach of contract by the host government in certain defined cases of denial of justice and war/revolution/civil disturbance. Coverage may be extended to other non-commercial risks with the exception of the exchange rate risk.

Eligible investments include both direct and portfolio equity investments as well as loans and loan guarantees by equity holders in the project enterprise; they furthermore encompass “such forms of direct investment as may be determined by the Board.” Under draft operational regulations unanimously approved by a preparatory committee of signatory countries of the Convention, these forms will from the outset include production-sharing contracts, profit-sharing contracts, management contracts, franchising agreements, licensing agreements, operating leasing agreements and turnkey contracts on the condition that they have terms of at least three years and that the contractor's payment substantially depends on the operating results of the project. Eligibility can be extended to further forms of investment, possibly including medium and long term project loans.

To ensure M.I.G.A.’s potential contribution to additional investment flows, eligibility is confined to new investments. However, investments are considered as new investments if they serve the modernization, expansion or financial restructuring of an existing enterprise, or if they assist the host country in restructuring its economy. This should enable M.I.G.A. to support privatization and debt-for-equity swap programs.

M.I.G.A.’s guarantees will be available to investors which are nationals of a member country of M.I.G.A. or, in the case of corporate investors, which either are incorporated and have their principal place of business in a member country or whose capital stock is chiefly owned by nationals of member countries. Eligibility includes publicly-owned investors operating on a commercial basis. On the application of the host government concerned, eligibility can be extended to nationals of the host country that transfer assets which they have invested abroad. This innovative feature is meant to help reverse capital flight.

To qualify for coverage, the investment must normally be made in a developing member country of M.I.G.A. However, investments in industrial member countries (for instance by an O.P.E.C. member country or its investors) may also be covered under the so-called sponsorship facility (see infra).

The aforementioned Draft Operational Regulations guide M.I.G.A. in its underwriting decisions to give priority to investments in lesser developed countries, investments among developing countries and joint ventures between domestic and foreign investors. Before underwriting any project, M.I.G.A. must satisfy itself as to the project’s economic soundness,
contribution to the host country’s development and compliance with the host country’s laws and regulations; M.I.G.A. must also satisfy itself that the investment will be accorded adequate legal protection by the host country. In its risk assessments, M.I.G.A. is directed to focus on the particular characteristics of each investment project rather than on the host country at large with a view to facilitating coverage of viable investment projects in spite of difficulties (notably balance-of-payments problems) of the host country.

M.I.G.A. “shall not conclude any contract of guarantee before the host government has approved the issuance of the guarantee ... against the risks designated for cover.” Every host government will hence freely determine whether, and to what extent, M.I.G.A. will become involved in investments in its territory and thus freely subscribe to any legal consequence from such involvement.

If M.I.G.A. pays a claim, it will be subrogated to “such rights or claims related to the guaranteed investment as the holder of a guarantee may have had against the host country or the obligor.” Disputes which might arise between M.I.G.A. as subrogee of an indemnified investor and a host country are expected to be settled by negotiation; if negotiations fail, the dispute may be submitted to conciliation and, ultimately, international arbitration. However, M.I.G.A. may agree with individual host countries on alternative dispute resolution mechanisms.

Consultative and Technical Assistance Programs

In addition to its guarantee operations, M.I.G.A. will conduct research on such issues as the factors determining investment flows and the effectiveness of investment incentive programs; help identify suitable investment opportunities and disseminate information on them to potential foreign investors (e.g. by setting up a data bank on investment opportunities and organizing investor missions to developing member governments on the design and efficient implementation of investment policies; organize consultations among member governments on experiences with particular investment policies and programs; and negotiate agreements on the treatment of guaranteed investments with interested member governments. Services will be provided to member governments at their request only. Guarantee operations and consultative/technical assistance activities are designed to be complementary and mutually supportive.

Institutional Structure and External Relations

M.I.G.A. will have full juridical personality and be both legally and financially independent from the World Bank and any other institution. Membership is open, on a voluntary basis, to all member states of the World Bank and Switzerland. M.I.G.A. will have a Council of Governors composed of one representative of each member country (and his alternate), a Board of Directors elected by the Council, and a President elected by the Board.

Its institutional autonomy notwithstanding, M.I.G.A. is directed to complement the activities of other international financial institutions, especially the World Bank and the International Finance Corporation (I.F.C.), and to co-operate with these institutions on technical and administrative matters. To facilitate this co-operation, the President of the World Bank will ex officio be Chairman of M.I.G.A.’s Board of Directors and in this capacity nominate its President.
M.I.G.A. is designed to complement the operations of national investment guarantee programs of member countries, of regional investment guarantee programs the majority of whose capital is owned by member countries (such as the Inter-Arab Investment Guarantee Corporation), and of private political risk insurers. It shall seek these insurance operators’ cooperation and is authorized to enter with them into arrangements on administrative cooperation, as well as co-insurance and reinsurance operations.

Financial Structure

M.I.G.A. is required to operate on a self-sustaining basis, i.e. to pay claims and meet other liabilities from premium income and other revenues such as returns on investment. In order to establish M.I.G.A. as a credible insurer, its guarantees will be backed by a share capital in the initially authorized amount of U.S. $1.082 billion and a “sponsorship trust fund.”

All member countries must subscribe to shares of M.I.G.A.'s capital, each in proportion to its relative economic strength as measured in accordance with its allocation of shares in the capital of the World Bank as of March 1, 1985. The subscriptions of countries that become members by April 30, 1988 are set out opposite their names in Schedule A to the Convention.

Ten per cent of the subscriptions must be paid in cash within three months of the effectiveness of the Convention with respect to the member country concerned. This 10 per cent must be paid in freely usable currency, except that developing member countries may pay up to 25 per cent of this 10 per cent in their own currencies. An additional 10 per cent will be paid in the form of non-negotiable, non-interest bearing promissory notes to be encashed by M.I.G.A. in the case of need only. The remainder of the subscribed capital will be subject to call in the unlikely event that M.I.G.A. is unable to meet its obligations from accumulated reserves or the encashment of the promissory notes.

The aggregate amount of guarantees which M.I.G.A. may issue is initially no more than one and one-half times its actually subscribed capital plus reserves and a portion of reinsurance coverage obtained. This risk-to-asset ratio may be increased up to a maximum of five-to-one.

Voting Structure

The voting system is designed to achieve equal voting power of capital-exporting (industrial) countries and capital-importing (developing) countries as groups. Each member country will receive 177 membership votes and one additional vote per share subscribed. This formula will establish voting parity between the two groups of countries when all member countries of the World Bank join. During M.I.G.A.’s first three years, each group of countries is assured a minimum of 40 per cent of the total voting power, by the allocation of supplementary votes if necessary. All decisions, during this initial period will require a special majority vote of at least two-thirds of the total voting power representing 55 per cent of the subscribed shares of M.I.G.A.’s capital stock. While the supplementary votes and the special majority requirements will be cancelled at the end of the three-year period, unsubscribed shares will then be reallocated so as to achieve voting parity of the two groups of countries on the basis of membership votes and subscription votes. Appropriate measures will be taken to enable developing member countries to subscribe to shares allocated to them.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

Comments on the draft Convention by Governments
(Japan and Spain)

GENERAL OBSERVATIONS

Japan

In order to facilitate the understanding of the provisions of this Convention, it would be advisable to divide the body of the text of the Convention into three parts: Articles 1 to 3 would be grouped under the heading of Chapter I, entitled “Sphere of application”, Articles 4 to 9 under the heading of Chapter II, entitled “Rights and duties of the parties” and Articles 10 and 11 under the heading of Chapter III, entitled “General provisions”, following the form of the text of the draft Convention on international financial leasing.

If, with regard to the draft Convention on international financial leasing, Chapter III is absorbed into Chapter I, following the model of the Geneva Agency Convention, it would be appropriate, with respect to the Convention on international factoring, to merge Chapter III as is proposed above into Chapter I for the sake of uniformity between the two Conventions. In that case, the title of a new Chapter I could be “Sphere of application and general provisions”.

Re Article 1 (1)(a)

Spain

The last part of this sub-paragraph could be drafted in an affirmative manner so as to contain an express reference to the professional nature of the contract governed by the Convention. The present wording is confusing for those countries which apply a double regime to private obligations and which moreover lay down special rules of a civil law character based on territorial considerations.

The confusion which could arise from the language contained in the draft could be avoided by replacing it by the following wording: “provided that they relate to goods bought for business purposes”.

Re Article 1 (1)(c)

Japan

The words “in writing” were added in paragraph 1(c) of Article 1 by the Unidroit committee of governmental experts (hereinafter referred to as “the committee”) at its third session in order to remove inconsistency between the said paragraph and paragraph 1(a) of Article 7. However, this addition has the effect of limiting the sphere of application of the Convention - under the present text, it does not apply to the case where a factoring contract does
not provide that notice of the assignment is to be given in writing even if notice of the assignment of the receivables is in fact given in writing to debtors. It is, therefore, proposed that the words "in writing" be deleted from paragraph 1(c) of Article 1.

If the words "in writing" were to be retained in paragraph 1(c) of Article 1 with a view to maintaining the above-mentioned consistency, the question arises as to why it is not necessary to add in paragraph 1(c) of Article 1 the same words "by the supplier or by the factor with the supplier’s authority" as in paragraph 1(a) of Article 7.

Re Article 1 (3)

Spain

The last part of this provision does not in general raise particular difficulties and it is generally speaking even desirable in the light of the constant increase in recourse to electronic means of communication in international trade.

However, the significant legal effect attributed to notice in writing to which Article 7, paragraph 1(a) of the draft refers – effectiveness of the assignment or transfer of the receivable, and creation of a duty for the debtor to pay a new creditor (the factor) – seems scarcely to be compatible with the absence of a signature in the notice.

Given the importance of the notice referred to in Article 7, paragraph 1(a), a signature should be required in such cases.

Re Article 3

Japan

Paragraph 3 of Article 3 provides that the application of this Convention may be excluded only as a whole. Some of the provisions of this Convention, however, may not be applicable in certain States, so that paragraph 3 of this article would lead to the limited number of the Contracting States to this Convention. It is therefore proposed that partial application of the Convention be allowed. Article 6 of the United Nations Convention on Contracts for the International Sale of Goods (hereinafter referred to as “the Vienna Sale Convention”) and Article 5 of the Convention on Agency in the International Sale of Goods (hereinafter referred to as “the Geneva Agency Convention”) for instance, making provision to this effect. It is further pointed out that even if paragraph 3 of Article 3 were to be retained as it is, only admitting the exclusion of the application of this Convention as a whole, the parties involved in factoring transactions could include selectively some of the provisions of this Convention in their contracts so as to obtain substantially the same result as would partial exclusion, if admitted, of the Convention, providing that the applicable law acknowledges party autonomy with regard to international factoring transactions.

If the Convention were to admit only the exclusion of its application as a whole, clarification would be needed with respect to the effects of the parties’ agreement to exclude some of the provisions of the Convention. Namely, is such agreement deemed to be valid as an agreement to exclude all the provisions of the Convention, or to be invalid because of the contravention of paragraph 3 of Article 3?
Re Article 6

Spain

Language to the following effect might be added at the end of the provision: “provided that it satisfies the relevant conditions as to form of the law of the principal place of business of the debtor”.

Wording of the kind proposed would ensure compliance with the rules requiring the drawing up of a public document or registration, which are to be found in many legal systems for the purpose of creating security interests in movable property which may be set up against third parties, for example reservation of title or pledges. It is doubtful whether, in the event of failure to respect the requirements of national law, courts would recognize the creation or the transfer of such security interests solely on the basis of the provisions of Article 6 of the Convention.

Re Article 7 (1)(a)

Spain

In conformity with what has already been suggested in connection with Article 1, paragraph 3, it is proposed to add the words “and signed” after the word “writing” contained in this provision.

Re Article 8

Japan

(1) Paragraph 1 of Article 8 says that the debtor may set up against the factor all defences of which the debtor could have availed himself under [a] contract of sale of goods if a claim for payment had been made by the supplier. In accordance with the provision, it is interpreted as follows: the debtor may not set up against the factor any defences which are not stipulated in a contract of sale of goods but of which, under the applicable law, the debtor could have availed himself concerning that contract. It is, therefore, proposed to replace the words “under that contract” by the words “concerning that contract”.

(2) The committee made an alteration to paragraph 2 of Article 8, substituting the words “any other defences, including any right of set-off” for the words “any right of set-off” at its third session. This alteration is explained, in paragraph 20 of the summary report of that session, as being of a purely drafting nature, resulting from terminological differences in British and American usage. However, it is not. There is a big difference in a grammatical sense between the old text and the new one; while in accordance with the latter it may be understood that there are defences other than right of set-off, it is highly doubtful that there are such defences, and thus the new text must be said to be misleading. It is, therefore, proposed that the old wording be reintroduced in paragraph 2 of Article 8.
Re Article 10

Japan

(1) It is proposed that the words “Articles 3 to 9” in paragraph 1(a) of Article 10 be replaced by the words “Articles 4 to 9”, since Article 3 is the former Article 11, which was not previously intended to apply to any subsequent assignment of the receivable.

(2) It is preferable that the words “an assignment” in paragraph 3 of Article 10 be replaced by the words “any subsequent assignment” in order to avoid any ambiguities in this paragraph.

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CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Comments on the draft Convention by Governments
(South Africa)

Re Article 1

1. 1 - Despite careful drafting, Article 1 is still drafted in such a way that it may include certain forms of receivable financing that cannot be described as factoring. The reason for this is that the continuous nature of factoring is not sufficiently reflected in Article 1. Most writers on factoring seem to agree that a transaction in terms of which a financier is obliged to make only a single advance against his client's receivables does not qualify as a factoring contract, the reason being that the element of continuity is absent. As Article 1 now stands, the Convention may be applicable to such a form of receivables financing. This point was made by the South African delegation at the third meeting (April 1987 in Rome) of the committee of governmental experts for the preparation of a draft Convention on international factoring. The feeling of the committee was, however, that continuity was sufficiently expressed by the word “contracts” in Article 1(a) and the description of the services provided by the factor in Article 1(b).

The word “contracts” in Article 1(a) is not an implied reference to continuity - at most it indicates that more than one receivable is to be assigned to the factor. Moreover, the services provided for in Article 1(b) are capable of being provided on a continuous basis or once only with reference to specific receivables. The mere description of the services provided by a factor is therefore not necessarily an implied reference to continuity. It is therefore submitted that some reference to continuity should be included in article 1(b).

1. 2 - It should be noted that no time-limit for the credit granted to the buyer under the sales contract to which the receivables relate is mentioned in the draft Convention. According to factoring practice the credit term of the sales contract varies between 14 and 180 days. As no term is fixed in the rules, it should be noted that receivables arising from sales contracts with far longer terms than 180 days could form the subject-matter of an international factoring
transaction. This could perhaps have the effect that the Convention will be applicable to some forms of "forfeiting". (Forfeiting is concerned with accounts receivables deriving from sales of capital goods with credit terms of up to 7 years).

Re Article 2

It is recognised that the purpose of Article 2, paragraph 1(b) is to extend the scope of application of the Convention. The problem that might occur here is not only the fact that it might be costly to determine whether the mentioned contracts are both governed by the law of a contracting state, although this is serious enough in itself, it is furthermore the fact that it might lead to serious misconceptions by parties to the various contracts as to the applicable law.

To illustrate this point, the following example may be set:

A and B want to enter into a factoring agreement. A is doing business in a contracting state and B in a non-contracting state. If A determines the applicable law according to rules of the conflict of laws applicable in his country he might come to the conclusion that the contract is governed by the law of his own country. B may, in accordance with the rules of the conflict of laws in his country, come to the opposite conclusion. The question is then simply which view would prevail. To compound the problem it might conceivably happen that A and B enter into the contract and only afterwards realise that they must determine which country's laws are applicable in order to decide whether the Convention apply or not. It will distinctly be a catch 22 situation. In order to avoid this it is suggested that this article be amended as follows:

The renumbering of paragraph 2 as paragraph 2(a) and the insertion after paragraph 2(a) of a new paragraph 2(b). Paragraph 2(b) will then read as follows:

"2(b). For the purpose of this article the rules of the conflict of laws applicable in Italy shall be used to determine whether a contract of sale or a factoring contract is governed by the law of a Contracting State".

The choice of Italy is based thereupon for conformity and that Unidroit is based there but by the same token it could be another country.

Re Article 4

The third part of Article 4 does not make sense in legal systems such as the South African and German legal systems where a clear distinction is made between an agreement creating rights and obligations (i.e. a contract or an obligatory agreement) and an agreement whereby rights are transferred (i.e. a real agreement e.g. an agreement of cession). The third part of Article 4 provides that "a provision in a factoring contract by which future receivables are assigned operates to transfer...". According to South African law a factoring contract cannot as a contract operate to transfer a right (receivable) – at most it can create an obligation to transfer a receivable. The only possible interpretation that can be given to this part of Article 4 is that the supplier will commit a breach of contract if he attempts to collect from the debtor or cedes the receivables to someone else before an agreement of cession is in fact concluded between the supplier and the factor. Although this is acceptable from a South African perspective it is doubtful whether this result was intended when the article was drafted.
The effect that was intended with Article 4 can best be understood if viewed from an Anglo-American perspective. In English and American law there is no distinction between an agreement that creates rights (a contract) and an agreement by which rights are transferred (also called a contract). A provision in a factoring contract for the assignment of receivables therefore is an assignment of receivables (provided, of course, that the other requirements for an assignment are met). It is not necessary to enter into another agreement for the transfer of the receivables. In English law a “contractual provision” could therefore have the effect to transfer a receivable. Article 4 makes such a transfer effective “as between the parties to the factoring contract” when the receivables “come into existence without the need for any new act of transfer”. The official commentary on Article 4 by the Unidroit Secretariat makes it clear that the intention of the last part of the article is to clarify the time from which the factor will be entitled to the rights (receivables) ceded to him (cf. Unidroit Study LVIII - Doc. 25, p. 16).

This object of the article could only be realised in legal systems such as the South African legal system if it is made clear that Article 4 deals with the agreement of cession (the transfer agreement). It is therefore submitted that the words “a contractual provision” in Article 4(a) and the words “a provision in the factoring contract” be replaced by the words “an agreement”.

Re Article 8

Article 8 embodies the rule common to virtually all legal systems that an assignment cannot place the debtor in a worse position vis-à-vis the assignee than that in which he would have been as regards the assignor.

Article 8, paragraph 2 is intended to deal with the question of the debtor’s exercise against the factor (assignee) of rights of set-off he may have against the supplier (assignor). Such rights of set-off are also recognised in South African law (cf. Scott, The Law of Cession, 67 ff). However, Article 8, paragraph 2 creates the impression that defences and claims other than those mentioned in Article 8, paragraph 1 and those raised by way of set-off may be raised in terms of Article 8, paragraph 2. It is submitted that Article 8, paragraph 2 should be amended to read as follows:

“2. The debtor may, subject to the provisions of paragraph 1, assert against the factor other defences, including but not limited to any right of set-off, existing and enforceable against the supplier in whose favour the receivable arose, and available to the debtor at the time the debtor received a notice of assignment conforming to Article 7 of this Convention”.

Alternatively, if the above amendment is not acceptable, consideration should be given to have the words “and enforceable” inserted after the word “existing” in Article 8, paragraph 2. The reason for this amendment is that a contingent claim is an existing claim according to South African law but not an enforceable claim capable of set-off against another claim.

Re Article 9

Inherent in Article 9 are certain difficulties for factors which might well be prohibitive. International factoring implies that in certain instances supplier and factor will not do business in the same country. To expect a factor to guarantee the proper performance of a contract by a supplier, especially in view of the substantial sums of money involved, is rather extraordinary.
It could not be expected of a factor whose business is finance to carry the risk for proper performance by a supplier.

While it is generally accepted that a debtor is entitled to raise all defences against the cessionary that would have been available if it was the cedent who claimed from him, it cannot be said that claims (as opposed to defences) available against the cedent are available against the cessionary. Article 9, paragraph 1 embodies the rule that the cessionary generally does not incur liabilities to the debtor. This rule also forms part of South African law as part of the principle that only rights (and not obligations) are transferred by cession (cf. Van Zyl v. Credit Corporation of SA, 1960 4 SA 582 (A)). The debtor would therefore, in the circumstances outlined in Article 9, paragraph 1, have to content himself with an action against the supplier (cedent). This rule seems to be equitable as there is no reason why the cessionary should guarantee the cedent’s performance.

In some legal systems a debtor who has made payment to the creditor would in the absence of cession have two remedies available against the creditor if the creditor did not properly perform his obligations i.e. one for damages and the other for the recovery of the price. The fact that payment was made to a cessionary (factor) after assignment would deprive the debtor of the possibility of bringing an action for recovery against the creditor (supplier) because it was not the latter to whom he had made payment. In these legal systems the debtor’s position would therefore be worsened by the assignment. Article 9, paragraph 2 represents an attempt to accommodate those legal systems.

However, Article 9, paragraph 2 is in conflict with South African law. According to South African law the debtor’s position would not be prejudiced in the circumstances outlined above because he would retain his right of bringing an action against the cedent (supplier) for the recovery of the purchase price (cf. Van Zyl v. Credit Corporation of SA, 1960 4 SA 582 A). Article 9, paragraph 2 is in conflict with the principle that only rights are transferred by assignment and is not therefore acceptable from a South African perspective.

The practical problems caused by Article 9, paragraph 2 are such that this article needs to be amended either by further limiting the debtor’s right of recourse or preferably by deleting paragraph 2 in toto.

Re Article 10

Provisions dealing with subsequent assignments by the factor

Goode (“The Legal Aspects of International Factoring”: Factoring-Handbuch edited by Hagenmüller and Sommer) describes an international factoring transaction as follows:

“An international factoring transaction is characterised by the fact that the debtor D carries on business abroad, so that the supply transaction involves the export of goods or services by S to D. As in a domestic transaction, S transfers the debt to a factor in his own country, who may proceed to notify D of the assignment and get in the debt directly, but usually finds it more convenient to pass the debt on to another factor in D’s country. The first factor is known as the export factor (EF), the second the import factor (IF). EF may assign receivables to IF for collection only, the risk of non-payment remaining with EF or S, or may sell on a non-recourse basis in which event the risk of non-payment is carried
by IF, within the limits of the agreement between the parties”.

From the above description of an international transaction it should be clear that in most cases it is made possible by a further assignment of the receivables by the export factor to the import factor. The object of Article 10, paragraph 1 is merely to make the provisions of the Convention applicable to such subsequent assignments.

In practice the supplier often gives notice to the debtor that he must make payment to a person who is in fact a subsequent assignee while no notice of the first assignment was given. Article 10, paragraph 2 is an attempt to prevent the subsequent assignment being invalid merely because no notice was given of the first assignment. Article 10, paragraph 2 is acceptable as it facilitates international factoring without affecting the interests of debtors.

Article 10, paragraph 3 was introduced at the request of a delegation of a socialist country which explained that its own country’s legal system did not permit subsequent assignments and that effect should therefore be given, under the terms of the Convention, to prohibition on subsequent assignments contained in factoring contracts. Article 10, paragraph 3 attempts to do this by providing that the Convention would not be applicable to subsequent assignments that are prohibited by factoring contracts. It is submitted that Article 10, paragraph 3 is inconsistent with the general approach of Article 5. For the sake of consistency it should perhaps not be included in the Convention.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

Comments on the draft Convention by Governments
(United States of America)

GENERAL OBSERVATIONS

We believe that the purposes of the Convention are worthwhile and reflect a positive attitude in unifying private international law for a relatively new mechensim for financing international trade in which there are sometimes drastic differences in the laws of different nations. The United States is a nation which has a relatively unified statutory framework governing the rights of the various parties affected by the financing and factoring of accounts receivable in the Uniform Commercial Code in effect in the states of the United States for the last 20 years.

SPECIFIC OBSERVATIONS AND RECOMMENDATIONS

Re Article 1

Sub-paragraph (c) of paragraph 1 should be amended to clarify that the required notice of assignment need not be given only at the time of execution of a contract or creation of a
receivable, but may also be given at a later date, as follows:

“(c) notice of the assignment of the receivables is to be given to debtors pursuant to the factoring contract in writing at any time by the supplier or the factor.”

Article 1 should also be clarified to indicate that there may be more than one factor of a supplier by adding:

“4. - This Convention shall also apply when the supplier has concluded factoring contracts with more than one factor.”

Re Article 4

The provisions of Article 4 as to a factoring contract should be binding upon third parties, in order to give a greater degree of certainty to the effect of the factoring and financing relationship, unless there is a specific rule of domestic law to the contrary which governs under the applicable rules of private international law. Moreover, under Article 7, the debtor is in effect bound by Article 4, subject to the additional requirements of Article 7. Accordingly, an additional paragraph (c) should be added to Article 4 as follows:

“(c) The provisions of subparagraphs (a) and (b) of this Article shall also be effective as to third parties unless such provisions are not enforceable as to such third parties under other Articles of this Convention or the domestic law applicable under the rules of private international law.”

Re Article 5

The first paragraph of Article 5, on the prohibition of enforcement against the factor of a non-assignability agreement between the debtor and the supplier, applies only to the prohibition of assignments of rights of payment due to the supplier from the debtor and does not apply to performance under the sales contract. This concept protects the factor against the need to review each sales contract of the supplier for prohibitions on assignment. It also enables the supplier, who may have less economic bargaining power than the debtor, to obtain financing or factoring of the receivable without obtaining the debtor’s consent or granting concessions to the debtor in exchange for such consent.

Absent paragraph 1 of Article 5, the factor would either need to rely upon a representation of the supplier (which may have limited financial resources to satisfy any breach of warranty claim) or examine each of the supplier’s sales contracts, which may be in a foreign language, and unreasonably delay the consummation of the transaction. Even if the prohibition on assignment is not effective, the debtor is still protected by Article 8, (which permits set-off of claims existing at the time of notification of the assignment) and Article 3 (which permits the complete exclusion of the Convention under a sales contract upon notice to the factor, except as to receivables arising prior to such notice). In addition, the debtor would retain its claims against the supplier for any damages suffered as a result of the breach of the non-assignability provision.

The enactment in the United States more than twenty years ago of the Uniform Commercial Code rendering ineffective prohibitions on assignments of rights to payment, which overruled
the then existing laws of states such as New York, has not resulted in any inequities or demands for its revocation in the United States.

The opponents of Article 5 at the third session of the committee of governmental experts argued that it was in contravention of freedom of contract, but this argument seemingly begs the issues that (a) the prohibition on assignment is often inserted because the debtor has greater economic leverage than the supplier, (b) rendering the prohibition ineffective as to rights of payment does not violate any rights of the debtor if the supplier has performed its obligations or the debtor has a right of set-off for damages resulting from non-performance of such obligations, and (c) from a practical and operational viewpoint, the continued validity of such non-assignability provisions will severely impede the growth of international factoring.

The prohibition on assignment provides an unfair economic disadvantage to States that have laws or that otherwise make prohibitions on assignments invalid as to debtors located within its border as against States that have not accepted this rule. The financing of imports into these “accepting nations” is facilitated by these laws and rules. On the other hand, the financing of exports from “accepting nations” is discouraged if the debtor is located in a nation in which possible prohibitions on assignments of payments under the sales contract are valid. Examining all of the supplier’s sales contracts, often in a foreign language, is not a realistic solution for the factor.

For the above reasons, inclusion of the reservation in paragraph 2 of Article 5 would derogate from the purposes of the Preamble and the uniformity of law which is a primary purpose of the Convention.

However, since there appears to be a good deal of support for the reservation in paragraph 2 from other Unidroit member States, a compromise might be the clarification of paragraph 2 as set forth below, plus the addition of a new paragraph 3, which tracks the virtually similar provisions of Article 55 of 1983 Revisions of Uniform Customs and Practices for Documentary Credits (the “U.C.P.”) with respect to non-transferable letters of credit:

"2. - However, such an assignment shall not be effective against the debtor when:

(a) There is a written agreement between the supplier and the debtor prohibiting such assignment, and

(b) The debtor has his place of business, at the time of the contract of sale of goods from which such receivable arises, in a Contracting State which has made a declaration under Article X of this Convention.

3. - The fact that an assignment of a receivable is not effective under paragraph 2 of this Article shall not affect the supplier’s rights to assign to the factor any proceeds to which he may be, or may become, entitled in connection with such receivable in accordance with the provisions of applicable law."

Re Article 7

Paragraph 1(a) of Article 7 should be clarified to indicate that the notice of assignment must be received by the debtor. In some States a requirement that a notice is “given” may mean only that the notice must be transmitted and not that the notice must be received by the person to whom it is addressed.
It would be manifestly unfair to a debtor to require payment to a factor pursuant to a notice of assignment which the debtor has not received.

Accordingly, paragraph 1(a) of Article 7 should read:

“(a) is received by the debtor in writing from the supplier or from the factor with the supplier's authority;”.

Re Article 9

Paragraph 1 of this Article should be clarified to indicate that the claim of the debtor which may not be asserted against the factor would be for recovery of any excess payment and not necessarily for the entire price of the goods under the contract of sale. Accordingly, the United States recommends that paragraph 1 be amended as follows:

“1. Without prejudice to the debtor's rights under Article 8 of this Convention, non-performance or defective or late performance or other breach of the contract of sale by the supplier shall not alone entitle the debtor to recover from the factor money paid by the debtor to the factor if the debtor has a claim against the supplier for recovery of such money.”

In addition, since a factoring contract under the Convention may be one which provides not only for payments of the purchase price of receivables but also a financing agreement providing for advances to the supplier with recourse (i.e. with the assigned receivables as security), paragraph 2 should be revised as follows:

“2. The debtor who has such a valid claim against the supplier shall nevertheless be entitled to recover money paid to the supplier's factor for the goods under the contract of sale:

(a) to the extent that the factor has an outstanding obligation to make future payments to the supplier under the factoring contract; or

(b) to the extent that the factor made payments to the supplier under the factoring contract after receiving such money from the debtor and with knowledge by the factor of the debtor's claim at the time of such payment to the supplier.”

Additional Article on Priorities

A major omission in the scope of the Convention is the failure to enunciate any substantive rule or even a conflicts rule on priorities between or among competing claims to the supplier's accounts receivable.

In this regard, paragraph 10 of the Explanatory Notes on the draft Convention prepared by the Unidroit Secretariat noted "the widely expressed regret that the Convention failed to regulate an aspect of the question which created very great difficulties at an international level". This omission was particularly emphasized by the United States at the third session and, among others, by Japan in its written comments.

The committee suggested at the end of the third session that the issues relating to an additional Article in the Convention on priorities be deferred until the diplomatic Conference.
The United States recommends that a new Article be added to the Convention relating to priorities as set forth below.

Generally, conflicting claims to a receivable will arise upon the supplier’s insolvency. These competing claims will generally fall into the following categories:

(a) Multiple assignees of the same receivables by the supplier (“voluntary assignees”) either as security or by sale. Although it has been commented that “non-notification” factoring does not fall within the scope of the Convention by virtue of the notice requirement of Article 1, this is not completely correct. The voluntary assignee may initially not notify debtors to make payment pursuant to Article 7, but at a later date by agreement or after default by the supplier, such notification may be delivered to the debtor. At that point, the assignment may become a “factoring contract” as defined in Article 1.

For example, under the Uniform Commercial Code, the voluntary assignee may at any time by agreement with the supplier, and in any event upon default, notify the debtor of the assignment. Thus, when a “non-notification” factor enforces its rights under its agreement, its contract becomes a “factoring contract” as defined in Article 1 if two of the other functions required under Article 1, paragraph 1(b), are provided in the factoring contract. The “finance” condition will almost invariably be met because the factor would have no incentive to claim an interest in the receivable if it had not advanced funds to the supplier. Thus, if any one of the other functions is present, the “non-notification” factor would then be within the scope of the Convention. Accordingly, each of the competing voluntary assignees at the time when the dispute on priority arises (generally when the supplier becomes insolvent) will in all probability be within the scope of the Convention.

(b) Creditors of the supplier having claims or judgment or other involuntary liens against receivables of the supplier under domestic law or applicable rules of private international law (“involuntary claims”).

(c) Claims of bankruptcy trustees, receivers and the like who take control of the supplier and its assets under substantive applicable domestic law (“trustee’s claims”).

(d) Tax liens and other claims of Governments against the supplier and its assets under applicable law (“Government claims”).

As to the priority of involuntary claims, trustee’s claims and government claims vis-à-vis the rights of the factor in the supplier’s receivables, valid policy arguments can be made that these issues should be resolved under applicable substantive laws and conflict of law rules of the State in which the supplier is located.

However, there is no valid reason why the substantive priorities between or among voluntary assignees in the supplier’s receivables should not be determined by the Convention, particularly since their agreement with the supplier and in relation to the debtor in other respects are subject to the Convention.

The issue then arises as to what substantive rule of priority should govern when the supplier has more than one voluntary assignee of the same receivable, subject to any agreement as to priority between such voluntary assignees.

Obviously, reliance upon representatives by the supplier are not sufficient as the supplier
will often be insolvent when the priority issues arise. Even without international “double assignments” by the supplier, the supplier may have executed or granted two or more assignments in the same receivable without being aware of their conflict, (e.g. when the supplier has a factor for domestic sales, a factor for foreign sales and another creditor which has been granted a security interest in its inventory and the proceeds thereof).

The method for determining priority among voluntary assignees should provide a means for determining whether there has been a prior assignment. The easiest and most expeditious method is by a public filing or recording system in the State in which the supplier is located, which is the system recognized in the 1948 Geneva Convention on the International Recognition of Rights in Aircraft, which has been adopted by more than forty States. At present, Canada and the United States have such public filing systems which govern the priority of competing assignments of receivables under factoring contracts.

Each factor under a public recording or filing system can determine the priority of its assignments of receivables from a supplier by means of a search of the public filing or recording records in the State where the supplier is located.

Accordingly, where the supplier is located in a State which has such filing or recording system, the order of priority should be determined by priority in time of recordation or filing.

In the absence of a public filing or recording system in the State in which the supplier is located, the order of notice to the debtor offers an alternative (although less desirable) means of determining priority.

In addition, the notice of assignment to the debtor is a key aspect of the Convention. The notice is required for a factoring contract to be subject to the Convention under Article 1, paragraph 1(c). The notice of assignment is necessary for the debtor’s obligation to pay the factor under Article 7. The notice of assignment also cuts off the debtor’s right of set-off under Article 7, paragraph 2.

Therefore, when there is no contrary agreement among factors or where the supplier is not located in a State which has a public recording or filing system, priority of conflicting assignments to voluntary assignees in the same receivables should be determined in the order of notification to the debtor.

For the reasons indicated above, the United States recommends that the following Article be added to the Convention:

**Article Z - Priorities**

‘1. - Priority in receivables due from a debtor, including the proceeds thereof, and assigned by a supplier to more than one factor under more than one factoring contract shall be determined either by mutual agreement of such factors or, in the absence of such mutual agreement, as follows:

(a) if the supplier’s place of business is located in a Contracting State which provides for the recordation or filing in a public office in such State of such assignment or notice thereof, priority shall rank according to priority in time of such recordation or filing in such public office; or
(b) if there is no such recordation or filing by any factor in such public office or if the supplier’s place of business is located in a Contracting State which does not provide for such recordation or filing, priority shall rank according to priority in time of the notice to the debtor conforming to Article 7 of this Convention.”

One of the principal requirements of an orderly credit system is that the legal consequences of a particular credit transaction can be reliably anticipated. It has long been recognized that the use of international factoring would be impeded unless there is a means of determining the law of which State determines the priority of the factor's and third parties' rights in the receivables due from a debtor. See Pfar, Legal Aspects of International Factoring, 25 Business Lawyer 1505 (1970).

Accordingly, it is also desirable that a general conflicts rule be established for determining the applicable law governing the competing claims of factors and third parties to receivables due from a debtor.

Since payments of the receivables due from the debtor are made from the State in which the debtor has its place of business and the debtor would only make payment in accordance with the law of that State, the United States recommends that a second paragraph be added to the new Article on priorities as follows:

“2. - As between an assignment of a receivable by the supplier to a factor and conflicting claims to the same receivables of other persons who are not factors, the law (including the conflict of law rules) of the Contracting State in which the debtor's place of business is located governs the priority of the rights of the factor and such other persons to such receivable. Such conflicting claims of other persons may arise, without limitation, under applicable taxation, bankruptcy, insolvency, force majeure, employment, judgment, debtor and creditor, lien or similar laws, statutes or government regulations.”
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Comments on the draft Convention by international Organisations
(Hague Conference on Private International Law)

With a view to the diplomatic Conference for the adoption of the draft Unidroit Conventions on international factoring and international financial leasing, to be held in Ottawa (Canada) from 9 to 28 May 1988 and pursuant to the President of Unidroit’s letter of 14 December 1987 to the Secretary-General of the Hague Conference on Private International Law, the Permanent Bureau of the latter Organisation hereunder submits comments relating to two problems arising in both the draft Convention on international factoring and the draft Convention on international financial leasing, problems which have not apparently been sufficiently examined during the various sessions of the two Unidroit committees of governmental experts. One problem concerns the reservation to the geographical sphere of application of the two draft Conventions, the other whether or not the parties to the contract should be able to derogate, wholly or partly, from the provisions of the future Conventions.

Re Article F
Reservation to the geographical sphere of application

In both sets of draft final provisions drawn up by the Unidroit Secretariat is to be found an Article F which would authorise any Contracting State to declare that it will not be bound by Article 2 (1)(b).

In the supporting notes to this Article F, the Unidroit Secretariat simply recalls that an identical reservation clause is to be found in the Vienna Convention on the International Sale of Goods (Article 95) and in the Geneva Convention on Agency in the International Sale of Goods (Article 28), without providing any reason for adopting a similar reservation in the prospective Conventions on international factoring and international financial leasing. In effect, this reservation problem was never discussed in any depth at the sessions of the Unidroit committees of governmental experts and it would indeed appear that this reservation is included in these draft final provisions solely to ensure that these texts are aligned on the Vienna and Geneva Conventions.

While there can be no gainsaying the desirability of two or more international instruments, dealing with relatively identical subject-matters (in the case in point, what is identical is the contractual nature of the relationships addressed), being harmonised from the point of view of their textual presentation and in particular employing similar concepts and definitions, one should be on one’s guard not to sacrifice the coherence of a text, and in particular the sphere of application of a Convention, for the mere sake of one text being absolutely aligned on
another; in other words, to be specific it would be regrettable were the fact of seeking to align the reservation to the geographical sphere of application of the future Conventions on the Vienna and Geneva Conventions adversely to affect the balance and structure of the future Conventions. In this regard it is the opinion of the Permanent Bureau of the Hague Conference that purely and simply to repeat the reservation permitted under the Vienna and Geneva Conventions in the two draft Conventions could well have unexpected consequences which might jeopardise widespread application of the future Conventions and create delicate problems in practice, above all for leasing and factoring companies.

It should first of all be borne in mind that the reservation contained in Article 95 was adopted in the Vienna Convention at the request of certain delegations that did not want the judges of their countries to be obliged to apply the Vienna Convention where their conflict rules would lead to their own law being found to be applicable to a given sale contract. Thus the effect of Article 95 of the Vienna Convention for a State having availed itself of this reservation would be simply that where the conflicts rule of the judge of this State leads to the application of this judge’s own substantive law, then “he will not be bound” by Article 1 (1) (b) of the Convention. On this interpretation (an interpretation which is not shared by everybody), the reservation contained in Article 95 of the Vienna Convention (and the same of course is true for Article 28 of the Geneva Convention) has an application that is limited to the State availing itself of this reservation and moreover does not affect the normal operation of the conditions for the application of the Convention (Article 1) in other States.

The same is, however, not true for the draft Conventions on international factoring and international financial leasing, chiefly by virtue of the tripartite legal relationship covered by each of these two drafts. Two examples will help to bring out the difficulties which the adoption of Article F in the two Conventions would cause:

Let us take the case of the lessor’s place of business being located in State A, a Party to the future Convention, the lessee’s place of business in State B, also a Party to the future Convention and the supplier’s place of business in State C, which is not a Party to the Convention. In this case the future Convention on international financial leasing would not be applicable by virtue of Article 2 (1)(a), because the three parties to the legal relationship do not all have their place of business in a Contracting State. Let us now take the two following cases:

*Case I*

The leasing agreement is subject either to the law of A or to the law of B, both States Parties to the Convention. The supply agreement is subject to the law of A, either because the parties to the agreement have so decided (freedom of contract) or because the objective conflict rules of State A lead to the application of the law of this State. State A has availed itself of the reservation permitted under Article F. Is it reasonable in this case for the judges of State A, or indeed for that matter for the judges of State B, to be authorised not to apply the Convention, whereas the main agreement in the triangular relationship, the leasing agreement, was concluded between two parties whose places of business are both located in Contracting States, which is the fundamental requirement for the geographical application of the Convention, in so far as it is set forth in the opening words (the *chapeau*) of Article 2 (1) and whereas the parties to the supply agreement have expressly chosen the law of State A as the law to apply to their agreement so as to fall in line with the requirements of Article 2(1)(b)?
Case II

The leasing agreement is still subject either to the law of State A or to the law of State B but the supply agreement is subject to the law of State D (this could, for instance, be the State in which the leased equipment is to be used); State D is a Party to the Convention but has availed itself of the reservation permitted under Article F:

(a) Will the judges of State A be precluded from applying the Convention to the leasing agreement on the pretext that State D has availed itself of the reservation permitted under Article F?

(b) Is it again reasonable for the judges of State D to be allowed not to apply the Convention to relations between the lessor and the lessee, whereas that is what the parties expect and whereas, moreover, State D has introduced the rules embodied in the Convention on international financial leasing into its legal system?

These two examples (however, one could well imagine others) show that the reservation permitted under Article F in both draft Conventions has consequences which go well beyond those found in the Vienna Convention. In particular, Article F would have the effect of enabling one State to paralyse the operation of the Convention for the whole triangular relationship, even when the main agreement, the leasing agreement, is concluded between two parties whose places of business are situated in States which have not availed themselves of the reservation; this extraterritorial effect of a reservation has an element of exorbitance which would seem difficult to reconcile with the general principles of the law of treaties.

The Permanent Bureau feels that the inclusion of Article F in the two draft Conventions is all the more regrettable in so far as the geographical sphere of application of both Conventions is already extremely narrow, since it requires either that the places of business of all three parties to the triangular relationship be situated in Contracting States or that the leasing (or factoring) agreement and the supply (or sale) agreement be governed by the law of a Contracting State. To narrow still further this already narrow sphere of application by giving one of the States Parties to the Convention unilaterally the possibility to make a declaration leads one to doubt the usefulness of the attempt at unification undertaken by Unidroit in the field of international financial leasing and in that of international factoring. The Permanent Bureau would suggest that Article F be deleted or, at the very least, if there is a State that truly cannot manage without such a reservation, that its effects be strictly limited to within the State that avails itself of the reservation.

Re Article 14 of the draft Convention on international financial leasing/
Article 3 of the draft Convention on international factoring

Option for the parties to exclude the Convention
as a whole or in part

Article 14 of the draft Convention on international financial leasing and Article 3 of the draft Convention on international factoring each give the parties to the contract the opportunity to exclude the application of the Convention in a manner which is truly paradoxical.
Article 14 of the leasing draft seems in effect to leave open to the parties the option either to exclude the application of the Convention as a whole or to vary, depending on their needs, certain provisions of the Convention, although in this case with the exception of certain key articles from which the parties may not derogate. Article 3 of the factoring draft offers the same alternative, albeit formulated in a different way.

This approach is unusual and would not appear to be satisfactory. Of the two possibilities:

- either the parties should be authorised to exclude the Convention as a whole or to derogate from any of its provisions whatsoever (this is the system adopted in Article 6 of the Vienna Convention on the International Sale of Goods);

- or the parties should be either wholly or partly prohibited from derogating from the provisions of a Convention, which then implies that they should not be allowed to exclude the Convention as a whole (this is the system generally employed in international transport Conventions).

However, to adopt in a Convention an article which would give the parties both possibilities is illogical and results in an impasse: what attitude should judges take if the parties to the contract decide, at first, to exclude the Convention as a whole and then, subsequently, to include the provisions of the Convention in their contract, while varying the key provisions of the Convention, that is those provisions from which the parties are not entitled to derogate?

To be sure, the problem in both draft Conventions derives from the fact that they both address a triangular relationship: in fact it would appear difficult to accept that two parties to the contract may vary provisions of the Convention concerning a third party or the articles affecting the rights of third parties. In view of the fact that we are in a contractual situation and that accordingly the parties’ freedom of contract should be respected, it is suggested that Article 14 of the leasing draft and Article 3 of the factoring draft should be redrafted along the following lines:

“...In their relations with each other [alone], the lessor (the supplier) and the lessee (the factor), on the one hand, and the lessor (the supplier) and the supplier (the debtor), on the other, may exclude the application of this Convention or derogate from or vary the effect of any of its provisions.”
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the United Kingdom Delegation

SEQUENCE OF THE ARTICLES OF THE FINANCIAL LEASING CONVENTION

1. - The present draft distributes across the Convention provisions relating to its scope - in particular, Articles 1-3, 13 and 14. In the view of the U.K. these provisions should be brought together in Chapter I. In addition, it is noted that provisions relating to the transactional scope of the Convention (Articles 1 and 3) are separated by a provision (Article 2) embodying the connecting factors.

2. - The U.K. therefore proposes:

(i) to bring Article 3 forward to become Article 1(3), and renumber Article 1(3) as Article 1(4);
(ii) to bring Article 13 forward to become Article 2, and renumber Article 2 as Article 3;
(iii) to bring forward Article 14 as Article 4;
(iv) to renumber Articles 4-12 as Articles 5-13, and Article 15 as Article 14, and make such other consequential amendments as are necessary.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Swedish Delegation

The Swedish delegation proposes the following amendments to Articles 1-3 of the draft Convention on international financial leasing, namely that in:

204
Article 1

- paragraph 1, the words "financial leasing" be deleted from the introduction, to make it clear that it is of no importance what label the parties to the leasing contract put on that contract,
- paragraph 1, sub-paragraph (a), before the last word ("and") be inserted the words "or replaces the lessee in such an agreement", to cover a situation mentioned by the Government of Pakistan,
- paragraph 2, sub-paragraph (b), in the first line the words "by the lessor" be deleted, as a consequence of the amendment in paragraph 1, sub-paragraph (a),

Article 2

- paragraph 1, the last word of the chapeau ("when") be deleted, to make it clear that the requirement of the chapeau has to be completed by one of the requirements mentioned in sub-paragraphs (a) and (b), and

Article 3

- this article be relocated and renumbered Article 1, paragraph 3, thus making the present paragraph 3 ("This Convention ... household purposes") a new paragraph 4.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Finnish Delegation

Delete Article F.

COMMENTS

Reservations in respect to application of international private law rules in Conventions on commercial agreements are most problematic. Parties to the agreement should be able to know as easily as possible whether the Convention is applicable to their agreement or not. Finding out which countries have made the suggested reservation as to the applicability of the Convention may prove to be very difficult in practice. In the tripartite relationship of the leasing transaction this is even more true. Furthermore, in a leasing transaction the consequences of such a reservation may be most undesirable.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposals by the United States Delegation

Article 1 - Paragraph 3

1987 TEXT

"3. - This Convention does not apply to a transaction in which the equipment is to be used primarily for the lessee's personal, family or household purposes."

PROPOSED REVISIONS
(changes indicated in italics)

"3. - This Convention does not apply to a transaction in which the equipment is to be used primarily for the lessee's personal, family or household purposes, unless the lessor, at any time before or at the conclusion of the leasing agreement, neither knew nor ought to have known that the equipment was to be used by the lessee primarily for any such purposes."

PROPOSED REVISIONS
(changes not indicated)

"3. - This Convention does not apply to a transaction in which the equipment is to be used primarily for the lessee's personal, family or household purposes, unless the lessor, at any time before or at the conclusion of the leasing agreement, neither knew nor ought to have known that the equipment was to be used by the lessee primarily for any such purposes."

REASONS FOR PROPOSED REVISIONS


2. - The present text literally provides that it is the prospective use, in fact, which determines the applicability of the Convention. Presumably, the lessee's intentions might control, even though the lessor did not know, and ought not to have known, about the lessee's intended use. The principal problems with this test are ameliorated by the proposed revisions.
Article 1 - Proposed New Paragraph

"[4].- This Convention shall not cease to apply merely because the equipment may have become a fixture to or incorporated in land."

REASONS FOR PROPOSED REVISIONS

1. - Article 6 appears to contemplate that property which is the subject of a leasing transaction may "become a fixture to or incorporated in land." The implication is that such property may be subject to the Convention, but the present draft does not explicitly so state. Article 1 ought to be modified so as to state expressly what is so contemplated by Article 6.

2. - It should be emphasised that under Article 6 the question of whether goods have become fixtures and the rights as between a lessor and a landowner (or other person with real rights in the land) are left to the law of the State where the land is situated and are not governed by the Convention.

CONF. 7/C.1/W.P. 5
9 May 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Position paper submitted by the Comité Maritime International

1. - The C.M.I. is grateful to have been invited to send an observer to the Diplomatic Conference in Ottawa on the draft Unidroit Convention on International Financial Leasing and wishes to declare its willingness to co-operate on this matter.

The draft Convention has been studied by a working group within C.M.I. which submitted a report to the annual Assembly of the C.M.I. in April 1988. On the basis of the discussion in the Assembly the following is submitted.

2. - The principal recommendation by the C.M.I. is to exclude ships from the Convention.

3. - Ships are in many respects subject to special regimes due to their special character. This is particularly true with respect to such matters that are regulated by the Convention, i.e. the relationship between owners and operators of ships, the relationship to creditors and the rights of creditors, the registration of ships for public and private law purposes, and the liability towards third parties of the various groups involved in the shipping industry. There is already a great number of Conventions in force on these matters. The draft Convention does not seem to be in harmony with these Conventions. Examples will be given below.

4. - Ships are let by owners to operators also in situations which would be governed by the draft Convention according to its Articles 1 and 2. However, the situation covered by the
draft Convention is just one type of ship financing and only one example of the great number of situations where ships are hired across borders. Chartering-out of ships is a very common thing and that is true also of bareboat chartering-out or charter by demise which in fact corresponds to leasing of ships. Only, an ordinary lease contract for equipment is a very much more simple document than a bareboat-charter and it would not be possible to lease a ship by simple reference to the draft Convention. Standard bareboat charters exist but in general leasing contracts of ships/bareboat charters are very comprehensive documents, often incorporating a standard bareboat charter.

It is not purposeful to have a Convention for the specific situation foreseen in Articles 1 and 2 of the draft Convention when most of the same problems arise in many other situations where ships are chartered out across borders. Only very few of the problems arising in the situation covered by the draft Convention are particular to that situation. Most of the problems arise also in other bareboat charter situations.

5. - It is particularly unfortunate to regulate a specific situation of bareboat chartering, i.e. that covered by the draft Convention, in view of the fact that bareboat charters generally are on the agenda of U.N.C.T.A.D. and will become subject to international discussion and regulation in the near future. It will be unfortunate if it should prove impossible then to regulate bareboat charters in general and necessary to make exception for those situations already covered by the draft Convention.

Conversely, the fact that States would wish to have a general regime applying to all types of bareboat charters might lead to the non-ratification of the draft Convention if it were to include ships. It would be a pity if the inclusion of ships in the draft Convention were to make it a dead letter, seeing that it is a worthwhile piece of international legislation in the central area of application, the leasing of equipment.

6. - It seems worth noting that other U.N. Conventions such as the Vienna Convention on the international sale of goods and the Convention on prescription expressly exclude ships from their scope of application.

7. - The view expressed by the C.M.I. was shared by the working group originally examining the feasibility of drafting a Convention on the leasing contract, cf. Study LIX-Doc. 48 p. 8. It recommended excluding the leasing of ships from the Convention because of the special nature of the contract involved, which was considered to have more in common with charterparties. This was confirmed by the next working group set up by the Governing Council, cf. op. cit., p. 11. The study group later set up reversed this decision, op. cit., p. 13, without, however, any argument being given for this change of position, and this view has been maintained with reference to the wish to ensure as broad a scope of application of the Convention as possible, although it is at the same time admitted that there is an undeniable difficulty in classifying ships in the same category as the general body of capital goods, cf. op. cit., p. 37.

8. - Some remarks shall now be made in respect of details of the draft Convention.

9. - Art. 2 delineates the scope of application of the draft Convention by reference to the place of business of the parties to the lease contract. However, the place of business of the parties is of little relevance in the shipping industry. Hitherto, the country of registration of the ship has been decisive, but particularly in the field of leasing/bareboat chartering new uncertainty
has been introduced in this respect, cf. infra. This underlines the particularity of leasing of ships and makes it difficult to fit them into the rule as to the scope of application of the draft Convention which is the natural rule in respect of lease contracts for ordinary equipment.

10. - Art. 5 has been redrafted in Conf. 7/5. It has been found necessary to include a number of provisions for the purpose of ships. That is true of Articles 5(3)(a),(4) and (5). The rule would be much simpler if ships were to be excluded from the draft Convention. It also seems rather extraordinary to try to regulate the very complicated problems of the protection of rights in ships in private international law by means of some exceptions from exceptions. It would be preferable as suggested by someone at the meeting on 29 February, 1988, cf. Conf. 7/5 p. 6, paragraph 12 in fine if ships are to be included in the Convention to exclude Article 5 altogether in relation to ships.

11. - In the original draft of Article 5 reference was made to the law of the registration of the ship. In the new draft reference is made to the law of the flag State. Formerly, either reference would refer to the same law. Now, however, particularly in respect of bareboat chartering, neither reference is unambiguous. Dual registrations, suspended registrations etc. in respect of bareboat chartered ships have been introduced in the legislation of a number of countries, and it has even become possible in some countries for a bareboat chartered ship during the time of the charter to fly the flag of the charterer rather than, or as an alternative to the flag of the owner. Reference is made to U.N.C.T.A.D. doc. JIGE (IV)/2-TD/B/C.4/AC.8/12. The situation becomes even more complex when it is remembered that the lessor need not be the owner but may be a bareboat charterer himself, even by several degrees, who charters the ship out under a bareboat charter, a situation which is covered by the draft Convention, cf. Article 13.

12. - Article 5(5) of the redraft seems in some cases to nullify Article 5(2). The lessor's right may in some legal systems be regarded as a security interest. It will then be unaffected by the rule requiring compliance with rules as to public notice, if it arises under a different legal system which is applicable to it.

13. - Article 7(1)(b) and (c) distinguishes between the lessor as lessor and the lessor as owner. That is, of course, possible in cases of sub-leases/sub-charterers. In other cases the distinction seems to be without merit. In maritime law some Conventions channel responsibility to the owner of the ship. That is true, e.g. in respect of oil pollution damage and damage by nuclear ships and may well be extended to other damage. In such cases it seems meaningless to relieve the owner of a responsibility in his capacity of lessor which he cannot avoid in his capacity of owner. As a minimum there ought to be a general provision in the Convention reserving other international Conventions along the lines of the redrafted Article 5(4).

14. - Article 14(1) and (2) seem to be contradictory. A choice must be made between them. In respect of ships, if they are included in the Convention, there ought at least to be a possibility for the parties to exclude the application of the Convention which means the adoption of Article 14(1). If ships are to be included in the Convention it would, however, be preferable if States ratifying the Convention were permitted to make a reservation to the effect that they would not apply it to ships.

15. - Whether Article 14(1) or (2) is chosen it seems strange that the parties may determine the relationship to third parties by their own agreement which is the result of either provision since several provisions of the draft Convention regulate that relationship.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Observations and proposals by the Delegation of the People’s Republic of China

GENERAL OBSERVATIONS

Regarding the draft Convention as a whole, certain progress was made in respect of the maintenance of a fair balance of interests among the different parties to international leasing transactions and technical points as compared with the previous draft completed at the second session of the committee of governmental experts. The People’s Republic of China remains of the view that the Draft Convention will facilitate the development of financial leasing transactions on a cross-border basis and eliminate legal obstacles in this respect. Despite the progress made, there still exists the possibility to bring the draft Convention closer to the nature and practices of the international financial leasing transactions it governs.

SPECIFIC OBSERVATIONS AND PROPOSALS

Article 1

Article 1, Section 1(b) is rather vague in language regarding the parties to the leasing agreement. It is desirable to add “with lessee” after “enter into an agreement (the leasing agreement)” in order to illustrate the parties to the leasing agreement.

Proposed revised text of Article 1, Section 1(b):

“(b) enters into an agreement (the leasing agreement) with a lessee granting to the latter the right to use the equipment in return for the payment of rentals.”

Article 7

There are two Alternatives in this Article dealing with the quiet possession problem. The People’s Republic of China believes that each of the two Alternatives is intended to protect the lessee against any third party in the disturbance of its quiet possession of the equipment. Alternative I is more adequate to serve this purpose.

In a financial leasing transaction as may be governed by the present draft Convention, the most substantial interest of the lessee is to use the equipment within the duration of, and in conformity with the terms stipulated by the leasing agreement. Within such a duration, the lessor remains the owner of the leased equipment and consequently should be held responsible
for any disturbance by any third party relating to the quiet possession by the lessee of the equipment. To some extent, the lessor shall warrant to the lessee that his quiet possession is absolute and not subject to any conditions. Alternative I seems more appropriate regarding this.

Article 10

The provisions of Article 10 provided one of the major debating issues in preparing the draft Convention. The present text of this Article reached the purpose of maintaining the fair balance of interests among the different parties to international leasing transactions. Considering the recommendations and proposals raised or to be raised running counter to this end, the People’s Republic of China is pleased to present its specific proposals:

Paragraph 1

This paragraph stipulates that the lessee shall have the right to reject the equipment as against the lessor where the equipment is not in conformity with the terms of the supply agreement and the supplier fails to deliver it according to the stipulated time or the supplier fails to tender delivery within a reasonable time after the making of the leasing agreement. It reflects the fact that the relationship between the lessor and the lessee is not only a relationship of financing. The right vested in the lessee against the lessor to reject the non-conforming equipment derives from the following two aspects:

(a) The lessee is not a party to the supply agreement and there is no contractual relationship between the lessee and the supplier, the lessee having contractual relations with the lessor only. So the right of rejecting non-conforming equipment vested in the lessee can only be exercised against the lessor.

(b) The lessor is the owner of the equipment and he has to assume the obligations for the lessee in this capacity, namely the lessor shall not be released from such a status.

Article 14

The People’s Republic of China believes that Article 7 and Article 10 are substantially important stipulations on which, to a certain extent, the fair balance of interests is established. It is appropriate to consider them as a whole. The interplay of these two articles actually forms the framework of the rights and obligations concerning the parties. The People’s Republic of China remains of the view expressed through its representatives at the third session of the committee of governmental experts convened by Unidroit in Rome that parties may eliminate these two articles provided that such elimination is made regarding the two articles.

Article 15, paragraph 2

The language adopted by the draft Convention is rather vague and could easily lend the draft Convention to dispute or conflict in interpretation and in determining the applicable law. It is advisable to change the wording of this paragraph.
Proposed revised text:

"2. - Questions concerning matters governed by this Convention which are not expressly settled by it are to be settled in conformity with the general principles on which it is based and, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law."

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Finnish Delegation

PROPOSAL

Delete Article 5, paragraph (3), sub-paragraph (a) and make the consequential changes to the following sub-paragraph.

REASONS

The purpose of rules on public notice relating to leasing transactions is particularly to protect third parties who are contemplating entering into business relationships with the lessee. The rules on public notice should make it easier for them to know whether certain equipment is owned or leased by the lessee. The situation where such information is most valuable for these third parties is when there exists a threat of the lessee going bankrupt. The question therefore is where it is that third parties should look for possible public notice as to the lessor’s ownership. The most obvious country would be the one where the lessee has its place of business, this being the country where the bankruptcy proceedings would take place and whose rules would be followed in such proceedings. Thus the rule in Article 5(3)(b) should also be followed in this case of the equipment enumerated in Article 5(3)(a). The fact that there exists a requirement of registration for this equipment for other purposes would not change the situation as the purpose of such registration differs from the purpose of public notice in leasing transactions.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the United States Delegation

Article 2 - Proposed New Paragraph

"[3]. - The fact that the lessor and the lessee have their places of business in different States is to be disregarded whenever this fact does not appear either from the leasing agreement or from any dealings between the lessor and the lessee, or from information disclosed by the lessor or the lessee, at any time before or at the conclusion of the leasing agreement."

REASONS FOR PROPOSED REVISIONS

1. - The proposed new paragraph is derived substantially from Article 1(2) of the United Nations Convention on Contracts for the International Sale of Goods ("Sales Convention"). The facts that bear on the applicability of the Convention ought to be available to the parties before or at the time the leasing agreement is concluded. This point is particularly important in the case of transactions entered into by an agent on behalf of an undisclosed foreign principal.

2. - The proposed new paragraph supplements, and is consistent with, Article 2(2) of the present draft (which was derived from Article 10(a) of the Sales Convention). Article 2(2) provides that, in the case of a party having more than one place of business, determination of that party's place of business shall be made "having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that agreement." However, the proposed new paragraph is one of general application and, unlike Article 2(2), it is not limited to the situation where a party has more than one place of business.

Article 5 - Paragraphs 1 and 4

1987 TEXT

"1. - The lessor's real rights in the equipment shall be valid against the lessee's trustee in bankruptcy and creditors, including creditors who have obtained an attachment or execution.

........

4. - This article shall not affect the rights of any creditor of the lessee having a lien on or a security interest in the equipment."
PROPOSED REVISIONS  
(changes indicated)

"1. - The lessor’s real rights in the equipment shall be valid against:

(a) the lessee’s [trustee in bankruptcy and] creditors, including creditors who have obtained an attachment, [or] execution or similar judicial process; and

(b) any representative of the lessee or the lessee’s creditors (such as a trustee in bankruptcy or liquidator) in insolvency, liquidation, rehabilitation or similar proceedings.

.....

4. - This article shall not affect the rights of any creditor of the lessee having a lien on or a security interest in the equipment, unless such lien or security interest was obtained by attachment, execution or similar judicial process or is in favor of a representative of the lessee or the lessee’s creditors referred to in paragraph 1."

PROPOSED REVISIONS  
(changes not indicated)

"1. - The lessor’s real rights in the equipment shall be valid against:

(a) the lessee’s creditors, including creditors who have obtained an attachment, execution or similar judicial process; and

(b) any representative of the lessee or the lessee’s creditors (such as a trustee in bankruptcy or liquidator) in insolvency, liquidation, rehabilitation or similar proceedings.

.....

4. - This article shall not affect the rights of any creditor of the lessee having a lien on or a security interest in the equipment, unless such lien or security interest was obtained by attachment, execution or similar judicial process or is in favor of a representative of the lessee or the lessee’s creditors referred to in paragraph 1."

REASONS FOR PROPOSED REVISIONS

1. - None of the proposed revisions change the substance of what we believe was intended in the existing draft. Rather, they are intended to clarify certain ambiguities and inconsistencies and to rectify the narrowness of the language used in the present draft.

2. - The existing paragraph 1 is too limited. It could be read to exclude claims of creditors who obtain rights in the equipment through means that are similar to but different than attachment and execution. It is also too narrow in that it addresses only the rights of a “trustee in bankruptcy” but not other similar representatives.

3. - Paragraph 2 of the existing draft is inconsistent with paragraph 1. This is so because in many States creditors who obtain an execution or attachment thereby obtain a lien on the
goods seized or attached. Paragraph 1 says that the lessor’s real rights are valid against such creditors (and, presumably, valid against their judicial liens). But paragraph 4 then states that Article 5 does “not affect the rights of any creditor having a lien ... on the equipment.” (Emphasis added.) The proposed revisions to paragraph 4 serve to make clear what was intended - that liens obtained by executing and attaching creditors are subject to the rights of the lessor.

Article 5 - Paragraphs 2 and 3; New Paragraphs 4 and 5

1987 TEXT

“2. - Where by the applicable law the lessor’s real rights in the equipment are valid against a person referred to in the previous paragraph only on compliance with rules as to public notice, those rights shall be valid against that person only where they are valid according to such rules.

3. - For the purposes of the previous paragraph the applicable law is:

(a) [in the case of ships, aircraft, vehicles or other equipment subject to registration pursuant to the law of a State, the law of the State of registration];

(b) in the case of all other [mobile] equipment [normally used in more than one State], the law of the State where the lessee has its principal place of business; and

(c) in the case of all other equipment, the law of the State where the equipment is situated at the time when the person referred to in paragraph 1 is entitled to invoke the rules referred to in paragraph 2.”

PROPOSED REVISIONS
(changes indicated)

“2. - Where by the applicable law the lessor’s real rights in the equipment are valid against a [person] creditor or representative referred to in the previous paragraph only on compliance with rules as to public notice, those rights shall be valid against that [person] creditor or representative only where they are valid according to such rules.

3. - Subject to paragraph 4, for the purposes of the previous paragraph the applicable law is:

(a) [in the case of ships, aircraft, vehicles or other equipment subject to registration pursuant to the law of a State, the law of the State of registration];

(b) in the case of all other [[mobile]] equipment which is mobile and which is of a type [normally used in more than one State[]], the law of the State where the lessee has its principal place of business at the time of conclusion of the leasing agreement; and

(c) in the case of all other equipment, the law of the State where the equipment is situated at the time [when the person referred to in paragraph 1 is entitled to invoke the rules referred to in paragraph 2] of conclusion of the leasing agreement.

4. - If after the conclusion of the leasing agreement the principal place of business of the
lessee or the location of the equipment shall change, upon the expiration of [four] months after such change occurs the applicable law for the purposes of paragraph 2 shall be the law of the State where the lessee then has its principal place of business, in the case of equipment referred to in paragraph 3(b), or the State which the equipment is then situated, in the case of equipment referred to in paragraph 3(c).

5.- For the purposes of paragraphs 3 and 4, if the lessee has more than one place of business, the principal place of business of the lessee is the State where the chief executive office of the lessee is located.”

PROPOSED REVISIONS
(changes not indicated)

“2. - Where by the applicable law the lessor’s real rights in the equipment are valid against a creditor or representative referred to in the previous paragraph only on compliance with rules as to public notice, those rights shall be valid against that creditor or representative only where they are valid according to such rules.

3. - Subject to paragraph 4, for the purposes of the previous paragraph the applicable law is:

(a) [in the case of ships, aircraft, vehicles or other equipment subject to registration pursuant to the law of a State, the law of the State of registration];

(b) in the case of all other equipment which is mobile and which is of a type normally used in more than one State, the law of the State where the lessee has its principal place of business at the time of conclusion of the leasing agreement; and

(c) in the case of all other equipment, the law of the State where the equipment is situated at the time of conclusion of the leasing agreement.

4. - If after the conclusion of the leasing agreement the principal place of business of the lessee or the location of the equipment shall change, upon the expiration of [four] months after such change occurs the applicable law for the purposes of paragraph 2 shall be the law of the State where the lessee then has its principal place of business, in the case of equipment referred to in paragraph 3(b), or the State which the equipment is then situated, in the case of equipment referred to in paragraph 3(c).

5. - For the purposes of paragraphs 3 and 4, if the lessee has more than one place of business, the principal place of business of the lessee is the State where the chief executive office of the lessee is located.”

[NOTE: The addition of new paragraphs 4 and 5 would require renumbering existing paragraph 4 as paragraph 6.]

REASONS FOR PROPOSED REVISIONS

1. - The proposed revisions to paragraph 2 are intended merely to conform the terminology to revisions to paragraph 1 proposed elsewhere.
2. - The proposed revisions to paragraph 3(b) are important. It should not be necessary to inquire as to whether the specific equipment involved is itself normally used in more than one jurisdiction. Significantly, in most financial leasing transactions the equipment will be new and unused at the time that the transaction is consummated. Rather than have the test turn on actual use of the particular equipment, the proposed revisions would employ an objective test of whether the equipment "is of a type normally used in more than one State." (Emphasis supplied.)

3. - Proposed revisions to paragraphs 3(b) and (c) address the relevant time at which the lessee's principal place of business and the location of the equipment are to be determined for purposes of the applicable law. Paragraph 3(b) now contains no reference to the relevant time. Paragraph 3(c) contains the confusing reference to "the time when the [creditor] is entitled to invoke the rules referred to in paragraph 2." It is proposed that the time of conclusion of the leasing agreement is the most appropriate time for determination of applicable law and, therefore, the applicability of any requirements for public notice.

4. - The proposed new paragraph 4 supplements paragraphs 3(b) and (c). It expressly contemplates situations where, subsequent to the conclusion of the leasing agreement, equipment is moved to another State or the lessee's principal place of business is changed. The proposed resolution seeks to strike a fair balance between the interests of third parties and the lessor. For example, it can be argued that it would be unfair for the lessor's real rights to be made subject to creditors' claims instantly upon the movement of the equipment (even if wrongful) to a State which requires public filing for leases. Similarly, it might be unfair to allow the lessor's real rights to remain permanently superior to creditors' claims in the destination State even though that State's public policy and laws required public notice by filing. The proposed new paragraph 4, therefore, provides a convenient grace period (four months is suggested) for the lessor to react to a change in equipment location or principal place of business. Yet, it also requires some reasonable level of diligence on the part of the lessor with respect to monitoring the equipment or the lessee's principal place of business, whichever is relevant.

5. - The proposed new paragraph 5 is intended to clarify the meaning of the lessee's "principal place of business," as used in paragraphs 3(b) and 4. The designation of the lessee's "chief executive office" is derived from Section 9-103(3)(d) of the Uniform Commercial Code. It is a more rational choice than the "place of business" test based on the relationship between the State and the transaction that is specified in Article 2(2). Article 5(2) concerns third party rights and, unlike the lessor and lessee in the situation contemplated by Article 2(2), third parties may know nothing about the particular financial leasing transaction. A more objective test, such as that proposed, is called for.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Swedish Delegation

The Swedish delegation proposes the following drafting of Article 14 of the draft Convention on international financial leasing. The proposal is founded basically on the comments put forward by the Hague Conference (Conf.7/4 Add.2, p. 180 supra) and also on the comments concerning Article 14(1) put forward by the Government of Switzerland (Conf. 7/3 Add. 1, pp. 163-164 supra). As it is the opinion of the Swedish delegation that some of the provisions of the Convention should be made mandatory, the drafting we propose does, however, not allow the parties to exclude the Convention altogether.

"Article 14

In their relations with each other, the lessor and the supplier, on the one hand, and the lessor and the lessee, on the other, may derogate from or vary this Convention except for the provisions of Article[s 7(2)], 11(3) and (4)."

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the United Kingdom Delegation

Article 10

"1. - Where the equipment is not delivered or is delivered late or fails to conform to the terms of the supply agreement:

(a) the lessee may exercise any right to reject the equipment or to terminate the leasing agreement; and

(b) the lessor may exercise any right to make a fresh tender of equipment in conformity with the supply agreement,

which would have been exercisable if the lessee had agreed to buy the equipment from the lessor under the terms of the supply agreement."
2. - A right conferred by paragraph 1 shall be exercisable in the same manner and shall be lost in the same circumstances as it would have been exercisable or lost if the lessee had agreed to buy the equipment from the lessor under the terms of the supply agreement.

3. - Where the lessee has exercised a right to reject the equipment and the supplier fails to exercise a right to make a fresh tender in accordance with this Article, the lessee shall be entitled to terminate the leasing agreement, meanwhile having the right to withhold rentals payable thereunder, and to recover any rentals and other sums paid in advance. Nevertheless, the lessee shall be obliged to pay the lessor a reasonable sum for the benefit the lessee has derived from the equipment.

4. - [present paragraph 5].”

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the United Kingdom Delegation: Addendum

EXPLANATORY NOTE
by the United Kingdom Delegation
on its proposal for a revised Article 10
(Conf. 7/C. 1/W.P. 10)

The present text of Article 10 suffers from two weaknesses. First, it is restricted to late delivery and delivery of non-conforming equipment, and entirely fails to cover non-delivery of the equipment. Secondly, it prescribes rules for rejection and cure which differ from those applicable to contracts of sale under the Vienna Convention. This divergence, which is undesirable in itself, also increases the risk, which is not intended, that the lessee will exercise a right of rejection against the lessor at a time when the lessor has lost his right of rejection against the supplier.

The revised text substantially resolves these two problems by providing that the lessee’s right to reject or terminate and the lessor’s right to cure a non-conforming tender by making a fresh tender shall be exercisable and shall be lost in the same circumstances as if the lessee had agreed to buy the equipment from the lessor under the terms of the supply agreement. In this way, the rights of the lessee against the lessor are brought into line with the rights of the lessor against the supplier, and are at the same time made to accord with the Vienna Convention without the need to reproduce the elaborate provisions of that Convention.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposals by the United States Delegation

Article 7 - Paragraph 1(a)

1987 TEXT

“1.- (a) Except as otherwise provided by this Convention or the leasing agreement, the lessor shall not incur any liability to the lessee in respect of the equipment save to the extent that it has intervened in the selection of the supplier or the specifications of the equipment.”

PROPOSED REVISIONS
(changes indicated)

Alternative I

“1.- (a) Except as otherwise provided by this Convention or the leasing agreement, the lessor shall not incur any liability to the lessee in respect of the equipment [save to the extent that it has intervened in the selection of the supplier or the specifications of the equipment].”

Alternative II

“1.- (a) Except as otherwise provided by this Convention or the leasing agreement, the lessor shall not incur any liability to the lessee in respect of the equipment save to the extent [that it has intervened] of the lessee’s actual damages resulting primarily from the lessee’s reliance on the lessor’s skill and judgment and direct intervention in the selection of the supplier or the specifications of the equipment.”

PROPOSED REVISIONS
(changes not indicated)

Alternative I

“1.- (a) Except as otherwise provided by this Convention or the leasing agreement, the lessor shall not incur any liability to the lessee in respect of the equipment.”

Alternative II

“1.- (a) Except as otherwise provided by this Convention or the leasing agreement, the
leessor shall not incur any liability to the lessee in respect of the equipment save to the extent of the lessee’s actual damages resulting primarily from the lessee’s reliance on the lessor’s skill and judgment and direct intervention in the selection of the supplier or the specifications of the equipment.”

REASONS FOR PROPOSED REVISIONS

Alternative I

1. - Alternative I proposes to delete the reference to lessor liability arising from lessor intervention in the selection of the supplier or the specifications of the equipment. This would return the Convention to the original rule and intention of Article 7(1) as proposed by the Study Group in 1985. See Preliminary Draft Uniform Rules, Art. 7(1), UNIDROIT Study LIX - Doc. 17 (January 1985). We have become convinced that the introduction of lessor liability arising out of lessor influence or intervention, introduced in the First Meeting of Governmental Experts, is unwise and unwarranted. See UNIDROIT Summary Report, App. Art. 7(1)(a), UNIDROIT Study LIX - Doc. 24 (April 1985).

2. - The lessee’s protection intended by proponents of the existing Article 7(1)(a) is adequately covered by the scope provisions of the Convention. Under Article 1(2)(a), a financial leasing transaction will not be covered by the Convention unless “the lessee specifies the equipment and selects the supplier without relying primarily on the skill and judgment of the lessor.” That means that any reliance on the lessor’s skill and judgment must be secondary, at most, and not primary. Moreover, in the typical financial leasing transaction the lessor has virtually nothing to do with the selection of the supplier and the specifications of the equipment. See UNIDROIT Explanatory Report, UNIDROIT Study LIX - Doc. 18 (February 1985), at 41-42:

“Given that it is the lessee who relies on its own skill and judgment in selecting the equipment and supplier, and who typically conducts negotiations with the supplier as a reasonably informed user, and that if there is any reliance on another it is upon the supplier’s knowledge of the equipment or representations, so much so indeed that it is effectively the supplier who places the equipment in the stream of commerce, the drafters of the uniform rules were of the opinion that it is the supplier, not the lessor, whose function in the transaction remains at all times essentially financial, who should in principle be liable to the lessee if the equipment is defective or otherwise not in conformity with the supply agreement.”

3. - A principal purpose of the Convention is to provide background rules and principles that will “fill the gaps” in the situations where the express agreements of the parties do not do so. Another purpose is to provide a conceptual framework to guide the courts in their understanding of the sui generis nature of the tripartite financial leasing transaction. In the unusual event of lessor “intervention” (a confusing concept in itself) on which the lessee does not “primarily” rely but which, nevertheless, results in damage to the lessee, the lessee can protect itself by ensuring that the lessor’s liability is provided for in the leasing agreement. The supplier and specifications will be known to the parties at the time the leasing agreement is concluded and the lessee will be fully aware of any such lessor intervention that has occurred.

4. - The concept of lessor intervention is likely to confuse and confound the courts. For
example, if a lessor insists on entering into leasing transactions only covering equipment and suppliers that it "approves," will that be considered intervention? Financial lessors may prefer to deal only in transactions involving reputable suppliers and equipment of a known make and reputation. If a financial lessor declines to enter into a transaction covering an unproven "Brand X" computer to be supplied by an unknown supplier, and then agrees to enter into a transaction covering an I.B.M. computer to be supplied by a licensed I.B.M. dealer, has the lessor "intervened"? If some later trouble develops, will the lessee prevail in its contention that it was damaged by the lessor's "intervention" and that if it had leased the "Brand X" computer it would not have been damaged? The answer to each question should be an emphatic "NO." But will courts that are not familiar with financial leasing transactions understand this? The purpose of the Convention is to aid the courts in their understanding and not to mislead them as to the fundamental nature of financial leasing.

5. - If the concept of "intervention" is read too broadly there is also a danger that a court might read the words "to the extent" to mean "if." This would mean that any intervention by the lessor would result in some liability. (If the lessee suffers damages of $100 and the lessor's "intervention" is determined to represent 10% of the lessee's reliance, will the lessor necessarily be liable for $10?) Surely the existing draft ought not to be read in that manner, but the language is susceptible of that construction.

6. - The likely result of the existing text of Article 7(1)(a) would mean that in virtually all financial leasing transactions the leasing agreement would contain an express provision to the effect that the lessor will bear no responsibility or liability for the quality, selection or specifications of the equipment. Indeed, financial leasing transactions today include such provisions in the documentation. However, there are concerns, today, that courts in some States may view such agreements with scepticism even though they are rational, reasonable and standard. The Convention ought to clarify, not confuse, perceptions of usual and standard financial leasing transactions.

**Alternative II**

7. - Alternative II is not proposed as an equally acceptable alternative to Alternative I. By affirmatively imposing liability on financial lessors for intervention, Alternative II suffers many of the defects described above.

8. - If the desire of the Diplomatic Conference is to preserve the substance of the liability for intervention rule that Alternative I seeks to eliminate, Alternative II is a better, more precise means to that end.

**Article 10 - Paragraph 3 and Proposed New Paragraph**

**1987 TEXT**

"3. - The lessee shall lose its right to reject the equipment where, if the equipment had been supplied to it as buyer, it would have lost the right to reject."
PROPOSED REVISIONS
(changes indicated)

"3.- The lessee shall lose its right to reject the equipment where[]:

(a) if the equipment had been supplied to it as buyer, it would have lost the right to reject[]; or

(b) it has intimated to the lessor or the supplier its acceptance of the equipment and its agreement that it has no right to reject the equipment.

......

6.- This article shall not affect any agreement made by the lessee to reimburse the lessor for payments made by the lessor to the supplier."

PROPOSED REVISIONS
(changes not indicated)

"3.- The lessee shall lose its right to reject the equipment where:

(a) if the equipment had been supplied to it as buyer, it would have lost the right to reject; or

(b) it has intimated to the lessor or the supplier its acceptance of the equipment and its agreement that it has no right to reject the equipment.

......

6.- This article shall not affect any agreement made by the lessee to reimburse the lessor for payments made by the lessor to the supplier."

REASONS FOR PROPOSED REVISIONS

1. - Paragraph (b) would conform the Convention to standard practice and understanding in financial leasing transactions. It is customary for the lessor to receive a delivery and acceptance certificate (assuring the lessor that the lessee is satisfied in all respects with the equipment) before the lessor advances payment of the purchase price to the supplier.

2. - Financial leasing documentation normally provides, in several ways, that the lessor does not bear any risk with respect to the quality of the goods except any such risk that inheres in the anticipated residual value of the equipment to which the lessor will be entitled.

3. - Under the law of many States, the same result would occur under the existing paragraph (3) by virtue of application of sales law combined with the express agreements of the parties. However, the Convention should be more clear as to the effectiveness of typical financial leasing arrangements where all risk of quality after the lessee’s acceptance of the equipment is to be borne by the lessee.
4. - Were the lessee a buyer rather than a lessee, it would be wholly at risk after acceptance of and payment for the equipment. It would be left to its remedies under the supply agreement. The lessee receives the benefit of these remedies against the supplier under Article 9, with one exception - the denial to the lessee of the unilateral right to "terminate or rescind the supply agreement" as specified in Article 9(2). A well-intentioned argument could be made that the lessee's inability to terminate or rescind the supply agreement suggests that the lessee is inadequately protected by its ability to enforce the supply agreement against the supplier. However, in practice this scenario does not present serious problems. It is a simple matter of agreement between the lessee and lessor (in the leasing agreement or otherwise) as to the circumstances of enforcement and termination as against the supplier in the event of defective equipment. Surely the lessor has nothing to gain by preventing the lessee from achieving an effective remedy against the supplier.

5. - Proposed new paragraph 6 is intended to sanction, expressly, the typical agreement made by a lessee in a financial leasing transaction to the effect that the lessee will reimburse the lessor for any payments made by the lessor to the supplier, often with interest, if for any reason the leasing transaction is "unwound." Because Article 10(4) speaks of withholding and recovering rentals from the lessor in the event of a rejection of the equipment by the lessee, it is thought advisable to specify that those provisions do not override a reimbursement agreement made by the lessee. The problem envisaged by proposed new paragraph 6 is most often encountered in situations where the lessor makes advance payments to the supplier prior to delivery and acceptance of the equipment. (Often, such situations involve equipment that is being fabricated or specially made.) If the equipment is never delivered or is defective, leading to the lessee's rejection, Article 10(4) allows the lessee to terminate the leasing agreement. However, the lessee normally agrees that, in such situations, the advance payments made by the lessor will be treated essentially like loans by the lessor to the lessee.

6. - It is arguable that proposed new paragraph 6 is not necessary because nothing in Article 10 purports to restrict the enforceability of the reimbursement arrangement referred to in the new paragraph. However, because the provisions of Article 10(4) appear to be so alien to financial leasing transactions, it is thought necessary to make it especially clear that such reimbursement obligations are effective. A similar drafting technique is embodied in Article 5(4), Article 7(1)(c) and Article 9(2).

Article 11 - Paragraph 3

1987 Text

"3.- The leasing agreement may provide for the manner in which the compensation referred to in paragraph 2 (b) of this article is to be computed and such provision shall be enforceable between the parties unless such compensation is disproportionate to the compensation provided for under paragraph 2 (b)."

PROPOSED REVISIONS
(changes indicated in italics)

"3.- The leasing agreement may provide for the manner in which the compensation
referred to in paragraph 2 (b) of this article is to be computed and such provision shall be enforecable between the parties unless such compensation is disproportionate to the compensation provided for under paragraph 2 (b). Notwithstanding paragraph 4 of this Article, the value of future rentals under the leasing agreement may be taken into account in computing compensation under paragraph 2(b) of this Article and under this paragraph."

PROPOSED REVISIONS
(changes not indicated)

"3.- The leasing agreement may provide for the manner in which the compensation referred to in paragraph 2 (b) of this article is to be computed and such provision shall be enforceable between the parties unless such compensation is disproportionate to the compensation provided for under paragraph 2 (b). Notwithstanding paragraph 4 of this Article, the value of future rentals under the leasing agreement may be taken into account in computing compensation under paragraph 2(b) of this Article and under this paragraph."

REASONS FOR PROPOSED REVISIONS

1. - A fair measure of damages to a lessor that has taken possession of the equipment after the lessee’s default would be (i) the unpaid accrued rentals plus (ii) the present value of future rentals less (iii) the fair market value of the use of the equipment for the remainder of the lease term. Item (iii) represents mitigation of damages because the lessee is being deprived of the use of the equipment for which the lessee is required to make payment under item (ii). The lessor should not be entitled to both the equipment and future rentals, which would provide a double recovery, unless some element of mitigation is provided. In other words, the lessee must be credited with the use-value of the equipment if it has been deprived of possession. Although paragraph 2 does not spell out the measure of damages in such detail, it will fairly accommodate such a reasonable measure of damages.

2. - Paragraph 3 recognises that a “liquidated damages” provision in the leasing agreement may be employed by the parties to measure the damages recoverable under paragraph 2(b). However, paragraph 4 creates an ambiguity. As noted above in comment 1, the present value of future rentals may be an appropriate element of the lessor’s damages. The lessor should not be prevented from recovering damages intended to make it whole for the lessee’s breach merely because the lessor has taken the prudent steps of terminating the lease and taking possession of the equipment in order to protect its investment. Paragraph 4, as drafted, might be read to prevent the lessor’s measure of damages from taking into account the future rental stream. The proposed addition to paragraph 3 is intended to avoid such an unreasonable construction of paragraph 4.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Australian Delegation

Australia proposes the following amendment to Article 7.

In paragraph 1(a), insert the word “expressly” before “provided” in the opening clause:

“Except as otherwise expressly provided by this Convention or the leasing agreement...”.

The reason for the proposed amendment is the possibility that according to the present text the words “the leasing agreement” may be interpreted as including not only the express terms of that agreement but also implied terms (see explanatory report, paragraph 101). In many countries terms such as those relating to merchantability and fitness for purpose are implied mandatorily into some contracts by legislation. If implied terms of the leasing contract are to be exempted from the Article, in other words if immunity from liability for breach of those implied terms is not to be granted to the lessor, this substantially reduces the effect of Article 7 and undermines its primary purpose.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Swedish Delegation

Article 10

1. - The idea of this proposal is as follows: when there is a delay in delivery of the equipment or a delivery which does not conform to the terms of the supply agreement, the lessee shall have the right to withhold rentals payable under the leasing agreement until either the leasing agreement is terminated or there is a delivery in conformity with the terms of the supply agreement.

2. - The situation where the leasing agreement is terminated (which will normally be done by the lessee) seems to be sufficiently covered both by paragraph 4 in the present draft and by paragraph 3 in the proposal put forward by the United Kingdom (Conf.7/C.1/W.P.10).
3. Two other situations, however, do not seem to be covered. One is when there is a delay in delivery but the lessee does not terminate the leasing agreement, either because he does not have the right to, or because he does not want to.

4. The other situation is when the lessee rejects the equipment because of non-conformity but does not terminate the leasing agreement, again either because he does not have the right to, or because he does not want to. (We assume that the expression “rejects the equipment” includes the case where the lessee does not actually return the equipment to the supplier but gives notice of the non-conformity, whereupon the supplier agrees to make the necessary adjustments on the premises.)

5. We think that in these cases, too, the lessee should have the right to postpone the payment of rentals. This means that the risk of delayed or non-conforming delivery is to a limited extent (initially) placed on the lessor. The reason for this proposal is not that the lessor ought to be held responsible for the behaviour of the supplier. The reasons are as follows.

6. For the lessee a duty to start paying rentals before he can actually use the equipment could in individual cases have a very serious negative impact on his financial situation. It could also have the consequence that he finds it necessary to terminate the leasing agreement, although he would really have preferred to wait for a delivery in conformity with the supply agreement.

7. The lessor, on the other hand, may not know much about the supplier or the equipment in the individual case. The lessor is, however, in its capacity of a financing institution, able to calculate the risk of delayed and non-conforming deliveries overall and to distribute the cost of this risk among all its lessees.

8. The risk of a late or non-conforming delivery is one that faces almost all lessees, and the idea of paying rentals before the equipment can be used must be revolting to most of them. It is therefore our belief that practically all lessees will be willing to accept a small increase in rentals to be secured against that; it will be a kind of insurance that they are taking out. And as, in reality, only rather few of the lessees will have serious problems with their deliveries, and as it is only a matter of postponing payment, the premium will be small.

9. Apart from this, the Swedish delegation is in favour of the proposal put forward by the United Kingdom in working paper 10. Therefore we have drafted our proposal as a new paragraph 4 of that proposal. Otherwise our proposal would be a new paragraph 5 in the present draft. The proposal is as follows:

"Article 10"

4. If the equipment is delivered too late or fails to conform to the terms of the supply agreement but the leasing agreement is not terminated in accordance with paragraph 3 of this article, the lessee shall have the right to withhold rentals payable under the leasing agreement until delivery is made in conformity with the terms of the supply agreement."
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the United Kingdom Delegation

It is proposed to revise Article 11 as follows:

"Article 11

1. - In the event of default by the lessee, the lessor may recover accrued unpaid rentals, together with interest and damages.

2. - Where the lessee’s default is substantial, then subject to paragraph 5 of this article the lessor may also accelerate payment of the rentals or terminate the leasing agreement and after such termination may:

(a) recover possession of the equipment; and

(b) recover such damages as will place the lessor in the position in which it would have been had the lessee performed the leasing agreement in accordance with its terms.

3. - The leasing agreement may provide for the manner in which the damages recoverable under paragraph 2(b) of this article are to be computed and such provision shall be enforceable between the parties unless such compensation is disproportionate to the compensation provided for under paragraph 2(b).

4. - The lessor shall not be entitled to recover damages to the extent that it has failed to take all reasonable steps to mitigate its loss.

5. - Where the lessor has terminated the leasing agreement it shall not be entitled to enforce a term of the leasing agreement accelerating payment of the rentals, but the value of future rentals under the leasing agreement may be taken into account in computing damages under paragraphs 2(b) and 3 of this article.

6. - The lessor shall only be entitled to terminate the leasing agreement or accelerate payment of the rentals if it has by notice given the lessee a reasonable opportunity of remedying the default so far as the same may be remedied."

EXPLANATORY NOTE

Except for the right of acceleration inserted in paragraph 2, the proposed revisions are not intended to alter the policy embodied in the present text but simply to make it clearer.

In paragraph 1 the words “and damages” have been added to make it clear that the lessor’s right to damages is not dependent on his first terminating the agreement.
Paragraph 2 includes a right of acceleration of rentals, which is, however, subject to the provisions of paragraph 6. This right is new but reflects established leasing practice. The amendment also brings the text of paragraph 2 into line with that of paragraph 6. The word "damages" is substituted for "compensation", being the more usual term. The reference to the duty to mitigate loss has been deleted from this paragraph because it applies equally to damages recoverable under paragraph 1 of the revised text. Such duty is now reflected in an independent paragraph, namely paragraph 4.

Paragraph 5 (new numbering) follows the proposal of the United States delegation in making it clear that the value of future rentals may be taken into account in computing damages. Consultation showed that leasing interests had not appreciated that this was the effect of the original draft, and the revised text makes it explicit.

Paragraph 6 (old 5) is unchanged.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Swedish Delegation

Article 8(2)

PROPOSAL

That the words "its right to buy" be changed into "a right to buy".

REASON

The present wording indicates that the lessee always has a right to buy the equipment or to prolong the lease - cf. Article 3 in the 1987 Draft, now relocated and renumbered Article 1(3).
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Joint proposal by the Delegations of Canada, the United Kingdom and
the United States of America

Article 5

"1. - The lessor’s real rights in the equipment shall be valid against the lessee’s trustee in
bankruptcy and creditors, including creditors who have obtained an attachment or execution.

“Trustee in bankruptcy” includes a liquidator, administrator or other person appointed to
administer the lessee’s estate for the benefit of the general body of creditors.

[same as Working Group draft]

2. - Where by the applicable law the lessor’s real rights in the equipment are valid against
a person referred to in the previous paragraph only on compliance with rules as to public notice,
those rights shall be valid against that person only if there has been compliance with such rules.

[same as Working Group draft]

3. - For the purposes of the previous paragraph the applicable law is the law of the State
which is at the relevant time:

(a) in the case of a ship, the law applicable under the rules of private international law,

(b) in the case of an aircraft, the State in which the aircraft is registered as provided
by the Chicago Convention on International Civil Aviation 1944,

(c) in the case of other equipment, including an aircraft engine, that is of a kind
normally moved from one State to another, the State where the lessee has his principal place
of business,

(d) in the case of all other equipment the State where the equipment is situated.

[same as Working Group draft]

4. - For the purposes of paragraph 3, the “relevant time” is the time when the person
referred to in paragraph 1 becomes entitled to invoke the rules referred to in paragraph 2.

[same as Working Group draft]

5. - Paragraph 2 shall not affect the provisions of any international agreement under which
the lessor’s real rights in the equipment are required to be recognised.

[same as Working Group draft]
6. - (1) This article shall not affect the priority of any creditor having
   (a) a consensual or non-consensual lien or security interest in the equipment, or
   (b) any right of arrest, detention or disposition conferred by law specifically in
       relation to ships or aircraft.

   (2) For the purposes of paragraph (1)(a), the term "lien" does not include a lien arising
       by virtue of an execution.”

CONF. 7/C.1/W.P. 17
12 May 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Delegation of the Federal Republic of Germany

Article 7(2) should read as follows:

“The lessor warrants that the lessee’s quiet possession will not be disturbed by a
person who has at the time of delivery of the equipment a superior title or right. The same
applies when a superior title or right is derived from an act or omission of the lessor.”

CONF. 7/C.1/W.P. 18
12 May 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Chairman

Article 5: Proposed paragraph (3)

“3. - For the purposes of the previous paragraph the applicable law is the law of the State
that is applicable under the rules of private international law.”

REASONS FOR PROPOSED CHANGE

1. - Paragraph 3 has become too complex. The proposed substitute paragraph 3 would
   leave the applicable law relating to public notice requirements for leases exactly as it is today.

2. - All of the proposed texts of paragraphs 2 and 3 of Article 5 adopt a “neutral” approach
to public notice for leases. The Convention does not take a position as to whether public notice
is to be required. It defers to local law. Nevertheless, the various proposed texts of paragraph 3 attempt to intervene in and dictate the choice of law rules for public notice. Because these choice of law rules are essential elements of a system of public notice (i.e. who is entitled to notice and where such notice shall be given), the various proposed texts would undermine the intended neutrality of the Convention.

3. - Improving the choice of law rules applicable to public notice requirements for leases is not an important goal of the Convention, although such improvements may be a laudable goal. This subject may be an appropriate topic for another Convention or a model local law. But there is nothing peculiar to international financial leasing which dictates a change in the law applicable today.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Report by the Informal Working Group
on the proposal by the Comité Maritime International
regarding Article 5(3)(a) in relation to ships

The Special Informal Working Group on the proposal put forward by the distinguished observer of the Comité Maritime International has concluded that, in substance, the proposal is one that should be considered by the Committee of the Whole. The Special Working Group puts forward the following formulation of Article 5(3)(a) for consideration:

"Article 5

3. - ...

(a) in the case of a registered ship, the law of the State in which it has been registered by the owner."
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Informal Working Group on Article 14

The working group, composed of the delegations of Antigua and Barbuda, Australia, Brazil, the People’s Republic of China, Egypt, France, the Federal Republic of Germany, Poland, Switzerland and the U.S.A held one session on 11 May.

Following the mandate given to it by the Committee of the Whole, the group discussed possible ways of dealing with draft Article 14 on the basis of the indicative vote taken by that Committee.

The members of the working group decided to concentrate on the substance of Article 14, leaving aside drafting. They agreed that the drafting of that provision should be a matter to be dealt with by the Drafting Committee.

It was decided that draft Article 14 should be composed of two paragraphs.

Taking inspiration from the Vienna Convention on sales of goods but not considering drafting, the working group agreed that the first paragraph should express the idea that parties may exclude the application of the present Convention.

It was understood that the term “parties” meant the three parties involved in the financial leasing transaction: the lessee, the lessor and the supplier. The group also approved the understanding that, if all three parties do not exclude the application of the Convention, the Convention shall apply.

Paragraph 2 should state that when the Convention is not excluded, that is to say when it applies, certain provisions, to be listed individually, shall be considered as mandatory. The group agreed that the decision on which provisions are to be included in paragraph 2, a point which has a bearing on whether there will be any mandatory provisions, is to be decided by the Committee of the Whole.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Delegation of Colombia

Article 9
(proposed amendments in italics)

"1. - The duties of the supplier under the supply agreement shall also be owed to the lessee as if it were a party to that agreement and as if the equipment were to be supplied directly to the lessee.

The supplier shall not be liable as against the lessor and the lessee twice for the same reasons and damages caused.

2. - Nothing in this article shall entitle the lessee to terminate or rescind the supply agreement without the express consent and participation of the lessor."

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Delegation of the Philippines

Article 9

"1. - The duties of the supplier under the supply agreement shall also be owed to the lessee as if it were a party to that agreement and as if the equipment were to be supplied directly to the lessee.

2. - Nothing in this article shall entitle the lessee to terminate or rescind the supply agreement."

The proposal is to add to the first paragraph the clause "provided, however, that the supplier shall not be held liable twice for the same cause of action."

It is further proposed that the second paragraph be deleted.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Delegation of Colombia

The Colombian Delegation proposes including a new Article 13h, to be drafted as follows:

"1. - If unforeseen macroeconomic events, such as a drastic elevation of interest rates or some governmental provision, affect economic and financial burdens to any party arising from the leasing contract in such a manner that the affected party faces valuable losses, this party can claim the review of the respecting contractual provisions in order to adjust them.

2. - The decision concerning the evaluation of the economic events claimed by that affected party can lead this article’s application and if so to fix the adjustment will be made by three experts, whose judgment will be definite.

3. - The three experts will be appointed as follows: If the parties belong to two different continents, each expert will be appointed by the board of directors of the continental association or federation of each party and the third will be appointed by the International Chamber of Commerce.

If the parties belong to the same continent, the board of directors of the continental association or federation will appoint two experts and the third will be appointed by the International Chamber of Commerce.

4. - For the purposes of this article, there are understood as continental association or federation the following:
   - Asialease
   - American Association of Equipment Lessors (A.A.E.L.)
   - African Association or Federation of Equipment Lessors (if it is created)
   - Australian Leasing Association
   - Leaseurope
   - Felalease.”
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Swedish Delegation

Article 10(3) and (4)

"3. - Where the equipment is not delivered in time or the lessee has exercised a right to reject the equipment, the lessee shall be entitled to withhold rentals payable under the leasing agreement until the lessor has tendered equipment in conformity with the supply agreement or the leasing agreement is terminated.

4. - Where the lessee has exercised a right to terminate the leasing agreement, the lessee shall be entitled to recover any rentals and other sums paid in advance. Nevertheless, the lessee shall be obliged to pay the lessor a reasonable sum for any benefit the lessee has derived from the equipment."

"CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Swedish Delegation

Article 10(3) and (4)

Delete "and (4)" from the title.
Delete paragraph 4 from the text of the proposal."
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Delegations of France and Mexico

Reintroduce Article F (Reservation):

"A Contracting State may declare at the time of signature, ratification, acceptance, approval or accession that it will not be bound by Article 9(3)."

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Canadian Delegation

PROPOSAL

The draft Convention on international financial leasing should embody a provision referring to the usages of international commerce.

Insert after the text of Article 14 a new Article 15.

Proposed text:

"1. - The parties to the leasing agreement are bound by any usage to which they have agreed and by any practices which they have established between themselves.

2. - The parties to the leasing agreement are considered, unless otherwise agreed, to have impliedly made applicable to their agreement or its formation a usage of which the parties knew or ought to have known and which in international trade is widely known to, and regularly observed by, parties to contracts of the type involved in the particular trade concerned."

REASONS FOR THIS PROPOSAL

Such a rule would permit the draft Convention on international financial leasing to be harmonised on this question with the Vienna Convention on the International Sale of Goods (Article 9) and the Geneva Convention on Agency in the International Sale of Goods (Article 7).
The text proposed reproduces Article 9 of the Vienna Convention with the necessary adjustments.

This rule would be in line with the principle of freedom of contract of the parties embodied in Article 14(2) of the draft Convention. The effect of the text proposed would be to enable the parties to derogate from the rules of the Convention on the basis of the practices which they have established between themselves as well as the usages to which they have agreed. By referring to the discussions on the question of “terms approved” (Article 1(1)(a) of the draft) we can see how such a rule would help us to identify the terms which are to be approved, depending on the type of equipment leased in the different leasing agreements or the nature of the lessor’s activities.

The means of financing involved in financial leasing originates in business practice. It has been developed by international economic operators to meet particular needs. It accordingly behoves us to ensure that practice continues to be recognised as an important source of law in this field.

RESULT

Renumber Article 15 of the draft Convention.

CONF.7/C.1/W.P.27
16 May 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Working Group on Article 7(2)

The Working Group on Article 7(2) met three times, twice on 13 and once on 16 May. It comprised elements of the delegations of Australia, Austria, Brazil, Canada, the People’s Republic of China, Egypt, the Federal Republic of Germany, Hungary and Japan. It concluded with a proposal for a new text of the present Article 7(2) that would involve a new Article 7(3). This proposal would read as follows:

“Article 7

2. - The lessor warrants that the lessee’s quiet possession will not be disturbed by a person who has a superior title or right or who claims a superior title or right and acts under the authority of a court where such title, right or claim is derived from an act or omission of any person other than the lessee.

3. - The provisions of the previous paragraph are not subject to limitation by agreement
between the parties to the extent that the superior title, right or claim is derived from an intentional or grossly negligent act or omission of the lessor.”

CONF.7/C.1/W.P. 28
16 May 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Swedish Delegation

PROPOSED AMENDMENT TO ARTICLE 14(2)

The provisions that are being contemplated as possibly mandatory are all to the advantage of the lessee. A natural interpretation of Article 14 would be that they are also mandatory only to the advantage of the lessee. Thus any term of the leasing agreement, derogating to the advantage of the lessee from one of the mandatory provisions, would be valid. If, for instance, a minimum payment clause of the kind mentioned in Article 11(3) would indicate a sum considerably smaller than the sum that would follow from the application of paragraph 2(b), such a clause would be valid (subject to a presumably more narrow unfair-terms-of-contract provision in the applicable law).

This nature of the mandatory provisions is, however, not expressly shown by the present language of Article 14(2). We therefore propose amending it as follows:

“Article 14

2. - The parties may, in their relations with each other, derogate from or vary this Convention except for the provisions of Articles [................]. The parties may, however, derogate from or vary the provisions of these articles to the extent that this is to the advantage of the lessee.”
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Delegation of the Federal Republic of Germany

Article 8

Delete the words “inter se” in Article 8.

REASONS

1. - Real rights in the equipment are concerned. Real rights by their nature are valid or not valid against all third persons, including for instance the creditors of the owner of the land.

2. - Divergence between the French text (“droits respectifs”) and the English text (“rights inter se”).

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Canadian Delegation

PROPOSAL

The Canadian Delegation proposes the addition of the following new paragraph 4 to Article 9:

“4. - Paragraphs 2 and 3 shall not affect any broader warranty of quiet possession by the lessor which is mandatory under the applicable law.”

REASONS

1. - The proposed article takes up again the former Article 7 (3) (Alternative II) of the draft Convention.
2. - The reintroduction of this provision could make it easier for States for which Article 9 (2) and (3) are too restrictive having regard to the mandatory rules of their legal system to accede to the Convention.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Observations and proposals by the Swedish Delegation

OBSERVATIONS AND PROPOSALS TO THE TEXT
SUBMITTED BY THE DRAFTING COMMITTEE IN DOC. CONF. 7/D.C/1

The Preamble, the paragraph starting “CONSCIOUS”

As the final words “the financial leasing transaction” are in the singular form, we feel that the word “relationships”, too, ought to be put in that form.

Article 2

1. - The words “otherwise subject to this Convention” indicate that some of the requirements or characteristics spelled out in Article 1 can be absent in a sub-leasing transaction, but there is no indication as to which. This creates an ambiguity with respect to the sphere of application of the Convention. We assume that the only difference allowed is that the lessor has not bought the equipment but taken it on a lease himself, and we think that this has to be made clear.

2. - Perhaps the most important characteristic of a financial leasing transaction under the Convention is that it is the lessee who specifies the equipment and selects the supplier; several of the following articles have this characteristic as their basis. This seems to mean that, in a chain of leasing and sub-leasing transactions, there can be only one financial leasing agreement in the sense of the Convention, as only one lessee can specify the equipment and select the supplier. Therefore, it would not seem appropriate to say that the Convention “applies to each transaction which is a financial leasing transaction”.

Article 4

We would prefer the text originally proposed by the delegation of the United States in working paper CONF. 7/C.1/WP 4, which shows more clearly the limited ambition of the article. Consequently, we propose Article 4 to be amended as follows:

“This Convention shall not cease to apply merely because the equipment may have become a fixture to or incorporated in land”.

241
Article 5(2)

It would, of course, be illustrative to enumerate the mandatory provisions in the manner proposed. Still, we feel that a legal text should not give the same rule twice. Besides, the technique chosen has the somewhat strange consequence that Article 5(2) prohibits the parties from derogating from the provisions of a paragraph [9(3)], the only provision of which prohibits the parties from derogating from the provisions of another paragraph [9(2)]. We propose that Article 5(2) be amended to end:

"... except as otherwise stated in the Convention".

Article 7(3)

1. - To make the meaning of the final words of the chapeau more clear, we suggest that it should end:

"... the law of the State which, at the time specified in paragraph 4, is :".

2. - In the earlier discussion of what is now sub-paragraph (b) of Article 7(3) there was a suggestion that this provision should apply only to "a registered aircraft". This suggestion has not been taken up by the Drafting Committee. We would, however, like to suggest an alternative drafting, which will make it clear that an aircraft which is not registered pursuant to the Chicago Convention is covered by sub-paragraph (c) (or, on rare occasions, sub-paragraph (d)):

"(b) in the case of an aircraft which is registered pursuant to the Convention on International Civil Aviation done at Chicago on 7 December 1944, the State in which it is so registered;".

Article 8

Although important enough, this article does not seem to contain any provision of substance. It does not in itself deal with the "rights and duties of the parties" (which is the heading of this chapter) but is merely a rule on the choice of law. It would therefore seem that its place is in Chapter I – Sphere of application and general provisions. We would suggest that Article 8 be relocated and renumbered a new Article 4(2).

Article 9(2)

The draft distinctly places the burden of proof on the lessee. We propose that paragraph 2 be amended to end as follows:

"... where such title, right or claim is not derived from an act or omission of the lessee".

Article 11(1)

Just as a matter of clarification we would like to have it stated that the new sentence of this
paragraph does not exclude the possibility of the supplier being liable to both the lessor and the lessee on account of the same default by the supplier. The new provision simply means that the same cost shall not be compensated twice by the supplier.

**Article 13**

With this new, very clear drafting of paragraph 1, it is hard to see what is said in paragraph 2, which does not follow already from paragraph 1. However, as there seems to be no harm in retaining paragraph 2, we do not want to raise a proposal for its deletion but simply to submit this observation.

**CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION**
**ON INTERNATIONAL FINANCIAL LEASING**

*Draft Convention on International Financial Leasing: Concordance of the original and revised texts*  
(prepared by the Chairman of the Drafting Committee)

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**CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING**

*Proposal by the United Kingdom Delegation*

**New Article F**

"A contracting State may declare at the time of signature, ratification, acceptance, approval or accession that it will not be bound by any part of this Convention in respect of financial leasing transactions as described in Articles 1 and 2 if they relate to the supply of ships."

244
REASON FOR PROPOSAL

In the light of the uncertainty as to whether provisions of the Convention will be mandatory, and the involvement of U.N.C.T.A.D. in the field of shipping generally it is the view of the U.K. delegation that parties should have the freedom to make a reservation in order to avoid any prejudice to their position in both the above respects.

CONF.7/C.1/W.P. 34
18 May 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Delegation of the Federal Republic of Germany

Article 13(6)

Paragraph 6 should be amended as follows:

"Once the lessee has terminated the leasing agreement, it may not invoke performance of the supply agreement".

CONF. 7/C.1/W.P. 35
19 May 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Proposals by the Cuban Delegation

Article 1

This article contains definitions of the terms "factoring contract" and "supplier". We would like to make the following points:

The factor performs the functions set out in the draft Convention but in our case moreover he acts essentially as an agent for the recovery of receivables and the payment of debts. In consequence, contracts concluded with a factor respond to the interests of the supplier.

Paragraph 1(c): the duties of debtors are not specified. We believe that regard should be had to them since "the factoring contract" refers not only to the assignment of receivables but also to the sale, to the purchase of goods and the supply of services.
Paragraph 3: it is stated that “writing” includes any form of writing, whether or not signed. We think that the writing should always be signed.

Article 2

Paragraph 2 provides that “the place of business is that which has the closest relationship to the contract and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that contract”.

We find this formulation rather ambiguous: it specifies neither what the circumstances are nor whether the contract must be concluded at the place of business or in the usual Contracting State.

Article 3

Paragraphs 2 and 3: the wording of these provisions may give rise to confusion. We believe that there should be clarification of what is meant when it is said that any exception in relation to the receivables “may be made only as regards the Convention as a whole”.

Article 5

Paragraph 2: this provision does not describe how the mechanism of renvoi operates, whether the receivable will be paid or not since certain circumstances such as the place of business of the debtor are mentioned. As a result it is not indicated who must make payment.

Article 6

This provision states that the factoring contract “may validly provide ... for the transfer, with or without a new act of transfer, of all or any of the supplier’s rights ...”.

We do not share this view as we believe that a separate act should always be necessary to complete the assignment.

Article 7

Sub-paragraph (c) of paragraph 1 provides that the debtor is under a duty to pay the factor if notice of the assignment relates to receivables arising under a contract of sale of goods made at or before the time notice is given.

The sale contract is always concluded before the giving of notice and not at the same time. We therefore take the view that the words “at or” are redundant.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Proposals by the Italian Delegation

Article 1 (1), sub-paragraph (b)

The wording "maintenance of accounts (ledgering)" seems to be too wide. The following wording is therefore proposed: "maintenance of accounts (ledgering) with regard to the receivables".

The same can be said of the wording: "protection against default in payment by debtors". The following wording is therefore proposed: "protection against default in payment by debtors due solely to their financial inability to pay".

Article 3, paragraph (2),
Article 4 (1), sub-paragraphs (a) and (b)

In respect of these provisions, it is important to determine when the receivables "arise" or when "they come into existence". It appears that the coming into existence of receivables is perceived differently in different legal systems. In some systems the receivables come into existence at the time of the conclusion of the contract of sale; in other systems the receivables come into existence only when the goods are delivered.

It seems therefore necessary to determine exactly what the Convention means by "arise" or "when they come into existence", and to replace the present wording by a wording which is not confusing.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Proposals by the Swedish Delegation

Article 1

1. - We think it is preferable if a definition in a legal text does not diverge too much from the common language understanding of the expression defined. We therefore think that the
exclusion of consumer transactions (paragraph 1, subparagraph (a)) would be better put in a paragraph or article of its own. Perhaps the wording could be taken from the leasing convention in the following way:

“This Convention applies to a factoring transaction in relation to all goods save those which are to be used primarily for the debtor’s personal, family or household purposes”.

2. - Neither does the requirement that notice of the assignment is to be given in writing (sub-paragraph (c)) seem to form a natural part of a definition of the expression “factoring contract” (cf. comments by the Government of Japan in Conf. 7/6, p. 186, supra). It could form part of the rules on the sphere of application, but it would seem even more natural as a rule of substance.

And as this requirement actually is a rule of substance in the only article where it would seem to be necessary, which is Article 7 (1) (a), our first preference would be to delete Article 1 (1) (c). This way the convention would operate in a “normal” way in the case where notice is given in writing, although there is no provision to that effect in the factoring contract. The convention would also serve as a protection for the debtor – through Article 7 – when notice is not given in writing.

3. - The provision of paragraph 3 seems to raise more questions than it solves, as it does not seem to take account of e.g. messages that are transmitted electronically by way of computers. We understand from the explanatory report (para. 19, p. 92, supra) that the Secretariat will suggest a different formulation to the conference, but in its present form we would prefer to have the paragraph deleted and the understanding of the expression “in writing” left to the applicable law.

CONF. 7/C.1/W.P. 38
19 May 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

Proposal by the Finnish Delegation

Article F

PROPOSAL

Delete Article F.

REASONS

Reservations of the type contained in Article F are most problematic for parties to international commercial agreements.

Reservation may lead to undesired consequences.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

Proposal by the Secretariat

Article 1, paragraph 3

"For the purposes of this Convention writing includes telegram, telex and any electronic means of communication [whether or not signed]."

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

Proposal by the Swedish Delegation

Article 3 (1) and (2)

PROPOSAL

Alternative (a): Add to paragraph 1 a provision corresponding to that of paragraph 2: "... only in respect of receivables arising from supply agreements entered into at or after the time when the debtor has received notice in writing of such exclusion".

Alternative (b): Substitute the following text for both paragraph 1 and paragraph 2: "The application of this Convention may be excluded only if the supplier, the debtor and the factor all agree to exclude it".

REASONS

It seems that the present draft can lead to unreasonable results for the debtor,

— both where he wishes the convention to apply and has reasons to think that it will, but the supplier and the factor later agree to exclude it,

— and where the debtor has agreed with the supplier to exclude the convention, but there is no corresponding term in the factoring agreement — especially when the factoring contract is entered into later than the supply agreement, so that the debtor has not got even a theoretical chance of notifying the factor in time.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

Proposal by the Delegation of the Federal Republic of Germany

Article 3, paragraph 2

Delete paragraph 2.

REASON

Academic approach. No interest of the creditor for exclusion of the Convention.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

Proposal by the Italian Delegation

Article 9, paragraph 1

PROPOSAL

Substitute: "... if the debtor has a claim against the supplier for recovery of the price", by the following text: "if the debtor has not been deprived by the assignment of his claim against the supplier for recovery of the price".

REASONS

In the Explanatory Report prepared by the Unidroit Secretariat (Unidroit 1987, Study LVIII - Doc. 33, para. 46, see p. 101, supra) it is said that the general rule of Article 9, paragraph 1 "is ... restricted ... to those cases where, under the applicable ... law, the debtor has not been deprived by the assignment of his claim against the supplier for recovery of the price". It seems better to precise Article 9, paragraph 1 according to that explanation. The present wording could include every case in which the debtor has lost his claim.
Article 9(2), sub-paragraph (a)

It is not clear if the word “paid” includes for example set-off. It would be better to substitute the word “paid” by broader language.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Proposal by the Delegations of France, Mexico and the Philippines

Article 5

Article 5 should be drafted as follows:

“1. - The assignment of a receivable by the supplier to the factor shall not be effective against the debtor when such assignment has been prohibited by the contract of sale of goods.

2. - However the assignment may be effective notwithstanding any agreement to the contrary when the debtor has his place of business in a Contracting State which has made a declaration under Article X of this Convention.”

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Proposal by the Swedish Delegation

Article 9 (2) (b)

Proposed new text: “where at the time the factor paid such purchase price he knew of the debtor's claim against the supplier [or of the supplier's non-performance as regards the goods to which the debtor’s payment relates].”

REASON

It should not be a defence for the factor that he deemed the debtor not to have any cause for his claim and that he (the factor) therefore “did not know of any non-performance as regards the goods”.
Article 10

1. - We propose that in paragraph 1 (b) Article 9 be mentioned together with Articles 7 and 8.

2. - As an alternative to paragraph 3 we propose that the reference to Article 5 be excluded from paragraph 1 (a). This way the convention will not itself allow a “prohibited” assignment, but it will apply to such an assignment when it is allowed by the applicable law.

The preamble

We propose a preamble along the following lines:

"THE STATES PARTIES TO THIS CONVENTION

CONSCIOUS of the fact that international factoring has an important role to play in the development of international trade,

RECOGNISING therefore the need to provide a legal framework that will facilitate international factoring, while maintaining a fair balance of interests between the different parties involved in factoring transactions,

HAVE AGREED as follows:”.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Proposal by the Czechoslovakian Delegation

Article 10, paragraph 3

“This Convention shall not apply to an assignment which is prohibited by the terms of the factoring contract”.

EXPLANATORY REPORT

Paragraph 3 shall be applied and understood as follows:

Prohibition of subsequent assignment settled in the factoring contract shall refer to any assignment made by the import factor. It means:

(a) in the case of “direct factoring” (supplier versus import factor) the second and any further assignment shall be prohibited;
(b) in the case of “classical factoring” (supplier versus export factor versus import factor) the third and any further assignment shall be prohibited.

REASON

The exclusion of those dispositions with the receivable and all documents referring to it which would be inconvenient to the supplier upon his commercial decision.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

Report of the Working Group on Article 1(1)(c) and (3)

The Working Group met to consider two questions referred to it by the Committee of the Whole:

1. - Whether the words “in writing” in Article 1(1)(c) should be retained or deleted.

2. - A reformulation of the definition of “writing” in Article 1(3).

On the first point, the Working Group was unanimously of the opinion that the words “in writing” in Article 1(1)(c) be deleted. On the second point the Working Group offers the following definition of “writing”:

“3. - For the purposes of this Convention:

(a) a writing need not be signed;

(b) “writing” includes, but is not limited to, telegrams, telex and any other telecommunication capable of being reproduced in tangible form.”

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

Report of the Working Group on Article 5

The Working Group on Article 5 met to consider the existing text and proposals for amendment. After detailed consideration of a number of alternatives, the Working Group agreed that the following revised text be submitted to the Committee of the Whole for approval.
Article 5

"1. - The assignment of a receivable by the supplier to the factor shall be effective notwithstanding any agreement between the supplier and the debtor prohibiting such assignment.

2. - However, such assignment shall not be effective against the debtor when he has his place of business in a Contracting State which has made a declaration under Article X of this Convention.

3. - Nothing in paragraph 1 shall affect any obligation of good faith owed by the supplier to the debtor or any liability of the supplier to the debtor in respect of an assignment made in breach of the terms of the contract of sale of goods."

CONF. 7/C.1/W.P. 48
25 May 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Draft Convention on International Factoring:
Concordance of the original and revised texts
(prepared by the Chairman of the Drafting Committee)

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CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Text of the Preamble and Chapters I and II
submitted by the Drafting Committee
to the Committee of the Whole

[CONVENTION ON INTERNATIONAL FINANCIAL LEASING]

PREAMBLE

THE STATES PARTIES TO THIS CONVENTION,

RECOGNISING the importance of removing certain legal impediments to the interna-
tional financial leasing of equipment, while maintaining a fair balance of interests between the
different parties to the transaction,

AWARE of the need to make international financial leasing more available,

CONSCIOUS of the fact that the rules of law governing the traditional contract of hire
need to be adapted to the distinctive triangular relationships created by the financial leasing
transaction,

RECOGNISING therefore the desirability of formulating certain uniform rules relating
primarily to the civil and commercial law aspects of international financial leasing,

HAVE AGREED as follows:

CHAPTER 1 - SPHERE OF APPLICATION AND GENERAL PROVISIONS

Article 1

1. - This Convention governs a financial leasing transaction as described in paragraph 2
of this article in which one party (the lessor),

(a) on the specifications of another party (the lessee), enters into an agreement (the
supply agreement) with a third party (the supplier) under which the lessor acquires plant, capital
goods or other equipment (the equipment) on terms approved by the lessee so far as they
concern its interests, and

(b) enters into an agreement (the leasing agreement) with the lessee, granting to the
lessee the right to use the equipment in return for the payment of rentals.

2. - The financial leasing transaction referred to in the previous paragraph is a transaction
which includes the following characteristics:
(a) the lessee specifies the equipment and selects the supplier without relying primarily on the skill and judgment of the lessor;

(b) the equipment is acquired by the lessor in connection with a leasing agreement which, to the knowledge of the supplier, either has been made or is to be made between the lessor and the lessee; and

(c) the rentals payable under the leasing agreement are calculated so as to take into account in particular the amortisation of the whole or a substantial part of the cost of the equipment.

3. - This Convention applies whether or not the lessee has or subsequently acquires the option to buy the equipment or to hold it on lease for a further period, and whether or not for a nominal price or rental.

4. - This Convention applies to financial leasing transactions in relation to all equipment save that which is to be used primarily for the lessee’s personal, family or household purposes.

Article 2

In the case of one or more sub-leasing transactions involving the same equipment, this Convention applies to each transaction which is a financial leasing transaction otherwise subject to this Convention as if the person from whom the first lessor (as defined in paragraph 1 of the previous article) acquired the equipment were the supplier and as if the agreement under which the equipment was so acquired were the supply agreement.

Article 3

1. - This Convention applies when the lessor and the lessee have their places of business in different States and:

(a) those States and the State in which the supplier has its place of business are Contracting States; or

(b) both the supply agreement and the leasing agreement are governed by the law of a Contracting State.

2. - A reference in this article to a party’s place of business shall, if it has more than one place of business, mean the place of business which has the closest relationship to the relevant agreement and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that agreement.

Article 4

The provisions of this Convention shall continue to apply even if the equipment becomes a fixture to or incorporated in land.

Article 5

1. - The lessor, the lessee and the supplier may agree to exclude the application of this Convention.
2. - Where the application of this Convention has not been excluded in accordance with the previous paragraph, the parties may, in their relations with each other, derogate from or vary the effect of any of its provisions except Articles 9(3) and 14(3)(b) and (4).

Article 6

1. - In the interpretation of this Convention, regard is to be had to its object and purpose as set forth in the Preamble, to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.

2. - Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law.

CHAPTER II - RIGHTS AND DUTIES OF THE PARTIES

Article 7

1. - (a) The lessor’s real rights in the equipment shall be valid against the lessee’s trustee in bankruptcy and creditors, including creditors who have obtained an attachment or execution.

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

2. - Where by the applicable law the lessor’s real rights in the equipment are valid against a person referred to in the previous paragraph only on compliance with rules as to public notice, those rights shall be valid against that person only if there has been compliance with such rules.

3. - For the purposes of the previous paragraph the applicable law is the law of the State which is at the time specified in paragraph 4:

(a) in the case of a registered ship, the State where it is registered in the name of the owner (for the purposes of this sub-paragraph a bareboat charterer is deemed not to be the owner);

(b) in the case of an aircraft, the State in which it is registered pursuant to the Convention on International Civil Aviation done at Chicago on 7 December 1944;

(c) in the case of other equipment of a kind normally moved from one State to another, including an aircraft engine, the State where the lessee has its principal place of business;

(d) in the case of all other equipment, the State where it is situated.

4. - For the purposes of paragraph 3, the relevant time is the time when a person referred to in paragraph 1 becomes entitled to invoke the rules referred to in paragraph 2.

5. - Paragraph 2 shall not affect the provisions of any other Convention under which the lessor’s real rights in the equipment are required to be recognised.
6. - This article shall not affect the priority of any creditor having:

(a) a consensual or non-consensual lien or security interest in the equipment arising otherwise than by virtue of an attachment or execution, or

(b) any right of arrest, detention or disposition conferred specifically in relation to ships or aircraft under the law applicable by virtue of the rules of private international law.

Article 8

Any question whether or not the equipment has become a fixture to or incorporated in land, and if so the effect on the rights inter se of the lessor and a person having real rights in the land, shall be determined by the law of the State where the land is situated.

Article 9

1. - (a) Except as otherwise provided by this Convention or stated in the leasing agreement, the lessor shall not incur any liability to the lessee in respect of the equipment save to the extent that the lessee has suffered loss as the result of its reliance on the lessor’s skill and judgment and of the lessor’s intervention in the selection of the supplier or the specifications of the equipment.

(b) The lessor shall not, in its capacity of lessor, be liable to third parties for death, personal injury or damage to property caused by the equipment.

(c) The above provisions of this paragraph shall not govern any liability of the lessor in any other capacity, for example as owner.

2. - The lessor warrants that the lessee’s quiet possession will not be disturbed by a person who has a superior title or right, or who claims a superior title or right and acts under the authority of a court, where such title, right or claim is derived from an act or omission of any person other than the lessee.

3. - The parties may not exclude or vary the provisions of the previous paragraph in so far as the superior title, right or claim is derived from an intentional or grossly negligent act or omission of the lessor.

Article 10

1. - The lessee shall take proper care of the equipment, use it in a reasonable manner and keep it in the condition in which it was delivered, subject to fair wear and tear.

2. - When the leasing agreement comes to an end the lessee, unless exercising a right to buy the equipment or to hold the equipment on lease for a further period, shall return the equipment to the lessor in the condition specified in the previous paragraph.

Article 11

1. - The duties of the supplier under the supply agreement shall also be owed to the lessee as if it were a party to that agreement and as if the equipment were to be supplied directly to the lessee. However, the supplier shall not be liable to both the lessor and the lessee in respect of the same damage.
2. - Nothing in this article shall entitle the lessee to terminate or rescind the supply agreement without the consent of the lessor.

Article 12

The lessee's rights derived from the supply agreement under this Convention shall not be affected by a variation of any term of the supply agreement previously approved by the lessee unless it consented to that variation.

Article 13

1. - Where the equipment is not delivered or is delivered late or fails to conform to the supply agreement:

   (a) the lessee has the right as against the lessor to reject the equipment or to terminate the leasing agreement; and

   (b) the lessor has the right to remedy the failure to perform any of its duties, as if the lessee had agreed to buy the equipment from the lessor under the supply agreement.

2. - A right conferred by the previous paragraph shall be exercisable in the same manner and shall be lost in the same circumstances as if the lessee had agreed to buy the equipment from the lessor under the same terms as those of the supply agreement.

3. - The lessee shall be entitled to withhold rentals payable under the leasing agreement until the lessor has tendered equipment in conformity with the supply agreement or the lessee has lost the right to reject the equipment.

4. - Where the lessee has exercised a right to terminate the leasing agreement, the lessee shall be entitled to recover any rentals and other sums paid in advance, less a reasonable sum for any benefit the lessee has derived from the equipment.

5. - The lessee shall have no other claim against the lessor for non-delivery, delay in delivery or delivery of non-conforming equipment except to the extent to which this results from the act or omission of the lessor.

6. - Nothing in this article shall affect the lessee's rights against the supplier under Article 11.

Article 14

1. - In the event of default by the lessee, the lessor may recover accrued unpaid rentals, together with interest and damages.

2. - Where the lessee's default is substantial, then subject to paragraph 5 the lessor may also require accelerated payment of the value of the future rentals, where the leasing agreement so provides, or may terminate the leasing agreement and after such termination:

   (a) recover possession of the equipment; and

   (b) recover such damages as will place the lessor in the position in which it would have been had the lessee performed the leasing agreement in accordance with its terms.
3. - (a) The leasing agreement may provide for the manner in which the damages recoverable under paragraph 2 (b) are to be computed.

(b) Such provision shall be enforceable between the parties unless it would result in damages substantially in excess of those provided for under paragraph 2 (b). The parties may not derogate from or vary the effect of the present sub-paragraph.

4. - Where the lessor has terminated the leasing agreement, it shall not be entitled to enforce a term of that agreement providing for acceleration of payment of future rentals, but the value of such rentals may be taken into account in computing damages under paragraphs 2(b) and 3. The parties may not derogate from or vary the effect of the present paragraph.

5. - The lessor shall not be entitled to exercise its right of acceleration or its right of termination under paragraph 2 unless it has by notice given the lessee a reasonable opportunity of remedying the default so far as the same may be remedied.

6. - The lessor shall not be entitled to recover damages to the extent that it has failed to take all reasonable steps to mitigate its loss.

**Article 15**

1. - The lessor may transfer or otherwise deal with all or any of its rights in the equipment or under the leasing agreement. Such a transfer shall not relieve the lessor of any of its duties under the leasing agreement or alter either the nature of the leasing agreement or its legal treatment as provided in this Convention.

2. - The lessee may transfer the right to the use of the equipment or any other rights under the leasing agreement only with the consent of the lessor and subject to the rights of third parties

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

*Revised text of Article 5
submitted by the Drafting Committee to the Committee of the Whole*

**Article 5**

1. - The application of this Convention may be excluded only if the lessor, the lessee and the supplier each agree to exclude it.

2. - Where the application of this Convention has not been excluded in accordance with the previous paragraph, the parties may, in their relations with each other, derogate from or vary the effect of any of its provisions except as stated in Articles 9(3) and 14(3)(b) and (4).
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Preliminary text of Chapters I and II submitted by
the Drafting Committee to the Committee of the Whole

CHAPTER I - SPHERE OF APPLICATION AND GENERAL PROVISIONS

Article 1

1. - This Convention governs factoring contracts and assignments of receivables as described in this Chapter.

2. - For the purposes of this Convention, “factoring contract” means a contract concluded between one party (the supplier) and another party (the factor) pursuant to which:

   (a) the supplier may or will assign to the factor receivables arising from contracts of sale of goods made between the supplier and its customers (debtors) other than those for the sale of goods bought primarily for their personal, family or household use;

   (b) the factor is to perform at least two of the following functions:
       – finance for the supplier, including loans and advance payments;
       – maintenance of accounts (ledging) relating to the receivables;
       – collection of receivables;
       – protection against default in payment by debtors;

   (c) notice of the assignment of the receivables is to be given to debtors.

3. - In this Convention references to “goods” and “sale of goods” shall include services and the supply of services.

4. - For the purposes of this Convention:

   (a) a notice in writing need not be signed but must identify the person by whom or in whose name it is given;

   (b) “notice in writing” includes, but is not limited to, telegrams, telex and any other telecommunication capable of being reproduced in tangible form.

Article 2

1. - This Convention applies whenever the receivables assigned pursuant to a factoring contract arise from a contract of sale of goods between a supplier and a debtor whose places of business are in different States and:
(a) those States and the State in which the factor has its place of business are Contracting States; or

(b) both the contract of sale of goods and the factoring contract are governed by the law of a Contracting State.

2. - A reference in this Convention to a party’s place of business shall, if it has more than one place of business, mean the place of business which has the closest relationship to the relevant contract and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that contract.

Article 3

1. - The application of this Convention may be excluded:

(a) by the parties to the factoring contract; or

(b) by the parties to the contract of sale of goods, as regards receivables arising at or after the time when the factor has received notice in writing of such exclusion.

2. - Where the application of this Convention is excluded in accordance with the previous paragraph, such exclusion may be made only as regards the Convention as a whole.

Article 4

1. - In the interpretation of this Convention, regard is to be had to its object and purpose as set forth in the Preamble, to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.

2. - Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law.

CHAPTER II – RIGHTS AND DUTIES OF THE PARTIES

Article 5

As between the parties to the factoring contract:

(a) a provision in the factoring contract for the assignment of existing or future receivables shall not be rendered invalid by the fact that the contract does not specify them individually, if at the time of conclusion of the contract or when they come into existence they can be identified to the contract;

(b) a provision in the factoring contract by which future receivables are assigned operates to transfer the receivables to the factor when they come into existence without the need for any new act of transfer.
Article 6

[Defer until the Report of the Working Group on the former Article 5]

Article 7

A factoring contract may validly provide as between the parties thereto for the transfer, with or without a new act of transfer, of all or any of the supplier’s rights deriving from the sale of goods, including the benefit of any provision in the contract of sale of goods reserving to the supplier title to the goods or creating any security interest.

Article 8

1. - The debtor is under a duty to pay the factor if, and only if, the debtor does not have knowledge of any other person’s superior right to payment and notice of the assignment:

   (a) is given to the debtor in writing by the supplier or by the factor with the supplier’s authority;

   (b) reasonably identifies the receivables which have been assigned and the factor to whom or for whose account the debtor is required to make payment; and

   (c) relates to receivables arising under a contract of sale of goods made at or before the time the notice is given.

2. - Irrespective of any other ground on which payment by the debtor to the factor discharges the debtor from liability, payment shall be effective for this purpose if made in accordance with the previous paragraph.

Article 9

1. - In a claim by the factor against the debtor for payment of a receivable arising under a contract of sale of goods the debtor may set up against the factor all defences arising under that contract of which the debtor could have availed itself if such claim had been made by the supplier.

2. - The debtor may also assert against the factor any right of set-off in respect of claims existing against the supplier in whose favour the receivable arose, and available to the debtor at the time the debtor received a notice of assignment conforming to Article 8(1).

Article 10

1. - Without prejudice to the debtor’s rights under Article 9, non-performance or defective or late performance of the contract of sale of goods shall not by itself entitle the debtor to recover a sum paid by the debtor to the factor if the debtor has a right to recover that sum from the supplier.

2. - The debtor who has such a right to recover from the supplier a sum paid to the factor in respect of a receivable shall nevertheless be entitled to recover that sum from the factor to
the extent that:

(a) the factor has not discharged an obligation to make payment to the supplier in respect of that receivable; or

(b) the factor made such payment at a time when it knew of the supplier's non-performance or defective or late performance as regards the goods to which the debtor's payment relates.

Article 11

1. - Where a receivable is assigned by a supplier to a factor pursuant to a factoring contract governed by this Convention:

(a) the rules set out in Articles 5 to 10 shall, subject to sub-paragraph (b) of this paragraph, apply to any subsequent assignment of the receivable by the factor or by a subsequent assignee;

(b) the provisions of Articles 8 to 10 shall apply as if the subsequent assignee were the factor.

2. - For the purposes of this Convention, notice to the debtor of the subsequent assignment also constitutes notice of the assignment to the factor.

3. - This Convention shall not apply to a subsequent assignment which is prohibited by the terms of the factoring contract.

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

Preliminary text of the Preamble and Articles 6 and X submitted by the Drafting Committee to the Committee of the Whole

PREAMBLE

THE STATES PARTIES TO THIS CONVENTION,

CONSCIOUS of the fact that international factoring has a major role to play in the development of international trade,

RECOGNISING therefore the importance of adopting uniform rules to provide a legal framework that will facilitate international factoring, while maintaining a fair balance of interests between the different parties involved in factoring transactions,

HAVE AGREED as follows:

*****
Article 6

1. - The assignment of a receivable by the supplier to the factor shall be effective notwithstanding any agreement between the supplier and the debtor prohibiting such assignment.

2. - However, such assignment shall not be effective against the debtor when, at the time of conclusion of the contract of sale of goods, he has his place of business in a Contracting State which has made a declaration under Article X of this Convention.

3. - Nothing in paragraph 1 shall affect any obligation of good faith owed by the supplier to the debtor or any liability of the supplier to the debtor in respect of an assignment made in breach of the terms of the contract of sale of goods.

Article X

A Contracting State may at any time make a declaration in accordance with Article 6, paragraph 2 of this Convention that an assignment under Article 6, paragraph 1 shall not be effective against the debtor when, at the time of conclusion of the contract of sale of goods, he has his place of business in that State.
PART III

FINAL CLAUSES COMMITTEE

Basic papers

Comments on the draft final provisions capable of embodiment in the draft Convention on international financial leasing by Governments (Japan) .................................................. 269

Comments on the draft final provisions capable of embodiment in the draft Convention on international factoring by Governments (Japan) .................................................. 270

Working papers on the draft final provisions capable of embodiment in the draft Convention on international financial leasing submitted by:

Comité Maritime International .......................................................... 271
Netherlands .................................................................................. 271
Final Clauses Committee ............................................................... 272
United Kingdom .......................................................................... 276
United Kingdom .......................................................................... 276

Texts submitted by the Drafting Committee on the draft final provisions capable of embodiment in the draft Convention on international financial leasing:

Text of Chapter III ..................................................................... 277
Text of Chapter III approved by the Drafting Committee on 23 May 1988 .................................................. 280
Text of Chapter III approved by the Drafting Committee on 24 May 1988 .................................................. 284

Text submitted by the Drafting Committee on the draft final provisions capable of embodiment in the draft Convention on international factoring:

Text of Chapter IV approved by the Drafting Committee on 24 May 1988 .................................................. 287
CONSIDERATION OF THE DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Comments on the draft final provisions
by Governments (Japan) ¹¹

Re Article A

It is preferable that paragraph 4 of Article A be amended, following the examples of paragraph 4 of Article 91 of the Vienna Sale Convention and paragraph 4 of Article 22 of the Convention on Agency in the International Sale of Goods (hereinafter referred to as "the Geneva Agency Convention") as follows:

"Instruments of ratification, acceptance, approval or accession shall be deposited with the depositary."

Re Article B

Three is too small a number as the number of instruments necessary for the entry into force of this Convention. Ten, as in Article 99 of the Vienna Sale Convention and Article 33 of the Geneva Agency Convention, would be preferable.

Re Article C

It is appropriate to retain Article C in the final provisions since it is based on Article 90 of the Vienna Sale Convention and Article 23 of the Geneva Agency Convention. It is, therefore, desirable to remove the square brackets.

Re Article J

If the proposed amendment with regard to Article A (see above) is supported, it is then preferable to amend paragraph 2 of Article J as follows:

"Instruments of denunciation shall be deposited with the depositary."

¹¹ These comments were circulated in Conference document CONF. 7/3 together with the comments by the Governments of Japan, Spain and the United States of America on the draft Convention on international financial leasing, reproduced at pp. 151-160 supra.
CONSIDERATION OF THE DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION
ON INTERNATIONAL FACTORING

Comments on the draft final provisions
by Governments (Japan) (1)

Re Article A

It is preferable that paragraph 4 of Article A be amended, following the example of paragraph 4 of Article 91 of the Vienna Sale Convention and paragraph 4 of Article 22 of the Geneva Agency Convention, as follows:

"Instruments of ratification, acceptance, approval or accession shall be deposited with the depositary".

Re Article B

Three is too small a number of instruments necessary for the entry into force of this Convention. Ten, the same as in Article 99 of the Vienna Sale Convention and in Article 33 of the Geneva Agency Convention, is preferable.

Re Article C

It is appropriate to maintain Article C in the final provisions since it is based on Article 90 of the Vienna Sale Convention and Article 23 of the Geneva Agency Convention. It is, therefore, desirable to remove the square brackets.

Re Article J

If the proposed amendment with regard to Article A is accepted, it would then be preferable to amend paragraph 2 of Article J as follows:

"Instruments of denunciation shall be deposited with the depositary".

(1) These comments were circulated in Conference document CONF. 7/6 together with the comments by the Governments of Japan and Spain on the draft Convention on international factoring, reproduced at pp. 186-189 supra.
CONSIDERATION OF THE DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Comité Maritime International

Article C

The C.M.I. recommends that this Article be included in the Convention in order to avoid any conflicts with existing or future maritime Conventions.

However, attention is drawn to the fact that maritime Conventions as a rule are global in scope and that their scope of application in many cases, therefore, does not depend upon reciprocity or upon the existence of certain ties to the Contracting States. Particularly, it may be noted that the existence of a place of business in a State is not a condition for their application.

The requirement in the proviso of Article C would, therefore, normally have the effect that this Convention would prevail and that conflicts of Conventions would arise.

It is, therefore, recommended to delete the words: “provided that the supplier, the lessor and the lessee have their places of business in the States parties to such agreement”.

If this is accepted Article 5, paragraph 4 may be superfluous.

CONF. 7/C.2/W.P. 2
12 May 1988

CONSIDERATION OF THE DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Proposals by the Netherlands Delegation

Article A

Paragraph 1

Replace the words “the Unidroit draft Conventions” by “the text of the Unidroit Conventions”.

It is suggested that the Convention be open for signature until 31 December 1989.
Paragraph 4

Replace the words “is effected” by “shall be effected”.
Replace the words “a formal instrument to that effect” by “the appropriate instrument”.
Add the words “as defined in Article K” to the words “the depositary”.

Article B

Paragraphs 1 and 2

Replace the words “enters into force” by “shall enter into force”.

Article C

The Netherlands delegation is in favour of the deletion of Article C, because it is unusual to include a provision like this in a Convention and because of the negative conflict of Conventions which could arise.

Witness Clause

Insert the words “for that purpose” before “by their respective Governments”.

CONF. 7/C.2/W.P. 3
13 May 1988

CONSIDERATION OF THE DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Text of the Final Clauses of the draft Convention
on International Financial Leasing as provisionally
approved by the Final Clauses Committee
at its first session on 12 May 1988

Article A

1. - This Convention is open for signature at the concluding meeting of the Diplomatic Conference for the adoption of the draft Unidroit Conventions on international factoring and international financial leasing and will remain open for signature by all States at Ottawa until 31 December 1990.

2. - This Convention is subject to ratification, acceptance or approval by States which have signed it.
3. - This Convention is open for accession by all States which are not signatory States as from the date it is open for signature.

4. - Ratification, acceptance, approval or accession is effected by the deposit of a formal instrument to that effect with the depositary.

Article B

1. - This Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the fifth instrument of ratification, acceptance, approval or accession.

2. - For each State that ratifies, accepts, approves, or accedes to this Convention after the deposit of the fifth instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.

[Article C]

This Convention does not prevail over any international agreement which has already been or may be entered into and which contains provisions concerning matters governed by this Convention, provided that the supplier, the lessor and the lessee have their places of business in States parties to such agreement.\(^1\)

Article D

1. - If a Contracting State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may substitute its declaration by another declaration at any time.

2. - These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. - If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

4. - If a Contracting State makes no declaration under paragraph 1 of this article, the Convention is to extend to all territorial units of that State.

Article E

1. - Two or more Contracting States which have the same or closely related legal rules on

\(^1\) At its first session the Final Clauses Committee decided to resume consideration of this article at a later session.
matters governed by this Convention may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States. Such declarations may be made jointly or by reciprocal unilateral declarations.

2. - A Contracting State which has the same or closely related legal rules on matters governed by this Convention as one or more non-Contracting States may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States.

3. - If a State which is the object of a declaration under the previous paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which the Convention enters into force in respect of the new Contracting State, have the effect of a declaration made under paragraph 1 of this article, provided that the new Contracting State joins in such declaration or makes a reciprocal unilateral declaration.

Article G

1. - Declarations made under this Convention at the time of signature are subject to confirmation upon ratification, acceptance or approval.

2. - Declarations and confirmations of declarations are to be in writing and to be formally notified to the depositary.

3. - A declaration takes effect simultaneously with the entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral declarations under Article E take effect on the first day of the month following the expiration of six months after the receipt of the latest declaration by the depository.

4. - Any State which makes a declaration under this Convention may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal is to take effect on the first day of the month following the expiration of six months after the date of the receipt of the notification by the depositary.

5. - A withdrawal of a declaration made under Article E renders inoperative, as from the date on which the withdrawal takes effect, any reciprocal declaration made by another State under that article.\(^{(2)}\)

Article H

No reservations are permitted [except those expressly authorised in] [to] this Convention.\(^{(3)}\)

Article I

This Convention applies when the leasing agreement and the supply agreement are both

\(^{(2)}\) The Final Clauses Committee agreed at its first session to reconsider this paragraph at a later session.

\(^{(3)}\) The formulation of this article will depend upon whether any reservations to the Convention will be permitted.
concluded on or after the date on which the Convention enters into force in respect of the Contracting States referred to in Article 2 (1)(a), or of the Contracting State or States referred to in paragraph 1 (b) of that article.

Article J

1. - This Convention may be denounced by any Contracting State at any time after the date on which it enters into force for that State.

2. - Denunciation is effected by the deposit of an instrument to that effect with the depositary.

3. - A denunciation takes effect on the first day of the month following the expiration of twelve months after the deposit of the instrument of denunciation with the depositary. Where a longer period for the denunciation to take effect is specified in the instrument of denunciation it takes effect upon the expiration of such longer period after its deposit with the depositary.

Article K

1. - This Convention shall be deposited with the Government of Canada.

2. - The Government of Canada shall:

   (a) inform all States which have signed or acceded to this Convention and the President of the International Institute for the Unification of Private Law (Unidroit) of:

   (i) each new signature or deposit of an instrument of ratification, acceptance, approval or accession, together with the date thereof;

   (ii) each declaration made under Articles D, E;

   (iii) the withdrawal of any declaration made under Article G (4);

   (iv) the date of entry into force of this Convention;

   (v) the deposit of an instrument of denunciation of this Convention together with the date of its deposit and the date on which it takes effect;

   (b) transmit certified true copies of this Convention to all signatory States, to all States acceding to the Convention and to the President of the International Institute for the Unification of Private Law (Unidroit).

Authentic text and witness clause

IN WITNESS WHEREOF the undersigned plenipotentiaries, being duly authorised by their respective Governments, have signed this Convention.

DONE at Ottawa, this ..........day of May, one thousand nine hundred and eighty-eight, in a single original, of which the English and French texts are equally authentic.
CONSIDERATION OF THE DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the United Kingdom Delegation

Article C

Proposed new paragraph 2:

"2. - This Convention shall not affect any liability imposed on any person by existing or future Conventions."

REASONS FOR PROPOSAL

The U.K. delegation is particularly concerned to ensure that the present Convention does not detract from the Convention on civil liability for oil pollution damage. While Article 7 of the draft leasing Convention limits the exclusion of the lessor’s liability to third parties to liability arising in its capacity as lessor there remains room for doubt as to how the phrase “in its capacity of lessor” might be interpreted in particular contexts such as those covered by the Convention on oil pollution damage.

CONSIDERATION OF THE DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the United Kingdom Delegation

New Article F

“A contracting State may declare at the time of signature, ratification, acceptance, approval or accession that it will not be bound by any part of this Convention in respect of financial leasing transactions as described in Articles 1 and 2 if they relate to the supply of ships.”

REASON FOR PROPOSAL

In the light of the uncertainty as to whether provisions of the Convention will be mandatory, and the involvement of U.N.C.T.A.D. in the field of shipping generally it is the view of the U.K. delegation that parties should have the freedom to make a reservation in order to avoid any prejudice to their position in both the above respects.
CONSIDERATION OF THE DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Text of Chapter III
submitted by the Drafting Committee
to the Final Clauses Committee

UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

CHAPTER III - FINAL PROVISIONS

Article A

1. - This Convention is open for signature at the concluding meeting of the Diplomatic Conference for the Adoption of the Draft Unidroit Conventions on International Factoring and International Financial Leasing and will remain open for signature by all States at Ottawa until 31 December 1990.

2. - This Convention is subject to ratification, acceptance or approval by States which have signed it.

3. - This Convention is open for accession by all States which are not signatory States as from the date it is open for signature.

4. - Ratification, acceptance, approval or accession is effected by the deposit of a formal instrument to that effect with the depositary.

Article B

1. - This Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the fifth instrument of ratification, acceptance, approval or accession.

2. - For each State that ratifies, accepts, approves, or accedes to this Convention after the deposit of the fifth instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.
Article C

This Convention does not prevail over any international agreement which has already been or may be entered into. This Convention shall not affect any liability imposed on any person by existing or future conventions.

Article D

1. - If a Contracting State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may substitute its declaration by another declaration at any time.

2. - These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. - If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

4. - If a Contracting State makes no declaration under paragraph 1 of this article, the Convention is to extend to all territorial units of that State.

Article E

1. - Two or more Contracting States which have the same or closely related legal rules on matters governed by this Convention may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States. Such declarations may be made jointly or by reciprocal unilateral declarations.

2. - A Contracting State which has the same or closely related legal rules on matters governed by this Convention as one or more non-Contracting States may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States.

3. - If a State which is the object of a declaration under the previous paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which the Convention enters into force in respect of the new Contracting State, have the effect of a declaration made under paragraph 1 of this article, provided that the new Contracting State joins in such declaration or makes a reciprocal unilateral declaration.

Article G

1. - Declarations made under this Convention at the time of signature are subject to confirmation upon ratification, acceptance or approval.

2. - Declarations and confirmations of declarations are to be in writing and to be formally
notified to the depositary.

3. - A declaration takes effect simultaneously with the entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral declarations under Article E take effect on the first day of the month following the expiration of six months after the receipt of the latest declaration by the depositary.

4. - Any State which makes a declaration under this Convention may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal is to take effect on the first day of the month following the expiration of six months after the date of the receipt of the notification by the depositary.

5. - A withdrawal of a declaration made under Article E renders inoperative in relation to the withdrawing State, as from the date on which the withdrawal takes effect, any [joint or] reciprocal [unilateral] declaration made by another State under that article.

Article H

No reservations are permitted [except those expressly authorised in] [to] this Convention.(1)

Article I

This Convention applies to a financial leasing transaction when the leasing agreement and the supply agreement are both concluded on or after the date on which the Convention enters into force in respect of the Contracting States referred to in Article 3 (1)(a), or of the Contracting State or States referred to in paragraph 1 (b) of that article.

Article J

1. - This Convention may be denounced by any Contracting State at any time after the date on which it enters into force for that State.

2. - Denunciation is effected by the deposit of an instrument to that effect with the depositary.

3. - A denunciation takes effect on the first day of the month following the expiration of twelve months after the deposit of the instrument of denunciation with the depositary. Where a longer period for the denunciation to take effect is specified in the instrument of denunciation it takes effect upon the expiration of such longer period after its deposit with the depositary.

Article K

1. - This Convention shall be deposited with the Government of Canada.

(1) The formulation and placing of this provision will depend upon whether any reservations to the Convention will be permitted.
2. - The Government of Canada shall:

(a) inform all States which have signed or acceded to this Convention and the President of the International Institute for the Unification of Private Law (Unidroit) of:

(i) each new signature or deposit of an instrument of ratification, acceptance, approval or accession, together with the date thereof;

(ii) each declaration made under Articles D, E, [H];

(iii) the withdrawal of any declaration made under Article G (4);

(iv) the date of entry into force of this Convention;

(v) the deposit of an instrument of denunciation of this Convention together with the date of its deposit and the date on which it takes effect;

(b) transmit certified true copies of this Convention to all signatory States, to all States acceding to the Convention and to the President of the International Institute for the Unification of Private Law (Unidroit).

**Authentic text and witness clause**

IN WITNESS WHEREOF the undersigned plenipotentiaries, being duly authorised by their respective Governments, have signed this Convention.

DONE at Ottawa, this ...........day of May, one thousand nine hundred and eighty-eight, in a single original, of which the English and French texts are equally authentic.

CONF. 7/D.C./3 24 May 1988

CONSIDERATION OF THE DRAFT FINAL PROVISIONS CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

**Text of Chapter III**

*approved by the Drafting Committee on 23 May 1988*

UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

CHAPTER III - FINAL PROVISIONS

*Article 15*

1. - This Convention is open for signature at the concluding meeting of the Diplomatic
Conference for the Adoption of the Draft Unidroit Conventions on International Factoring and International Financial Leasing and will remain open for signature by all States at Ottawa until 31 December 1990.

2. - This Convention is subject to ratification, acceptance or approval by States which have signed it.

3. - This Convention is open for accession by all States which are not signatory States as from the date it is open for signature.

4. - Ratification, acceptance, approval or accession is effected by the deposit of a formal instrument to that effect with the depositary.

Article 16

1. - This Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the third instrument of ratification, acceptance, approval or accession.

2. - For each State that ratifies, accepts, approves, or accedes to this Convention after the deposit of the third instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.

Article 17

This Convention does not prevail over any treaty which has already been or may be entered into; in particular it shall not affect any liability imposed on any person by existing or future treaties.

Article 18

1. - If a Contracting State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may substitute its declaration by another declaration at any time.

2. - These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. - If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

4. - If a Contracting State makes no declaration under paragraph 1, the Convention is to extend to all territorial units of that State.
Article 19

1. - Two or more Contracting States which have the same or closely related legal rules on matters governed by this Convention may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States. Such declarations may be made jointly or by reciprocal unilateral declarations.

2. - A Contracting State which has the same or closely related legal rules on matters governed by this Convention as one or more non-Contracting States may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States.

3. - If a State which is the object of a declaration under the previous paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which the Convention enters into force in respect of the new Contracting State, have the effect of a declaration made under paragraph 1, provided that the new Contracting State joins in such declaration or makes a reciprocal unilateral declaration.

Article 21

1. - Declarations made under this Convention at the time of signature are subject to confirmation upon ratification, acceptance or approval.

2. - Declarations and confirmations of declarations are to be in writing and to be formally notified to the depositary.

3. - A declaration takes effect simultaneously with the entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral declarations under Article 19 take effect on the first day of the month following the expiration of six months after the receipt of the latest declaration by the depositary.

4. - Any State which makes a declaration under this Convention may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal is to take effect on the first day of the month following the expiration of six months after the date of the receipt of the notification by the depositary.

5. - A withdrawal of a declaration made under Article 19 renders inoperative in relation to the withdrawing State, as from the date on which the withdrawal takes effect, any joint or reciprocal unilateral declaration made by another State under that article.

Article 22

No reservations are permitted except those expressly authorised in this Convention.

Article 23

This Convention applies to a financial leasing transaction when the leasing agreement and
the supply agreement are both concluded on or after the date on which the Convention enters into force in respect of the Contracting States referred to in Article 3 (1)(a), or of the Contracting State or States referred to in paragraph 1 (b) of that article.

Article 24

1. - This Convention may be denounced by any Contracting State at any time after the date on which it enters into force for that State.

2. - Denunciation is effected by the deposit of an instrument to that effect with the depositary.

3. - A denunciation takes effect on the first day of the month following the expiration of six months after the deposit of the instrument of denunciation with the depositary. Where a longer period for the denunciation to take effect is specified in the instrument of denunciation it takes effect upon the expiration of such longer period after its deposit with the depositary.

Article 25

1. - This Convention shall be deposited with the Government of Canada.

2. - The Government of Canada shall:

   (a) inform all States which have signed or acceded to this Convention and the President of the International Institute for the Unification of Private Law (Unidroit) of:

      (i) each new signature or deposit of an instrument of ratification, acceptance, approval or accession, together with the date thereof;

      (ii) each declaration made under Articles 18, 19 and 20;

      (iii) the withdrawal of any declaration made under Article 21 (4);

      (iv) the date of entry into force of this Convention;

      (v) the deposit of an instrument of denunciation of this Convention together with the date of its deposit and the date on which it takes effect;

   (b) transmit certified true copies of this Convention to all signatory States, to all States acceding to the Convention and to the President of the International Institute for the Unification of Private Law (Unidroit).

Authentic text and witness clause

IN WITNESS WHEREOF the undersigned plenipotentiaries, being duly authorised by their respective Governments, have signed this Convention.

DONE at Ottawa, this ..........day of May, one thousand nine hundred and eighty-eight, in a single original, of which the English and French texts are equally authentic.
CONSIDERATION OF THE DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Text of Chapter III
approved by the Drafting Committee
on 24 May 1988

UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

CHAPTER III - FINAL PROVISIONS

Article 15

1. - This Convention is open for signature at the concluding meeting of the Diplomatic Conference for the Adoption of the Draft Unidroit Conventions on International Factoring and International Financial Leasing and will remain open for signature by all States at Ottawa until 31 December 1990.

2. - This Convention is subject to ratification, acceptance or approval by States which have signed it.

3. - This Convention is open for accession by all States which are not signatory States as from the date it is open for signature.

4. - Ratification, acceptance, approval or accession is effected by the deposit of a formal instrument to that effect with the depositary.

Article 16

1. - This Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the third instrument of ratification, acceptance, approval or accession.

2. - For each State that ratifies, accepts, approves, or accedes to this Convention after the deposit of the third instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.

Article 17

This Convention does not prevail over any treaty which has already been or may be entered
into; in particular it shall not affect any liability imposed on any person by existing or future treaties.

Article 18

1. - If a Contracting State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may substitute its declaration by another declaration at any time.

2. - These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. - If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

4. - If a Contracting State makes no declaration under paragraph 1, the Convention is to extend to all territorial units of that State.

Article 19

1. - Two or more Contracting States which have the same or closely related legal rules on matters governed by this Convention may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States. Such declarations may be made jointly or by reciprocal unilateral declarations.

2. - A Contracting State which has the same or closely related legal rules on matters governed by this Convention as one or more non-Contracting States may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States.

3. - If a State which is the object of a declaration under the previous paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which the Convention enters into force in respect of the new Contracting State, have the effect of a declaration made under paragraph 1, provided that the new Contracting State joins in such declaration or makes a reciprocal unilateral declaration.

[Article 20 - Article F as adopted by the Conference on 19 May 1988]

Article 21

1. - Declarations made under this Convention at the time of signature are subject to confirmation upon ratification, acceptance or approval.

2. - Declarations and confirmations of declarations are to be in writing and to be formally
notified to the depositary.

3. - A declaration takes effect simultaneously with the entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral declarations under Article 19 take effect on the first day of the month following the expiration of six months after the receipt of the latest declaration by the depositary.

4. - Any State which makes a declaration under this Convention may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal is to take effect on the first day of the month following the expiration of six months after the date of the receipt of the notification by the depositary.

5. - A withdrawal of a declaration made under Article 19 renders inoperative in relation to the withdrawing State, as from the date on which the withdrawal takes effect, any joint or reciprocal unilateral declaration made by another State under that article.

Article 22

No reservations are permitted except those expressly authorised in this Convention.

Article 23

This Convention applies to a financial leasing transaction when the leasing agreement and the supply agreement are both concluded on or after the date on which the Convention enters into force in respect of the Contracting States referred to in Article 3 (1)(a), or of the Contracting State or States referred to in paragraph 1 (b) of that article.

Article 24

1. - This Convention may be denounced by any Contracting State at any time after the date on which it enters into force for that State.

2. - Denunciation is effected by the deposit of an instrument to that effect with the depositary.

3. - A denunciation takes effect on the first day of the month following the expiration of six months after the deposit of the instrument of denunciation with the depositary. Where a longer period for the denunciation to take effect is specified in the instrument of denunciation it takes effect upon the expiration of such longer period after its deposit with the depositary.

Article 25

1. - This Convention shall be deposited with the Government of Canada.

2. - The Government of Canada shall:

(a) inform all States which have signed or acceded to this Convention and the President of the International Institute for the Unification of Private Law (Unidroit) of:
(i) each new signature or deposit of an instrument of ratification, acceptance, approval or accession, together with the date thereof;

(ii) each declaration made under Articles 18, 19 and 20;

(iii) the withdrawal of any declaration made under Article 21 (4);

(iv) the date of entry into force of this Convention;

(v) the deposit of an instrument of denunciation of this Convention together with the date of its deposit and the date on which it takes effect;

(b) transmit certified true copies of this Convention to all signatory States, to all States acceding to the Convention and to the President of the International Institute for the Unification of Private Law (Unidroit).

IN WITNESS WHEREOF the undersigned plenipotentiaries, being duly authorised by their respective Governments, have signed this Convention.

DONE at Ottawa, this ............day of May, one thousand nine hundred and eighty-eight, in a single original, of which the English and French texts are equally authentic.

CONF. 7/D.C./5
25 May 1988

CONSIDERATION OF THE DRAFT FINAL PROVISIONS
CAPABLE OF EMBODIMENT IN THE DRAFT CONVENTION
ON INTERNATIONAL FACTORING

Text of Chapter IV
approved by the Drafting Committee
on 24 May 1988

CHAPTER IV - FINAL PROVISIONS

Article 13

1. - This Convention is open for signature at the concluding meeting of the Diplomatic Conference for the Adoption of the Draft Unidroit Conventions on International Factoring and International Financial Leasing and will remain open for signature by all States at Ottawa until 31 December 1990.

2. - This Convention is subject to ratification, acceptance or approval by States which have signed it.

3. - This Convention is open for accession by all States which are not signatory States as from the date it is open for signature.
4. - Ratification, acceptance, approval or accession is effected by the deposit of a formal instrument to that effect with the depositary.

Article 14

1. - This Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the third instrument of ratification, acceptance, approval or accession.

2. - For each State that ratifies, accepts, approves, or accedes to this Convention after the deposit of the third instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.

Article 15

This Convention does not prevail over any treaty which has already been or may be entered into.

Article 16

1. - If a Contracting State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may substitute its declaration by another declaration at any time.

2. - These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. - If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

4. - If a Contracting State makes no declaration under paragraph 1, the Convention is to extend to all territorial units of that State.

Article 17

1. - Two or more Contracting States which have the same or closely related legal rules on matters governed by this Convention may at any time declare that the Convention is not to apply where the supplier, the factor and the debtor have their places of business in those States. Such declarations may be made jointly or by reciprocal unilateral declarations.

2. - A Contracting State which has the same or closely related legal rules on matters governed by this Convention as one or more non-Contracting States may at any time declare that the Convention is not to apply where the supplier, the factor and the debtor have their places of business in those States.
3. - If a State which is the object of a declaration under the previous paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which the Convention enters into force in respect of the new Contracting State, have the effect of a declaration made under paragraph 1, provided that the new Contracting State joins in such declaration or makes a reciprocal unilateral declaration.

[Article 18 - Article X as adopted by the Committee of the Whole]

Article 19

1. - Declarations made under this Convention at the time of signature are subject to confirmation upon ratification, acceptance or approval.

2. - Declarations and confirmations of declarations are to be in writing and to be formally notified to the depositary.

3. - A declaration takes effect simultaneously with the entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral declarations under Article 17 take effect on the first day of the month following the expiration of six months after the receipt of the latest declaration by the depositary.

4. - Any State which makes a declaration under this Convention may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal is to take effect on the first day of the month following the expiration of six months after the date of the receipt of the notification by the depositary.

5. - A withdrawal of a declaration made under Article 17 renders inoperative in relation to the withdrawing State, as from the date on which the withdrawal takes effect, any joint or reciprocal unilateral declaration made by another State under that article.

Article 20

No reservations are permitted except those expressly authorised in this Convention.

Article 21

This Convention applies when receivables assigned pursuant to a factoring contract arise from a contract of sale of goods concluded on or after the date on which the Convention enters into force in respect of the Contracting States referred to in Article 2, paragraph 1(a), or the Contracting State or States referred to in paragraph 1(b) of that article, provided that:

(a) the factoring contract is concluded on or after that date; or

(b) the parties to the factoring contract have agreed that the Convention shall apply.
Article 22

1. - This Convention may be denounced by any Contracting State at any time after the date on which it enters into force for that State.

2. - Denunciation is effected by the deposit of an instrument to that effect with the depositary.

3. - A denunciation takes effect on the first day of the month following the expiration of six months after the deposit of the instrument of denunciation with the depositary. Where a longer period for the denunciation to take effect is specified in the instrument of denunciation it takes effect upon the expiration of such longer period after its deposit with the depositary.

Article 23

1. - This Convention shall be deposited with the Government of Canada.

2. - The Government of Canada shall:

   (a) inform all States which have signed or acceded to this Convention and the President of the International Institute for the Unification of Private Law (Unidroit) of:

      (i) each new signature or deposit of an instrument of ratification, acceptance, approval or accession, together with the date thereof;

      (ii) each declaration made under Articles 16, 17 and 18;

      (iii) the withdrawal of any declaration made under Article 19 (4);

      (iv) the date of entry into force of this Convention;

      (v) the deposit of an instrument of denunciation of this Convention together with the date of its deposit and the date on which it takes effect;

   (b) transmit certified true copies of this Convention to all signatory States, to all States acceding to the Convention and to the President of the International Institute for the Unification of Private Law (Unidroit).

IN WITNESS WHEREOF the undersigned plenipotentiaries, being duly authorised by their respective Governments, have signed this Convention.

DONE at Ottawa, this ........ day of May, one thousand nine hundred and eighty-eight, in a single original, of which the English and French texts are equally authentic.
PART IV
PLENUM

Working papers on the draft Unidroit Convention on international financial leasing submitted by:

France, Mexico and Philippines .......................................................... 293
France, Mexico and Philippines .......................................................... 293
Canada .................................................................................................. 293

Reports to Plenum

Report of the Committee of the Whole (on the draft Unidroit Convention on international financial leasing) .......................................................... 294
Second report of the Committee of the Whole (on the draft Unidroit Convention on international factoring) .......................................................... 300
Report of the Final Clauses Committee (on the draft final provisions capable of embodiment in the draft Convention on international financial leasing) .......................................................... 305
Second report of the Final Clauses Committee (on the draft final provisions capable of embodiment in the draft Convention on international factoring) .......................................................... 309
Report of the Credentials Committee .......................................................... 313

Draft Final Act submitted by the Drafting Committee .......................................................... 315
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Delegations of France, Mexico and the Philippines

Reintroduce Article F (Reservation):

"A Contracting State may declare at the time of signature, ratification, acceptance, approval or accession that it will not apply Article 8(3)."

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Delegations of France, Mexico and the Philippines

Reintroduce Article F (Reservation):

"A Contracting State may declare at the time of signature, ratification, acceptance, approval or accession that it will substitute its domestic law for Article 8(3) if its domestic law does not permit the lessor to exclude its liability for its default or negligence."

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Proposal by the Canadian Delegation

It is proposed that the word "article" in paragraph 2 of Article 3 of the Convention on International Financial Leasing be deleted and the word "Convention" be substituted.

REASONS

1. The rule of paragraph 2 should apply to Articles 18 and 19 as well.

2. The Leasing Convention should in this respect parallel Draft Article 2(2) of the Factoring Convention.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

Report of the Committee of the Whole to the Conference

1. - The Committee of the Whole held 14 sessions between 9 and 18 May 1988 at which it examined the draft Unidroit Convention on International Financial Leasing which had been prepared by a Unidroit committee of governmental experts (Study LIX - Doc. 48).

2. - Mr L. Sevón (Finland), who had been appointed Chairman of the Committee of the Whole by the Conference under Rule 6 of its Rules of Procedure, chaired all the sessions of the Committee.

3. - Acting under Rule 51 of the Rules of Procedure, the Committee elected Mr J.-P. Beraudo (France) and Mr M.A. Thiam (Guinea) as its first and second Vice-Chairmen respectively.

4. - At its final session the Committee of the Whole adopted, on second reading, the following text of Articles 1 to 14 (Chapters I and II) of the draft Unidroit Convention on International Financial Leasing:

[UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING]

PREAMBLE

THE STATES PARTIES TO THIS CONVENTION,

RECOGNISING the importance of removing certain legal impediments to the international financial leasing of equipment, while maintaining a fair balance of interests between the different parties to the transaction,

AWARE of the need to make international financial leasing more available,

CONSCIOUS of the fact that the rules of law governing the traditional contract of hire need to be adapted to the distinctive triangular relationship created by the financial leasing transaction,

RECOGNISING therefore the desirability of formulating certain uniform rules relating primarily to the civil and commercial law aspects of international financial leasing,

HAVE AGREED as follows:
CHAPTER I - SPHERE OF APPLICATION AND GENERAL PROVISIONS

Article 1

1. - This Convention governs a financial leasing transaction as described in paragraph 2 in which one party (the lessor),

(a) on the specifications of another party (the lessee), enters into an agreement (the supply agreement) with a third party (the supplier) under which the lessor acquires plant, capital goods or other equipment (the equipment) on terms approved by the lessee so far as they concern its interests, and

(b) enters into an agreement (the leasing agreement) with the lessee, granting to the lessee the right to use the equipment in return for the payment of rentals.

2. - The financial leasing transaction referred to in the previous paragraph is a transaction which includes the following characteristics:

(a) the lessee specifies the equipment and selects the supplier without relying primarily on the skill and judgment of the lessor;

(b) the equipment is acquired by the lessor in connection with a leasing agreement which, to the knowledge of the supplier, either has been made or is to be made between the lessor and the lessee; and

(c) the rentals payable under the leasing agreement are calculated so as to take into account in particular the amortisation of the whole or a substantial part of the cost of the equipment.

3. - This Convention applies whether or not the lessee has or subsequently acquires the option to buy the equipment or to hold it on lease for a further period, and whether or not for a nominal price or rental.

4. - This Convention applies to financial leasing transactions in relation to all equipment save that which is to be used primarily for the lessee’s personal, family or household purposes.

Article 2

In the case of one or more sub-leasing transactions involving the same equipment, this Convention applies to each transaction which is a financial leasing transaction and is otherwise subject to this Convention as if the person from whom the first lessor (as defined in paragraph 1 of the previous article) acquired the equipment were the supplier and as if the agreement under which the equipment was so acquired were the supply agreement.

Article 3

1. - This Convention applies when the lessor and the lessee have their places of business in different States and:
(a) those States and the State in which the supplier has its place of business are Contracting States; or

(b) both the supply agreement and the leasing agreement are governed by the law of a Contracting State.

2. - A reference in this article to a party’s place of business shall, if it has more than one place of business, mean the place of business which has the closest relationship to the relevant agreement and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that agreement.

Article 4

1. - The provisions of this Convention shall not cease to apply merely because the equipment has become a fixture to or incorporated in land.

2. - Any question whether or not the equipment has become a fixture to or incorporated in land, and if so the effect on the rights inter se of the lessor and a person having real rights in the land, shall be determined by the law of the State where the land is situated.

Article 5

1. - The application of this Convention may be excluded only if each of the parties to the supply agreement and each of the parties to the leasing agreement agree to exclude it.

2. - Where the application of this Convention has not been excluded in accordance with the previous paragraph, the parties may, in their relations with each other, derogate from or vary the effect of any of its provisions except as stated in Articles 8(3) and 13(3)(b) and (4).

Article 6

1. - In the interpretation of this Convention, regard is to be had to its object and purpose as set forth in the Preamble, to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.

2. - Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law.

CHAPTER II - RIGHTS AND DUTIES OF THE PARTIES

Article 7

1. - (a) The lessor’s real rights in the equipment shall be valid against the lessee’s trustee in bankruptcy and creditors, including creditors who have obtained an attachment or execution.

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

2. - Where by the applicable law the lessor’s real rights in the equipment are valid against
a person referred to in the previous paragraph only on compliance with rules as to public notice,
those rights shall be valid against that person only if there has been compliance with such rules.

3. - For the purposes of the previous paragraph the applicable law is the law of the State
which, at the time when a person referred to in paragraph 1 becomes entitled to invoke the rules
referred to in the previous paragraph, is :

(a) in the case of a registered ship, the State in which it is registered in the name of the
owner (for the purposes of this sub-paragraph a bareboat charterer is deemed not to be the
owner);

(b) in the case of an aircraft which is registered pursuant to the Convention on
International Civil Aviation done at Chicago on 7 December 1944, the State in which it is so
registered;

(c) in the case of other equipment of a kind normally moved from one State to another,
including an aircraft engine, the State in which the lessee has its principal place of business;

(d) in the case of all other equipment, the State in which the equipment is situated.

4. - Paragraph 2 shall not affect the provisions of any other treaty under which the lessor’s
real rights in the equipment are required to be recognised.

5. - This article shall not affect the priority of any creditor having:

(a) a consensual or non-consensual lien or security interest in the equipment arising
otherwise than by virtue of an attachment or execution, or

(b) any right of arrest, detention or disposition conferred specifically in relation to
ships or aircraft under the law applicable by virtue of the rules of private international law.

Article 8

1. - (a) Except as otherwise provided by this Convention or stated in the leasing agree-
ment, the lessor shall not incur any liability to the lessee in respect of the equipment save to the
extent that the lessee has suffered loss as the result of its reliance on the lessor’s skill and
judgment and of the lessor’s intervention in the selection of the supplier or the specifications
of the equipment.

(b) The lessor shall not, in its capacity of lessor, be liable to third parties for death,
personal injury or damage to property caused by the equipment.

(c) The above provisions of this paragraph shall not govern any liability of the lessor
in any other capacity, for example as owner.

2. - The lessor warrants that the lessee’s quiet possession will not be disturbed by a person
who has a superior title or right, or who claims a superior title or right and acts under the
authority of a court, where such title, right or claim is not derived from an act or omission of
the lessee.
3. - The parties may not derogate from or vary the effect of the provisions of the previous paragraph in so far as the superior title, right or claim is derived from an intentional or grossly negligent act or omission of the lessor.

4. - The provisions of paragraphs 2 and 3 shall not affect any broader warranty of quiet possession by the lessor which is mandatory under the law applicable by virtue of the rules of private international law.

Article 9

1. - The lessee shall take proper care of the equipment, use it in a reasonable manner and keep it in the condition in which it was delivered, subject to fair wear and tear and to any modification of the equipment agreed by the parties.

2. - When the leasing agreement comes to an end the lessee, unless exercising a right to buy the equipment or to hold the equipment on lease for a further period, shall return the equipment to the lessor in the condition specified in the previous paragraph.

Article 10

1. - The duties of the supplier under the supply agreement shall also be owed to the lessee as if it were a party to that agreement and as if the equipment were to be supplied directly to the lessee. However, the supplier shall not be liable to both the lessor and the lessee in respect of the same damage.

2. - Nothing in this article shall entitle the lessee to terminate or rescind the supply agreement without the consent of the lessor.

Article 11

The lessee’s rights derived from the supply agreement under this Convention shall not be affected by a variation of any term of the supply agreement previously approved by the lessee unless it consented to that variation.

Article 12

1. - Where the equipment is not delivered or is delivered late or fails to conform to the supply agreement:

   (a) the lessee has the right as against the lessor to reject the equipment or to terminate the leasing agreement; and

   (b) the lessor has the right to remedy its failure to tender equipment in conformity with the supply agreement,

as if the lessee had agreed to buy the equipment from the lessor under the same terms as those of the supply agreement.

2. - A right conferred by the previous paragraph shall be exercisable in the same manner and shall be lost in the same circumstances as if the lessee had agreed to buy the equipment from the lessor under the same terms as those of the supply agreement.
3. - The lessee shall be entitled to withhold rentals payable under the leasing agreement until the lessor has remedied its failure to tender equipment in conformity with the supply agreement or the lessee has lost the right to reject the equipment.

4. - Where the lessee has exercised a right to terminate the leasing agreement, the lessee shall be entitled to recover any rentals and other sums paid in advance, less a reasonable sum for any benefit the lessee has derived from the equipment.

5. - The lessee shall have no other claim against the lessor for non-delivery, delay in delivery or delivery of non-conforming equipment except to the extent to which this results from the act or omission of the lessor.

6. - Nothing in this article shall affect the lessee’s rights against the supplier under Article 10.

Article 13

1. - In the event of default by the lessee, the lessor may recover accrued unpaid rentals, together with interest and damages.

2. - Where the lessee’s default is substantial, then subject to paragraph 5 the lessor may also require accelerated payment of the value of the future rentals, where the leasing agreement so provides, or may terminate the leasing agreement and after such termination:

   (a) recover possession of the equipment; and

   (b) recover such damages as will place the lessor in the position in which it would have been had the lessee performed the leasing agreement in accordance with its terms.

3. - (a) The leasing agreement may provide for the manner in which the damages recoverable under paragraph 2 (b) are to be computed.

   (b) Such provision shall be enforceable between the parties unless it would result in damages substantially in excess of those provided for under paragraph 2 (b). The parties may not derogate from or vary the effect of the provisions of the present sub-paragraph.

4. - Where the lessor has terminated the leasing agreement, it shall not be entitled to enforce a term of that agreement providing for acceleration of payment of future rentals, but the value of such rentals may be taken into account in computing damages under paragraphs 2(b) and 3. The parties may not derogate from or vary the effect of the provisions of the present paragraph.

5. - The lessor shall not be entitled to exercise its right of acceleration or its right of termination under paragraph 2 unless it has by notice given the lessee a reasonable opportunity of remedying the default so far as the same may be remedied.

6. - The lessor shall not be entitled to recover damages to the extent that it has failed to take all reasonable steps to mitigate its loss.

Article 14

1. - The lessor may transfer or otherwise deal with all or any of its rights in the equipment or under the leasing agreement. Such a transfer shall not relieve the lessor of any of its duties
under the leasing agreement or alter either the nature of the leasing agreement or its legal
treatment as provided in this Convention.

2. - The lessee may transfer the right to the use of the equipment or any other rights under
the leasing agreement only with the consent of the lessor and subject to the rights of third parties.

CONF. 7/C.1/Doc. 2
26 May 1988

CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Second report of the Committee of the Whole to the Conference

1. - The Committee of the Whole held seven sessions between 19 and 25 May 1988 at
which it examined the draft Unidroit Convention on international factoring which had been
prepared by a Unidroit committee of governmental experts (Study LVIII - Doc.33).

2. - Mr L. Sevón (Finland), who had been appointed Chairman of the Committee of the
Whole by the Conference under Rule 6 of its Rules of Procedure, chaired all the sessions of the
Committee.

3. - Pursuant to their election under Rule 51 of the Rules of Procedure, Mr J.-P. Beraudo
(France) and Mr M.A. Thiam (Guinea) continued to act as first and second Vice-Chairmen of
the Committee of the Whole respectively.

4. - At its final session the Committee of the Whole adopted, on second reading, the
following text of the Preamble to, and Articles 1 to 12 (Chapters I, II and III) and 18 (part of
Chapter IV) of, the draft Unidroit Convention on international factoring:

UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

THE STATES PARTIES TO THIS CONVENTION,

CONSCIOUS of the fact that international factoring has a significant role to play in the
development of international trade,

RECOGNISING therefore the importance of adopting uniform rules to provide a legal
framework that will facilitate international factoring, while maintaining a fair balance of
interests between the different parties involved in factoring transactions,

HAVE AGREED as follows:
CHAPTER I - SPHERE OF APPLICATION AND GENERAL PROVISIONS

Article 1

1. - This Convention governs factoring contracts and assignments of receivables as described in this Chapter.

2. - For the purposes of this Convention, “factoring contract” means a contract concluded between one party (the supplier) and another party (the factor) pursuant to which:

   (a) the supplier may or will assign to the factor receivables arising from contracts of sale of goods made between the supplier and its customers (debtors) other than those for the sale of goods bought primarily for their personal, family or household use;

   (b) the factor is to perform at least two of the following functions:
       - finance for the supplier, including loans and advance payments;
       - maintenance of accounts (ledging) relating to the receivables;
       - collection of receivables;
       - protection against default in payment by debtors;

   (c) notice of the assignment of the receivables is to be given to debtors.

3. - In this Convention references to “goods” and “sale of goods” shall include services and the supply of services.

4. - For the purposes of this Convention:

   (a) a notice in writing need not be signed but must identify the person by whom or in whose name it is given;

   (b) “notice in writing” includes, but is not limited to, telegrams, telex and any other telecommunication capable of being reproduced in tangible form.

Article 2

1. - This Convention applies whenever the receivables assigned pursuant to a factoring contract arise from a contract of sale of goods between a supplier and a debtor whose places of business are in different States and:

   (a) those States and the State in which the factor has its place of business are Contracting States; or

   (b) both the contract of sale of goods and the factoring contract are governed by the law of a Contracting State.

2. - A reference in this Convention to a party’s place of business shall, if it has more than one place of business, mean the place of business which has the closest relationship to the relevant contract and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that contract.
Article 3

1. - The application of this Convention may be excluded:

(a) by the parties to the factoring contract; or

(b) by the parties to the contract of sale of goods, as regards receivables arising at or after the time when the factor has been given notice in writing of such exclusion.

2. - Where the application of this Convention is excluded in accordance with the previous paragraph, such exclusion may be made only as regards the Convention as a whole.

Article 4

1. - In the interpretation of this Convention, regard is to be had to its object and purpose as set forth in the Preamble, to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.

2. - Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law.

CHAPTER II - RIGHTS AND DUTIES OF THE PARTIES

Article 5

As between the parties to the factoring contract:

(a) a provision in the factoring contract for the assignment of existing or future receivables shall not be rendered invalid by the fact that the contract does not specify them individually, if at the time of conclusion of the contract or when they come into existence they can be identified to the contract;

(b) a provision in the factoring contract by which future receivables are assigned operates to transfer the receivables to the factor when they come into existence without the need for any new act of transfer.

Article 6

1. - The assignment of a receivable by the supplier to the factor shall be effective notwithstanding any agreement between the supplier and the debtor prohibiting such assignment.

2. - However, such assignment shall not be effective against the debtor when, at the time of conclusion of the contract of sale of goods, it has its place of business in a Contracting State which has made a declaration under Article 18 of this Convention.

3. - Nothing in paragraph 1 shall affect any obligation of good faith owed by the supplier
to the debtor or any liability of the supplier to the debtor in respect of an assignment made in breach of the terms of the contract of sale of goods.

Article 7

A factoring contract may validly provide as between the parties thereto for the transfer, with or without a new act of transfer, of all or any of the supplier’s rights deriving from the sale of goods, including the benefit of any provision in the contract of sale of goods reserving to the supplier title to the goods or creating any security interest.

Article 8

1. - The debtor is under a duty to pay the factor if, and only if, the debtor does not have knowledge of any other person’s superior right to payment and notice in writing of the assignment:

   (a) is given to the debtor by the supplier or by the factor with the supplier’s authority;

   (b) reasonably identifies the receivables which have been assigned and the factor to whom or for whose account the debtor is required to make payment; and

   (c) relates to receivables arising under a contract of sale of goods made at or before the time the notice is given.

2. - Irrespective of any other ground on which payment by the debtor to the factor discharges the debtor from liability, payment shall be effective for this purpose if made in accordance with the previous paragraph.

Article 9

1. - In a claim by the factor against the debtor for payment of a receivable arising under a contract of sale of goods the debtor may set up against the factor all defences arising under that contract of which the debtor could have availed itself if such claim had been made by the supplier.

2. - The debtor may also assert against the factor any right of set-off in respect of claims existing against the supplier in whose favour the receivable arose, and available to the debtor at the time a notice in writing of assignment conforming to Article 8(1) was given to the debtor.

Article 10

1. - Without prejudice to the debtor’s rights under Article 9, non-performance or defective or late performance of the contract of sale of goods shall not by itself entitle the debtor to recover a sum paid by the debtor to the factor if the debtor has a right to recover that sum from the supplier.

2. - The debtor who has such a right to recover from the supplier a sum paid to the factor in respect of a receivable shall nevertheless be entitled to recover that sum from the factor to the extent that:
(a) the factor has not discharged an obligation to make payment to the supplier in respect of that receivable; or

(b) the factor made such payment at a time when it knew of the supplier’s non-performance or defective or late performance as regards the goods to which the debtor’s payment relates.

CHAPTER III - SUBSEQUENT ASSIGNMENTS

Article 11

1. - Where a receivable is assigned by a supplier to a factor pursuant to a factoring contract governed by this Convention:

(a) the rules set out in Articles 5 to 10 shall, subject to sub-paragraph (b) of this paragraph, apply to any subsequent assignment of the receivable by the factor or by a subsequent assignee;

(b) the provisions of Articles 8 to 10 shall apply as if the subsequent assignee were the factor.

2. - For the purposes of this Convention, notice to the debtor of the subsequent assignment also constitutes notice of the assignment to the factor.

Article 12

This Convention shall not apply to a subsequent assignment which is prohibited by the terms of the factoring contract.

[CHAPTER IV - FINAL PROVISIONS]

Article 18

A Contracting State may at any time make a declaration in accordance with Article 6(2) that an assignment under Article 6(1) shall not be effective against the debtor when, at the time of conclusion of the contract of sale of goods, it has its place of business in that State.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FINANCIAL LEASING

Report of the Final Clauses Committee

to the Conference

1. - The Final Clauses Committee held three meetings on 12, 17 and 20 May 1988 at which it considered the draft final provisions (with the exception of Article F) capable of embodiment in the draft Convention on international financial leasing prepared by the Unidroit Secretariat (Study LIX - Doc.49) as well as the title of the draft Convention, the text of which had been approved by the Unidroit committee of governmental experts for the preparation of a draft Convention on international financial leasing (Study LIX-Doc. 48). Representatives of 20 States participated in the work of the Committee, namely representatives of Antigua and Barbuda, Australia, Austria, Brazil, Canada, China, Finland, France, Italy, Japan, Mexico, Netherlands, Philippines, Portugal, Spain, Sweden, Thailand, the Union of Soviet Socialist Republics, the United Kingdom and the United States of America.

2. - On a proposal by the representative of the United States of America, seconded by the representative of the Netherlands, the Committee, acting in conformity with Rule 51 of the Rules of Procedure of the Conference, elected Mr G. Brennan (Australia) as Chairman of the Committee and Mr A. Amamchian (Union of Soviet Socialist Republics) as Vice-Chairman. All meetings of the Committee were chaired by Mr Brennan.

3. - The representative of Brazil stated that he favoured a different formula for Article 16 of the future Convention on international financial leasing from the one adopted by the Final Clauses Committee at its third meeting. At its first meeting the Committee had decided on a compromise formula. He was of the opinion that the question should not have been reopened.

4. - At its third meeting, the Final Clauses Committee adopted, on second reading, the proposed title as well as the following text of the final draft provisions (Chapter III) of the draft Unidroit Convention on international financial leasing (with the exception of Article 20):

UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

CHAPTER III - FINAL PROVISIONS

Article 15

1. - This Convention is open for signature at the concluding meeting of the Diplomatic Conference for the Adoption of the Draft Unidroit Conventions on International Factoring and International Financial Leasing and will remain open for signature by all States at Ottawa until 31 December 1990.
2. - This Convention is subject to ratification, acceptance or approval by States which have signed it.

3. - This Convention is open for accession by all States which are not signatory States as from the date it is open for signature.

4. - Ratification, acceptance, approval or accession is effected by the deposit of a formal instrument to that effect with the depositary.

Article 16

1. - This Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the third instrument of ratification, acceptance, approval or accession.

2. - For each State that ratifies, accepts, approves, or accedes to this Convention after the deposit of the third instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.

Article 17

This Convention does not prevail over any treaty which has already been or may be entered into; in particular it shall not affect any liability imposed on any person by existing or future treaties.

Article 18

1. - If a Contracting State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may substitute its declaration by another declaration at any time.

2. - These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. - If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

4. - If a Contracting State makes no declaration under paragraph 1, the Convention is to extend to all territorial units of that State.

Article 19

1. - Two or more Contracting States which have the same or closely related legal rules on matters governed by this Convention may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States. Such
declarations may be made jointly or by reciprocal unilateral declarations.

2. - A Contracting State which has the same or closely related legal rules on matters governed by this Convention as one or more non-Contracting States may at any time declare that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States.

3. - If a State which is the object of a declaration under the previous paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which the Convention enters into force in respect of the new Contracting State, have the effect of a declaration made under paragraph 1, provided that the new Contracting State joins in such declaration or makes a reciprocal unilateral declaration.

[Article 20 - Article F as adopted by the Conference on 19 May 1988]

Article 21

1. - Declarations made under this Convention at the time of signature are subject to confirmation upon ratification, acceptance or approval.

2. - Declarations and confirmations of declarations are to be in writing and to be formally notified to the depositary.

3. - A declaration takes effect simultaneously with the entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral declarations under Article 19 take effect on the first day of the month following the expiration of six months after the receipt of the latest declaration by the depositary.

4. - Any State which makes a declaration under this Convention may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal is to take effect on the first day of the month following the expiration of six months after the date of the receipt of the notification by the depositary.

5. - A withdrawal of a declaration made under Article 19 renders inoperative in relation to the withdrawing State, as from the date on which the withdrawal takes effect, any joint or reciprocal unilateral declaration made by another State under that article.

Article 22

No reservations are permitted except those expressly authorised in this Convention.

Article 23

This Convention applies to a financial leasing transaction when the leasing agreement and the supply agreement are both concluded on or after the date on which the Convention enters into force in respect of the Contracting States referred to in Article 3 (1)(a), or of the Contracting
State or States referred to in paragraph 1 (b) of that article.

**Article 24**

1. - This Convention may be denounced by any Contracting State at any time after the date on which it enters into force for that State.

2. - Denunciation is effected by the deposit of an instrument to that effect with the depository.

3. - A denunciation takes effect on the first day of the month following the expiration of six months after the deposit of the instrument of denunciation with the depository. Where a longer period for the denunciation to take effect is specified in the instrument of denunciation it takes effect upon the expiration of such longer period after its deposit with the depository.

**Article 25**

1. - This Convention shall be deposited with the Government of Canada.

2. - The Government of Canada shall:

   (a) inform all States which have signed or acceded to this Convention and the President of the International Institute for the Unification of Private Law (Unidroit) of:

      (i) each new signature or deposit of an instrument of ratification, acceptance, approval or accession, together with the date thereof;

      (ii) each declaration made under Articles 18, 19 and 20;

      (iii) the withdrawal of any declaration made under Article 21 (4);

      (iv) the date of entry into force of this Convention;

      (v) the deposit of an instrument of denunciation of this Convention together with the date of its deposit and the date on which it takes effect;

   (b) transmit certified true copies of this Convention to all signatory States, to all States acceding to the Convention and to the President of the International Institute for the Unification of Private Law (Unidroit).

IN WITNESS WHEREOF the undersigned plenipotentiaries, being duly authorised by their respective Governments, have signed this Convention.

DONE at Ottawa, this ........day of May, one thousand nine hundred and eighty-eight, in a single original, of which the English and French texts are equally authentic.
CONSIDERATION OF THE DRAFT UNIDROIT CONVENTION
ON INTERNATIONAL FACTORING

Second report of the Final Clauses Committee to the Conference

1. - The Final Clauses Committee held two meetings on 24 and 25 May 1988 at which it considered the draft final provisions (with the exception of Article F) capable of embodiment in the draft Unidroit Convention on international factoring prepared by the Unidroit Secretariat in the light of the observations and suggestions made by the Unidroit committee of governmental experts for the preparation of a draft Convention on certain aspects of international factoring (Study LVIII - Doc. 34) as well as the title of the draft Convention, the text of which had been approved by the aforesaid Unidroit committee (Study LVIII - Doc. 33).

2. - Mr G. Brennan (Australia), who had been elected Chairman of the Final Clauses Committee by the Committee itself under Rule 51 of the Rules of Procedure of the Conference, chaired both meetings of the Committee.

3. - Pursuant to his election under Rule 51 of the Rules of Procedure, Mr A. Amamchian (Union of Soviet Socialist Republics) continued to act as Vice-Chairman of the Committee.

4. - At its final meeting the Final Clauses Committee adopted, on second reading, the proposed title as well as the following text of the draft final provisions (Chapter IV) of the draft Unidroit Convention on international factoring (with the exception of Article 18):

UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

CHAPTER IV - FINAL PROVISIONS

Article 13

1. - This Convention is open for signature at the concluding meeting of the Diplomatic Conference for the Adoption of the Draft Unidroit Conventions on International Factoring and International Financial Leasing and will remain open for signature by all States at Ottawa until 31 December 1990.

2. - This Convention is subject to ratification, acceptance or approval by States which have signed it.

3. - This Convention is open for accession by all States which are not signatory States as from the date it is open for signature.

4. - Ratification, acceptance, approval or accession is effected by the deposit of a formal instrument to that effect with the depositary.
Article 14

1. - This Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the third instrument of ratification, acceptance, approval or accession.

2. - For each State that ratifies, accepts, approves, or accedes to this Convention after the deposit of the third instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.

Article 15

This Convention does not prevail over any treaty which has already been or may be entered into.

Article 16

1. - If a Contracting State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may substitute its declaration by another declaration at any time.

2. - These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. - If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

4. - If a Contracting State makes no declaration under paragraph 1, the Convention is to extend to all territorial units of that State.

Article 17

1. - Two or more Contracting States which have the same or closely related legal rules on matters governed by this Convention may at any time declare that the Convention is not to apply where the supplier, the factor and the debtor have their places of business in those States. Such declarations may be made jointly or by reciprocal unilateral declarations.

2. - A Contracting State which has the same or closely related legal rules on matters governed by this Convention as one or more non-Contracting States may at any time declare that the Convention is not to apply where the supplier, the factor and the debtor have their places of business in those States.

3. - If a State which is the object of a declaration under the previous paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which the Convention enters into force in respect of the new Contracting State, have the effect of a
declaration made under paragraph 1, provided that the new Contracting State joins in such
declaration or makes a reciprocal unilateral declaration.

[Article 18 - Article X as adopted
by the Committee of the Whole on 25 May 1988]

Article 19

1. - Declarations made under this Convention at the time of signature are subject to
confirmation upon ratification, acceptance or approval.

2. - Declarations and confirmations of declarations are to be in writing and to be formally
notified to the depositary.

3. - A declaration takes effect simultaneously with the entry into force of this Convention
in respect of the State concerned. However, a declaration of which the depositary receives
formal notification after such entry into force takes effect on the first day of the month following
the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral
declarations under Article 17 take effect on the first day of the month following the expiration
of six months after the receipt of the latest declaration by the depositary.

4. - Any State which makes a declaration under this Convention may withdraw it at any
time by a formal notification in writing addressed to the depositary. Such withdrawal is to take
effect on the first day of the month following the expiration of six months after the date of the
receipt of the notification by the depositary.

5. - A withdrawal of a declaration made under Article 17 renders inoperative in relation
to the withdrawing State, as from the date on which the withdrawal takes effect, any joint or
reciprocal unilateral declaration made by another State under that article.

Article 20

No reservations are permitted except those expressly authorised in this Convention.

Article 21

This Convention applies when receivables assigned pursuant to a factoring contract arise
from a contract of sale of goods concluded on or after the date on which the Convention enters
into force in respect of the Contracting States referred to in Article 2, paragraph 1(a), or the
Contracting State or States referred to in paragraph 1(b) of that article, provided that:

(a) the factoring contract is concluded on or after that date; or

(b) the parties to the factoring contract have agreed that the Convention shall apply.

Article 22

1. - This Convention may be denounced by any Contracting State at any time after the date
on which it enters into force for that State.
2. - Denunciation is effected by the deposit of an instrument to that effect with the depositary.

3. - A denunciation takes effect on the first day of the month following the expiration of six months after the deposit of the instrument of denunciation with the depositary. Where a longer period for the denunciation to take effect is specified in the instrument of denunciation it takes effect upon the expiration of such longer period after its deposit with the depositary.

Article 23

1. - This Convention shall be deposited with the Government of Canada.

2. - The Government of Canada shall:

(a) inform all States which have signed or acceded to this Convention and the President of the International Institute for the Unification of Private Law (Unidroit) of:

(i) each new signature or deposit of an instrument of ratification, acceptance, approval or accession, together with the date thereof;

(ii) each declaration made under Articles 16, 17 and 18;

(iii) the withdrawal of any declaration made under Article 19 (4);

(iv) the date of entry into force of this Convention;

(v) the deposit of an instrument of denunciation of this Convention together with the date of its deposit and the date on which it takes effect;

(b) transmit certified true copies of this Convention to all signatory States, to all States acceding to the Convention and to the President of the International Institute for the Unification of Private Law (Unidroit).

IN WITNESS WHEREOF the undersigned plenipotentiaries, being duly authorised by their respective Governments, have signed this Convention.

DONE at Ottawa, this ..........day of May, one thousand nine hundred and eighty-eight, in a single original, of which the English and French texts are equally authentic.
REPORT OF THE CREDENTIALS COMMITTEE TO THE CONFERENCE

In accordance with Rule 4 of the Rules of Procedure of the Conference, following consultations with the Heads of Delegations, the Conference appointed a Credentials Committee on 11 May, comprising representatives of the following Governments:

Federal Republic of Germany, Japan, Nigeria, Switzerland and the Union of Soviet Socialist Republics.

The Committee met twice, on 12 and 16 May, its meetings being attended by the following representatives:

Mr W. ROLLAND (Federal Republic of Germany)
Mr M. HARA (Japan)
Chief H.F. DAVID-WEST (Nigeria)
Mr C. DUNANT (Switzerland)
Mr A.S. KOMAROV (Union of Soviet Socialist Republics)

In accordance with Rule 51 of the Rules of Procedure of the Conference it fell to the Committee to elect its own Chairman. On a proposal by the representative of Nigeria, the representative of the Federal Republic of Germany was elected Chairman.

The credentials of the delegations of the following States, transmitted to the Secretary-General of the Conference in accordance with Rule 3 of the Rules of Procedure, were examined and, subject to certain objections set out below, found to be in due and proper form:

the People’s Republic of Angola; Antigua and Barbuda; Australia; the Republic of Austria; the Kingdom of Belgium; the Federative Republic of Brazil; the People’s Republic of Bulgaria; the Republic of Cameroon; Canada; the Republic of Chile; the People’s Republic of China; the Republic of Colombia; the Kingdom of Denmark; the Dominican Republic; the Arab Republic of Egypt; the Republic of El Salvador; the Republic of Finland; the French Republic; Germany, Federal Republic of; the Republic of Ghana; the Hellenic Republic; the Republic of Guinea; the Hungarian People’s Republic; the Republic of India; Ireland; the Italian Republic; Japan; the Lebanese Republic; the United Mexican States; the Kingdom of Morocco; the Kingdom of the Netherlands; the Federal Republic of Nigeria; the Kingdom of Norway; the Republic of the Philippines; the Polish People’s Republic; the Portuguese Republic; the Republic of Korea; the Republic of South Africa; the Kingdom of Spain; the Kingdom of Sweden; the Swiss Confederation; the Kingdom of Thailand; the Republic of Turkey; the Union of Soviet Socialist Republics; the United Kingdom of Great Britain and Northern Ireland; the United Republic of Tanzania; the United States of America; the Republic of Venezuela.
The Committee noted that the following States were represented at the Conference by observers:

Malaysia; the Republic of Peru; the Republic of Uganda; the Eastern Republic of Uruguay.

The representative of Nigeria stated that he had been mandated by the delegations of the African States represented at the Conference to say that they would object to the credentials submitted by the delegation of South Africa. This was a diplomatic Conference of States and since South Africa had frequently flouted United Nations Resolutions condemning the policy of Apartheid his own delegation, as well as those of all the other African States represented at the Conference, was opposed to the participation of South Africa in the Conference.

The representative of the Union of Soviet Socialist Republics stated that he supported the position adopted by the representative of Nigeria and the delegations of the African States.

The representative of Japan took the view that the competence of the Committee only extended to the examination of the credentials of delegations from the point of view of their compliance with the formal requirements of the Rules of Procedure and did not entitle it to take a decision based on political considerations. He was supported in this view by the Chairman of the Committee and the representative of Switzerland.

25 May 1988

ADDENDUM TO THE
REPORT OF THE CREDENTIALS COMMITTEE TO THE CONFERENCE

Subsequent to the submission of its report to the Conference (CONF. 7/8) in accordance with Rule 4 of the Rules of Procedure of the Conference, the Credentials Committee met on 25 May to examine the credentials of the delegations of certain States which had not been transmitted to the Secretary-General of the Conference in time for examination by the Credentials Committee either at its first or its second meeting.

The meeting was attended by the following representatives:

Mr W. ROLLAND (Federal Republic of Germany)
Mr M. HARA (Japan)
Chief H.F. DAVID-WEST (Nigeria)
Mr G. RONCORONI (Switzerland)
Mr A.S. KOMAROV (Union of Soviet Socialist Republics)

The credentials of the delegations of the following States were examined and found to be in due and proper form:

the People's Democratic Republic of Algeria; the Republic of Burundi; the Republic of Cuba; the Czechoslovak Socialist Republic; the Republic of Senegal; the Democratic Republic of the Sudan; the Socialist Federal Republic of Yugoslavia; the Republic of Zaire.
DRAFT FINAL ACT OF THE DIPLOMATIC CONFERENCE
FOR THE ADOPTION OF THE DRAFT UNIDROIT
CONVENTIONS ON INTERNATIONAL FACTORING
AND INTERNATIONAL FINANCIAL LEASING

(submitted by the Drafting Committee)

1. - The Diplomatic Conference for the Adoption of the Draft Unidroit Conventions on International Factoring and International Financial Leasing was held in Ottawa, Canada from 9 to 28 May 1988.

2. - Representatives of 55 States participated in the Conference, namely representatives of:

   the People's Democratic Republic of Algeria; the People's Republic of Angola; Antigua and Barbuda; Australia; the Republic of Austria; the Kingdom of Belgium; the Federative Republic of Brazil; the People's Republic of Bulgaria; the Republic of Burundi; the Republic of Cameroon; Canada; the Republic of Chile; the People's Republic of China; the Republic of Colombia; the Republic of Cuba; the Czechoslovak Socialist Republic; the Kingdom of Denmark; the Dominican Republic; the Arab Republic of Egypt; the Republic of El Salvador; the Republic of Finland; the Republic of France; the Federal Republic of Germany; the Republic of Ghana; the Hellenic Republic; the Republic of Guinea; the Hungarian People's Republic; the Republic of India; Ireland; the Italian Republic; Japan; the Lebanese Republic; the United Mexican States; the Kingdom of Morocco; the Kingdom of the Netherlands; the Federal Republic of Nigeria; the Kingdom of Norway; the Republic of the Philippines; the Polish People's Republic; the Portuguese Republic; the Republic of Korea; the Republic of Senegal; the Kingdom of Spain; the Democratic Republic of the Sudan; the Kingdom of Sweden; the Swiss Confederation; the Kingdom of Thailand; the Republic of Turkey; the Union of Soviet Socialist Republics; the United Kingdom of Great Britain and Northern Ireland; the United Republic of Tanzania; the United States of America; the Republic of Venezuela; the Socialist Federal Republic of Yugoslavia; the Republic of Zaire.

3. - Four States sent observers to the Conference, namely:

   Malaysia; the Republic of Peru; the Republic of Uganda; the Eastern Republic of Uruguay.

4. - The following intergovernmental Organisations were represented by observers at the Conference:

   the Commission of the European Communities
   the Council of Europe
   the Hague Conference on Private International Law
   the Organization of American States
the United Nations Commission on International Trade Law
the United Nations Conference on Trade and Development
the World Bank.

5. - The following international non-governmental Organisation was represented by an observer at the Conference:

the International Maritime Committee.

6. - The following international professional associations were represented by observers at the Conference:

Factors Chain International
the World Leasing Council.

7. - The Conference elected Mr T.B. Smith (Canada) as President.

8. - The Conference elected as Vice-Presidents the following representatives:

   Mr I. El-Kattan (Egypt)
   Mr L. Récei (Hungary)
   Mr H. Ríos de Marimón (Chile)
   Mr W. Rolland (Federal Republic of Germany)
   Mr Z. Yuan (China).

9. - The following committees were set up by the Conference:

    Steering Committee

   Chairman: The President of the Conference
   Members: The President and the Vice-Presidents of the Conference and the Chairman of the Committee of the Whole
    
   In addition the Secretary-General of the Conference participated in the work of the Steering Committee, at the invitation of the Chairman
    
   Committee of the Whole

   Chairman: Mr L. Sevón (Finland)
   First Vice-Chairman: Mr J.-P. Beraudo (France)
   Second Vice-Chairman: Mr M.A. Thiam (Guinea)

    Final Clauses Committee

   Chairman: Mr G. Brennan (Australia)
   Vice-Chairman: Mr A. Amamchian (U.S.S.R.)
Drafting Committee

Chairman: Mr R.M. Goode (United Kingdom)

Members: Belgium; Brazil; China; Egypt; France; Japan; U.S.S.R.; United Kingdom; U.S.A.

Credentials Committee

Chairman: Mr W. Rolland (Federal Republic of Germany)

Members: Federal Republic of Germany; Japan; Nigeria; Switzerland; U.S.S.R.

10. - The Secretary-General of the Conference was Mr M. Evans, Secretary-General of Unidroit.

11. - The basic working materials used by the Conference and its organs were the draft Convention on international financial leasing as adopted by a Unidroit committee of governmental experts on 30 April 1987 with explanatory report prepared by the Unidroit Secretariat (Study LIX - Doc. 48), the draft Convention on international factoring as adopted by a Unidroit committee of governmental experts on 24 April 1987 with explanatory report prepared by the Unidroit Secretariat (Study LVIII-Doc. 33), the draft final provisions capable of embodiment in the draft Convention on international financial leasing drawn up by a Unidroit committee of governmental experts with explanatory notes drawn up by the Unidroit Secretariat (Study LIX - Doc. 49), the draft final provisions capable of embodiment in the draft Convention on international factoring drawn up by a Unidroit committee of governmental experts with explanatory notes drawn up by the Unidroit Secretariat (Study LVIII-Doc. 34), together with the report of the working group of technical experts on international financial leasing (Rome, 29 February 1988) prepared by the Unidroit Secretariat (CONF.7/5). The Conference and its organs also considered proposals and comments by Governments and international Organisations on the draft Convention on international financial leasing (CONF.7/3 and Addenda, CONF.7/4 and Addenda, CONF.7/W.P. 1-3 and CONF.7/C.1/W.P.1-34), on the draft final provisions capable of embodiment in the draft Convention on international financial leasing (CONF.7/C.2/W.P. 1, 2, 4 and 5) and on the draft Convention on international factoring (CONF.7/6 and Addenda, CONF.7/7 and CONF.7/C.1/W.P.35-48).

12. - The Conference assigned to the Committee of the Whole the first and second readings of the draft Convention on international financial leasing, including the draft Preamble thereto, Article F of the draft final provisions capable of embodiment in the draft Convention on international financial leasing, the draft Convention on international factoring, including the draft Preamble thereto and an Article X, and Article F of the draft final provisions capable of embodiment in the draft Convention on international factoring. The Conference assigned to the Final Clauses Committee the first and second readings of all but Article F of the draft final provisions capable of embodiment in the draft Convention on international financial leasing, all but Article F of the draft final provisions capable of embodiment in the draft Convention on international factoring and the titles of the draft Convention on international financial leasing and the draft Convention on international factoring.
13. - On the basis of the deliberations recorded in the summary records of the Conference (CONF.7/S.R.4-5), the summary records of the Committee of the Whole (CONF.7/C.1/S.R.1-14) and its report (CONF.7/C.1/Doc. 1) and the report of the Final Clauses Committee (CONF.7/C.2/Doc.1), the Conference drew up the UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING.

14. - On the basis of the deliberations recorded in the summary records of the Conference (CONF.7/S.R.6), the summary records of the Committee of the Whole (CONF.7/C.1/S.R.15-21) and its report (CONF.7/C.1/Doc.2) and the report of the Final Clauses Committee (CONF.7/C.2/Doc.2), the Conference drew up the UNIDROIT CONVENTION ON INTERNATIONAL FACTORING.

15. - The Unidroit Convention on International Financial Leasing, the text of which is set out in Appendix I to this Final Act, and the Unidroit Convention on International Factoring, the text of which is set out in Appendix II to this Final Act, were adopted by the Conference on 26 May 1988 and opened for signature at the closing session of the Conference on 28 May 1988. Both Conventions will remain open for signature in Ottawa, Canada until 31 December 1990. They were also opened for accession on 28 May 1988.

16. - Both Conventions are deposited with the Government of Canada.

IN WITNESS WHEREOF the representatives,

GRATEFUL to the Government of Canada for having invited the Conference to Canada and for its generous hospitality,

HAVE SIGNED this Final Act.

DONE at Ottawa, this twenty-eighth day of May, one thousand nine hundred and eighty-eight, in a single copy in the English and French languages, each text being equally authentic.
PART V

TEXTS/INSTRUMENTS ADOPTED BY THE CONFERENCE

Texts adopted by the Conference at its fourth plenary session .......................................................... 321
Final Act of the Conference .................................................................................................................. 327
Unidroit Convention on International Financial Leasing .................................................................. 331
Unidroit Convention on International Factoring .................................................................................... 340
TEXTS ADOPTED BY THE
CONFERENCE AT ITS FOURTH
PLENARY SESSION

At its fourth plenary session, held on 19 May 1988, the Conference adopted the text of the Preamble to, Articles 1 to 14 (Chapters I and II) of, and an Article F to be included in the Final Provisions (Chapter III) of, the [Unidroit Convention on International Financial Leasing] which are set out hereunder. The Conference agreed to defer its decision on the title and full text of the Final Provisions (Chapter III) of the Convention until such time as the Final Clauses Committee had reported.

[UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING]

PREAMBLE

THE STATES PARTIES TO THIS CONVENTION,

RECOGNISING the importance of removing certain legal impediments to the international financial leasing of equipment, while maintaining a fair balance of interests between the different parties to the transaction,

AWARE of the need to make international financial leasing more available,

CONSCIOUS of the fact that the rules of law governing the traditional contract of hire need to be adapted to the distinctive triangular relationship created by the financial leasing transaction,

RECOGNISING therefore the desirability of formulating certain uniform rules relating primarily to the civil and commercial law aspects of international financial leasing,

HAVE AGREED as follows:

CHAPTER I - SPHERE OF APPLICATION AND GENERAL PROVISIONS

Article 1

1. - This Convention governs a financial leasing transaction as described in paragraph 2 in which one party (the lessor),

(a) on the specifications of another party (the lessee), enters into an agreement (the supply agreement) with a third party (the supplier) under which the lessor acquires plant, capital goods or other equipment (the equipment) on terms approved by the lessee so far as they concern its interests, and
(b) enters into an agreement (the leasing agreement) with the lessee, granting to the
lessee the right to use the equipment in return for the payment of rentals.

2. - The financial leasing transaction referred to in the previous paragraph is a transaction
which includes the following characteristics:

(a) the lessee specifies the equipment and selects the supplier without relying
primarily on the skill and judgment of the lessor;

(b) the equipment is acquired by the lessor in connection with a leasing agreement
which, to the knowledge of the supplier, either has been made or is to be made between the lessor
and the lessee; and

(c) the rentals payable under the leasing agreement are calculated so as to take into
account in particular the amortisation of the whole or a substantial part of the cost of the
equipment.

3. - This Convention applies whether or not the lessee has or subsequently acquires the
option to buy the equipment or to hold it on lease for a further period, and whether or not for
a nominal price or rental.

4. - This Convention applies to financial leasing transactions in relation to all equipment
save that which is to be used primarily for the lessee’s personal, family or household purposes.

Article 2

In the case of one or more sub-leasing transactions involving the same equipment, this
Convention applies to each transaction which is a financial leasing transaction and is otherwise
subject to this Convention as if the person from whom the first lessor (as defined in paragraph
1 of the previous article) acquired the equipment were the supplier and as if the agreement under
which the equipment was so acquired were the supply agreement.

Article 3

1. - This Convention applies when the lessor and the lessee have their places of business
in different States and:

(a) those States and the State in which the supplier has its place of business are
Contracting States; or

(b) both the supply agreement and the leasing agreement are governed by the law of
a Contracting State.

2. - A reference in this article to a party’s place of business shall, if it has more than one
place of business, mean the place of business which has the closest relationship to the relevant
agreement and its performance, having regard to the circumstances known to or contemplated
by the parties at any time before or at the conclusion of that agreement.

Article 4

1. - The provisions of this Convention shall not cease to apply merely because the
equipment has become a fixture to or incorporated in land.

2. - Any question whether or not the equipment has become a fixture to or incorporated in land, and if so the effect on the rights inter se of the lessor and a person having real rights in the land, shall be determined by the law of the State where the land is situated.

Article 5

1. - The application of this Convention may be excluded only if each of the parties to the supply agreement and each of the parties to the leasing agreement agree to exclude it.

2. - Where the application of this Convention has not been excluded in accordance with the previous paragraph, the parties may, in their relations with each other, derogate from or vary the effect of any of its provisions except as stated in Articles 8(3) and 13(3)(b) and (4).

Article 6

1. - In the interpretation of this Convention, regard is to be had to its object and purpose as set forth in the Preamble, to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.

2. - Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law.

CHAPTER II - RIGHTS AND DUTIES OF THE PARTIES

Article 7

1. - (a) The lessor’s real rights in the equipment shall be valid against the lessee’s trustee in bankruptcy and creditors, including creditors who have obtained an attachment or execution.

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

2. - Where by the applicable law the lessor’s real rights in the equipment are valid against a person referred to in the previous paragraph only on compliance with rules as to public notice, those rights shall be valid against that person only if there has been compliance with such rules.

3. - For the purposes of the previous paragraph the applicable law is the law of the State which, at the time when a person referred to in paragraph 1 becomes entitled to invoke the rules referred to in the previous paragraph, is:

(a) in the case of a registered ship, the State in which it is registered in the name of the owner (for the purposes of this sub-paragraph a bareboat charterer is deemed not to be the owner);

(b) in the case of an aircraft which is registered pursuant to the Convention on
International Civil Aviation done at Chicago on 7 December 1944, the State in which it is so registered;

(c) in the case of other equipment of a kind normally moved from one State to another, including an aircraft engine, the State in which the lessee has its principal place of business;

(d) in the case of all other equipment, the State in which the equipment is situated.

4. - Paragraph 2 shall not affect the provisions of any other treaty under which the lessor’s real rights in the equipment are required to be recognised.

5. - This article shall not affect the priority of any creditor having:

(a) a consensual or non-consensual lien or security interest in the equipment arising otherwise than by virtue of an attachment or execution, or

(b) any right of arrest, detention or disposition conferred specifically in relation to ships or aircraft under the law applicable by virtue of the rules of private international law.

Article 8

1. - (a) Except as otherwise provided by this Convention or stated in the leasing agreement, the lessor shall not incur any liability to the lessee in respect of the equipment save to the extent that the lessee has suffered loss as the result of its reliance on the lessor’s skill and judgment and of the lessor’s intervention in the selection of the supplier or the specifications of the equipment.

(b) The lessor shall not, in its capacity of lessor, be liable to third parties for death, personal injury or damage to property caused by the equipment.

(c) The above provisions of this paragraph shall not govern any liability of the lessor in any other capacity, for example as owner.

2. - The lessor warrants that the lessee’s quiet possession will not be disturbed by a person who has a superior title or right, or who claims a superior title or right and acts under the authority of a court, where such title, right or claim is not derived from an act or omission of the lessee.

3. - The parties may not derogate from or vary the effect of the provisions of the previous paragraph in so far as the superior title, right or claim is derived from an intentional or grossly negligent act or omission of the lessor.

4. - The provisions of paragraphs 2 and 3 shall not affect any broader warranty of quiet possession by the lessor which is mandatory under the law applicable by virtue of the rules of private international law.

Article 9

1. - The lessee shall take proper care of the equipment, use it in a reasonable manner and keep it in the condition in which it was delivered, subject to fair wear and tear and to any modification of the equipment agreed by the parties.

2. - When the leasing agreement comes to an end the lessee, unless exercising a right to buy the equipment or to hold the equipment on lease for a further period, shall return the
equipment to the lessor in the condition specified in the previous paragraph.

**Article 10**

1. - The duties of the supplier under the supply agreement shall also be owed to the lessee as if it were a party to that agreement and as if the equipment were to be supplied directly to the lessee. However, the supplier shall not be liable to both the lessor and the lessee in respect of the same damage.

2. - Nothing in this article shall entitle the lessee to terminate or rescind the supply agreement without the consent of the lessor.

**Article 11**

The lessee's rights derived from the supply agreement under this Convention shall not be affected by a variation of any term of the supply agreement previously approved by the lessee unless it consented to that variation.

**Article 12**

1. - Where the equipment is not delivered or is delivered late or fails to conform to the supply agreement:

   (a) the lessee has the right as against the lessor to reject the equipment or to terminate the leasing agreement; and

   (b) the lessor has the right to remedy its failure to tender equipment in conformity with the supply agreement,

as if the lessee had agreed to buy the equipment from the lessor under the same terms as those of the supply agreement.

2. - A right conferred by the previous paragraph shall be exercisable in the same manner and shall be lost in the same circumstances as if the lessee had agreed to buy the equipment from the lessor under the same terms as those of the supply agreement.

3. - The lessee shall be entitled to withhold rentals payable under the leasing agreement until the lessor has remedied its failure to tender equipment in conformity with the supply agreement or the lessee has lost the right to reject the equipment.

4. - Where the lessee has exercised a right to terminate the leasing agreement, the lessee shall be entitled to recover any rentals and other sums paid in advance, less a reasonable sum for any benefit the lessee has derived from the equipment.

5. - The lessee shall have no other claim against the lessor for non-delivery, delay in delivery or delivery of non-conforming equipment except to the extent to which this results from the act or omission of the lessor.

6. - Nothing in this article shall affect the lessee's rights against the supplier under Article 10.
Article 13

1. - In the event of default by the lessee, the lessor may recover accrued unpaid rentals, together with interest and damages.

2. - Where the lessee's default is substantial, then subject to paragraph 5 the lessor may also require accelerated payment of the value of the future rentals, where the leasing agreement so provides, or may terminate the leasing agreement and after such termination:

(a) recover possession of the equipment; and

(b) recover such damages as will place the lessor in the position in which it would have been had the lessee performed the leasing agreement in accordance with its terms.

3. - (a) The leasing agreement may provide for the manner in which the damages recoverable under paragraph 2 (b) are to be computed.

(b) Such provision shall be enforceable between the parties unless it would result in damages substantially in excess of those provided for under paragraph 2 (b). The parties may not derogate from or vary the effect of the provisions of the present sub-paragraph.

4. - Where the lessor has terminated the leasing agreement, it shall not be entitled to enforce a term of that agreement providing for acceleration of payment of future rentals, but the value of such rentals may be taken into account in computing damages under paragraphs 2(b) and 3. The parties may not derogate from or vary the effect of the provisions of the present paragraph.

5. - The lessor shall not be entitled to exercise its right of acceleration or its right of termination under paragraph 2 unless it has by notice given the lessee a reasonable opportunity of remedying the default so far as the same may be remedied.

6. - The lessor shall not be entitled to recover damages to the extent that it has failed to take all reasonable steps to mitigate its loss.

Article 14

1. - The lessor may transfer or otherwise deal with all or any of its rights in the equipment or under the leasing agreement. Such a transfer shall not relieve the lessor of any of its duties under the leasing agreement or alter either the nature of the leasing agreement or its legal treatment as provided in this Convention.

2. - The lessee may transfer the right to the use of the equipment or any other rights under the leasing agreement only with the consent of the lessor and subject to the rights of third parties.

[ CHAPTER III - FINAL PROVISIONS ]

Article [F]

A Contracting State may declare at the time of signature, ratification, acceptance, approval or accession that it will substitute its domestic law for Article 8(3) if its domestic law does not permit the lessor to exclude its liability for its default or negligence.
FINAL ACT OF THE DIPLOMATIC CONFERENCE
FOR THE ADOPTION OF THE DRAFT UNIDROIT
CONVENTIONS ON INTERNATIONAL FACTORING
AND INTERNATIONAL FINANCIAL LEASING

1. - The Diplomatic Conference for the Adoption of the Draft Unidroit Conventions on International Factoring and International Financial Leasing was held in Ottawa, Canada from 9 to 28 May 1988.

2. - Representatives of 55 States participated in the Conference, namely representatives of:

   the People's Democratic Republic of Algeria; the People's Republic of Angola; Antigua and Barbuda; Australia; the Republic of Austria; the Kingdom of Belgium; the Federative Republic of Brazil; the People's Republic of Bulgaria; the Republic of Burundi; the Republic of Cameroon; Canada; the Republic of Chile; the People's Republic of China; the Republic of Colombia; the Republic of Cuba; the Czechoslovak Socialist Republic; the Kingdom of Denmark; the Dominican Republic; the Arab Republic of Egypt; the Republic of El Salvador; the Republic of Finland; the Republic of France; the Federal Republic of Germany; the Republic of Ghana; the Hellenic Republic; the Republic of Guinea; the Hungarian People's Republic; the Republic of India; Ireland; the Italian Republic; Japan; the Lebanese Republic; the United Mexican States; the Kingdom of Morocco; the Kingdom of the Netherlands; the Federal Republic of Nigeria; the Kingdom of Norway; the Republic of the Philippines; the Polish People's Republic; the Portuguese Republic; the Republic of Korea; the Republic of Senegal; the Kingdom of Spain; the Democratic Republic of the Sudan; the Kingdom of Sweden; the Swiss Confederation; the Kingdom of Thailand; the Republic of Turkey; the Union of Soviet Socialist Republics; the United Kingdom of Great Britain and Northern Ireland; the United Republic of Tanzania; the United States of America; the Republic of Venezuela; the Socialist Federal Republic of Yugoslavia; the Republic of Zaire.

3. - Four States sent observers to the Conference, namely:

   Malaysia; the Republic of Peru; the Republic of Uganda; the Eastern Republic of Uruguay.

4. - The following intergovernmental Organisations were represented by observers at the Conference:

   the Commission of the European Communities
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   the Hague Conference on Private International Law
   the Organization of American States
   the United Nations Commission on International Trade Law
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the World Bank.

5. - The following international non-governmental Organisation was represented by an
observer at the Conference:

the International Maritime Committee.

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at the Conference:

Factors Chain International
the World Leasing Council.

7. - The Conference elected Mr T.B. Smith (Canada) as President.

8. - The Conference elected as Vice-Presidents the following representatives:

Mr I. El-Kattan (Egypt)
Mr L. Récezi (Hungary)
Mr H. Ríos de Marimón (Chile)
Mr W. Rolland (Federal Republic of Germany)
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9. - The following committees were set up by the Conference:

Steering Committee

Chairman: The President of the Conference

Members: The President and the Vice-Presidents of the Conference and the Chairman
of the Committee of the Whole

In addition the Secretary-General of the Conference participated in the work
of the Steering Committee, at the invitation of the Chairman

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Chairman: Mr L. Sevón (Finland)

First Vice-Chairman: Mr J.-P. Beraudo (France)

Second Vice-Chairman: Mr M.A. Thiam (Guinea)

Final Clauses Committee

Chairman: Mr G. Brennan (Australia)

Vice-Chairman: Mr A. Amamchian (U.S.S.R.)
Drafting Committee

Chairman: Mr R.M. Goode (United Kingdom)

Members: Belgium; Brazil; China; Egypt; France; Japan; U.S.S.R.; United Kingdom; U.S.A.

Credentials Committee

Chairman: Mr W. Rolland (Federal Republic of Germany)

Members: Federal Republic of Germany; Japan; Nigeria; Switzerland; U.S.S.R.

10. - The Secretary-General of the Conference was Mr M. Evans, Secretary-General of Unidroit.

11. - The basic working materials used by the Conference and its organs were the draft Convention on international financial leasing as adopted by a Unidroit committee of governmental experts on 30 April 1987 with explanatory report prepared by the Unidroit Secretariat (Study LIX - Doc. 48), the draft Convention on international factoring as adopted by a Unidroit committee of governmental experts on 24 April 1987 with explanatory report prepared by the Unidroit Secretariat (Study LVIII - Doc. 33), the draft final provisions capable of embodiment in the draft Convention on international financial leasing drawn up by a Unidroit committee of governmental experts with explanatory notes drawn up by the Unidroit Secretariat (Study LIX - Doc. 49), the draft final provisions capable of embodiment in the draft Convention on international factoring drawn up by a Unidroit committee of governmental experts with explanatory notes drawn up by the Unidroit Secretariat (Study LVIII - Doc. 34), together with the report of the working group of technical experts on international financial leasing (Rome, 29 February 1988) prepared by the Unidroit Secretariat (CONF.7/5). The Conference and its organs also considered proposals and comments by Governments and international Organisations on the draft Convention on international financial leasing (CONF.7/3 and Addenda, CONF.7/4 and Addenda, CONF.7/W.P. 1-3 and CONF.7/C.1/W.P.1-34), on the draft final provisions capable of embodiment in the draft Convention on international financial leasing (CONF.7/C.2/W.P. 1, 2, 4 and 5) and on the draft Convention on international factoring (CONF.7/6 and Addenda, CONF.7/7 and CONF.7/C.1/W.P.35-48).

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14. - On the basis of the deliberations recorded in the summary records of the Conference (CONF.7/S.R.6), the summary records of the Committee of the Whole (CONF.7/C.1/S.R.15-21) and its report (CONF.7/C.1/Doc.2) and the report of the Final Clauses Committee (CONF.7/C.2/Doc.2), the Conference drew up the **UNIDROIT CONVENTION ON INTERNATIONAL FACTORING**.

15. - The Unidroit Convention on International Financial Leasing, the text of which is set out in Appendix I to this Final Act, and the Unidroit Convention on International Factoring, the text of which is set out in Appendix II to this Final Act, were adopted by the Conference on 26 May 1988 and opened for signature at the closing session of the Conference on 28 May 1988. Both Conventions will remain open for signature in Ottawa, Canada until 31 December 1990. They were also opened for accession on 28 May 1988.

16. - Both Conventions are deposited with the Government of Canada.

**IN WITNESS WHEREOF** the representatives,

GRATEFUL to the Government of Canada for having invited the Conference to Canada and for its generous hospitality,

HAVE SIGNED this Final Act.

DONE at Ottawa, this twenty-eighth day of May, one thousand nine hundred and eighty-eight, in a single copy in the English and French languages, each text being equally authentic.
APPENDIX I

UNIDROIT CONVENTION ON INTERNATIONAL FINANCIAL LEASING

THE STATES PARTIES TO THIS CONVENTION,

RECOGNISING the importance of removing certain legal impediments to the international financial leasing of equipment, while maintaining a fair balance of interests between the different parties to the transaction,

AWARE of the need to make international financial leasing more available,

CONSCIOUS of the fact that the rules of law governing the traditional contract of hire need to be adapted to the distinctive triangular relationship created by the financial leasing transaction,

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   (b) enters into an agreement (the leasing agreement) with the lessee, granting to the lessee the right to use the equipment in return for the payment of rentals.

2. - The financial leasing transaction referred to in the previous paragraph is a transaction which includes the following characteristics:

   (a) the lessee specifies the equipment and selects the supplier without relying primarily on the skill and judgment of the lessor;

   (b) the equipment is acquired by the lessor in connection with a leasing agreement which, to the knowledge of the supplier, either has been made or is to be made between the lessor and the lessee; and
(c) the rentals payable under the leasing agreement are calculated so as to take into account in particular the amortisation of the whole or a substantial part of the cost of the equipment.

3. - This Convention applies whether or not the lessee has or subsequently acquires the option to buy the equipment or to hold it on lease for a further period, and whether or not for a nominal price or rental.

4. - This Convention applies to financial leasing transactions in relation to all equipment save that which is to be used primarily for the lessee's personal, family or household purposes.

Article 2

In the case of one or more sub-leasing transactions involving the same equipment, this Convention applies to each transaction which is a financial leasing transaction and is otherwise subject to this Convention as if the person from whom the first lessor (as defined in paragraph 1 of the previous article) acquired the equipment were the supplier and as if the agreement under which the equipment was so acquired were the supply agreement.

Article 3

1. - This Convention applies when the lessor and the lessee have their places of business in different States and:

(a) those States and the State in which the supplier has its place of business are Contracting States; or

(b) both the supply agreement and the leasing agreement are governed by the law of a Contracting State.

2. - A reference in this Convention to a party's place of business shall, if it has more than one place of business, mean the place of business which has the closest relationship to the relevant agreement and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that agreement.

Article 4

1. - The provisions of this Convention shall not cease to apply merely because the equipment has become a fixture to or incorporated in land.

2. - Any question whether or not the equipment has become a fixture to or incorporated in land, and if so the effect on the rights inter se of the lessor and a person having real rights in the land, shall be determined by the law of the State where the land is situated.

Article 5

1. - The application of this Convention may be excluded only if each of the parties to the supply agreement and each of the parties to the leasing agreement agree to exclude it.

2. - Where the application of this Convention has not been excluded in accordance with
the previous paragraph, the parties may, in their relations with each other, derogate from or vary the effect of any of its provisions except as stated in Articles 8(3) and 13(3)(b) and (4).

Article 6

1. - In the interpretation of this Convention, regard is to be had to its object and purpose as set forth in the preamble, to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.

2. - Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law.

CHAPTER II - RIGHTS AND DUTIES OF THE PARTIES

Article 7

1. - (a) The lessor’s real rights in the equipment shall be valid against the lessee’s trustee in bankruptcy and creditors, including creditors who have obtained an attachment or execution.

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

2. - Where by the applicable law the lessor’s real rights in the equipment are valid against a person referred to in the previous paragraph only on compliance with rules as to public notice, those rights shall be valid against that person only if there has been compliance with such rules.

3. - For the purposes of the previous paragraph the applicable law is the law of the State which, at the time when a person referred to in paragraph 1 becomes entitled to invoke the rules referred to in the previous paragraph, is:

(a) in the case of a registered ship, the State in which it is registered in the name of the owner (for the purposes of this sub-paragraph a bareboat charterer is deemed not to be the owner);

(b) in the case of an aircraft which is registered pursuant to the Convention on International Civil Aviation done at Chicago on 7 December 1944, the State in which it is so registered;

(c) in the case of other equipment of a kind normally moved from one State to another, including an aircraft engine, the State in which the lessee has its principal place of business;

(d) in the case of all other equipment, the State in which the equipment is situated.

4. - Paragraph 2 shall not affect the provisions of any other treaty under which the lessor’s real rights in the equipment are required to be recognised.

5. - This article shall not affect the priority of any creditor having:
(a) a consensual or non-consensual lien or security interest in the equipment arising otherwise than by virtue of an attachment or execution, or

(b) any right of arrest, detention or disposition conferred specifically in relation to ships or aircraft under the law applicable by virtue of the rules of private international law.

Article 8

1. - (a) Except as otherwise provided by this Convention or stated in the leasing agreement, the lessor shall not incur any liability to the lessee in respect of the equipment save to the extent that the lessee has suffered loss as the result of its reliance on the lessor’s skill and judgment and of the lessor’s intervention in the selection of the supplier or the specifications of the equipment.

(b) The lessor shall not, in its capacity of lessor, be liable to third parties for death, personal injury or damage to property caused by the equipment.

(c) The above provisions of this paragraph shall not govern any liability of the lessor in any other capacity, for example as owner.

2. - The lessor warrants that the lessee’s quiet possession will not be disturbed by a person who has a superior title or right, or who claims a superior title or right and acts under the authority of a court, where such title, right or claim is not derived from an act or omission of the lessee.

3. - The parties may not derogate from or vary the effect of the provisions of the previous paragraph in so far as the superior title, right or claim is derived from an intentional or grossly negligent act or omission of the lessor.

4. - The provisions of paragraphs 2 and 3 shall not affect any broader warranty of quiet possession by the lessor which is mandatory under the law applicable by virtue of the rules of private international law.

Article 9

1. - The lessee shall take proper care of the equipment, use it in a reasonable manner and keep it in the condition in which it was delivered, subject to fair wear and tear and to any modification of the equipment agreed by the parties.

2. - When the leasing agreement comes to an end the lessee, unless exercising a right to buy the equipment or to hold the equipment on lease for a further period, shall return the equipment to the lessor in the condition specified in the previous paragraph.

Article 10

1. - The duties of the supplier under the supply agreement shall also be owed to the lessee as if it were a party to that agreement and as if the equipment were to be supplied directly to the lessee. However, the supplier shall not be liable to both the lessor and the lessee in respect of the same damage.
2. - Nothing in this article shall entitle the lessee to terminate or rescind the supply agreement without the consent of the lessor.

Article 11

The lessee’s rights derived from the supply agreement under this Convention shall not be affected by a variation of any term of the supply agreement previously approved by the lessee unless it consented to that variation.

Article 12

1. - Where the equipment is not delivered or is delivered late or fails to conform to the supply agreement:

   (a) the lessee has the right as against the lessor to reject the equipment or to terminate the leasing agreement; and

   (b) the lessor has the right to remedy its failure to tender equipment in conformity with the supply agreement,

as if the lessee had agreed to buy the equipment from the lessor under the same terms as those of the supply agreement.

2. - A right conferred by the previous paragraph shall be exercisable in the same manner and shall be lost in the same circumstances as if the lessee had agreed to buy the equipment from the lessor under the same terms as those of the supply agreement.

3. - The lessee shall be entitled to withhold rentals payable under the leasing agreement until the lessor has remedied its failure to tender equipment in conformity with the supply agreement or the lessee has lost the right to reject the equipment.

4. - Where the lessee has exercised a right to terminate the leasing agreement, the lessee shall be entitled to recover any rentals and other sums paid in advance, less a reasonable sum for any benefit the lessee has derived from the equipment.

5. - The lessee shall have no other claim against the lessor for non-delivery, delay in delivery or delivery of non-conforming equipment except to the extent to which this results from the act or omission of the lessor.

6. - Nothing in this article shall affect the lessee’s rights against the supplier under Article 10.

Article 13

1. - In the event of default by the lessee, the lessor may recover accrued unpaid rentals, together with interest and damages.

2. - Where the lessee’s default is substantial, then subject to paragraph 5 the lessor may also require accelerated payment of the value of the future rentals, where the leasing agreement so provides, or may terminate the leasing agreement and after such termination:
(a) recover possession of the equipment; and

(b) recover such damages as will place the lessor in the position in which it would have been had the lessee performed the leasing agreement in accordance with its terms.

3. - (a) The leasing agreement may provide for the manner in which the damages recoverable under paragraph 2 (b) are to be computed.

(b) Such provision shall be enforceable between the parties unless it would result in damages substantially in excess of those provided for under paragraph 2 (b). The parties may not derogate from or vary the effect of the provisions of the present sub-paragraph.

4. - Where the lessor has terminated the leasing agreement, it shall not be entitled to enforce a term of that agreement providing for acceleration of payment of future rentals, but the value of such rentals may be taken into account in computing damages under paragraphs 2(b) and 3. The parties may not derogate from or vary the effect of the provisions of the present paragraph.

5. - The lessor shall not be entitled to exercise its right of acceleration or its right of termination under paragraph 2 unless it has by notice given the lessee a reasonable opportunity of remedying the default so far as the same may be remedied.

6. - The lessor shall not be entitled to recover damages to the extent that it has failed to take all reasonable steps to mitigate its loss.

Article 14

1. - The lessor may transfer or otherwise deal with all or any of its rights in the equipment or under the leasing agreement. Such a transfer shall not relieve the lessor of any of its duties under the leasing agreement or alter either the nature of the leasing agreement or its legal treatment as provided in this Convention.

2. - The lessee may transfer the right to the use of the equipment or any other rights under the leasing agreement only with the consent of the lessor and subject to the rights of third parties.

CHAPTER III - FINAL PROVISIONS

Article 15

1. - This Convention is open for signature at the concluding meeting of the Diplomatic Conference for the Adoption of the Draft Unidroit Conventions on International Factoring and International Financial Leasing and will remain open for signature by all States at Ottawa until 31 December 1990.

2. - This Convention is subject to ratification, acceptance or approval by States which have signed it.

3. - This Convention is open for accession by all States which are not signatory States as from the date it is open for signature.
4. - Ratification, acceptance, approval or accession is effected by the deposit of a formal instrument to that effect with the depositary.

Article 16

1. - This Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the third instrument of ratification, acceptance, approval or accession.

2. - For each State that ratifies, accepts, approves, or accedes to this Convention after the deposit of the third instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.

Article 17

This Convention does not prevail over any treaty which has already been or may be entered into; in particular it shall not affect any liability imposed on any person by existing or future treaties.

Article 18

1. - If a Contracting State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may substitute its declaration by another declaration at any time.

2. - These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. - If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

4. - If a Contracting State makes no declaration under paragraph 1, the Convention is to extend to all territorial units of that State.

Article 19

1. - Two or more Contracting States which have the same or closely related legal rules on matters governed by this Convention may at any time declare that the Convention is not to apply where the supplier; the lessor and the lessee have their places of business in those States. Such declarations may be made jointly or by reciprocal unilateral declarations.

2. - A Contracting State which has the same or closely related legal rules on matters governed by this Convention as one or more non-Contracting States may at any time declare
that the Convention is not to apply where the supplier, the lessor and the lessee have their places of business in those States.

3. - If a State which is the object of a declaration under the previous paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which the Convention enters into force in respect of the new Contracting State, have the effect of a declaration made under paragraph 1, provided that the new Contracting State joins in such declaration or makes a reciprocal unilateral declaration.

Article 20

A Contracting State may declare at the time of signature, ratification, acceptance, approval or accession that it will substitute its domestic law for Article 8(3) if its domestic law does not permit the lessor to exclude its liability for its default or negligence.

Article 21

1. - Declarations made under this Convention at the time of signature are subject to confirmation upon ratification, acceptance or approval.

2. - Declarations and confirmations of declarations are to be in writing and to be formally notified to the depositary.

3. - A declaration takes effect simultaneously with the entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral declarations under Article 19 take effect on the first day of the month following the expiration of six months after the receipt of the latest declaration by the depositary.

4. - Any State which makes a declaration under this Convention may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal is to take effect on the first day of the month following the expiration of six months after the date of the receipt of the notification by the depositary.

5. - A withdrawal of a declaration made under Article 19 renders inoperative in relation to the withdrawing State, as from the date on which the withdrawal takes effect, any joint or reciprocal unilateral declaration made by another State under that article.

Article 22

No reservations are permitted except those expressly authorised in this Convention.

Article 23

This Convention applies to a financial leasing transaction when the leasing agreement and the supply agreement are both concluded on or after the date on which the Convention enters into force in respect of the Contracting States referred to in Article 3 (1)(a), or of the Contracting State or States referred to in paragraph 1 (b) of that article.
Article 24

1. - This Convention may be denounced by any Contracting State at any time after the date on which it enters into force for that State.

2. - Denunciation is effected by the deposit of an instrument to that effect with the depositary.

3. - A denunciation takes effect on the first day of the month following the expiration of six months after the deposit of the instrument of denunciation with the depositary. Where a longer period for the denunciation to take effect is specified in the instrument of denunciation it takes effect upon the expiration of such longer period after its deposit with the depositary.

Article 25

1. - This Convention shall be deposited with the Government of Canada.

2. - The Government of Canada shall:

   (a) inform all States which have signed or acceded to this Convention and the President of the International Institute for the Unification of Private Law (Unidroit) of

       (i) each new signature or deposit of an instrument of ratification, acceptance, approval or accession, together with the date thereof;

       (ii) each declaration made under Articles 18, 19 and 20;

       (iii) the withdrawal of any declaration made under Article 21 (4);

       (iv) the date of entry into force of this Convention;

       (v) the deposit of an instrument of denunciation of this Convention together with the date of its deposit and the date on which it takes effect;

   (b) transmit certified true copies of this Convention to all signatory States, to all States acceding to the Convention and to the President of the International Institute for the Unification of Private Law (Unidroit).

IN WITNESS WHEREOF the undersigned plenipotentiaries, being duly authorised by their respective Governments, have signed this Convention.

DONE at Ottawa, this twenty-eighth day of May, one thousand nine hundred and eighty-eight, in a single original, of which the English and French texts are equally authentic.
APPENDIX II

UNIDROIT CONVENTION ON INTERNATIONAL FACTORING

THE STATES PARTIES TO THIS CONVENTION,

CONSCIOUS of the fact that international factoring has a significant role to play in the development of international trade,

RECOGNISING therefore the importance of adopting uniform rules to provide a legal framework that will facilitate international factoring, while maintaining a fair balance of interests between the different parties involved in factoring transactions,

HAVE AGREED as follows:

CHAPTER I - SPHERE OF APPLICATION AND GENERAL PROVISIONS

Article 1

1. - This Convention governs factoring contracts and assignments of receivables as described in this Chapter.

2. - For the purposes of this Convention, “factoring contract” means a contract concluded between one party (the supplier) and another party (the factor) pursuant to which:

(a) the supplier may or will assign to the factor receivables arising from contracts of sale of goods made between the supplier and its customers (debtors) other than those for the sale of goods bought primarily for their personal, family or household use;

(b) the factor is to perform at least two of the following functions:

– finance for the supplier, including loans and advance payments;
– maintenance of accounts (ledgering) relating to the receivables;
– collection of receivables;
– protection against default in payment by debtors;

(c) notice of the assignment of the receivables is to be given to debtors.

3. - In this Convention references to “goods” and “sale of goods” shall include services and the supply of services.

4. - For the purposes of this Convention:

(a) a notice in writing need not be signed but must identify the person by whom or in whose name it is given;
(b) "notice in writing" includes, but is not limited to, telegrams, telex and any other telecommunication capable of being reproduced in tangible form;

(c) a notice in writing is given when it is received by the addressee.

Article 2

1. - This Convention applies whenever the receivables assigned pursuant to a factoring contract arise from a contract of sale of goods between a supplier and a debtor whose places of business are in different States and:

(a) those States and the State in which the factor has its place of business are Contracting States; or

(b) both the contract of sale of goods and the factoring contract are governed by the law of a Contracting State.

2. - A reference in this Convention to a party's place of business shall, if it has more than one place of business, mean the place of business which has the closest relationship to the relevant contract and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that contract.

Article 3

1. - The application of this Convention may be excluded:

(a) by the parties to the factoring contract; or

(b) by the parties to the contract of sale of goods, as regards receivables arising at or after the time when the factor has been given notice in writing of such exclusion.

2. - Where the application of this Convention is excluded in accordance with the previous paragraph, such exclusion may be made only as regards the Convention as a whole.

Article 4

1. - In the interpretation of this Convention, regard is to be had to its object and purpose as set forth in the preamble, to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.

2. - Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based or, in the absence of such principles, in conformity with the law applicable by virtue of the rules of private international law.
CHAPTER II - RIGHTS AND DUTIES OF THE PARTIES

Article 5

As between the parties to the factoring contract:

(a) a provision in the factoring contract for the assignment of existing or future receivables shall not be rendered invalid by the fact that the contract does not specify them individually, if at the time of conclusion of the contract or when they come into existence they can be identified to the contract;

(b) a provision in the factoring contract by which future receivables are assigned operates to transfer the receivables to the factor when they come into existence without the need for any new act of transfer.

Article 6

1. - The assignment of a receivable by the supplier to the factor shall be effective notwithstanding any agreement between the supplier and the debtor prohibiting such assignment.

2. - However, such assignment shall not be effective against the debtor when, at the time of conclusion of the contract of sale of goods, it has its place of business in a Contracting State which has made a declaration under Article 18 of this Convention.

3. - Nothing in paragraph 1 shall affect any obligation of good faith owed by the supplier to the debtor or any liability of the supplier to the debtor in respect of an assignment made in breach of the terms of the contract of sale of goods.

Article 7

A factoring contract may validly provide as between the parties thereto for the transfer, with or without a new act of transfer, of all or any of the supplier’s rights deriving from the contract of sale of goods, including the benefit of any provision in the contract of sale of goods reserving to the supplier title to the goods or creating any security interest.

Article 8

1. - The debtor is under a duty to pay the factor if, and only if, the debtor does not have knowledge of any other person’s superior right to payment and notice in writing of the assignment:

(a) is given to the debtor by the supplier or by the factor with the supplier’s authority;

(b) reasonably identifies the receivables which have been assigned and the factor to whom or for whose account the debtor is required to make payment; and

(c) relates to receivables arising under a contract of sale of goods made at or before the time the notice is given.

2. - Irrespective of any other ground on which payment by the debtor to the factor
discharges the debtor from liability, payment shall be effective for this purpose if made in accordance with the previous paragraph.

Article 9

1. - In a claim by the factor against the debtor for payment of a receivable arising under a contract of sale of goods the debtor may set up against the factor all defences arising under that contract of which the debtor could have availed itself if such claim had been made by the supplier.

2. - The debtor may also assert against the factor any right of set-off in respect of claims existing against the supplier in whose favour the receivable arose and available to the debtor at the time a notice in writing of assignment conforming to Article 8(1) was given to the debtor.

Article 10

1. - Without prejudice to the debtor's rights under Article 9, non-performance or defective or late performance of the contract of sale of goods shall not by itself entitle the debtor to recover a sum paid by the debtor to the factor if the debtor has a right to recover that sum from the supplier.

2. - The debtor who has such a right to recover from the supplier a sum paid to the factor in respect of a receivable shall nevertheless be entitled to recover that sum from the factor to the extent that:

   (a) the factor has not discharged an obligation to make payment to the supplier in respect of that receivable; or

   (b) the factor made such payment at a time when it knew of the supplier's non-performance or defective or late performance as regards the goods to which the debtor's payment relates.

CHAPTER III - SUBSEQUENT ASSIGNMENTS

Article 11

1. - Where a receivable is assigned by a supplier to a factor pursuant to a factoring contract governed by this Convention:

   (a) the rules set out in Articles 5 to 10 shall, subject to sub-paragraph (b) of this paragraph, apply to any subsequent assignment of the receivable by the factor or by a subsequent assignee;

   (b) the provisions of Articles 8 to 10 shall apply as if the subsequent assignee were the factor.

2. - For the purposes of this Convention, notice to the debtor of the subsequent assignment also constitutes notice of the assignment to the factor.
Article 12

This Convention shall not apply to a subsequent assignment which is prohibited by the terms of the factoring contract.

CHAPTER IV - FINAL PROVISIONS

Article 13

1. - This Convention is open for signature at the concluding meeting of the Diplomatic Conference for the Adoption of the Draft Unidroit Conventions on International Factoring and International Financial Leasing and will remain open for signature by all States at Ottawa until 31 December 1990.

2. - This Convention is subject to ratification, acceptance or approval by States which have signed it.

3. - This Convention is open for accession by all States which are not signatory States as from the date it is open for signature.

4. - Ratification, acceptance, approval or accession is effected by the deposit of a formal instrument to that effect with the depositary.

Article 14

1. - This Convention enters into force on the first day of the month following the expiration of six months after the date of deposit of the third instrument of ratification, acceptance, approval or accession.

2. - For each State that ratifies, accepts, approves, or accedes to this Convention after the deposit of the third instrument of ratification, acceptance, approval or accession, this Convention enters into force in respect of that State on the first day of the month following the expiration of six months after the date of the deposit of its instrument of ratification, acceptance, approval or accession.

Article 15

This Convention does not prevail over any treaty which has already been or may be entered into.

Article 16

1. - If a Contracting State has two or more territorial units in which different systems of law are applicable in relation to the matters dealt with in this Convention, it may, at the time of signature, ratification, acceptance, approval or accession, declare that this Convention is to extend to all its territorial units or only to one or more of them, and may substitute its declaration by another declaration at any time.
2. - These declarations are to be notified to the depositary and are to state expressly the territorial units to which the Convention extends.

3. - If, by virtue of a declaration under this article, this Convention extends to one or more but not all of the territorial units of a Contracting State, and if the place of business of a party is located in that State, this place of business, for the purposes of this Convention, is considered not to be in a Contracting State, unless it is in a territorial unit to which the Convention extends.

4. - If a Contracting State makes no declaration under paragraph 1, the Convention is to extend to all territorial units of that State.

Article 17

1. - Two or more Contracting States which have the same or closely related legal rules on matters governed by this Convention may at any time declare that the Convention is not to apply where the supplier, the factor and the debtor have their places of business in those States. Such declarations may be made jointly or by reciprocal unilateral declarations.

2. - A Contracting State which has the same or closely related legal rules on matters governed by this Convention as one or more non-Contracting States may at any time declare that the Convention is not to apply where the supplier, the factor and the debtor have their places of business in those States.

3. - If a State which is the object of a declaration under the previous paragraph subsequently becomes a Contracting State, the declaration made will, as from the date on which the Convention enters into force in respect of the new Contracting State, have the effect of a declaration made under paragraph 1, provided that the new Contracting State joins in such declaration or makes a reciprocal unilateral declaration.

Article 18

A Contracting State may at any time make a declaration in accordance with Article 6(2) that an assignment under Article 6(1) shall not be effective against the debtor when, at the time of conclusion of the contract of sale of goods, it has its place of business in that State.

Article 19

1. - Declarations made under this Convention at the time of signature are subject to confirmation upon ratification, acceptance or approval.

2. - Declarations and confirmations of declarations are to be in writing and to be formally notified to the depositary.

3. - A declaration takes effect simultaneously with the entry into force of this Convention in respect of the State concerned. However, a declaration of which the depositary receives formal notification after such entry into force takes effect on the first day of the month following the expiration of six months after the date of its receipt by the depositary. Reciprocal unilateral declarations under Article 17 take effect on the first day of the month following the expiration of six months after the receipt of the latest declaration by the depositary.
4. - Any State which makes a declaration under this Convention may withdraw it at any time by a formal notification in writing addressed to the depositary. Such withdrawal is to take effect on the first day of the month following the expiration of six months after the date of the receipt of the notification by the depositary.

5. - A withdrawal of a declaration made under Article 17 renders inoperative in relation to the withdrawing State, as from the date on which the withdrawal takes effect, any joint or reciprocal unilateral declaration made by another State under that article.

Article 20

No reservations are permitted except those expressly authorised in this Convention.

Article 21

This Convention applies when receivables assigned pursuant to a factoring contract arise from a contract of sale of goods concluded on or after the date on which the Convention enters into force in respect of the Contracting States referred to in Article 2 (1)(a), or the Contracting State or States referred to in paragraph 1(b) of that article, provided that:

(a) the factoring contract is concluded on or after that date; or
(b) the parties to the factoring contract have agreed that the Convention shall apply.

Article 22

1. - This Convention may be denounced by any Contracting State at any time after the date on which it enters into force for that State.

2. - Denunciation is effected by the deposit of an instrument to that effect with the depositary.

3. - A denunciation takes effect on the first day of the month following the expiration of six months after the deposit of the instrument of denunciation with the depositary. Where a longer period for the denunciation to take effect is specified in the instrument of denunciation it takes effect upon the expiration of such longer period after its deposit with the depositary.

Article 23

1. - This Convention shall be deposited with the Government of Canada.

2. - The Government of Canada shall:

   (a) inform all States which have signed or acceded to this Convention and the President of the International Institute for the Unification of Private Law (Unidroit) of:

      (i) each new signature or deposit of an instrument of ratification, acceptance, approval or accession, together with the date thereof;

      (ii) each declaration made under Articles 16, 17 and 18;
(iii) the withdrawal of any declaration made under Article 19 (4);
(iv) the date of entry into force of this Convention;
(v) the deposit of an instrument of denunciation of this Convention together with
the date of its deposit and the date on which it takes effect;

(b) transmit certified true copies of this Convention to all signatory States, to all States
acceding to the Convention and to the President of the International Institute for the Unification
of Private Law (Unidroit).

IN WITNESS WHEREOF the undersigned plenipotentiaries, being duly authorised by
their respective Governments, have signed this Convention.

DONE at Ottawa, this twenty-eighth day of May, one thousand nine hundred and eighty-
eight, in a single original, of which the English and French texts are equally authentic.