

Unidroit's legislative work designed to promote leasing internationally

By the International Institute for the Unification of Private Law (Unidroit)

IN THIS ARTICLE, BY NOW A REGULAR FEATURE OF THE *WORLD LEASING YEARBOOK*, the aim is to update the information provided in the 2013 edition regarding three legislative projects undertaken by the International Institute for the Unification of Private Law (Unidroit) for the promotion of leasing either at the cross-border level or in those parts of the world where the message of its unique potential as an engine for growth has still not got through properly.

These projects are, first, the Unidroit Convention on International Financial Leasing, opened to signature in Ottawa on May 28, 1988 (hereinafter referred to as the *Unidroit Convention*); secondly, the Convention on International Interests in Mobile Equipment, opened to signature in Cape Town on November 16, 2001 (hereinafter referred to as the *Cape Town Convention*); and the Protocols thereto opened to signature to date, namely the Protocol on Matters specific to Aircraft Equipment, also opened to signature in Cape Town on November 16, 2001 (hereinafter referred to as the *Aircraft Protocol*), the Protocol on Matters specific to Railway Rolling Stock, opened to signature in Luxembourg on February 23, 2007 (hereinafter referred to as the *Luxembourg Protocol*), and the Protocol on Matters specific to Space Assets, opened to signature in Berlin on March 9, 2012 (hereinafter referred to as the *Space Protocol*); and, thirdly, the Unidroit Model Law on Leasing, adopted in Rome on November 13, 2008 (hereinafter referred to as the *Model Law*).

The procedure for implementation of the Cape Town Convention and the Aircraft Protocol has continued to gather pace over the last year. At the time of writing (July 10, 2014), 59 States and the European Union (EU) had become Parties to the Cape Town Convention and 53 States and the EU had become Parties to the Aircraft Protocol.

Undoubtedly, a major fillip to the implementation procedure in respect of both the Cape Town Convention and the Aircraft Protocol has been given by the decision of the Export-Import Bank of the US to reduce by one-third its exposure fee on the export financing of large commercial aircraft for buyers in Contracting States to the Cape Town Convention and the Aircraft Protocol.

Equally, it is hoped that the signature of the Luxembourg and Space Protocols on November 21, 2012 by Germany may usher in further signatures from member States of the EU.

The Unidroit Convention

Status of implementation. The Contracting Parties to the Unidroit Convention (the text of which may be accessed via the Unidroit web site – www.unidroit.org) are, at the time of writing, as follows: Belarus (date of accession: August 18, 1998); France (date of approval: September 23, 1991); Hungary (date of accession: May 7, 1996); Italy (date of ratification: November 29, 1993); Latvia (date of accession: August 6, 1997); Nigeria (date of ratification: October 25, 1994); Panama (date of ratification: March 26, 1997), the Russian Federation (date of accession: June 3, 1998), Ukraine (date of accession: December 5, 2006) and Uzbekistan (date of accession: July 6, 2000).

With regard to the French Government's approval and the Russian Government's accession, it should be noted that France and the Russian Federation, in becoming Parties to the Unidroit Convention, both availed themselves of the reservation contained in Article 20, the effect of which is that they will substitute their domestic law rules for the provisions of Article 8(3).

It is worthy of note that the fact that the five most recent States to become Parties (Belarus, Latvia, the Russian Federation, Ukraine and Uzbekistan) all have emerging economies tends to bear out the opinion expressed in the past by different commentators (cf. S. Amembal, "Emerging lease markets" in *World Leasing Yearbook 1999*, 16 at 18) regarding the Unidroit Convention's particular aptness to meet the special needs of such economies.

Conditions for application. What are the circumstances in which the Unidroit Convention will apply to a given leasing transaction? In order to answer this question it is necessary to consider first the substantive conditions, then the territorial conditions and finally the temporal conditions for its application (cf. for a full commentary on the provisions of the Unidroit Convention: M.J. Stanford, "The Unidroit Convention on International Financial Leasing adopted in Ottawa on May 26, 1988" in *World Leasing Yearbook 1989*, pages 58 and 61–67).

Substantive conditions. To take the substantive conditions first, these are essentially set out in Article 1. A leasing transaction for the purposes of the Unidroit Convention, denominated a "financial leasing" transaction, is a transaction in which plant, capital goods or other equipment are acquired by a prospective lessor, on specifications provided by the prospective lessee and on terms approved by that party in so far as they concern its interests, from

a supplier and leased to that lessee by the lessor in return for the payment of rentals (cf. Article 1(1)).

It is thus a complex tripartite transaction involving the interaction of two agreements, a supply agreement and a leasing agreement.

Its distinguishing features are that, first, unlike a traditional hire contract, it is the lessee that specifies the equipment and selects the supplier without relying primarily on the lessor's skill and judgment (cf. Article 1(2)(a)); secondly, 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 (cf. Article 1(2)(b)); and thirdly, again unlike a traditional hire contract, the lease rentals 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 (cf. Article 1(2)(c)).

The inclusion or not of a purchase option in the leasing agreement is irrelevant for the purposes of the Unidroit Convention's application (cf. Article 1(3)). The Unidroit Convention is designed to apply to equipment to be used primarily for professional and therefore non-consumer purposes (cf. Article 1(4)).

Territorial conditions. Turning to the territorial conditions for the application of the Unidroit Convention, these are that the places of business of the lessor and the lessee should be situated in different States and that either both these States and that where the supplier's place of business is located should be Contracting States (cf. Article 3(1)(a)) or both the supply agreement and the leasing agreement are governed by the law of a Contracting State (cf. Article 3(1)(b)).

What this means at the present time is that for the Unidroit Convention to apply under the terms of Article 3(1)(a) the lessor's and the lessee's places of business must be situated in any two of Belarus, France, Hungary, Italy, Latvia, Nigeria, Panama, the Russian Federation, Ukraine and Uzbekistan and the supplier's in any one of these 10, it not mattering if, as will frequently be the case, the supplier's place of business is situated in the same State as either the lessor's or the lessee's place of business.

On the other hand, for the Unidroit Convention to apply under the terms of Article 3(1)(b) it will suffice for a judge in Belarus, France, Hungary, Italy, Latvia, Nigeria, Panama, the Russian Federation, Ukraine or Uzbekistan to find his own country's law applicable, by the operation of his conflict of law rules, to both the supply agreement and the leasing agreement.

Temporal conditions. The temporal conditions for the application of the Unidroit Convention to a given leasing transaction are set out in Article 23. These are that both the leasing agreement and the supply agreement must have been concluded on or after the date on which the Unidroit Convention enters into force in respect of the Contracting States referred to in Article 3(1)(a) and (b).

For the Unidroit Convention to be applicable, the two agreements must therefore have been concluded on or after May 1, 1995 (the date on which the Unidroit Convention entered into force for these countries) in respect of France, Italy and Nigeria, on or after December 1, 1996 (the date on which the Unidroit Convention entered into force for this country) in respect of

Hungary, on or after October 1, 1997 (the date on which the Unidroit Convention entered into force for this country) in respect of Panama, on or after March 1, 1998 (the date on which the Unidroit Convention entered into force for this country) in respect of Latvia, on or after January 1, 1999 (the date on which the Unidroit Convention entered into force for this country) in respect of the Russian Federation, on or after March 1, 1999 (the date on which the Unidroit Convention entered into force for this country) in respect of Belarus, on or after February 1, 2001 (the date on which the Unidroit Convention entered into force for this country) in respect of Uzbekistan and on or after July 1, 2007 (the date on which the Unidroit Convention entered into force for this country) in respect of Ukraine.

The Cape Town Convention

The Cape Town Convention is a treaty that seeks to extend the benefits of the Unidroit Convention and, in particular, the principle of the enforceability of the lessor's real rights against its lessee's trustee in bankruptcy and unsecured creditors, to security rights generally in high-value mobile equipment regularly moving across or beyond national frontiers.

It provides for the constitution and effects of an international interest in different categories of high-value mobile equipment and associated rights. The "international interest" created under the Cape Town Convention covers not only classic security interests but also those interests vested in a person who is the conditional seller under a title reservation agreement and those interests vested in a person who is the lessor under a leasing agreement.

The term "leasing agreement" is defined by the Cape Town Convention to mean an "agreement by which one person (the lessor) grants a right to possession or control of an object (with or without an option to purchase) to another person (the lessee) in return for a rental or other payment" (cf. Article 1(q) of that Convention). It should be borne in mind that it has been estimated that a good three-quarters of the transactions covered by the Cape Town Convention will take the form of leasing transactions.

It should be noted that the international regimen governing the taking of security in, and the leasing of high-value mobile equipment adopted in Cape Town – in which the general rules applicable to all the different classes of high-value mobile equipment intended to be covered by the Cape Town Convention are carried in that Convention itself and the special rules specific to each individual class of equipment are carried in equipment-specific Protocols – gives each Protocol the right to determine the relationship between the Cape Town Convention and the Unidroit Convention (cf. Article 46 of the Cape Town Convention).

The Aircraft Protocol provides that the Cape Town Convention is to supersede the Unidroit Convention *as the latter relates to aircraft objects, defined to mean airframes, aircraft engines and helicopters* (cf. Article XXV of the Aircraft Protocol).

The Luxembourg Protocol provides that the Cape Town Convention shall, to the extent of any inconsistency, prevail over the Unidroit Convention *as the latter relates to railway rolling stock, defined to mean vehicles movable on a fixed railway track or directly on, above or below a guideway, together with traction systems, engines, brakes,*

axles, bogies, pantographs, accessories and other components, equipment and parts, in each case installed on or incorporated in the vehicles, and together with all data, manuals and records relating thereto (cf. Article XIX of the Luxembourg Protocol).

Likewise, the Space Protocol provides that the Cape Town Convention as applied to *space assets* (defined as meaning any man-made uniquely identifiable asset in space or designed to be launched into space, and comprising (i) a spacecraft, such as a satellite, space station, space module, space capsule, space vehicle or reusable launch vehicle, whether or not including a space asset falling within (ii) or (iii); (ii) a payload (whether telecommunications, navigation, observation, scientific or otherwise) in respect of which a separate registration may be effected in accordance with the regulations; or (iii) a part of a spacecraft or payload such as a transponder, in respect of which a separate registration may be effected in accordance with the regulations, together with all installed, incorporated or attached accessories, parts and equipment and all data, manuals and records relating thereto) shall supersede the Unidroit Convention in respect of the subject matter of that Protocol, as between States Parties to both Conventions (cf. Article XXXIV of the Space Protocol).

It must be borne in mind, though, that the substantive sphere of application of the Unidroit Convention is much broader than that of the Cape Town Convention, delimited as the latter is by reference to specifically *high-value* mobile equipment.

Status of implementation. As indicated above, the Cape Town Convention has 60 Contracting Parties (59 States and the European Union) and the Aircraft Protocol has 54 (53 States plus the European Union). The texts of the Convention and Protocols and their status of ratifications are available on the Unidroit website at www.unidroit.org.

The Cape Town Convention entered into force on April 1, 2004 *albeit only as regards a category of objects to which a Protocol applies*, first as from the time of the entry into force of that Protocol, secondly subject to its terms and thirdly as between States Parties to the Cape Town Convention and that Protocol (cf. Article 49(1)).

With the entry into force of the Aircraft Protocol on March 1, 2006, the Cape Town Convention as applied to aircraft objects accordingly entered into force on that same date. With the entry into force of the Aircraft Protocol, moreover, the International Registry for aircraft objects under the Protocol entered into operation.

The principal database and centre of operations of the International Registry are located in Dublin but the Registry itself is completely electronic and thus accessible from any place in the world having connection to the Internet (cf. R.C.C. Cumming, "The International Registry for interests in aircraft: an overview of its structure" in *Uniform Law Review* 2006-1, pp. 18 *et seq.*).

The extent to which the new regimen now governs aviation financing transactions may be gleaned from the fact that as of mid-June, 2014, the significant figure of 500,000 registrations had been made in the International Registry for aircraft objects.

The Luxembourg Protocol (the text of which may be accessed via the Unidroit website: www.unidroit.org) has to date been signed by the EU and by five States. It was also ratified by Luxembourg on January 31, 2012.

It will enter into force on the later of, on the one hand, the first day of the month following the elapsing of three months after the deposit of the fourth instrument of ratification or accession and, on the other, the date of the deposit by the Intergovernmental Organisation for International Carriage by Rail (OTIF) – which will act as Secretariat to the future Supervisory Authority in respect of the International Registry for railway rolling stock (cf. sub-section (c)(ii), *infra*) – of a certificate confirming that that International Registry is fully operational (cf. Article XXIII(1) of the Luxembourg Protocol).

The Preparatory Commission established by the Luxembourg diplomatic Conference for the purpose of establishing this Registry is close to completion of its work.

The Space Protocol (the text of which may be accessed via the Unidroit website: www.unidroit.org) has to date been signed by four States. Like the Luxembourg Protocol, its entry into force is subject to a double condition: it will, in fact, enter into force on the later of, on the one hand, the first day of the month following the elapsing of three months after the deposit of the 10th instrument of ratification or accession and, on the other, the date of the deposit by the future Supervisory Authority of a certificate confirming that the International Registry for space assets is fully operational (cf. Article XXXVIII(1) of the Space Protocol).

The Preparatory Commission established by the Berlin diplomatic Conference for the purpose of establishing this Registry held its first session on May 6–7, 2013, its second session on January 27–28, 2014, and its third session will be held on September 11–12, 2014, all in Rome.

Conditions for application. What are the conditions under which the Cape Town Convention will apply to a given secured financing transaction? In order to answer this question, it is necessary first to consider the substantive conditions, secondly the territorial conditions and thirdly the formal requirements for its application.

Substantive conditions – types of proprietary interest covered. The international interest created by the Cape Town Convention, as mentioned above, encompasses both the classic *security interest* (cf. Article 2(2)(a)) and *the interest retained by a conditional seller* (cf. Article 2(2)(b)) or a *lessor* (cf. Article 2(2)(c)). On the other hand, the default remedies granted under the Cape Town Convention will differ according to whether the international interest is created under a security agreement (cf. Article 8) or under either a title reservation agreement or a leasing agreement (cf. Article 10).

Although the Cape Town Convention does not apply to outright sales, given the keenness of aviation interests to see the benefits of the international registration system and priority rules of the Cape Town Convention extended to such sales, that Convention provides for the possibility of such extension in respect of a particular category of equipment under the relevant Protocol (cf. Article 41 of the Cape Town Convention).

States will at the moment of ratification or accession moreover have the possibility of making certain types of non-consensual interest, such as a repairer's lien, registrable in the same way as if they were international interests (cf. Article 40 of the Cape Town Convention).

Types of property covered. The Cape Town Convention applies to international interests in three categories of *mobile equipment* and *associated rights* secured by, or associated with an agreement creating or providing for such an interest (cf. Article 2(1)).

The three categories of high-value mobile equipment primarily envisaged by the Cape Town Convention are, first, *airframes, aircraft engines and helicopters* (cf. Article 2(3)(a)) – generically referred to as “aircraft equipment” and, as such, the subject of the Aircraft Protocol – secondly, *railway rolling stock* (cf. Article 2(3)(b)) and, thirdly, *space assets* (cf. Article 2(3)(c)).

For most of the gestation of the Cape Town Convention its sphere of application was delimited by reference to a non-exhaustive list of categories of equipment: aircraft equipment, containers, oil rigs, railway rolling stock, registered ships and space property – complemented by a residual category made up of any other categories of equipment of uniquely identifiable object.

The requirement of unique identifiability was necessitated by the decision to underpin the Cape Town Convention with an asset-based (as opposed to a debtor-based) international registration system. The decision at a comparatively late stage to limit the ambit of the Cape Town Convention to just three categories of equipment was linked to the number of equipment-specific Protocols actively under preparation by Unidroit.

There was nevertheless recognition of the desirability of leaving open the possibility of extending the application of the Cape Town Convention to other categories of uniquely identifiable high-value equipment in future (cf. Article 51(1) of the Cape Town Convention). Considerable interest has for instance been expressed in the development of future Protocols on agricultural, mining and construction equipment and Unidroit is currently looking into the desirability of extending the Cape Town Convention to such categories of equipment.

The title of, and the preamble to the Cape Town Convention, as well as Article 2(1) and (2), indicate two additional criteria which determine the sphere of application of that Convention, namely that the equipment covered should be “mobile” and of “high value”. Nowhere are these concepts defined and this was intentional.

The criterion of “high value” will differ from one category of equipment to another and is therefore to be defined in the relevant Protocol. For aircraft engines, for example, this criterion is expressed in terms of thrust or horsepower (cf. Article I(2)(b) of the Aircraft Protocol) and for airframes in terms of their carrying capacity (cf. Article I(2)(e) of the Aircraft Protocol).

The Cape Town Convention applies only to objects of a kind that are *uniquely identifiable* (cf. Article 2(2)) and to associated rights capable of connection to a registered interest (cf. Article 2(1)). The reason for this was, as indicated above, to facilitate the establishment of an asset-based registration system.

Territorial condition. The only connecting factor provided for in the Cape Town Convention is that the debtor must be situated in a Contracting State at the time of the conclusion of the agreement creating or providing for the international interest (cf. Article 3(1)). As indicated above, the Cape Town Convention is furthermore intended to apply to *mobile equipment*.

The criterion of mobility, while nowhere defined, is intended to denote a category of equipment of a kind *likely* to be moving across or beyond national frontiers in the ordinary course of business, that is precisely those categories of equipment which do not particularly lend themselves to the application of the *lex rei sitae* for the settlement of disputes concerning the validity, enforceability and priority ranking of security rights.

However, the Cape Town Convention may in certain circumstances end up also applying to purely internal transactions where the particular asset does not actually realise its potential for cross-border movement, for example in the case of railway rolling stock which, whilst inherently capable of moving across frontiers, does not in fact so move.

Those States not happy with the ouster of the application of their domestic law rules that this may involve are free, however, at the time of ratification or accession, to exclude the application of the Cape Town Convention, with the exception of certain provisions – essentially the registration provisions of Chapter V and the priority rules of Article 29 – in respect of a transaction which is an internal transaction in relation to that State (cf. Article 50).

It is envisaged that each Protocol may moreover require one or more additional connecting factors for any one of the categories of equipment covered by the Cape Town Convention. Thus a helicopter or an airframe pertaining to an aircraft will be caught by the new international regimen where it is registered in the aircraft register of a Contracting State (cf. Article IV(1) of the Aircraft Protocol).

Formal requirements. For an international interest to be validly constituted, the agreement under which it is created or provided for has to meet certain formal requirements (cf. Article 7 of the Cape Town Convention).

First, the agreement in question must be in writing. Secondly, it must relate to an object of which the chargor, conditional seller or lessor has power under the applicable law to dispose. Thirdly, it must contain a description of that object sufficient to permit its identification. Finally, in the case of a security agreement, the agreement must permit the determination of the secured obligations, although without the need to state the sum or maximum sum secured.

Regulatory system of the Cape Town Convention. The regulatory system of the Cape Town Convention is analysed below from the point of view of, first, the default remedies available to the creditor, secondly, the international registration system established thereunder, thirdly, priority rules, fourthly, the effect of the international interest in insolvency, fifthly, assignments, sixthly, jurisdiction and, finally, the extent to which the parties are free to derogate from provisions of that Convention.

Default remedies. The availability of adequate and readily enforceable default remedies was recognised as being of critical importance for the success of the Cape Town Convention, in particular for the realisation of its objective of making secured financing facilities more widely available and at lower cost.

The creditor is accordingly armed under the Cape Town Convention with a set of basic default remedies that he may exercise in the event of the debtor's default. Registration not being required for the creation of an international interest, these reme-

dies may be exercised even where the international interest in question has not been registered. And it should be noted that the remedies granted under the Cape Town Convention are not exhaustive: a creditor may also exercise such additional remedies permitted by the applicable law as are not inconsistent with the mandatory provisions of that Convention on default remedies (cf. Article 12).

The remedies granted under the Cape Town Convention will differ depending on whether the creditor is a chargee under a security agreement or a conditional seller or lessor.

The remedies provided for chargees are more complex than those provided for conditional sellers and lessors: the remedies to be granted to a chargee must necessarily be more extensive because they involve the exercise of rights over another's property, whereas the remedies of a conditional seller or lessor simply involve his recovery of his own property.

In the case of a chargee, the remedies will be recovery of possession or control of the charged object (cf. Article 8(1)(a)), sale or lease of the object (cf. Article 8(1)(b)), collection or receipt of income or profits arising from the management or use of the object (cf. Article 8(1)(c)) and vesting of ownership of the object in satisfaction of the debt (cf. Article 9(1)).

The first three of these remedies require the agreement of the chargor (cf. Article 8(1)). With the exception of the last remedy – which requires a court order unless all interested persons, the chargor included, agree – they may all in principle be exercised by the chargee either with or without application to the court (cf. Article 8(2)).

However, States may, at the moment of ratifying or acceding to the Cape Town Convention, specify that such remedies may only be exercised with leave of the court (cf. Article 54(2)). This safeguard was inserted for those States not familiar with self-help.

The chargor and other interested persons (for instance, subsequent chargees) are however provided with certain safeguards in the event of the chargee's exercise of his remedies, in addition, that is, to the safeguard mentioned above in relation to the remedy of vesting of the object in satisfaction of the debt.

First, such remedies must be exercised in a commercially reasonable fashion (cf. Article 8(3)). Secondly, notice of a proposed sale or lease must be given to interested persons (cf. Article 8(4)). Thirdly, States may, at the moment of ratifying or acceding to the Cape Town Convention, specify that the chargee may not grant a lease of the object whilst it is situated in, or controlled from their territory (cf. Article 54(1)). Fourthly, the default must be one which substantially deprives the creditor of what it is entitled to expect, unless otherwise agreed (cf. Article 11(2)).

This last safeguard applies equally in respect of the remedies granted to conditional sellers and lessors. In the case of a conditional seller or lessor, these remedies will be termination of the title reservation or leasing agreement and recovery of possession or control (cf. Article 10). Here again, as with a chargee's remedies under Article 8(2), these remedies may be exercised either with or without application to the court (cf. Article 10(b)) and States will, at the moment of ratifying or acceding to the Cape Town Convention, have the opportunity of specifying that such remedies may only be exercised with leave of the court (cf. Article 54(2)).

Of crucial importance for financiers in the context of asset-based financing of the categories of equipment covered by the Cape Town Convention is the power granted to the court, upon evidence being adduced as to default, to grant a creditor various forms of speedy interim relief, namely preservation of the object and its value (cf. Article 13(1)(a)), possession, control or custody of the object (cf. Article 13(1)(b)), immobilisation of the object (cf. Article 13(1)(c)) or lease or management of the object and the income therefrom (cf. Article 13(1)(d)).

In respect of aircraft equipment an additional order may be granted by way of speedy interim relief, namely sale and application of the proceeds therefrom (cf. Article X(3) of the Aircraft Protocol).

This is one of a number of provisions of the Cape Town Convention and the Protocol which, albeit considered essential to the realisation of their commercial objectives, States will however, at the moment of ratification or accession, be free to opt out of.

This opt-in/opt-out approach commended itself to the authors of the Cape Town Convention as a means of balancing the commercial and diplomatic objectives of the exercise, that is leaving it to the individual State to choose whether or not the anticipated economic benefits of that Convention, in terms of increased access to international capital market financing, justify the sacrificing of non-economic considerations (such as debtor protection concerns) or other economic considerations (such as bankruptcy reorganisation).

International registration system. At the heart of the Cape Town Convention lies the international registration system. The international interest is registrable in an international registry (cf. Article 16(1)). Different registries are contemplated for each category of equipment (cf. Article 16(2)).

An international registry for aircraft objects has been established and is in operation (see <https://www.internationalregistry.aero/>). Registration serves a dual purpose. First, it serves to give public notice of the existence of the international interest. Secondly, it serves to preserve a creditor's priority and the effectiveness of the international interest in insolvency proceedings concerning the debtor (cf. Article 30(1)).

An early decision was taken to go for an asset-based registry. The idea of an asset-based registry, with assets being registered against currently owned and identified assets, was considered to be greatly facilitated by the types of asset covered by the Cape Town Convention, namely specific types of property that lend themselves to unique identification, typically by manufacturer's serial number. Registration is therefore against the object and not against the debtor.

Each international registry will be operated by a registrar (cf. Article 17(5)) appointed by, and under the supervision of a Supervisory Authority (cf. Article 17(2)(f)).

The conferring of the functions of Supervisory Authority on an already existing intergovernmental body of universal nature has to date been seen as an important guarantee of the credibility of the international registration system with prospective users.

The Cape Town diplomatic Conference formally invited the International Civil Aviation Organisation (I.C.A.O.) to accept the functions of Supervisory Authority in respect of the International

Registry for aircraft objects upon the entry into force of the Aircraft Protocol and, therefore, of the Cape Town Convention as applied to aircraft objects. On June 15, 2005 the I.C.A.O. Council accepted this invitation.

Of course, there may not always be an existing intergovernmental body of universal nature available to act as Supervisory Authority. This turned out to be the case with the International Registry for railway rolling stock.

The Luxembourg Protocol, accordingly, provides for the functions of Supervisory Authority in respect of the International Registry for railway rolling stock to be exercised by a new body to be established by representatives of States that will essentially be States Parties to the Luxembourg Protocol (cf. Article XII(1) of the Luxembourg Protocol).

By virtue of the fact that the international registration system is intended to be fully computerised, registrations and searches will be able to be made automatically from any point in the world.

Provided that the asset against which a lender is contemplating advancing funds is the subject of an international interest that has been registered in the international registry, that lender will thus be able to find out, more or less instantaneously, the precise status of the asset in question.

While there will be no direct reliance of the equipment-specific international registries on existing national registries or co-ordination between the two, States will be able, where the relevant Protocol so provides, to use such existing national registries – for instance, those registration offices operated by civil aviation authorities under the 1944 Chicago Convention on International Civil Aviation, which are also used for registering interests recognised by the 1948 Geneva Convention on the International Recognition of Rights in Aircraft – as an alternative or the exclusive conduit for the transmission of registration information to the international registry (cf. Article 18(5)).

The holder of an international interest would thus be able to register his national interest and his international interest in the same asset simultaneously.

Priorities. A registered interest has priority over both a subsequently registered interest and an unregistered interest (cf. Article 29(1)). One of the prime concerns of the authors of the Cape Town Convention was to keep the priority rules as simple as possible.

For this reason, the priority of the holder of a registered international interest will not be affected by the fact that he took with actual notice of an unregistered interest (cf. Article 29(2)(a)) and, in a case where the security agreement covers future advances, the creditor will have priority as to such advances even if they were made with knowledge of a subsequent interest (cf. Article 29(2)(b)).

These priority rules suffer three exceptions. The first of these is that, since the interest of an outright buyer is not registrable under the Cape Town Convention, such a buyer takes free from an international interest not registered prior to his acquisition of such an interest (cf. Article 29(3)). Secondly, since the interest or right of a conditional buyer or lessee is not registrable either under the Cape Town Convention, such a conditional buyer or lessee also takes free from an international interest not registered

prior to the registration of the international interest held by its conditional seller or lessor (cf. Article 29(4)). Thirdly, the priority rules may be varied by agreement between the holders of competing interests (cf. Article 29(4)).

Effect of the international interest in insolvency. An international interest is in principle effective in insolvency proceedings against the debtor provided that the interest was registered prior to the commencement of the insolvency proceedings in question (cf. Article 30(1)).

However, an international interest does not need to be so registered in order to be effective in the debtor's insolvency where it would already be effective for such purposes under the applicable law (cf. Article 30(2)). And the effectiveness of the international interest in insolvency is in any case subject to any special rules of law applicable in insolvency proceedings relating to the avoidance of preferences and transfers in fraud of creditors and any rules of insolvency procedure relating to the enforcement of rights under the control or supervision of an insolvency administrator (cf. Article 30(3)).

Reflecting the fact that “[i]nsolvency laws that prevent or modify security-type and leasing rights result in greater risk to financial institutions that, in turn, pass on this risk to borrowers in the form of higher interest and leasing rates” (cf. J. Wool, “The case for a commercial orientation to the proposed Unidroit Convention as applied to aircraft equipment” in *Uniform Law Review* 1999/2, 289 at 298) the Aircraft Protocol and the Luxembourg Protocol both contain special rules designed to strengthen the creditor's position *vis-à-vis* the insolvency administrator in the event of the debtor's insolvency.

This they seek to achieve by ensuring as far as possible that the creditor either secures recovery of the object within a limited time or obtains from the debtor or the insolvency administrator the curing of all past defaults and a commitment to perform the debtor's future obligations.

However, in recognition of the divide that opened up on this issue between those States prepared, on the model of Section 1110 of the American Federal Bankruptcy Code, to accept the idea of the court being precluded from exercising some of the powers it would normally have to stay proceedings or to modify the creditor's rights or remedies in such circumstances, in the interest of avoiding delay, and those States preferring to substitute the court's discretion for the creditor's entitlement to take possession, States will (under Article XXX(3) of the Aircraft Protocol and Article XXVII (3) of the Luxembourg Protocol) have the choice, at the moment of ratification or accession, between a “hard” (cf. Article XI, Alternative A of the Aircraft Protocol and Article IX, Alternative A of the Luxembourg Protocol) and a “soft” version (cf. Article XI, Alternative B of the Aircraft Protocol and Article IX, Alternatives B and C of the Luxembourg Protocol) of this special insolvency regimen.

Alternatively, it will be open to States to opt for neither the hard rule nor the soft rule and in this case the issue will fall to be dealt with under the applicable law.

Assignment. Associated rights may be assigned (cf. Article 31(1)) and such assignment registered in the international registry

(cf. Article 16(1)(b)) The formal requirements of a valid assignment follow those for the constitution of a valid international interest (cf. Article 32(1)).

An assignment of associated rights will transfer to the assignee, to the extent agreed by the parties to the assignment, the related international interest and all the interests and priorities of the assignor under the Cape Town Convention (cf. Article 31(1)).

Where there are competing assignments of associated rights and at least one of the assignments includes the related international interest and is registered, the priority rules of the Convention mentioned above apply *mutatis mutandis*, so that a registered assignment will have priority over an unregistered assignment and a subsequent assignment (cf. Article 35).

An assignee of associated rights will, however, only enjoy such priority over another assignee of the associated rights where the contract under which the associated rights arise states that they are secured by or associated with the object (cf. Article 36(1)(a)) and to the extent that the associated rights are related to an object as provided for under Article 36(2), which broadly covers obligations for the repayment of purchase-money loans and the payment of the prices and rentals of objects, together with all ancillary obligations under the financing transactions documents (cf. Article 36(1)(b)).

The remedies exercisable by an assignee in the event of the assignor's default under an assignment by way of security (cf. Article 34) and the effect of the assignor's insolvency (cf. Article 37) follow, *mutatis mutandis*, the rules laid down for the international interest itself.

Jurisdiction. The fundamental principle of jurisdiction embodied in the Cape Town Convention is the respect of freedom of contract. Thus, subject to three exceptions, the parties to a transaction will be free to confer jurisdiction in respect of any claim brought under the Cape Town Convention upon the courts of any Contracting State and such courts will, unless otherwise agreed between the parties, have *exclusive* jurisdiction, even if the forum chosen has no connection with the parties or the transaction (cf. Article 42).

The three exceptions to this rule concern insolvency proceedings, the making of orders against the registrar and the granting of speedy interim relief under the Cape Town Convention.

First, the jurisdiction rules of that Convention will not be applicable to insolvency proceedings (cf. Article 45).

Secondly, the parties will not be able to confer jurisdiction to make orders against the registrar (cf. Article 44(4)); the courts of the place in which the registrar has its centre of administration are to have exclusive jurisdiction to award damages or make orders against the registrar under Article 28 (cf. Article 44(1)) and to make orders requiring the registrar in certain circumstances to discharge a registration (cf. Article 44(2)).

Thirdly, the courts of the Contracting State on the territory of which the object is situated are to have *concurrent* jurisdiction to make orders for interim relief under the Cape Town Convention other than orders for the lease or management of the object and the income therefrom (cf. Article 43(1)) and the courts of a Contracting State on the territory of which the debtor is situated are to have *concurrent* jurisdiction to make orders under the Cape

Town Convention for the lease or management of the object and the income therefrom (cf. Article 43(2)).

Freedom of contract under the Cape Town Convention. A good portion of the provisions of the Cape Town Convention are clearly not amenable to exercise of the parties' freedom of contract in that they affect third-party rights. Subject to that limitation, though, the Cape Town Convention upholds the principle of freedom of contract, so firmly entrenched in international commercial law Conventions. Thus the parties, in their relations with each other, are, with eight exceptions, free to derogate from or vary the effect of any of the provisions of Chapter III of the Cape Town Convention (Default remedies) (cf. Article 15).

The eight provisions of Chapter III that are mandatory are, first, those requiring the chargee to exercise the default remedies that he is granted under Articles 8(1)(a), (b) and (c) and 13 in a commercially reasonable manner (cf. Article 8(3)); secondly, those requiring a chargee to give notice of an intended sale or lease (cf. Article 8(4)); thirdly, those requiring the chargee to apply any sum that he has realised by exercise of his remedies under Article 8(1) towards discharge of the amount of the secured obligations (cf. Article 8(5)); fourthly, those indicating how the chargee is to apply any surplus that he may have realised by exercise of his remedies under Article 8(1) (cf. Article 8(6)); fifthly, those restricting the grant of a vesting order (cf. Article 9(3)); sixthly, those permitting the chargor to redeem the charged object so long as the chargee has not exercised his power of sale (cf. Article 9(4)); seventhly, those permitting the court, when granting orders for speedy interim relief under Article 13(1), to impose such terms as it deems necessary for the protection of interested persons (cf. Article 13(2)); and finally, those requiring the remedies provided under Chapter III to be exercised in accordance with the procedure prescribed by the law of the place where the remedy in question is to be exercised (cf. Article 14).

Unidroit model law on leasing

Background to, and preparation of the Model Law. Readers of the *World Leasing Yearbook* will be familiar with the fact that countries enacting legislation on leasing have generally modelled their laws on the Unidroit Convention, in particular in those cases where the enactment of such legislation has resulted from the International Finance Corporation (IFC)'s activities designed to introduce leasing as an alternative source of equipment finance for industrial, agricultural and commercial enterprises in its member developing countries (cf. S. Amemba, *op. cit.*).

Inter alia given the IFC's continuing efforts in this respect as also requests for assistance in the drafting of leasing legislation that it had itself received from different quarters, the Unidroit Governing Council at its 84th session, held in Rome from April 18–20, 2005, instructed the Secretariat to launch the preparation of a model law on leasing, principally designed for use by developing countries and countries engaged in the transition to a market economy.

The Unidroit Convention provided the main point of departure, where appropriate, for the drafting of the model law. A Unidroit Advisory Board was set up for the purpose of preparing a first draft. The Advisory Board met in Rome on three occasions,

on October 17, 2005, on February 6 and 7, 2006 and April 3–5, 2006. On it served experts from North Africa, sub-Saharan Africa, Asia, Europe, Latin America, North America, the Russian Federation and the IFC itself.

Over its three sessions the Advisory Board prepared the text of a preliminary draft model law, which was laid before the Unidroit Governing Council at its 85th session, held in Rome May 8–10, 2006, for advice as to the most appropriate follow-up action.

On that occasion, the Governing Council authorised the transmission of the preliminary draft, subject to the amendment of certain provisions (in particular with a view to bringing it fully into line with the Unidroit Principles of International Commercial Contracts), to governments for finalisation.

Governments and organisations were subsequently invited to formulate comments on the preliminary draft and the scale of the response to this invitation (with comments coming from the governments of Austria, Bolivia, Bulgaria, Cameroon, the People's Republic of China, Germany, Japan, Latvia, Mongolia, Morocco, the Russian Federation, Tunisia, the UK and the US, as well as the International Civil Aviation Organisation, the then Equipment Leasing Association of America, the European Federation of Leasing Company Associations (Leaseurope), the International Chamber of Commerce (ICC) and the Latin American Leasing Federation (Felalease)) testified to the interest that the project had aroused all over the world.

Two sessions of a Unidroit Committee of governmental experts responsible for converting the preliminary draft into a draft model law were held in Johannesburg on May 7–10, 2007 and in Muscat on April 6–9, 2008.

The preliminary draft model law as reviewed by the Committee of governmental experts at the Johannesburg and Muscat sessions was laid before the Unidroit Governing Council at its 87th session, held in Rome from April 21–23, 2008, for advice as to the most appropriate follow-up action.

Subject to the making of a number of amendments, principally to the French-language version, the Governing Council authorised the transmission of a draft model law on leasing to Governments and Organisations for finalisation and adoption, at a joint session of the General Assembly of Unidroit Member States and the Committee of governmental experts.

In recommending such a novel procedure for adoption of the draft model law, the Governing Council showed its desire, on the one hand, to ensure maximum transparency *vis-à-vis* the entirety of Unidroit's membership and, on the other, to reflect the key role played in the development of the draft model law by a significant number of non-Member States, from those parts of the world for which it was principally intended.

The Joint Session was held in Rome from November 10–13, 2008. In addition to representatives of most of the States, organisations and professional associations having participated in the Johannesburg and Muscat sessions of governmental experts, representatives of Argentina, Canada, Croatia, Egypt, France, Greece, Hungary, Italy, Lithuania, Mexico, Nicaragua, the Republic of Korea, Turkey and Uruguay and observers representing the Aviation Working Group, the International Bar Association and Leaseurope participated in the finalisation of the draft model law

and witnessed adoption of the Unidroit Model Law on Leasing on November 13, 2008.

The Joint Session passed a Resolution calling upon the Unidroit Secretariat to draw up an official commentary on the Model Law, in close co-operation with the Reporter to the Joint Session, the Secretary to the Joint Session, the Chairman of the Committee of governmental experts and members of the Drafting Committee.

The Official Commentary in question had been envisaged throughout the intergovernmental negotiations, essentially as a means of clarifying certain provisions of the Model Law. Publication of the Official Commentary (the text of which may be accessed via the Unidroit website (www.unidroit.org)) was authorised by the Unidroit Governing Council at its 89th session.

Principal features of the Model Law. Introduction. Unidroit's Model Law (the text of which may be accessed via the Unidroit website: www.unidroit.org) was prepared, *inter alia*, with the needs of those countries contemplating the preparation of domestic legislation specifically in mind. It may, therefore, be considered to provide a useful model on the desirable shape of a country's leasing law.

Of course, a State, when enacting the Model Law, is entirely free to take this or that part of the Model Law and, likewise, to dispense with this or that part, in particular with a view to respecting special national exigencies.

The Model Law was always designed to be both compact and flexible, the idea being to facilitate the development of a particular country's leasing market in the manner most appropriate at the time of its enactment. It is important to remember that, subject to two exceptions, the Model Law permits total freedom of contract (Article 5).

Again, though, the enacting State will, of course, be free to alter the manner in which this principle is implemented under the Model Law. At the same time, it is important to see the balance between the rights and duties of the parties reflected in the Model Law as corresponding to the desire of its authors to enunciate a fair and balanced legal framework properly suitable to countries at all levels of economic development.

Sphere of application. At the same time, it is important to bear in mind that certain areas of the law which do not particularly lend themselves to a uniform international treatment are excluded. These are areas which are seen as particularly sensitive at the domestic law level.

Furthermore, there are other international instruments, in neighbouring areas of the law, which it was felt should not be undermined by the Model Law. And these, subject to certain limitations, are likewise excluded.

Matters excluded. Those areas of the law specifically left outside the sphere of application of the Model Law are four in number.

First, the Model Law is concerned essentially with the disposition of the rights and duties of the parties to leases and, therefore, in common with most uniform international private law instruments, including the Unidroit Convention, a decision was taken early on not to deal with the fiscal, accounting and supervisory sides of leasing. This decision is reflected in the seventh clause of the preamble to the Model Law.

The idea here is that the work of Unidroit is to clarify the private law framework of such transactions and that it would not be appropriate for it to get into such other aspects. Moreover, there was a definite feeling that the question of the most appropriate fiscal, accounting and supervisory treatment of leasing was a matter that could only be dealt with at such time as the relative rights and duties of the parties to such transactions had been first clearly defined.

Secondly, again in common with most uniform international private law instruments, the coverage of the Model Law is limited to commercial leases and, as is indicated by the definition of the types of “asset” covered in Article 2, does not extend to consumer leases, not least because of the different philosophies underlying the two types of transaction, in particular from the point of view of the special protections considered to be merited in the case of consumers.

This means, moreover, that the Model Law focuses on the sort of transactions which are most critical for a country's economic development.

Thirdly, as indicated in Article 3(1), in States that have a law governing security rights in general, the Model Law will not govern leases that function as security rights. While the line between a financial lease and a security right is not always clear, it was felt appropriate for the Model Law to defer to whatever other domestic law may govern in cases where the lessor's ownership of the leased asset functions as a security right.

The authors of the Model Law were particularly conscious in this context of the UNCITRAL Legislative Guide on Secured Transactions, adopted in Vienna in December 2007, and were anxious to safeguard the position of those States that may choose to adopt legislation based on that Guide.

Fourthly, as indicated in Article 3(2), the Model Law is not intended to apply to a lease of large aircraft equipment, unless the lessor, lessee and supplier have otherwise agreed in writing. This exclusion is intended to safeguard the application of the Aircraft Protocol and thus removes a potential source of conflict between the Model Law and that Protocol.

Matters included. In considering what is, on the other hand, within the sphere of application of the Model Law, it is necessary to distinguish between the Model Law's geographic and substantive spheres of application.

Looking first at the Model Law's *geographic sphere of application*, Article 1 specifies that the Model Law applies to any lease of an asset if that asset is within the enacting State, if the centre of main interests of the lessee is within the enacting State or if the parties agree to make the law of the enacting State applicable to their transaction.

The term “centre of main interests” is intended to catch the idea encapsulated in the 1997 UNCITRAL Model Law on Cross-Border Insolvency of something like a registered office or habitual place of business.

Turning now to the *substantive sphere of application* of the Model Law, it is appropriate, first, to focus on the two specific types of leasing covered, on the one hand, *financial leases* and, on the other, those *other leases* basically approximating to a traditional bailment.

The basic type of leasing covered by the Model Law is the second and this is termed a “lease”, which in Article 2 is defined broadly as a “transaction in which one person provides another person with the right to possess and use an asset for a specific term in return for rentals”. The definition of lease specifically indicates that it includes sub-leases.

The term “lease”, therefore, contemplates a basically bilateral agreement in which the “lessor” is the person *providing* the other person with the right to possess and use the asset under the lease and the “lessee” is the person *acquiring* the right to possess and use the asset under that lease. The lessee's basic duty, to pay rentals to the lessor, is the counterpart of the lessor's duty to provide the lessee with the right to possess and use the asset in respect of which those rentals are to be paid.

Some leases will, by virtue of the presence of certain additional ingredients, three in number, be termed “financial leases”.

The first such additional criterion is that the lessee specifies the asset and selects the supplier: in a financial lease, it is very much the lessee – and not the lessor – that plays the dynamic role in the transaction, providing the justification for the special exclusions from liability for the lessor.

The second is that the lessor acquires the asset in connection with a lease and the supplier is aware of that; this again serves to explain the exonerations from liability recognised in favour of the lessor under a financial lease: in such a lease the party from whom the lessee will need to seek redress is the supplier. Hence the importance of the supplier knowing that the asset being acquired by the lessor is being acquired for the specific purpose of being given on lease.

The third additional criterion is that the rentals or other funds payable under the lease take into account – or do not take into account – the amortisation of the whole or a substantial part of the lessor's investment.

The fact that the amortisation of the lessor's investment over the term of the financial lease is treated as an optional ingredient, whereas traditionally it has been considered a mandatory ingredient of a financial lease, is in line with the concern of the authors of the Model Law to keep it as flexible as possible, in this case by opening up the class of financial leases to cover those financial leases that are more in the nature of short-term leases.

Traditionally, another mandatory ingredient of financial leases in many jurisdictions, essentially Civil Law jurisdictions, is the inclusion of a purchase option. In the definition of financial leases for the purposes of the Model Law, this ingredient is, however, again treated as optional, with a view to keeping the Model Law as flexible as possible.

Under the Model Law, a lease that does not qualify as a “financial lease” is termed a “lease other than a financial lease”.

During the development process, some suggested creating additional statutory categories of lease, to reflect the commercial realities of leasing in particular parts of the world. It was finally, though, decided that the freedom of contract principle enshrined in Article 5 made such additional categories unnecessary.

The other defining element of the sphere of application of the Model Law is contained in the definition of “asset”: the Model Law covers leases of a wide range of assets. “Asset” as

defined in Article 2 is stated to mean “all property used in the craft, trade or business of the lessee, including immovables, capital assets, equipment, future assets, specially manufactured assets, plants and living and unborn animals”.

The only specific exclusions from the definition of “asset” under the Model Law are money and investment securities.

The use of the language “all property” means that for States that do not have laws governing leases of real property the Model Law will cover such leases. Where States do have laws governing real property leases, the Model Law may be unsuitable.

There should not, though, be any conflict, in that a law specific to leases of real property will normally prevail over a law that applies to leases generally. The Model Law is to be read as deferring to such specific laws.

The definition of “asset” is sufficiently broad in certain cases to cover intellectual property, notably software. Two cases do, though, need to be distinguished in this regard.

On the one hand, the software may be embodied in a tangible asset so as to form a single functional item, for example a motor-car. Here, the subject matter of the lease would be the motor-car, not the software, so that the question of whether the asset includes the software does not arise.

On the other hand, there may be cases where the software is not embodied in a tangible asset, for example a software programme designed to be installed in a computer. Here, one has to take into account the fact that a “lease” is defined as requiring a lessor to “grant a right to possession and use of the asset”. “Possession”, though, is not defined in the Model Law, which means that for the definition of the concept of possession one has to look to the general law of each State.

In States in which the term “possession” means actual *physical* possession of a *tangible* asset, then “possession” cannot refer to intangible assets such as intellectual property and the Model Law would not apply to a transaction in which a lessee acquires the right to use intellectual property.

In States, though, in which “possession” is given an extended meaning, to include *functional control* or *constructive possession*, the Model Law might, subject to the requirement that the lessor, under a financial lease, has to acquire the asset in connection with the lease and the supplier has to have knowledge of that fact, apply to a transaction involving a lease of an intangible asset.

Rights and duties of the parties. The rights and duties of the parties to leasing transactions need to be distinguished according to whether the lease is in the nature of a financial lease or is, rather, a lease other than a financial lease.

Certain rights and duties are common to both.

Rights and duties common to financial leases and leases other than financial leases. Already, the basic right and duty of the parties has been touched on when considering the definition of “lease”, that is the duty of the lessor to provide the lessee with the right to possess and use an asset for a specific term and the duty of the lessee, in return, to pay the lessor rentals. These duties (and the corresponding rights) arise under both leases and financial leases.

Another duty that arises under both leases and financial leases is the lessee’s duty to take proper care of the leased asset, taking account of the manner in which such assets would ordi-

narily be used, and to keep the asset in the condition in which it was delivered, subject to fair wear and tear (Article 18(1)(a)).

When there is also a duty under the lease to maintain the asset or when the manufacturer or supplier of the asset issues technical instructions for its use, then for the lessee to be considered to have taken “proper care” of the asset and kept it in the condition in which it was delivered it will have needed to comply with such a term of the lease or such instructions (Article 18(1)(b)).

Likewise, common to both types of lease is the lessee’s duty when the lease comes to an end or is terminated, where not exercising a right to buy or re-lease the asset, to return the asset to the lessor in the condition corresponding to a reasonable user (Article 18(2)).

Rights and duties that will differ depending on whether the transaction is a financial lease or a lease other than a financial lease. Other rights and duties, though, will differ according to whether the transaction is a financial lease or a lease other than a financial lease.

Quiet possession is just one such case. Under leases other than financial leases, the lessor warrants that the quiet possession of the lessee will not be disturbed by a person who has or claims a superior title or right to the asset or acts under the authority of a court (Article 16(2)).

Under a financial lease, on the other hand, the lessor’s warranty is limited to a disturbance of quiet possession by a third party whose superior title, right or claim derives from a negligent or intentional act or omission of the lessor (Article 16(1)(a)).

This limitation recognises that in a financial lease the lessee is responsible for the selection of the supplier and, therefore, bears responsibility for ascertaining the quality of the supplier’s rights in the leased asset.

Another such case is the warranty of suitability for purpose. Under a financial lease, the supplier warrants that the asset being leased conforms to what is accepted in the trade under the description in the lease and is fit for its ordinary purposes. This warranty is enforceable by the lessee only as against the supplier, unless the lessor is deemed to have assumed the supplier’s duties as a result of not acceding to the lessee’s request to assign its rights under the supply agreement to the lessee (Article 17(1)).

Under a lease other than a financial lease, on the other hand, the lessor has the same warranty obligation as a supplier, provided that the lessor deals regularly in assets of the kind described in the lease and can, therefore, be expected to have specialised knowledge of the expectations of the trade (Article 17(2)).

It is important also to note that the rule on the irrevocability and independence of the duties of the lessor and the lessee will vary according to whether the transaction is a financial lease or a lease other than a financial lease.

Under a financial lease, the lessor and lessee’s duties become irrevocable and independent when the asset subject to the lease has been delivered to, and accepted by the lessee (Article 10(1)(a)), whereas under a lease other than a financial lease the lessor and lessee may agree to make any of their duties irrevocable and independent, by specifically identifying each duty that is irrevocable and independent (Article 10(1)(b)).

Similarly, the risk of loss will differ depending on whether the transaction is a financial lease or a lease other than a financial lease. Under a financial lease, the risk of loss will, in principle, pass to the lessee when the lease is entered into (Article 11(1)(a)), whereas under a lease other than a financial lease the risk of loss will be retained by the lessor (Article 11(2)).

Rights and duties special to financial leases. In view of the special characteristics of a financial lease, mentioned above, the lessee under a financial lease is treated as the beneficiary of the supplier's duties *vis-à-vis* the lessor under the supply agreement (Article 7(1)). The lessee is thus entitled to go directly against the supplier, regardless of the doctrine of privity of contract.

The supplier, though, will not be liable to both the lessor and the lessee in respect of the same damage (*idem*). And the rights of the lessee with respect to a supply agreement that was approved by the lessee will not be affected by a variation of any term of such agreement, unless consented to by the lessee (Article 7(3)).

Again in line with the special features of a financial lease, the lessor, in its capacity of lessor, will not, under a financial lease, be liable to the lessee or third parties for death, personal injury or damage to property caused by the leased asset or use of that asset (Article 9).

Default and termination – events constituting default. The parties are free to agree on the events that will constitute default (Article 19(1)). Where they do not do so, default occurs when one party fails to perform a duty arising under the lease or the Model Law (Article 19(2)).

Notices to be given on default. Upon default, an aggrieved party shall give a defaulting party notice of default, notice of enforcement, notice of termination and a reasonable opportunity to cure (Article 20). Whether the notice is adequate will be governed by other laws of the enacting State. Whether the opportunity to cure is reasonable will, likewise, be determined by other laws of the enacting State.

Damages. An aggrieved party is entitled to recover damages in an amount sufficient to place it in the position in which it would have been in the absence of default (Article 20(1)). The measure of damages can, however, be modified by agreement to the contrary or by a liquidated damages clause in the lease (*idem*).

The lessor and the lessee may agree on an amount of liquidated damages to be paid in the event of default (Article 21(1)). Such sum may, however, be reduced to a reasonable amount where it is found to be grossly excessive in relation to the harm resulting from the default (Article 21(2)).

Such a sum may only be deemed to be grossly excessive where account is taken of, on the one hand, the actual harm resulting from the default and, on the other, the dual purpose served by the liquidated damages clause (as both a deterrent and compensation).

Termination. Termination of a lease may be brought about by operation of law, by agreement of the parties or by an aggrieved party upon fundamental default by the lessee or lessor (Article 23(1)(a)). In the case of a lease other than a financial lease, the lease may also be terminated by the lessee in the event of a total or partial loss occurring without fault on the part of either the lessee or the lessor (*idem*).

Termination, in principle, discharges all the parties' future

duties but does not discharge any right based on prior default or performance (Article 23(2)).

In a financial lease, the lessee is debarred from terminating the lease for a fundamental default by the lessor or the supplier occurring after the asset has been delivered to, and accepted by the lessee (Article 23(1)(b)) (remaining, however, entitled in such a case to such other remedies as are provided by the agreement of the parties and by the law of the enacting State (*idem*)), except in the case of a fundamental default of the lessor in respect of its warranty of quiet possession (Article 23(1)(c)).

Implementation of the Model Law. A representative of the IFC has gone on record stating that “the Model Law can further strengthen the IFC's role in advising Governments on how to improve the legal framework for leasing” and that “the IFC has ... started to use the ... Model Law as part of its advisory services programmes” (cf. M. Sultanov: “Equipment lease: relevance of the legal framework – IFC experiences and practices” in *Uniform Law Review* 2012, 377 at 386–387).

That same representative of the IFC has also pointed out that “the Model Law can [also] help to create an effective legal environment for leasing in those jurisdictions in which the IFC does not have active projects; to increase the sustainability of the IFC's legislative work to improve the legal framework for leasing; and to promote consistency and uniformity of leasing legislation on a global scale” (*idem*).

In fact, the IFC has incorporated key principles of the Model Law in its Leasing Manual, which, *inter alia*, discusses best practices and provides useful guidelines and recommendations for governments on how to create an effective legal framework for leasing.

It is thus that Jordan, Tanzania and Yemen have already all adopted leasing legislation incorporating portions of the Model Law and that the IFC has put forward legislation in Afghanistan and the West Bank based in its entirety on the Model Law.

In Palestine, the draft leasing law was reviewed by the President's Legal Council, and Latvia has also adopted the Model Law. Furthermore, the Model Law was the main point of reference in the drafting of legislation in Laos and Vietnam and was considered by the Chinese authorities with a view to seeing if it contained provisions of interest to China.

Promotion of the Model Law. The Unidroit Governing Council at its 89th session, held in Rome from May 10–12, 2010, having, subject to the finding of the necessary extra-budgetary funding, authorised a programme of promotional seminars for the Model Law in the parts of the world for which it is principally designed, namely developing countries and transition economies, a first seminar, co-hosted by Unidroit, the China Association of Enterprises with Foreign Investment (C.A.E.F.I.) and the China Banking Association, was held in Beijing on May 19, 2011. Further seminars are contemplated.

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