

The Law of the Lawyer

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Securing Mobile Assets: The Cape Town Convention And The Proposed Protocol On Security Interests In Space Assets

There have been substantial developments affecting the way in which a security interest in space assets, including satellites, will be perfected and enforced in the future.

The perfection and enforcement of security interests in mobile equipment that moves across national borders in the ordinary course of business have always been a concern for secured creditors because there is no assurance that other jurisdictions will recognize and enforce rights obtained under Article 9 of the Uniform Commercial Code (“U.C.C.”). The Cape Town Convention on International Interests in Mobile Equipment (“Convention”), which was co-sponsored by the International Institute for the Unification of Private Law (“Unidroit”) and the International Civil Aviation Organization, addresses these concerns by providing uniform rules relating to the creation, perfection, priority, and enforcement of security interests internationally and by establishing an international registry system for secured creditors that finance mobile assets (“Inter-



national Registry”). The Convention includes protocols for three types of mobile assets:

- Airframes, aircraft equipment, and helicopters (the “Aircraft Protocol”);
- Railway rolling stock (the “Luxembourg Protocol”); and
- Space assets (the “Space Assets Protocol” and, together with the “Aircraft Protocol” and the “Luxembourg Protocol,” the “Protocols”).

Each of the Protocols has industry-specific terms that must be read in conjunction with the Convention. The Convention becomes effective in

a state that is party to the Convention (“Contracting State”) as modified by the applicable Protocol when the applicable Protocol becomes effective in such Contracting State. To date, the Aircraft Protocol is effective in 42 jurisdictions (including the United States), and the Luxembourg Protocol was adopted and has been open to signature since February 23, 2007, but is not yet in force.

Unidroit is now working on the Space Assets Protocol. A fifth and final meeting of the Unidroit

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Committee of Governmental Experts concluded its deliberations, producing a draft of the Space Assets Protocol that was submitted to and approved by the Governing Council of Unidroit in May 2011 for transmission to the Diplomatic Conference to be held in Berlin February 27 through March 9, 2012. While there are still issues to be decided and text to be further negotiated, the Space Assets Protocol is likely to be adopted at the Diplomatic Conference. Following is a general description of the terms to date, although such terms may be changed before the Protocol becomes effective.

The Space Assets Protocol covers objects such as satellites, reusable launch vehicles, space stations, any high-value, uniquely identifiable component of these objects and any other man-made asset that is intended to be launched and placed in space or that is manufactured in space (collectively, “space assets”). It includes objects that are under construction on the ground to the extent such objects have reached the stage of manufacture where they can be identified as satellites, transponders, or other kinds of space assets, and are uniquely identifiable as required by the Space Assets Protocol and the International Registry regulations. The definition of “space assets” was drafted broadly in order to include space assets developed in the future. (“Space assets” is defined under Article 1(2)(g) of the preliminary draft of the Space Assets Protocol as:

- Any identifiable asset that is intended to be launched and placed in space or that is in space;
- Any identifiable asset assembled or manufactured in space;
- Any identifiable launch vehicle that is expendable or can be reused to transport persons or goods to and from space; and
- Any separately identifiable component forming part of an asset referred to in Article 1(2)(g) of the Space Assets Protocol or attached to or contained within such asset.)

The Space Assets Protocol will apply to security interests that are documented and that:

- Identify the space asset (by serial number, model designation and manufacturer’s name and by such other data as may be required by the International Registry regulations);
- Identify the secured obligations; and
- Relate to an object over which a grantor, conditional seller, or lessor has power to dispose.

(The Space Assets Protocol also applies to a security interest vested in a person who is the conditional seller under a title reservation agreement, and a lessor under a leasing agreement.)

A Contracting State has the option under the Convention to have the Space Assets Protocol apply to non-consensual rights in space assets as well, if the space asset is identifiable. The space asset must be uniquely identifiable in order to be registered in the International Registry. The International Registry gives priority to whichever security interest is registered first, regardless of whether a creditor has knowledge of a preexisting security interest in the same asset that was not registered. This ensures that creditors considering extending credit for a space asset can search the International Registry and be assured that the search results are conclusive. A prospective security interest may also be registered and will retain the date filed for priority purposes when it becomes an actual security interest. Registration with the International Registry also makes the security interest effective against a trustee in bankruptcy of the debtor if the security interest was registered before the commencement of bankruptcy proceedings. If a secured creditor’s security interest is not registered in the International Registry, the secured creditor’s security interest can be effective against a trustee in bankruptcy if such security interest was valid under applicable insolvency law, i.e., in the United States a security interest perfected by a properly filed financing statement that is not subject

to a preference risk. Parties can agree in writing to vary priorities under the International Registry, and such a subordination agreement can also be registered in the International Registry (and should be so registered if it is to bind an assignee of the subordinated security interest). Once an international security interest is properly registered, the International Registry provides the creditor with a certificate as prima facie proof of the facts recited in it. Searches are against the asset, not against the debtor, hence the need for unique identification. The International Registry will compensate parties that suffer loss due to an error in the registry. The jurisdiction of the state where the International Registry is located will govern such liability claims.

If a default by the debtor of the secured obligations occurs, a secured creditor may, pursuant to the Convention:

- Take possession or control of the space asset (to the extent feasible);
- Sell or grant a lease on the space asset;
- Collect any incoming rentals from the space asset; and
- Seek a court order for any of the preceding three options.

See Article 8 of the Convention.

Since enforcing a right of possession to an object in space is impractical, recourse to the physical asset is of limited value as a remedy. That is why the Space Assets Protocol provides for the assignment to the creditor of “debtor’s rights” and for recording of the assignment against the registration of the space asset in the International Registry. “Debtor’s rights” are defined as all rights to payment and performance due to a debtor by any person with respect to a space asset. Such rights include:

- Special permits, licenses, and contractual rights (if they can be assigned under local law) granted to a debtor for the manufacture, launch and operation of a space asset;

- Intangible rights needed to control, operate or transfer ownership of or rights in the space asset; and
- Proceeds and receivables derived from the operation of the space asset.

The parties may define remedies in their written agreement, with three limitations:

- The secured party cannot take possession or control of a space asset in a manner that contravenes “public order” (e.g., causes a significant disruption of communications or a threat to safety);
- The secured party must give junior creditors at least 10 business days’ prior written notice of a sale; and
- No remedy may be exercised without the prior written consent of any creditor whose security interest has been registered prior to the security interest of the secured party exercising the remedy. All remedies under the Space Assets Protocol apply unless specifically excluded by the parties’ security agreement.

All U.C.C. remedies will also apply to the extent such remedies are not inconsistent with the mandatory provisions of the Space Assets Protocol. There will also be provisions limiting the exercise of remedies in certain cases. These have yet to be finalized.

If a space asset, particularly a satellite, has already been placed in space, it is necessary for the secured creditor to have access and command codes to the space asset in order to take constructive re-possession. The preliminary draft of the Space Assets Protocol provides for the placement of such codes with an escrow agent or other third party to give the creditor an opportunity to take control of the space asset in the event of a default. The transfer of any such data must be in accordance with all relevant national laws. Upon the occurrence of a default, the secured creditor may change the access or command codes used to control the operation of

the space asset. Parties are not required to put the codes into escrow. They may agree to do so, however, subject to applicable restrictions under the Space Assets Protocol. These provisions are not exhaustive and are in addition to other remedies available under the applicable law of the Contracting State, including judicial relief.

If immediate relief is vital to the preservation of the value of the international security interest in a space asset, the Convention permits jurisdictions to opt into expedited relief provisions under which a creditor may adduce prima facie evidence of default before a national court and, pending final relief, obtain a judicial order for:

- Preservation of the space asset and its value;
- Possession, control, custody or management of the space asset;
- Sale or lease of the space asset;
- Application of any proceeds or income from the space asset; and/or
- Immobilization of the space asset.

See Article 13 of the Convention.

If a debtor:

- Grants a secured party (SP I) a lien on customer contracts relating to a satellite; and
- Thereafter grants another secured party (SP II) a lien on the satellite and debtor's rights to the satellite; and then
- Defaults in its payments to both SP I and SP II, and SP II recorded its lien with the International Registry, the Space Assets Protocol gives SP II priority over SP I to the preexisting customer agreements relating to the satellite.

Since SP I has not taken and registered an international security interest in the satellite, the Convention and the Space Assets Protocol do not confer on SP I any right to record a security interest in customer contracts relating to the satellite with the

International Registry, so SP I's security interest will be subordinate to SP II's security interest if SP II registers its security interest with the International Registry, even though SP II obtained its security interest after SP I, and SP I perfected its security interest in the customer contracts relating to the satellite by properly filing a U.C.C. financing statement. If an issue is not expressly decided in the Convention as modified by the Space Assets Protocol as ratified, the applicable law under the rules of private international law of the forum state governs the issue.

The courts of a Contracting State will have jurisdiction over a claim brought under the Convention if such jurisdiction has been conferred by agreement of the parties. In addition, jurisdiction as regards interim relief is conferred on a Contracting State if:

- The space asset is within or is physically controlled from the Contracting State;
- One of the parties or the defendant is located within the Contracting State; or
- The parties agreed in their written agreement to submit to the jurisdiction of the courts of the Contracting State. Remedies are to be exercised in conformity with the procedural laws of the governing jurisdiction.

Conclusion

In conclusion, the Space Assets Protocol will have a significant effect on the financing of space assets. To best protect secured creditors' rights to enforce a security interest against space assets, secured creditors need to require their debtors to comply with the Space Assets Protocol when it becomes effective. Secured creditors lending to space assets providers that enter into credit facilities due on or after the Space Assets Protocol becomes effective should include further assurance clauses in their loan documents that ensure compliance with the Space Assets Protocol.