The requirement of ‘power to dispose’ in the Cape Town Convention and its protocols

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Abstract
The concept of an ‘international interest’ is central to the Cape Town Convention on International Interests in Mobile Equipment. Once an international interest is created, it can be registered in the International Registry, established under the Convention, in which case it will be given priority over competing interests and enforced if the debtor defaults. One of the essential requirements for the constitution of an international interest is that a chargor, conditional seller, and lessor must have the ‘power to dispose’ of the interest held by them in the object. This article evaluates the basis and meaning of the power to dispose requirement under the Convention. It argues that power to dispose (where it arises without the right to dispose) is a matter governed by the Convention and constructs and proposes an internationally uniform concept of power to dispose under the Convention, autonomous from national law.

I. Introduction
The 2001 Convention on International Interests in Mobile Equipment (Cape Town Convention or CTC) and its protocols¹ aim to facilitate the acquisition and financing of certain types of high-value mobile equipment, such as aircraft, railway rolling stock, space and mining, and agricultural and construction equipment.² To this end, the Convention establishes a uniform legal regime for the creation, priority, registration, and enforcement of international interests in mobile equipment. This international regime is intended to give the financiers a sense of confidence in the security of the interests held by them in these types of equipment and thereby to enhance the availability of financing for the

¹ Presently, the Convention is supported by four Protocols: Protocol on Matters Specific to Aircraft Equipment (AP), entered into force in 2006; Protocol on Matters Specific to Railway Rolling Stock (RP), adopted in 2007; Protocol on Matters Specific to Space Assets (SP), adopted in 2012; Protocol on Matters Specific to Mining, Agricultural and Construction Equipment (MACP), adopted in 2019. Currently, only the AP is in force.
² As they are defined by the Convention and the relevant Protocols.
borrowers at a reduced cost. The CTC is one of the most successful international commercial law instruments to date. Having already been ratified by 83 countries since its adoption in 2001,3 the Convention is widely used by creditors, borrowers, manufacturers, and suppliers of the aircraft equipment across the world,4 as evidenced by these parties resorting routinely to the International Registry (IR) for aircraft objects, established under the Convention. This IR for aircraft objects is presently the only one in operation, and separate international registries for the registration of interests in other types of mobile equipment covered by the CTC will be established in the future.5

Central to the Convention’s regime is the concept of an ‘international interest’, which arises solely from the Convention and is autonomous from national law. This concept is truly unique because it transcends over the different approaches taken by legal systems to the characterization of security interests, title reservation, and lease agreements, which are the main forms of financing the types of equipment governed by the Convention. The international interest can be granted by a chargor under a security agreement, vested in a conditional seller under a title reservation agreement or vested in a lessor under a lease.6 Once an international interest is created, it can be enforced if the debtor defaults and, if registered in the IR, granted priority over competing interests.

The Convention provides for a set of formal requirements for the constitution of an international interest—namely, that the agreement creating or providing for the interest must: (i) be in writing; (ii) relate to the object of which the chargor, conditional seller, or lessor has the power to dispose; (iii) enable the object to be identified in conformity with the protocols; and (iv) in the case of a security agreement, enable the secured obligations to be determined, but without the need to state a sum or maximum sum secured.7

These requirements are relatively simple, except for the ‘power to dispose’ requirement, the source and meaning of which is unclear. This uncertainty is highly undesirable due to the significance of this requirement. Unless there is power to dispose, an international interest will not come into existence, its purported registration will be ineffective, its holder will not be able to assert priority, and it will lack validity if the debtor becomes insolvent. In short, the existing uncertainty as to the meaning of this requirement can undermine considerably the financiers’ confidence, increasing the cost of borrowing, and, ultimately, weaken the value and strength of the Convention’s regime.

The purpose of this article is to evaluate the basis and meaning of the ‘power to dispose’ under the Convention. There is little scholarship exploring this

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3 See <http://www.unidroit.org>.
4 As noted, the other Protocols are not yet in force.
5 The IR for aircraft objects is based in Dublin, operated by Aviareto Ltd and supervised by the Council of the International Civil Aviation Organisation (ICAO). The IR is a fully electronic, asset-based notice filing system accessible worldwide.
6 Art 2(2) CTC.
7 Art 7 CTC.
concept in the Convention’s context. The Official Commentary (Commentary)\(^8\) suggests that power to dispose can be derived from the Convention or the applicable law and that, if it is to be based on the Convention, then it should be premised on the debtor’s possession of the object. Some other commentators\(^9\) suggest that power to dispose should derive from national law as a result of various exceptions to the rule of *nemo dat quod non habet* (one cannot give what one does not have) that is known to many legal systems. The power to dispose must be distinguished from the right to dispose. The right to dispose arises if a party dealing with the object: (i) is the owner of the object; (ii) only transfers to the other party an interest not greater than its own; or (iii) if transferring an interest greater that its own, is authorized to do so. The right to dispose includes the power to dispose. For instance, where the owner grants a security interest to a secured creditor, it will have both the right and the power to dispose. But, in some circumstances, the power to dispose can exist without the right to dispose—that is to say, when the person dealing with the object is not the owner and has no authority to dispose of it but is still able to create a valid international interest. For instance, a lessee who is not the owner and lacks the authority (no right to dispose) may still have the power to dispose and create a valid international interest by granting a security interest. While the question of whether a person dealing with the object is its owner or has the authority to deal with it (right to dispose) is relatively straightforward, the question of whether a person who is neither the owner of the object nor has the authority to deal with it, can nevertheless transfer an interest greater than the one it holds to another person and create a valid international interest (power to dispose) is more difficult. For this reason, the article focuses on and examines the source and meaning of the power to dispose in the circumstances where it arises without the right to dispose.

This article contributes to legal scholarship by taking a distinct position that differs from both the Official Commentary and that thus far advanced by other commentators by arguing that the ‘power to dispose’ (where it arises without the right to dispose) is a matter governed by the Convention and the Convention’s general principles and provisions, as well as those of its protocols, are sufficient to develop the internationally uniform concept of power of dispose, autonomous from national law. On this basis, the article develops and proposes this newly constructed concept under the Convention.

In section I, this article starts by explaining the significance of power to dispose. Section II explores the relationship between this requirement and the Convention’s priority rules. Section III examines whether power to dispose should be governed by the Convention or be delegated to the applicable

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national law. Section IV constructs the contours of the power to dispose concept under the Convention and develops its individual elements. Section V analyses the viability of the proposed concept by testing it in the context of some typical factual scenarios. The conclusions are drawn in the final section of this article.

II. The significance of ‘power to dispose’ in the Convention’s scheme

1. An ‘international interest’

One of the Convention’s key features is the creation of an ‘international interest’ in mobile equipment, the concept autonomous from national law. This is a truly innovative concept because it overcomes the differences in the characterization of security interests in legal systems. While some jurisdictions characterize a conditional sale and some leases as security interests, others distinguish between the ‘true’ security interests and the interests of a conditional seller and lessor. The search for a uniform approach to the characterization proved impracticable and a solution had to be found to reflect the differences between these interests and subject them to the uniform legal regime where possible.

This is what the concept of an international interest has achieved. An international interest is a proprietary interest in mobile equipment that can be granted by a chargor under a security agreement, vested in a conditional seller under a title reservation agreement or vested in a lessor under a lease. Whether an interest is governed by the Convention at all must be determined in accordance with the Convention’s definitions of the lease, security, and title reservation agreements. Once it is established that the interest falls into one of these categories, it is for the applicable law to characterize it as the interest of a lessor, chargor, or a conditional seller. The characterization under the applicable law is required to determine which provisions of the Convention (such as the Convention’s remedial regime) are applicable to that international interest. Once constituted, an international interest can be enforced if the debtor defaults and, if registered in the IR, granted priority over unregistered and subsequently registered interests.


Commentary (n 8) 319.

Art 2(2) CTC. Art 2(4) CTC delegates the characterization of interests to the applicable law.

These terms are defined in Art 1(p); (hh); (kk) CTC.

Art 2(4) CTC. Commentary (n 8) 318.
2. **Formal requirements**

The Convention provides the formal requirements for the constitution of an international interest, which cannot be modified or added to by national law. Once formal requirements are complied with, a valid international interest comes into existence. An interest is constituted as an international interest where the agreement creating or providing for the interest: (i) is in writing; (ii) relates to the object of which the chargor, conditional seller, or lessor has power to dispose (PD); (iii) enables the object to be identified in conformity with the protocols; and (iv) in the case of a security agreement, enables the secured obligations to be determined but without the need to state a sum or maximum sum secured.\(^{16}\)

The Convention does not govern an outright sale of mobile equipment but two of its protocols, the Aircraft Protocol (AP) and Space Protocol (SP), extend the Convention’s regime to a sale of aircraft and space objects and render registrable the interest of buyers of such objects.\(^{17}\) The formal requirements for a sale contract mirror the Convention’s requirements for the constitution of an international interest.\(^{18}\) The contract of sale must relate to an aircraft or space object of which the seller has PD. In contrast, the Rail Protocol (RP) and Mining, Agriculture and Construction Protocol (MACP) do not govern the sale of the railway rolling stock and mining, agriculture, and construction (MAC) equipment. When the IRs for these types of equipment are established, it will only be possible to register a notice of sale of such objects.\(^{19}\) These notices can be useful in providing valuable information to the persons searching the IRs and, possibly, affect the issue of priority under domestic law, but notices of sale are ineffective under the Convention. Since the RP and MACP do not govern the sale of the relevant types of equipment, the question of whether the seller has PD does not arise under these protocols. However, a chargor, conditional seller, or lessor creating an international interest in the rail rolling stock and MAC objects must still satisfy the PD requirement.

The formal requirements are relatively simple, except for the PD requirement, the source and meaning of which are unclear. This uncertainty is highly undesirable due to the significance of this requirement. Unless the requirement of PD is satisfied, an international interest (or a contract of sale of aircraft or space objects) will not come into existence, its purported registration will be ineffective, its holder will not be able to assert priority, and it will lack validity if the debtor becomes insolvent. The purpose of this article is to evaluate the basis and meaning of PD under the Convention, to which the discussion now turns.

\(^{16}\) Art 7 CTC.
\(^{17}\) Art III AP and Art IV SP.
\(^{18}\) Art V AP and Art V SP.
\(^{19}\) Art XVII RP and Art XX MACP. On potential effects of a notice of sale under RP and MACP, see Gullifer (n 9) 115–20.
3. **The meaning of ‘power to dispose’**

Despite its significance, the Convention does not define the concept of ‘PD’. Some guidance on its meaning is given in the Commentary, explaining that the word ‘dispose’ is to be interpreted broadly to refer to every form of a consensual grant of a property interest.\(^{20}\) If the conferred interest is merely contractual, then a transaction does not amount to a ‘disposition’. The Commentary distinguishes between a *power* and a *right* to dispose.\(^{21}\) The latter exists where the transferor is either: (i) an unencumbered owner of the object; (ii) not an unencumbered owner, who transfers an interest not greater than the one it holds; or (iii) not an owner, who is authorized to transfer an interest greater than its own.\(^{22}\)

Examples of the exercise of the right to dispose include owners granting a security interest, leasing, or selling the object but are not limited to cases where the transferor is the owner. A transferor may be a conditional buyer or lessee, authorized by the owner to sub-lease or sell the object. The Convention and the protocols offer a wide range of remedies to the creditor if the debtor defaults. These remedies, which include taking possession, sale, and lease of the object, are enforceable on obtaining the debtor’s consent.\(^{23}\) By granting consent, the debtor confers on the creditor a right to dispose of the object enabling it to transfer an interest greater than its own.\(^{24}\) For instance, an enforcing secured creditor, whose interest in the object is less than ownership, can sell the object and transfer to the transferee the defaulting debtor’s absolute ownership. While the term ‘right to dispose’ is not used in the Convention, it seems clear that the requirement of PD is met where the right to dispose is present.\(^{25}\) This must be so because the Convention requires that it is the chargor, conditional seller, and lessor who must have PD. In most cases, the chargor will be the owner of the object. Similarly, the conditional seller or lessor may either be the owners or have the authority to deal with the object. In these cases, the chargor, conditional seller, and lessor will have both the right to dispose and PD.

At the same time, PD is wider than the right to dispose.\(^{26}\) PD allows the party, who is not the owner and/or does not have the authority to transfer an interest in the object, to transfer an interest greater than its own.\(^{27}\) As noted, when the

\(^{20}\) Commentary (n 8) 61.

\(^{21}\) Ibid, 327.


\(^{23}\) See, eg, Art 8, 9, 10 CTC and Art IX(1) AP.

\(^{24}\) Commentary (n 8) 62, 327–8.

\(^{25}\) This position is different from that adopted by: the UNCITRAL Model Law on Secured Transactions (2016) that requires the grantor of a security interest to have either the ‘right’ or the ‘power to encumber’ the object (Art 6(1) and (2)); and the US Uniform Commercial Code that distinguishes between the ‘right in the collateral’ and the ‘power to transfer’ rights in the collateral which must be present for the creation of an enforceable security interest (§ 9-203(b)).


\(^{27}\) Commentary (n 8) 327.
charger, conditional seller, and lessor are owners or are authorized to deal with the object, they will have not only PD but also the right to dispose. A more difficult question and the one on which this article focuses is whether these parties have PD when they do not own, or are unauthorized to deal with, the object.

For instance, it is unclear whether a conditional buyer or lessee wrongfully sub-leasing or reselling the object under a conditional sale (and therefore acting as a lessor or conditional seller) has PD, enabling them to create a valid international interest. Similarly, it is unclear whether a conditional buyer or lessee wrongfully granting a security interest (and therefore acting as a chargor who is not the owner and lacks authority) has PD that enables them to create a valid international interest.

For convenience and unless a distinction is required, this article will refer to: the chargor, conditional buyer, lessee, and seller of the aircraft and space objects—that is, the parties whose PD needs to be ascertained—as ‘debtor(s)’; the parties who granted the debtors their interests or who have a prior interest in the object—that is, the conditional seller, lessor, the secured creditor, and the first buyer of the aircraft and space objects—as ‘creditor(s)’; and the party, in whose favour the debtor creates an international interest or to whom the aircraft or space object is sold, as the ‘receiver’.28

III. PD and priority rules

According to the Commentary, it is implicit in the Convention’s priority rules that PD derives from the Convention and is not limited to the applicable law.30 Under Article 29(1) and Article 29(2)(a), the holder of a registered interest has priority over the unregistered or subsequently registered interest despite actual knowledge of such interest. If the chargor grants security interests to A, B, and C, and A fails to register, C registers first, and B registers second, then C will have priority over A and B despite C’s actual knowledge of their interests. Similarly, if a conditional buyer or lessee grants a security interest to a secured creditor who registers its interest ahead of the conditional seller or lessor, the secured creditor will have priority over the unregistered or subsequently registered interests of the conditional seller and lessor. In these scenarios, some

28 As noted, although the Convention does not govern a sale of mobile equipment, its regime is extended to a sale of aircraft and space objects under the AP and SP.


30 The Commentary’s position is that PD can arise either under the Convention or the applicable law. The Commentary explains that PD can arise under the applicable law as a result of exceptions to the rule of nemo dat quod non habet (one cannot give what one does not have) (see Commentary (n 8) 63). For the general discussion of nemo dat, see, eg, M Bridge, L Gullifer, G McMeel, K Low, The Law of Personal Property, 3rd edn (London, Sweet & Maxwell 2021) Ch 31; Gullifer (n 9) 98. The main statutory exceptions to nemo dat in English law can be found in ss 2 (mercantile agency), 8 (seller in possession), 9 (buyer in possession) Factors Act 1889; ss 24 (seller in possession), 25 (buyer in possession) Sale of Goods Act 1979 (SGA). For further discussion, see M Bridge, Personal Property Law, 4th edn (Oxford, Oxford University Press 2015) 209–24.
commentators suggest that if the debtor is not the owner and/or is unauthorized to transfer the interest to the receiver but the receiver obtains priority over the creditors’ prior interests, this must mean that the debtor had PD under the Convention.  

It has also been argued that Article 29(3)(b), providing that a buyer of an object acquires its interest in it free from an unregistered interest, implicitly indicates that PD derives from the Convention’s priority rules. For instance, if the debtor (conditional buyer or lessee) sells the object to the buyer, the latter will take free from the creditor’s (conditional seller or lessor) interest if it fails to register its interest. Since the debtor is not the owner and does not have the authority from the creditor to sell the object to the buyer, but the latter is able to take the object free from the creditor’s prior unregistered interest, this must mean that the debtor has PD under the CTC. Given that, in these examples, the debtor, not the owner, and without authority to dispose of the object, can create an international interest or sell the object to the receiver, and that this interest binds the prior creditor, it may seem that the CTC priority rules constitute the source from which PD under the CTC derives.

However, it is submitted that the priority rules can only be invoked if an international interest or sale is validly created in the first place. It is only when the debtor has PD that it will be able to create a valid international interest or sell the object. Absent PD, the international interest will not be validly created and its purported registration will be ineffective. The receiver, a holder of such an invalid international interest, will not be able to invoke the priority rules to gain priority over the creditor’s competing interest. While the priority rules can demonstrate how the priority disputes between competing interests can be settled, they cannot be used as the source and basis of PD under the CTC. PD must be acquired by the debtor independently from the priority rules.

IV. Should PD be governed by the Convention or national law?

The Convention says very little on PD in general and on PD where it does not overlap with the right to dispose, which gives rise to the question of whether the concept of PD is governed by, and has its legal basis in, the Convention or the applicable law. The starting point in answering this question is Article 5(1) of the CTC, which provides that its provisions must be interpreted in line with its international character and the need to promote uniformity and predictability in its application. The CTC has created the international regime for the

31 Commentary (n 8) 327, 387; Gullifer (n 9) 104–6.
32 Gullifer (n 9) 105.
33 For an argument that PD cannot be arise under Art 29(3)(b) CTC where the debtor sells the same object to two consecutive buyers and that in these circumstances PD (if any) must arise under the applicable law, see Gullifer (n 9) 105.
34 The requirement of uniform application and regard to their international character is a common feature of international private law conventions. See, eg, Art 7(1) of the Convention on
constitution of an international interest, which is a uniquely international concept created by the Convention, and autonomous from domestic legal systems. PD, being a critical element in constituting an international interest, must also be governed by the Convention. Doing so is necessary to promote the Convention’s international character, given the centrality and significance of the concept of an international interest to the Convention’s scheme, and to ensure a uniform interpretation of PD and, ultimately, of the notion of international interest. It is true that the characterization of interests is expressly delegated to the applicable law. However, once an interest is characterized as an interest of a secured creditor, conditional seller, or lessor, it is treated as an international interest subject to the Convention’s uniform regime. The requirements constituting an international interest are prescribed by the Convention and cannot be varied by national law. An international interest will come into existence even if compliance with these requirements does not suffice under domestic law. If the meaning of one of its formative requirements, including the PD requirement, is to be delegated to the applicable law, the integrity of the international interest as an internationally uniform concept will be undermined.

The international character of the PD concept under the Convention is further evident when it is contrasted with its counterparts in domestic legal systems, in which PD usually arises as a result of exceptions to nemo dat. The receiver’s protection is frequently limited to cases where it takes the interest in good faith and without notice of the transaction between the debtor and creditor. Under the Convention, in contrast, the receiver’s knowledge of the previous transaction is irrelevant and the priority between the creditor and the receiver depends on the order of registration of their interests. The Convention also substitutes the principle of good faith for predictability. The irrelevance of notice and the substitution of good faith for predictability are deliberate policy choices made under the Convention to minimize factual disputes and avoid uncertainty associated with these concepts. Interpreting PD under the CTC with reference to the domestic law concepts, such as good faith and notice, would go against the Convention’s structure, as it was intended by the drafters, its international character, and the need to promote uniformity in its application.


35 See section I.1.
36 Art 2(4) CTC; Commentary (n 8) 319.
38 See further n 34.
39 For the position in English law, see, eg, ss 24 and 25 SGA.
40 Art 29 CTC.
41 Art 5(1) CTC.
42 Commentary (n 8) 63.
Further, the Convention aims to reduce credit risks and promote asset-based financing of the types of equipment governed by it. The main risks faced by a creditor, which can affect the availability and cost of financing, include whether the creditor can be certain that its international interest in fact exists and can be protected and enforced. To alleviate these risks, the Convention’s requirements for the constitution of an international interest must be few in number and simple to satisfy. This will give the creditor confidence that if it complies with these formal requirements, its international interest will be validly created, its priority will be secured by registration, and, if needed, its international interest can be enforced. However, if the meaning of PD is to be derived from domestic law, this can unnecessarily and unjustifiably complicate the constitution of an international interest. The creditor would then have to ascertain the applicable rules of conflict of laws, the applicable law, and whether, under that law, the debtor has PD. These inquiries can be lengthy and produce uncertain results, increasing the risks for the creditor and the financing cost for the debtor, all of which goes against the Convention’s aims and its general principle of predictability.

On this basis, it is submitted that where PD does not overlap with the right to dispose, PD is a matter governed by the CTC, although not expressly settled by it. In this case, Article 5(2) requires the legal issues relating to PD and, specifically, its meaning to be constructed based on the Convention’s general principles. These include party autonomy, transparency, and predictability. Only if the issue cannot be settled in conformity with the Convention’s general principles, can it be delegated to the applicable law. At the same time, it is suggested that if PD does overlap with the right to dispose, the right to dispose can arise under either the applicable law or, in a specific case, the Convention. Where the debtor is the owner of or has the authority to deal with the object under the applicable law, it is submitted that the right to dispose will arise under the applicable law. This must be so because the Convention is not concerned with, and therefore does not govern, the issues of ownership and authority to deal with the object, except for a limited circumstance. This limited circumstance concerns a creditor’s ability to exercise its remedies under the Convention and the protocols, which is premised on obtaining the defaulting party’s consent (authority). In this limited case, the right to dispose will arise under the Convention and not the applicable law.

V. PD under the CTC: the proposed concept

1. General

This article proposes the following concept of PD under the CTC. Whenever the creditor, the owner of, or the holder of a lesser prior proprietary interest in
the object, consents to give possession of the object to the debtor, the debtor has PD and can create a valid international interest in favour of the receiver, a holder of a subsequent proprietary interest, in the way that can bind the creditor. For instance, if the debtor/lessee takes a lease of an aircraft object from the creditor/lessor and obtains possession of the object with the creditor’s consent, the debtor has PD. This means that the debtor can create a valid international interest or sell the aircraft object to the receiver and this disposition can bind the creditor. PD, based on the debtor’s possession obtained with the creditor’s consent, allows the debtor to transfer to the receiver an interest greater than the debtor’s. The notion of ‘possession’ must be broadly defined and include actual/physical and constructive possession, as explained below.

Although the debtor must be in possession to have PD, there should be no requirement that the debtor must transfer possession of the object to the receiver. Some jurisdictions require the transfer of possession for certain exceptions to nemo dat to apply, but there is no reason why such a requirement should be adopted under the Convention. Given the international nature of the transactions governed by the Convention and that the receiver, who may be a secured creditor or a buyer reselling the object, may not wish to take possession, this requirement would serve no useful purpose.

Depending on the agreement between the debtor and the receiver and on the order of registration of the interests held by the creditor and the receiver, the receiver’s interest can either subordinate the creditor’s prior interest or extinguish it. If the debtor/lessee takes a lease and possession of the object from the creditor/lessor and then grants a security interest to the receiver/secured creditor, the creditor’s prior interest can be subjected to the receiver’s subsequently created interest. In the case of an outright sale of an aircraft object by the seller to the second buyer/receiver, the first buyer/creditor’s proprietary interest can be ousted by the second buyer’s/receiver’s interest.

2. The requirement of ‘consent’

As noted, the first element in the proposed concept of PD should be that the creditor must consent to give possession of the object to the debtor. Although Article 7 of the CTC does not expressly state that the debtor’s PD is based on the creditor’s consent to give possession, it is argued that there are good reasons for this requirement.

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46 Provided that other formal requirements of Art 7 CTC or, in the case of an outright sale of aircraft and space objects, Art V(1) AP and Art V(1) SP are met.
47 Commentary (n 8) 63.
48 See, eg, ss 24 and 25 SGA.
49 Goode and Gullifer (n 26) 9.
50 Provided that the secured creditor registers its international interest ahead of the registration of the lessor’s interest in the IR (see Art 29(1) CTC).
51 Provided that the first buyer of the same object does not register its interest in it or registers its interest after the registration of the second buyer’s interest (see Art XIV AP).
52 The position is the same under Art V(1) AP and Art V(1) SP.
First, although PD is required to constitute an international interest, once this requirement is satisfied and an international interest is validly created, this interest can give rise to a priority dispute between the creditor (the holder of the previously created interest) and the receiver (the holder of the newly created international interest). For example, a lessee (debtor) can sell and transfer ownership of the aircraft object to the buyer (receiver) and, provided that the receiver registers its interest in the object ahead of the lessor (creditor), the receiver’s interest will oust the creditor’s interest.\(^{53}\)

This priority dispute, in turn, highlights the tension between two competing policies. On the one hand, the creditor’s interest requires protection because it is proprietary and first in time of creation. On the other hand, given the Convention’s aim to promote commerce and facilitate asset-based financing, it must be possible to dispose of an interest in the least cumbersome manner. The receiver should not be expected to make time and resource consuming inquiries as to the debtor’s entitlement to deal with the object. If the creditor’s interest is not registered in the IR and the debtor is in possession, the receiver should be able to rely on the debtor’s possession and the results of the search in the IR and not be expected to enquire further whether the debtor is the owner or is authorized to make the disposition.\(^{54}\) These two policies, of protecting property interests and facilitating asset-based financing, are equally important and the requirement of consent to give possession can balance them appropriately. If the debtor has PD, the creditor can lose its property interest. For this reason, the debtor should only have PD if the creditor consents to give possession of the object to the debtor.\(^{55}\) Furthermore, the creditor, who allows the debtor to remain in or take possession, must realize that the debtor can dispose of the object. This is why, if the debtor obtains possession with the creditor’s consent, it should be able to transfer a better title than it holds to the receiver.

Despite a potentially undesirable impact of the debtor’s disposition on the creditor’s interest, the creditor is best placed to control this impact by refusing to give possession or registering its interest in the IR. The debtor, who obtains possession without the creditor’s consent or lacks possession, should not have PD and not be able to create a valid international interest. Any purported disposition to the receiver and the registration of such an interest should be ineffective.

Second, the requirement of consent accords with the Convention’s principle of party autonomy. Contracting parties in high-value international transactions governed by the Convention are knowledgeable and experienced in such

\(^{53}\) Art XIV AP.

\(^{54}\) For example, a lessee in possession with the lessor’s consent can obtain finance by granting a charge over the leased object to a secured creditor, sub-lease it to a sub-lessee or sell it on a conditional sale basis or outright.

transactions and their agreements should be enforced. If the creditor consents to give possession to the debtor, it must realize that the debtor can dispose of the object. The debtor should then be able to create a valid international interest in the receiver’s favour that can bind the creditor.\(^{56}\)

Finally, the requirement of consent already exists in the Convention and its protocols. For instance, under the CTC a secured creditor’s remedies of taking possession, selling, or leasing the object are exercisable on obtaining the debtor’s consent.\(^{57}\) Similarly, the remedies under the protocols are available on obtaining the consent of the debtor and the holders of prior ranking registered interests.\(^{58}\) Since the availability of remedies is premised on securing consent, the enforcing creditor has the authority or the right to dispose of the object in a specific way. For instance, provided that the debtor agrees, the creditor can de-register and transfer an aircraft object from the territory where it is located.\(^{59}\)

As noted, PD overlaps with the right to dispose. But PD is broader because it allows the debtor to create a valid interest greater than its own, which can bind the creditor despite the lack of the creditor’s agreement. The difference between the right\(^{60}\) and power to dispose in relation to the nature of consent is this. In regard to the right to dispose, the nature of consent is specific, such as consent to taking possession, leasing, or selling the object. As to PD, the nature of consent is broad in that possession of the object must be held with the creditor’s consent. Once this broad consent to hold possession is acquired, the debtor obtains PD in various ways that are not authorized by, but may bind, the creditor. For example, if the lessee holds the object with the lessor’s consent, it has PD and can grant a sub-lease although it has no authority from the head lessor to do so and this disposition may bind the head lessor if it fails to register its interest in the IR. Since the Convention’s right to dispose is premised on obtaining consent to act in a specific manner, it is submitted that consent to give possession as the basis for PD constitutes a natural extension of the already existing concept of consent in the Convention.

3. **The requirement of ‘possession’\(^ {61}\)**

**A. Rationale**

The Convention does not expressly require the debtor to possess the object to have PD. The Commentary explains that the debtor in possession should have PD because it is best placed to deal with the object and create competing interests.\(^ {62}\)

\(^{56}\) As noted in section II, the priority between the creditor and the receiver depends on the order of registration of their interests in the IR.

\(^{57}\) Art 8(1) CTC.

\(^{58}\) Art IX (1), (2) AP; see also Art VII (1), (2) RP, Art VIII(1), (2) MACP and Art XIX SP.

\(^{59}\) Art IX(1), (2) AP.

\(^{60}\) At least when such a right to dispose arises under the CTC and the Protocols.


\(^{62}\) Commentary (n 8) 327.
It is for this reason, according to the Commentary, that the interests of a secured creditor, conditional seller, or lessor are registrable under the Convention.63 The ability to register their interests in the IR protects the secured creditor, conditional seller, and lessor against the competing interests, which can be created by the debtor in possession. Possession enables the debtor to appear as the owner of the object. By giving consent to the debtor’s possession, the creditor confers PD on the debtor.

A further justification for possession being the basis of PD can be advanced. The main function of PD is to enable the debtor to create an international interest, which is proprietary in nature. Accordingly, the debtor with PD should be able to create and transfer a proprietary interest. If possession held by a conditional buyer and lessee is proprietary, this must mean that as long as the conditional buyer/lessee hold on to possession, they have PD.64

It can be objected that since the conditional buyer cannot become the owner until all conditions, such as payment of the purchase price, are fulfilled and the lessee is not intended to become the owner of the object, their possession is not proprietary.65 Alternatively, it can be argued that the Convention’s reference to a conditional buyer’s ‘interest’ and a lessee’s ‘right’ must mean that while the conditional buyer’s possession is proprietary, the lessee’s possession is merely contractual. However, because the CTC treats conditional buyers and lessees in the same manner, both should be either proprietary or contractual. For instance, under Article 29(4)(b), if the conditional seller and lessor first register their interest and then grant a security interest to a secured creditor, who fails to register or registers its interest at a later stage, the conditional buyer and lessee will take free from the secured creditor’s unregistered or subsequently registered interest.

It is suggested that the conditional buyer’s and lessee’s possession under the Convention should be proprietary. One reason for this suggestion is that although the interests of the conditional buyer/lessee are not registrable, they can resist the claims of the conditional seller’s and lessor’s creditors if these creditors fail to register or register their interests after the conditional seller/lessor register their interests in the IR.66 The conditional buyer’s/lessee’s ability to resist a third party’s claims indicates that their possession must be proprietary. The second reason is that the protection of the conditional buyer/lessee in possession is strengthened by the regime of quiet possession available under all protocols.67 If there is no default, the conditional buyer/lessee is entitled to enjoy quiet possession and use of the object. This right is exercisable against their own creditor.

63 Ibid, 63.
65 Tettenborn (n 55) 174.
66 Art 29(4)(b) CTC.
67 Art XVI AP, Art XXV SP, Art XI RP and Art XIII MACP.
and against third parties, from whom the conditional buyer/lessee is protected under Article 29(4) of the CTC. The Aircraft Protocol further provides\(^\text{68}\) that the conditional buyer/lessee can even be entitled to quiet possession as against third parties to whom their interests are subjected under Article 29(4)(a) of the CTC.\(^\text{69}\) The regime of quiet possession is clearly premised on the fact of possession, the absence of which makes this protection unavailable to the conditional buyer/lessee. This regime strongly indicates the importance the CTC attaches to the conditional buyer’s/lessee’s possession and its proprietary nature. It follows that the conditional buyer/lessee in possession have PD under the CTC.

**B. Legal nature of possession**

(i) General

Once it is established that the debtor in possession has PD under the CTC, the next question concerns the nature of possession. The Convention does not define ‘possession’, although this term is mentioned in the CTC and its protocols. For instance, the Convention defines the leasing agreement as an agreement by which the lessor grants a right to possession to the lessee in return for rental payments\(^\text{70}\) and the creditors’ remedies include taking possession.\(^\text{71}\) All protocols provide for the regime of quiet possession for the conditional buyer and lessee. The Commentary explains that possession is to be understood broadly and to include actual/physical and constructive possession.\(^\text{72}\)

(ii) Broad interpretation of possession

The concept of possession is notoriously difficult to articulate and different definitions are given in various legal systems. In some civil law systems, possession requires a combination of two elements: factual possession of the object and an intention to hold it as the owner.\(^\text{73}\) Since this last element is absent in leases, the lessee is considered to be not in possession but in detention of the object.\(^\text{74}\) The rights of a lessee-detainer are not proprietary but contractual. In some common law systems, possession requires the combination of factual control of the object and the intention to exclude others from the exercise of control.\(^\text{75}\) Under this definition, the lessee does not merely detain the object but possesses it.\(^\text{76}\) The

\(^{68}\) Art XVI(1)(b) AP.

\(^{69}\) For instance, if the conditional seller or lessor grants a security interest to the secured creditor who registers its interest ahead of the registration of the conditional seller or lessor’s interest, the interests of the conditional buyer and lessee will be subjected to the secured creditor. However, the secured creditor may allow the conditional buyer and lessee to continue enjoying the use and quiet possession of the object.

\(^{70}\) Art 1(q) CTC.

\(^{71}\) Arts 8, 10, 13 CTC.

\(^{72}\) *Commentary* (n 8) 63.

\(^{73}\) Ibid, 27.

\(^{74}\) Ibid, 27.

\(^{75}\) *The Tubantia* [1924] P 78; *Young v Hichens* (1844) 6 QB 606.

\(^{76}\) Bridge (n 30), 33.
Commentary indicates that possession under the Convention must be interpreted broadly to cover both ‘possession’ as understood by the common law and ‘detention’ as viewed in some civil law systems. Given that the lessee and conditional buyer in possession can resist the claims of their own creditor and third parties under the Convention and its protocols, it is submitted that possession under the Convention should be proprietary.

(iii) ‘Actual’ and ‘constructive’ possession

Possession can be actual or constructive. The debtor is in actual possession when it has exclusive physical control of the object. The lessee or conditional buyer having physical control of the object in fact possesses it. The debtor constructively possesses the object when physical control of the object is held by another party but the debtor can control it by other means. For example, the object can be stored in a warehouse but the warehouse person holds it on debtor’s behalf, who possesses it constructively. The debtor can instruct the warehouse person to hold the object on the receiver’s behalf, thereby constructively delivering the object to the receiver. In this case, the object’s physical location does not change but the party holding constructive possession does.

As another example of constructive possession, consider S who sells the object to B1 who immediately leases the object back to S and then S sells the same object to B2. In this case, S remains in actual/physical possession of the object at the time of the sale and leaseback. Accordingly, it can be argued that S is in possession and has PD by selling it to B2. However, to grant the lease B1, as the new owner, must be able to transfer possession to S. For this to happen, S must constructively transfer possession to B1 under the sale. In other words, S now holds actual possession of the object as B1’s bailee and B1 holds constructive possession before granting the lease.

The requirement of debtor in possession as a prerequisite of PD is justified by the creditor (B1) having the opportunity to take delivery but allowing the debtor (S) to remain in possession, making the debtor appear as the owner. By allowing the debtor to remain in possession, actual or constructive, the creditor confers PD on it. To curtail the debtor’s ability to create a valid competing interest binding the creditor, the creditor must remove possession from the debtor. Devoid of possession, the debtor cannot appear as the owner or having the requisite authority to deal with the object.

77 Commentary (n 8) 27, 308.
78 Merrett (n 61) 383.
79 Eg, s 29(4) SGA; see also Re Atlantic Computers Ltd [1992] Ch 505 (CA). For a general discussion of constructive possession, see Bridge (n 30) 35–7.
80 This example is based on the facts of Michael Gerson (Leasing) Ltd v Wilkinson [2001] QB 514.
81 Under the AP and SP, the registration of the creditor’s (B1’s) interest will make this interest visible to the receiver (B2).
82 The right to dispose (where the debtor is the owner/authorized to deal with the object) can still arise under the applicable law.
But in a sale and leaseback arrangement, the object is constructively delivered to B1. Actual and constructive possession are merely different ways in which the object can be held and should be treated in the same manner.\textsuperscript{83} If so, and the object is constructively delivered to B1, will S holding actual possession of the object still have PD? The answer must be ‘yes’. First, although B1 constructively possesses the object, it is B1’s consent to grant the leaseback that entitles S to remain in possession. Second, the transfer of constructive possession to B1 under the sale will not be known to B2. Even if the object is physically delivered to B1 under the sale and redelivered back to S under the leaseback, this will not be known to B2. Seeing S in possession can make S appear as the owner of or having the authority to deal with the object. For this reason, it is submitted that, despite constructive delivery to B1 under the sale, S in possession with B1’s consent should have PD under the Convention.

This does not mean that B1 leaving S in possession has no means of protecting its interest. Although under the Convention B1’s interest is not registrable, in a sale and leaseback transaction B1 can register its international interest as a lessor. This registration will alert B2 that S may not be the owner or lack the requisite authority. It will then be up to B2 to inquire further from B1, at which point B2 will learn about B1’s ownership. Alternatively, if B2 decides to proceed with purchasing the object, its interest will be subjected to the earlier registered international interest of B1/lessor. B1’s failure to register as a lessor will leave it without protection and B2 will take free from its interest despite actual knowledge.\textsuperscript{84}

Treating possession obtained with the creditor’s consent as the necessary requirement of PD is in line with the Convention’s principles of transparency of the registration system and promotion of asset-based financing and leasing. Knowing that possession is the basis of PD that can bind it will encourage the creditor to proactively protect its interest by withholding possession (which will not be commercially practicable and hinder the circulation of valuable assets in commerce) and/or registering its interest in the IR. Since the IR is a transparent Internet-based system, searching and discovering the creditor’s previously registered interest is not unduly burdensome for the receiver. If the IR search does not reveal a prior registered interest and the debtor holds possession, these circumstances should suffice to convince the receiver that the debtor has PD under the Convention and can create a valid international interest. Possession as the

\textsuperscript{83} Merrett (n 61) 386–7.

\textsuperscript{84} This example involves a dispute between two innocent buyers from the same seller in possession but other examples can also be given. The debtor can be a conditional buyer/lessee taking possession of the object from the conditional seller/lessor and then selling the same object outright, on title reservation terms, sub-leasing or granting a security interest in it to a receiver. Alternatively, the debtor can be a chargor granting a security interest to the creditor and retaining possession who sells the object outright or on title reservation terms, leases or grants another security interest to a receiver. In all these cases, the debtor in possession has PD and can create a valid international interest or sale.
necessary element of the debtor’s PD and the receiver’s ability to search the IR speedily can considerably reduce the need, time, and cost of investigating the debtor’s title. This, in turn, can increase the receiver’s confidence and willingness to participate in the transaction offered by the debtor, which can promote asset-based financing.

VI. Testing the proposed concept of PD

1. General

There is little value in creating a valid international interest unless it can be effectively protected against competing interests and enforced if the debtor defaults. Although PD is a requirement for constituting an international interest, the proposed position that PD exists under the CTC where the debtor is in possession with the creditor’s consent is best tested under the Convention’s priority rules. The priority rules help demonstrate a range of potential disputes between competing interests and how they are likely to be resolved provided that the international interests are validly constituted.

Under Article 29(1) and (2), a holder of a registered interest has priority over unregistered and subsequently registered interests despite the holder’s actual knowledge of them. ‘Registered’ and ‘unregistered’ interests are terms defined by the Convention and are wider than an international interest. Accordingly, the first transaction between the creditor and the debtor can be any disposition that can be considered as a (subsequently) registered or unregistered interest. However, the second transaction between the debtor and the receiver must be one creating an international interest or the sale of an aircraft or space object. This is because PD is required to constitute an international interest and enable the seller to effectively sell the aircraft or space object.

It is now time to test the proposed concept of PD, based on the debtor’s possession, in the context of the priority rules. While it is not possible to identify all conceivable factual scenarios that can arise under the CTC priority rules, this article will test the proposed concept with reference to some of the most common situations. This exercise demonstrates that the proposed concept works well in these typical cases and shows how PD affects the operation of the Convention’s priority rules.

85 Art 1(bb) CTC.
86 Art 1 (ll) CTC.
87 ‘Registered interests’ are not confined to international interests and can include any interest registrable in the IR, such as a national interest or a non-consensual right or interest. See Art 1(bb) CTC.
88 Art 7 CTC.
89 Art V AP and Art V SP.
2. **Examples under Article 29(1) and (2)**

**Example 1**
The debtor grants a security interest to the secured creditor\(^{90}\) and then grants another security interest in the same object, or sells the object under a conditional sale, or grants a lease to the receiver. Following the first disposition to the secured creditor, the debtor is likely to remain in possession with the creditor’s consent, unless the security interest is possessory (which is rare in transactions governed by the Convention).\(^{91}\) Even if the security interest is possessory, the creditor can agree to possess constructively and grant actual/physical possession to the debtor to enable it to use the object. If the debtor is in possession with the creditor’s consent, the debtor has PD and can create the international interest in the receiver’s favour. The priority between the creditor and the receiver depends on the order of registration. The fact that the debtor has PD does not necessarily mean that the creditor’s interest will be postponed to that of the receiver. The creditor will only lose to the receiver if it fails to register or registers its interest after the receiver registers its own interest in the IR.

**Example 2**
The debtor buys the object from the creditor under a conditional sale and then grants a security interest or sells the object under a conditional sale, or leases the object to the receiver. Alternatively, the debtor takes the lease from the creditor and then grants a security interest, sells the object under a conditional sale, or subleases it to the receiver. If the debtor is in possession with the creditor’s consent, it has PD and can create a valid international interest in the receiver’s favour.

If the receiver’s interests are created before possession is transferred to the debtor, the international interest will not be validly created and its purported registration will be ineffective.\(^{92}\) Consequently, even if the creditor’s interest is registered after the registration of the receiver’s invalid interest, the creditor will retain its priority over the receiver. Similarly, if the creditor lawfully terminates its agreement with the debtor and takes possession, the debtor, who is out of possession, will not have PD enabling it to create a valid international interest.\(^{93}\)

\(^{90}\) If the first interest created by the debtor amounts to an international interest, the debtor must also have PD under Art 7 CTC.

\(^{91}\) For instance, in the case of a pledge under English law, where possession is transferred to the creditor/pledgee, PD based on the debtor’s possession and arising under the CTC cannot be established. However, the debtor/pledgor will retain ownership and therefore will have the right to dispose under the applicable law. Under the Convention, the order of priority between the creditor and the receiver will still depend on the order of registration.

\(^{92}\) Alternatively, it is possible to register a prospective international interest and once the necessary requirement(s) is (are) satisfied, the prospective interest will be converted into an actual international interest and the effectiveness of registration will date back to its registration as a prospective interest. So, if the only requirement for the conversion of the prospective interest into an actual one were that the debtor acquired PD, this requirement would be met once the debtor acquired possession. From this moment, the prospective interest will be converted into an actual interest.

\(^{93}\) *Commentary* (n 8) 63.
3. **Examples under Article 29(3)(a) and (b)**

**Example 1**

The Convention does not regulate an outright sale but Article 29(3) provides a special regime for buyers whose interests are not registrable in the IR. The rules in Article 29(3)(a) and (b) are an exception to the general rule that a registered interest takes priority over the subsequently registered and unregistered interest. Article 29(3)(a) provides that a buyer acquires its interest in the object subject to an interest registered at the time of acquisition. If the debtor grants a security interest to a secured creditor or takes a lease from a lessor, or buys from a conditional seller (creditors) and the creditor register its interest and the debtor then sells the object to the buyer (receiver), the receiver will take the object subject to the creditor’s registered interest. If at the time of sale to the receiver, the debtor is in possession with the creditor’s consent, it has PD and can create a valid interest. Accordingly, the receiver’s interest is valid but it is subjected to the creditor’s interest.

To take the object free of these interests, the receiver will have to discharge secured obligations, repay rental payments under the lease, or perform the conditions under the conditional sale. This is because the issues of PD and priority are separate. Even if PD is established and the international interest is validly created, the priority of competing interests is determined by the priority rules.

Under Article 29(3)(b), a buyer will take free from an unregistered interest (even if such interest cannot be registered) even if it has actual knowledge of it. If the debtor buys the object under a conditional sale or leases it from the lessor and the conditional seller or lessor do not register their interests and allow the debtor to remain in possession, the debtor will have PD. If the debtor sells the same object to the buyer, it will take free from the unregistered (or registered after the buyer acquires its interest) interest of the conditional seller or lessor despite the buyer’s actual knowledge of their existence.

This position under Article 29(3)(b) can be justified on the ground that the creditor could have taken possession of the object (if the interest is unregistered because it cannot be registered in the IR) or registered its interest in the IR before the object is acquired by the buyer. The fact that the buyer is protected despite its actual knowledge of the prior interest signals that the burden of protecting its interest must be on the creditor.

4. **Examples under the AP and SP**

The position of the AP and SP is different from that of the Convention (whereby interests of buyers are not registrable) in that the interests of B1 and B2 are rendered registrable and the priority between them depends on the order of

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94 Commentary (n 8) 312.
95 Art 1(II) CTC.
96 Art 29(3) CTC.
registration.\textsuperscript{97} If the seller of an aircraft/space object, sells it to B1 who fails to register (or registers after B2 registers its interest) and then sells the same object to B2 who registers its interest in the IR, B2’s interest would override B1’s ownership even if B2 was aware of B1’s existence at the time of acquisition.\textsuperscript{98} However, S’s PD under the protocols cannot derive from this priority rule. The priority rule under the protocols only becomes operative once it is established that S has PD, enabling it to create a valid interest.

S will have PD, if following the sale, B1 allows it to remain in possession of the object. In this case, S has PD and can sell the same object to B2, which can bind B1. Once PD is established, the priority rule can help determine which interest prevails. If B1 registers its interest first, B2 will lose. If B2 registers its interest ahead of B1, B1’s interest will be defeated.

\textbf{VII. Conclusion}

This article has demonstrated the centrality of the concept of an international interest to the Convention. Being an essential element in constituting an international instrument, the concept of PD plays an important role in the Convention’s regime. In the light of the existing uncertainty as to the basis and meaning of this concept and the divergence of views in relation to these issues, this article has taken a distinct stance by arguing that the PD concept (where it arises without the right to dispose) should be governed by the Convention, as is required by the Convention’s international character and the need to promote uniformity and predictability in its application. On this basis, the article has developed this concept based on the Convention’s framework, consisting of its aims and policies, general principles and specific provisions, including those in its protocols.

Specifically, it has been suggested that PD under the CTC should exist whenever the creditor consents to give possession of an object to the debtor, enabling the debtor to create a valid international interest, greater than the one held by the debtor, in the receiver’s favour. Possession must be understood broadly and include actual and constructive possession. While the debtor must be in possession, there should be no requirement of the transfer of possession to the receiver. The receiver’s ‘good faith’ and ‘notice’ should not form part of the PD concept under the Convention. To conclude, it is submitted that interpreting the PD concept under the CTC in this way will bring greater legal certainty as to the basis and meaning of PD than is currently the case. Doing so will also strike the optimum balance between two competing but equally important policies of protecting the creditor’s prior property interest, on the one hand, and promoting commerce and facilitating asset-based financing of mobile equipment, on the other.

\textsuperscript{97} Art XIV AP and Art XXIII SP.
\textsuperscript{98} Art XIV AP and Art XXIII SP.