The Space Assets Protocol One Year Later: An Update and Reassessment

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More than a year has passed since the UNIDROIT Space Assets Protocol to the Convention on International Interests in Mobile Equipment (CIIME) was opened for signature on March 9, 2012, at the Diplomatic Conference in Berlin. This first anniversary of its adoption affords an opportunity not only to provide an update on the ratification process, but also to take a second look at the Protocol’s substance. Although the Protocol was criticized during the drafting process for not sufficiently addressing the space industry’s concerns, the drafters produced a final version of the Protocol that responded to many points of criticism. These changes should assuage industry’s (and others’) concerns and encourage states to ratify the Protocol.

The Space Assets Protocol

The Space Assets Protocol is the third protocol to the CIIME to have been opened for signature since the Convention was adopted in 2001—the other two being the Aircraft Protocol and the Railway Rolling Stock Protocol, respectively. Briefly stated, the CIIME created an international legal regime governing security interests in (as well as leases and sales of) certain categories of high-value mobile equipment. The purpose of the Convention was to facilitate asset-backed financing by replacing the patchwork of inconsistent domestic laws with a uniform international system of priority rules and remedies. Although some countries, such as the United States and Australia, have adopted highly efficient secured transactions statutes, many jurisdictions around the world retain an approach to secured transactions that fails to incorporate the fundamental principles of efficient asset-backed finance such as (1) clear priority rules coupled with a publicly searchable registration system to clarify the priority positions of competing claimants, (2) the ability of a creditor to exercise remedies in the event of a debtor’s default without the need to seek a court order, and (3) the ability of a creditor to exercise remedies against a debtor’s assets even in the context of the debtor’s bankruptcy. Creating an international law of secured transactions with these features had been the goal of previous, unsuccessful efforts by UNCITRAL among others. UNIDROIT succeeded where others have failed by restricting the CIIME to a narrow band of collateral (thus reducing the range of affected industries) and due to strong industry support at critical junctures, particularly from the aircraft industry. UNIDROIT’s efforts resulted in a new international law of secured transactions that contains reliable remedies and a clear “first-to-file” priority rule. This priority rule relies on a single centralized online registry of “international interests” (i.e., security interests, lease interests, and the interests of a conditional seller under a title reservation agreement) that is indexed by asset and can be easily searched by prospective lenders or buyers to determine whether a particular asset, such as a passenger jet or a satellite, is subject to an existing interest that would have priority.

The CIIME is implemented through asset-specific protocols that contain provisions addressing the idiosyncratic nature of transactions involving aircraft, rolling stock, and space assets. For example, the method of identifying these assets for purposes of registering an international interest varies. Pursuant to the Aircraft Protocol, an aircraft is described by serial number, the name of the manufacturer, and its model designation, while other approaches are taken for the description of rolling stock and space assets. The Aircraft Protocol entered into force in 2006 and has been successful by multiple measures. It has been broadly ratified (with 51 states having deposited instruments of ratification so far) and has been widely utilized (with many thousands of international interests having been registered to date). The benefit of the Aircraft Protocol was concretely illustrated when the Export-Import Bank of the United States reduced by one-third its exposure fee on the export financing of certain commercial aircraft for buyers in states that are parties to the Convention. The Rolling Stock Protocol is still gaining momentum, having not yet received the four ratifications required for its entry into force. Although five states and the European Union have signed this Protocol, it has only been ratified by Luxembourg.

One year after having been opened for signature, the Space Assets Protocol has been signed by four states (Burkina Faso, Germany, Saudi Arabia, and Zimbabwe). Germany signed the Protocol on November 21, 2012, while the other three states signed the Protocol at
the Diplomatic Conference. No instruments of ratification have yet been deposited—and 10 are required for the Protocol to enter into force. If Germany’s signature is a first sign of European support for the Protocol, 10 ratifications may not be far off. The willingness of states to ratify the Protocol, however, has been hampered by sharp criticism leveled by members of the commercial space industry in the course of its drafting. This criticism was voiced in a letter that was delivered to the then-Deputy Secretary General of UNIDROIT, Martin Stanford, in advance of the Diplomatic Conference in Berlin and was signed by a number of satellite operators and manufacturers, launch service providers, insurers, and members of the financial community.

More detailed explanations of the industry’s concerns were provided previously in statements released by the Satellite Industry Association and the European Satellite Operators Association. These industry groups opposed the Protocol’s adoption on the grounds that existing methods of financing satellites were sufficient and that the Protocol would introduce a new layer of law that would create significant burdens on space actors while introducing greater uncertainty and risk into satellite finance.

Response to Criticism of the Protocol

To the extent that criticism of the Protocol arose from the substance of its provisions, the Protocol deserves a second look. Industry concerns arising from the substance of the Protocol were based on earlier drafts of the Protocol and many of these concerns were resolved in the Protocol’s final version. As described in the following paragraphs, comments submitted by industry representatives resulted in significant revision of provisions regarding (1) the salvage rights of insurers, (2) the financing of components, (3) the application of the Protocol to preexisting interests, (4) the method of describing space assets for purposes of registration, (5) the definition of “space asset,” and (6) the stay on remedies for public services.

Salvage Rights

In an early version of the Protocol, the inclusion of an insurer’s salvage rights within the scope of the Protocol caused serious concern in the industry because it afforded these rights priority over secured parties in a manner that was not consistent with current practice. This resulted from the Protocol’s treatment of salvage rights as if they were interests acquired by way of a sale. This enabled the interest to be registered and, as a result, gain priority over subsequently registered secured lenders. In addition, upon the discharge of a creditor’s debt by payment of insurance proceeds, the insurer would have been subrogated to any interest held by a creditor in the insured’s assets—once again potentially giving the insurer priority over other secured lenders. In a later iteration of the Protocol, salvage interests could not be registered, but salvage rights were still subject to the Protocol in that they would be deemed “unregistered interests” and, as such, would be subordinate to any registered international interests. Representatives of the insurance industry submitted comments during the final stage of the drafting process expressing their concern that an insurer would risk losing its properly vested salvage rights to a party that had registered an international interest in the same asset. In order to avoid the unintended negative consequences of bringing salvage rights within the scope of the Protocol, the drafters deleted these provisions and inserted a new article that made clear that the Protocol did not affect salvage rights existing under other applicable law.

Financing of Components

Members of the satellite industry also voiced concerns over a proposal made during the drafting process that would have effectively granted a right of quiet enjoyment to owners of, or creditors with security interests in, satellite components. The proposed provision concerned the exercise of remedies against a space asset that was physically linked to another space asset (such as transponders or hosted payloads that are integrated with a satellite). The proposed provision prohibited the exercise of any remedy against one space asset that would impair ownership rights in another space asset to which it was physically linked. The concern arose from the possibility that a creditor with a security interest in a satellite would be prevented from enforcing that security interest if the remedy would interfere with the operation of any components of the satellite (such as hosted payloads). It was feared that this impediment to pursuing remedies would deter the financing of satellites. The alternative approach recommended by the industry was to leave the issue of enforcing remedies with respect to linked assets to intercreditor agreements, as is current practice. The drafters ultimately adopted language that allowed for the use of intercreditor agreements to govern the financing of components. Although the default rule is that a remedy cannot be pursued if it impairs the operation of another space asset to which it is physically linked, this limitation only applies if the other space asset is subject to a previously registered interest. Moreover, the Protocol explicitly states that parties are free to agree otherwise, thus permitting such issues to be handled through intercreditor agreements.

The Protocol’s Application to Preexisting Interests

Another issue of concern to the satellite industry was the requirement under the draft Protocol that holders of preexisting interests in satellites register their interests to ensure their priority over interests registered after the Protocol enters into force. This not only
Another perceived flaw in the definition of “space asset” that persisted in the later versions of the Protocol was the requirement that an item be “capable of being individually owned, used or controlled” in order to qualify as a space asset. Critics viewed this requirement as being unnecessarily restrictive to the extent that certain components that might serve as valuable collateral would fall outside the scope of the Protocol if they were not individually controlled. This argument ultimately persuaded the drafters to omit this element from the final version of the definition of “space asset.”

Description of Space Assets

Because the registry of international interests will be indexed by asset, it is critical that assets be identified in a consistent manner to ensure that all registrations against a particular asset are discovered upon a search in the registry for that asset. Critics of the initial approach to this issue in the draft Protocol found fault with the proposal that the descriptors used to describe a space asset when the interest was registered prior to launch (which included the name of the manufacturer, the serial number, and the model number) were different than the descriptors to be used to describe a space asset when the interest was registered post-launch (which included the name of the manufacturer, the launch site, and the launch provider). It was feared that this bifurcated approach to describing assets would result in confusion that might place a creditor’s priority in jeopardy. Responding to this concern, the drafters abandoned this approach. Although the method of describing a space asset under the final version of the Protocol will vary depending on the type of asset (because assets of different types will have different identifying marks or features), the method of describing a particular type of asset will be consistent and will no longer change depending on whether the interest was registered pre-launch or post-launch.

The original definition of what constituted a “space asset” that would be subject to the Protocol also drew criticism for a number of reasons and, in response to this criticism, the definition underwent multiple iterations. One such concern related to the original requirement that an asset be either “in space or intended to be launched into space” in order to qualify as a “space asset.” Some industry participants considered this to be an impossibly vague criterion because it would be difficult to ascertain the existence of such intentions (or to document exactly when such intentions arose). In order to address this concern, the drafters changed “intended to be launched into space” to “designed to be launched into space.” Although the question of whether or not an item has been designed for use in space may be debatable in some cases, the special design requirements of an asset that will survive the space environment (such as ruggedization) make this criterion a substantial improvement over the more nebulous question of intention.

Stay on Remedies for Public Services

Finally, concerns were voiced regarding the limitation placed on a creditor’s enforcement of remedies when a space asset is being used for the provision of public services. Early in the drafting process, there was general agreement among government representatives that it was necessary to include a “public services limitation” in order to protect against the interruption of vital public services that rely on satellite data, such as air-traffic control systems and natural disaster warning systems. A similar limitation was included in the Rolling Stock Protocol. In its early incarnation, this limitation was drafted broadly to allow a state to impose any limitations it wished on the exercise of remedies with respect to assets involved in the provision of public services. Not surprisingly, this created consternation due to the open-ended nature of the limitation. In order to strike a proper balance between the need to protect the public interest while not eviscerating a creditor’s remedies, the public services limitation evolved into a final version that set a number of limits on the use of this stay on remedies and provided other features that were intended to minimize the economic impact on the creditor. First, the stay applies only to those remedies that would interrupt the provision of certain public services with respect to which the state had registered a “public service notice” on the Protocol registry. This means that, upon default, a creditor, for example, would still be permitted to collect any income streams flowing from a satellite because this remedy would not interfere with the provision of a public service. In addition, if the public service provider defaults on its obligations to the debtor (e.g., by failing to make a transponder lease payment), the stay is immediately lifted so that the creditor may pursue the entire range of remedies. Second, the stay on remedies is limited to a maximum duration of six months (and could be briefer if so declared by the relevant state). Third, the stay generally does not apply to the enforcement of those international interests registered prior to the debtor entering into an agreement to provide public services (provided that the creditor had no knowledge of any such agreement when registering its interest).

Finally, the debtor must agree to the registration of a

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public service notice—something which the creditor could prohibit the debtor from doing in its security agreement in order to gain some additional protection against the stay.33 Taken together, these multiple controls on the public services limitation reduce the burden on creditors to a reasonable degree, while still meeting the public interest needs of contracting states.

Conclusion
Although some grounds for opposing the ratification of the Protocol may persist, the final version of the Protocol alleviates many industry concerns and therefore deserves a second look from its critics. States should take the changes made in the final drafting stages into account when assessing whether the Protocol’s potential benefits now outweigh any potential costs and risks. This assessment should be undertaken with a view to the future. Although established space companies may not see a pressing need for a new international law for financing their space assets, the needs of new market entrants in the coming years (as well as the needs of governments that may increasingly need to take advantage of private financing mechanisms) should be considered. The opportunity to create an international law of secured transactions for the space industry may not present itself again. We should think twice before letting this opportunity pass.

Endnotes
5. CIIME, supra note 1, at art. 29(1).
6. Id. at arts. 16, 22(1).
7. Aircraft Protocol, supra note 2, at art. XX(1).
9. Id.
12. Id.
14. Id.
15. Space Assets Protocol, supra note 1, at art. XXXVIII(1)(a).
19. CIIME, supra note 1, at art. 29(1).
22. This requirement to register preexisting interests resulted from the absence of any carve-out of existing interests. If preexisting interests were not carved out, the
requirement of registration in order to preserve priority would have applied to existing interests just as it applies to interests created after the Protocol goes into effect.

23. Space Assets Protocol, supra note 1, at art. XL(2).


27. Space Assets Protocol, supra note 1, at art. I(2)(k).


29. Rolling Stock Protocol, supra note 3, at art. XXV.

30. Space Assets Protocol, supra note 1, at art. XXVII(3).

31. Id. at art. XXVII(4).

32. Id. at art. XXVII(9).

33. Id. at art. XXVII(1).