

# The Contours of 'Commercial Reasonableness' under the Cape Town Convention

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## Abstract

*Within the uniform legal regime introduced by the Cape Town Convention, a central role is played by the detailed set of remedies put at the disposal of creditors to enforce their rights in the case of debtor's default and insolvency. While the whole purpose of this part of the uniform law regime is to facilitate efficient and speedy recovery by creditors, some provisions tailored to the protection of debtors and third parties were introduced. The aim of this article is to specifically focus on one of them, namely that creditors shall exercise remedies in a 'commercially reasonable manner'. Reference to this general parameter as an ex post control of creditor's enforcement measures is consistent with modern principles of secured transactions law. This article, however, supports the view that in the light of the language of the instrument as well as the uniform law's own goals and principles, the term 'commercial reasonableness' within the Cape Town Convention should be interpreted autonomously, taking into account the contractual agreement and the market practice for the financing of the specific high value assets covered by the treaty.*

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## I. Introduction and aim of this article

Within the uniform legal regime introduced by the Cape Town Convention and its protocols,<sup>1</sup> a central role is undoubtedly played by the detailed set of remedies put at the disposal of secured creditors,

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<sup>1</sup> 2001 Convention on International Interests in Mobile Equipment ('Cape Town Convention', 'Convention'); 2001 Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment ('Aircraft Protocol', 'AP'); 2007 Luxembourg Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Railway Rolling Stock ('Rail Protocol', 'RP'); 2012 Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Space Assets ('Space Protocol', 'SP'); draft Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Mining, Agricultural and Construction Equipment reproduced in UNIDROIT, *Study 72k - CGE1 - DC - Doc. 3* (2018) <[www.unidroit.org/english/documents/2018/study72k/dc/s-72k-dc-03-e.pdf](http://www.unidroit.org/english/documents/2018/study72k/dc/s-72k-dc-03-e.pdf)> accessed 27 March 2019 ('MAC Protocol'). In this article, the AP, RP, SP and the MAC Protocol are jointly referred to as the 'Protocols' (and each individually, a 'Protocol'). The entire treaty system established by the Convention and its Protocols is referred to as 'CTC'. The texts of the Convention and its Protocols are available on the UNIDROIT website at UNIDROIT, 'UNIDROIT Work and Instruments in the Area of Secured Transactions' <<https://unidroit.org/secured-transactions>> accessed 26 March 2019.

conditional sellers and lessors that created (and registered)<sup>2</sup> an international interest, to protect and enforce their rights in the case of debtor's default and insolvency. Such remedies fulfil the primary goal of the CTC, namely, to facilitate efficient (international) asset-based financing of specific high value equipment and enhance certainty and predictability in these transactions. This requires a remedial system that guarantees prompt and adequate enforcement of creditor's rights.<sup>3</sup>

It should be underlined that strong and effective creditor's enforcement rights do not exclusively function in the creditor's interest. Ultimately, they benefit all parties to financing transactions since they bear a direct influence on the cost of credit, and in some circumstances – especially considering developing countries – may determine whether financing is available at all.<sup>4</sup>

In the part on enforcement of creditors' rights, the Convention and the Protocols also contain provisions tailored to the protection of debtor and third parties. The aim of this article is to specifically focus on one of them, namely a duty of creditors to exercise remedies in a 'commercially reasonable manner'.<sup>5</sup> Reference to a general parameter of 'commercial reasonableness' as an ex post control of creditor's enforcement measures is consistent with modern principles of secured transactions law, and goes hand in hand with the trend towards strengthening party autonomy, reducing excessive formality and allowing more flexibility and efficiency generally, and particularly in enforcement.<sup>6</sup> This parameter is often found alongside other safeguards for the debtor and interested third parties, such as reasonable prior notice of the intention to exercise an out-of-court remedy to qualified persons and rules for the distribution of any surplus deriving from the liquidation of the value of the collateral.<sup>7</sup> In the present article, however, I will support the view that in the light of the conventional language as well as the uniform law's own goals and principles, the term 'commercial reasonableness' within the CTC should be interpreted autonomously, taking into account the contractual agreement

<sup>2</sup> Whilst registration is required to exercise said rights when qualified third parties are involved and in insolvency, the creation of an international interest is sufficient to trigger the application of the rules on enforcement. See Roy Goode, *Convention on International Interests in Mobile Equipment and Protocol Thereto on Matters Specific to Aircraft Equipment: Official Commentary* (4<sup>th</sup> edn, UNIDROIT 2019) para 2.100.

<sup>3</sup> 'The availability of adequate and readily enforceable default remedies is of crucial importance to the creditor, who must be able to predict with confidence its ability to exercise a default remedy expeditiously'. *ibid.*

<sup>4</sup> As further evidence of the centrality of the provisions on remedies we can refer to the experience in aviation finance, where the beneficial effects of the Aircraft Protocol's enhanced default and insolvency provisions on the cost of credit are concretely measurable. For example, under the OECD umbrella, a reduced fee or interest rate for export credit may be applied if a contracting state to both the Convention and the Aircraft Protocol has made 'qualifying declarations', which include the opt-in declarations in respect of enforcement measures. See Organisation for Economic Co-operation and Development (OECD), *Sector Understanding on Export Credits for Civil Aircraft* (2011). See also Vadim Linetsky, 'Economic Benefits of the Cape Town Treaty' (2009) <[www.awg.aero/assets/docs/economicbenefitsofCapeTown.pdf](http://www.awg.aero/assets/docs/economicbenefitsofCapeTown.pdf)> accessed 26 March 2019. See more generally Jeffrey Wool, 'Treaty Design, Implementation, and Compliance Benchmarking Economic Benefit: A Framework as Applied to the Cape Town Convention' (2012) 17 *Unif L Rev* 633.

<sup>5</sup> Article 8(3) of the Convention as modified by Article IX(3) of the AP, Article VII(3) of the RP and Article XVII(1) of the SP. See also the identical provision in Article VIII(3) of the draft MAC Protocol.

<sup>6</sup> See UNCITRAL, *UNCITRAL Legislative Guide on Secured Transactions* (2007) ('UNCITRAL Legislative Guide'), Recommendation 131; UNCITRAL, *UNCITRAL Model Law on Secured Transactions* (2016) ('UNCITRAL Model Law'), Article 4. See also n 42.

<sup>7</sup> See, eg, UNCITRAL, *UNCITRAL Model Law*, Articles 77(2)(3); 78(4)-(8); 79(c)-(d). For more guidance on the latter's provisions, see *UNCITRAL Model Law on Secured Transactions – Guide to Enactment* (2017) ('UNCITRAL Guide to Enactment'), paras 440ff; 446ff; 451ff <[http://www.uncitral.org/pdf/english/texts/security/MLST\\_Guide\\_to\\_enactment\\_E.pdf](http://www.uncitral.org/pdf/english/texts/security/MLST_Guide_to_enactment_E.pdf)> accessed 27 March 2019.

and the market practice for the financing of the specific high value assets covered by the Convention.<sup>8</sup>

## II. Remedies under the CTC: a brief overview and underlying principles

The CTC sets out detailed provisions regulating default remedies, which are crucial to its effective operation.<sup>9</sup> This section offers, with no attempt at completeness, an overview to highlight the principles underlying enforcement under the uniform legal regime established by the Convention.<sup>10</sup> As a consequence of the two-tiered structure of the CTC, remedies are covered both in the Convention and in the Protocols. The Convention lays out a set of basic remedies available to the creditor, triggered by debtor's default. Article 8 makes available to the chargee (that is the creditor under a security agreement),<sup>11</sup> if the chargor has at any time so agreed,<sup>12</sup> a set of remedies that may be alternatively exercised out-of-court or by applying for a court order authorizing or directing them (subject to the mandatory declaration of contracting states contained in Article 54(2) of the Convention that determines whether remedies under the CTC can be exercised by self-help or require leave of the court<sup>13</sup>): take possession or control of the charged object, sell or grant a lease over it, as well as collect or receive any income or profits arising from the management of it.<sup>14</sup> In relation to these remedies, the Convention introduces several safeguards for the debtor and interested third parties. In addition to the requirement of commercial reasonableness, it also mandates the creditor to give reasonable prior notice in the case of a proposed sale or lease to qualified persons including the debtor, and it dictates rules for the distribution of any surplus.<sup>15</sup> Another remedy available to the chargee is the vesting of the object in satisfaction (appropriation), regulated in Article 9 of the Convention with additional rules to protect chargor's and third parties' interests. Conditional sellers and lessors, on the other hand, may, according to Article 10 of the Convention, terminate the agreement and take possession or control of the charged object (or apply for a court order authorising or directing the same, subject to a contracting state's declaration under Article 54(2)). Furthermore, the Convention contains a key provision on 'relief pending final determination', which allows creditors to obtain from a court speedy advance relief subject to certain requirements.<sup>16</sup> Finally, the CTC does not preclude

<sup>8</sup> 'Commercial reasonableness is based on an autonomous Convention interpretation, not on the concept of commercial reasonableness in any particular national legal system, so that in a Contracting State the exercise of a remedy which meets the Convention test of reasonableness cannot be struck down because of a more stringent test under national law.' Goode (n 2) para 2.112.

<sup>9</sup> Antony Saunders and others, 'The Economic Implications of International Secured Transactions Law Reform: A Case Study' 20 U Pa J Int'l Econ L (1999), 309ff.

<sup>10</sup> For more details see Goode (n 2) para 2.100ff.

<sup>11</sup> cf the definition of 'security agreement' as an agreement between a chargor (the grantor of the interest) and a chargee (the grantee) in Article 1(ii) of the Convention and the broader definition of 'creditor' in Article 1(i), which states that "creditor" means a chargee under a security agreement, a conditional seller under a title reservation agreement or a lessor under a leasing agreement.

<sup>12</sup> This agreement is not subject to formalities, and it may be satisfied by a general reference in the contract to 'all remedies under the Convention'. See Goode (n 2) para 2.101.

<sup>13</sup> More precisely, under Article 54(2) of the Convention contracting states are required to declare whether or not any remedy available to the creditor under any provision of the CTC which is not there expressed to require application to the court may be exercised only with leave of the court.

<sup>14</sup> Article 8(1) of the Convention.

<sup>15</sup> See Article 8(3)-(6) of the Convention.

<sup>16</sup> Article 13 of the Convention. A creditor can obtain an order towards (i) preservation of the object and its value; (ii) granting the creditor possession, control or custody of the object; (iii) immobilisation of the object or (iv) lease or management of the object and the income therefrom. States may introduce modifications in the regulation of advance relief by way of opting into the provisions in the Protocols enhancing creditors' rights. See n 18.

the use of any additional (eg contractual) remedies that may be permitted by the applicable law but allows creditors to exercise them if the creditors are entitled to do so, provided such remedies are consistent with the mandatory provisions of the Convention (the latter include, among others, the standard of commercial reasonableness).<sup>17</sup>

The Protocols introduce a few important modifications to the Convention enforcement rules (including, as we will see, the provision on 'commercial reasonableness'). They further allow contracting states to opt into additional provisions which generally aim at ensuring greater confidence and predictability of the outcome by strengthening creditor's rights (such as, for example, a more effective regulation of relief pending final determination and specific provisions on insolvency).<sup>18</sup> The Protocols also add certain equipment-specific remedies (such as, for example, the right of the creditor to procure the de-registration and the export and physical transfer of the aircraft object under the Aircraft Protocol).<sup>19</sup>

This brief overview was given to highlight some of the fundamental principles underpinning the CTC rules on enforcement. One of the most important among them is the prominence of parties' agreement.<sup>20</sup> The CTC fundamentally respects contractual self-regulation. Most of the provisions in the Convention take the form of rules from which parties to a financing transaction can derogate. Parties have an ample possibility to choose from and/or modify the basic set of Convention's remedies, except as regards a few mandatory rules, which include, in fact, the requirement of commercial reasonableness. As we will see in section V, however, the contract plays a pivotal role in shaping the commercial reasonableness requirement notwithstanding the characterisation of the rule as mandatory. Another important principle is predictability,<sup>21</sup> which entails that creditors' rights should be promptly and adequately protected and enforced upon debtor's default. The emphasis throughout the Convention's regime is on effective enforcement, even if always within the framework of the contracting states' prerogative to make declarations under the Convention and the Protocols affecting, *inter alia*, creditor's remedies (either limiting or enhancing them).

### III. 'Commercial reasonableness' in the Convention and in the Protocols

According to Article 8 of the Convention, which applies specifically to the chargee,<sup>22</sup> the remedies listed in its first paragraph, as well as in Article 13, shall be exercised by the chargee 'in a commercially reasonable manner'. Thus, the Convention applies this standard to the creditor under a security agreement only, when it has the right to specified post-default remedies listed in the Convention (taking of possession or control; selling or granting of a lease; collecting or receiving any income or profit arising from the management of the collateral), irrespective of whether they are exercised as self-help or under a court order authorising or directing them. The Convention further extends this standard to the advance relief measures that may be obtained by creditors during court proceedings

<sup>17</sup> Article 12 of the Convention.

<sup>18</sup> See, for example, Articles X and XI of the AP.

<sup>19</sup> Article IX(1) of the AP.

<sup>20</sup> As stated in the Preamble to the Convention. See also Goode (n 2) para 2.23 (citing the following among the general principles underpinning the CTC: 'Party autonomy in contractual relationships, reflecting the fact that parties to a high-value cross-border transaction in equipment of the kind covered by the Convention will be knowledgeable and experienced in such transactions and expertly represented, so that in general their agreements should be respected and enforced').

<sup>21</sup> See Article 5(1) of the Convention (on the interpretation of the CTC).

<sup>22</sup> See n 10 and the accompanying text.

under Article 13 of the Convention.<sup>23</sup> While the language of the Convention is not entirely clear, the placing of the reference to commercial reasonableness within Article 8 seems to indicate that it would apply to advance relief only when exercised by a chargee, notwithstanding the more general scope of application of Article 13. In any event, a discussion on this first sentence of Article 8(3) of the Convention is largely theoretical, since this provision represents one of the instances where all Protocols override the Convention in a consistent manner: following the lead of the Aircraft Protocol in its Article IX(3), the Rail, the Space and the draft MAC Protocols all derogate from Article 8(3) by substituting it with a provision whereby 'any remedy given by the Convention in relation to' the objects covered by the relevant Protocol shall be exercised in a commercially reasonable manner.<sup>24</sup> As it is well known, the Convention only applies to equipment in connection with a corresponding Protocol, the provisions of which prevail over the ones of the Convention.<sup>25</sup> In the light of a consistent pattern of derogating from the Convention on this point, it is unlikely that drafters of future protocols to the Convention would revert to the original text or introduce an alternative wording, unless there were compelling reasons to do so on the basis of the type of equipment covered by such future protocols and the characteristics of financing of such equipment coupled with a strong backing of the relevant industry.<sup>26</sup>

Thus, under the operational rule of the CTC any remedy given by the Convention to the creditor is to be exercised in accordance with the standard in question, including remedies of conditional sellers and lessors,<sup>27</sup> though the more usual instances of application of the standard will be the ones connected with the exercise of the remedies of repossession and sale of the equipment by the creditor.<sup>28</sup>

Concerning the meaning of the term 'commercial reasonableness', however, the Convention and Protocols contain the same guidance (repeated verbatim) that 'a remedy shall be deemed to be exercised in a commercially reasonable manner where it is exercised in conformity with a provision of the security agreement except where such provision is manifestly unreasonable.'<sup>29</sup> As we will see, this express language sets apart the CTC from most national legal systems, as well as international instruments, which adopt, in one way or another, the standard of commercial reasonableness in the field of secured transactions. It is therefore crucial in interpreting the meaning of the provision in an autonomous manner and in narrowing down the discretion of interpreters of this open-ended concept as applied within the CTC.

#### **IV. The standard of 'commercial reasonableness' in national secured transactions laws and in harmonisation instruments**

It has already been mentioned that the test of 'commercial reasonableness' of creditor's behaviour (also) in enforcement is not exclusive to the CTC but appears, in one way or the other, in a number

<sup>23</sup> Under Article 13(2), courts may impose additional terms considered necessary to protect the interested persons should the creditor breach any of its obligations under the CTC or fail to establish its claim on the final determination of such claim. The application of Article 8(3), however, is expressly safeguarded in Article 13(4).

<sup>24</sup> Article IX(3) of the AP; Article VII(3) of the RP; Article XVII(1) of the SP; Article VIII(3) of the draft MAC Protocol.

<sup>25</sup> Articles 49 and 6 of the Convention.

<sup>26</sup> For more general considerations along this line regarding the MAC Protocol, see Charles Mooney, Marek Dubovec and William Brydie-Watson, 'The Mining, Agricultural and Construction Equipment Protocol to the Cape Town Convention Project: The Current Status' (2016) 21 *Unif L Rev* 332.

<sup>27</sup> See Article 10 of the Convention (covering termination and taking possession or control of the object).

<sup>28</sup> As highlighted by Sanam Saidova. See Sanam Saidova, 'The Cape Town Convention: Repossession and Sale of Charged Aircraft Objects in a Commercially Reasonable Manner' [2013] *LMCLQ* 180, 182.

<sup>29</sup> Article 8(3) of the Convention; Article IX(3) of the AP; Article VII(3) of the RP; Article XVII(1) of the SP; Article VIII(3) of the draft MAC Protocol.

of modern systems of secured transactions law. Taking into account the specific aim and the limits of this article, I will only refer to some examples of the formulation and interpretation of this standard in national laws and in harmonisation instruments.<sup>30</sup> In particular, this parameter is found in the US Uniform Commercial Code (UCC)<sup>31</sup> and those legislations that adapted its model, such as the personal property security acts (PPSA) adopted in Canada,<sup>32</sup> New Zealand<sup>33</sup> and Australia<sup>34</sup>. It is also included, again with some nuances, in international instruments aiming at offering a blueprint for domestic law modernisation and reform in the area of secured transactions, such as the UNCITRAL Legislative Guide and the UNCITRAL Model Law.<sup>35</sup>

As regards its application in enforcement, it is possible to detect an underlying policy common to those national legislations that expressly rely on the standard of commercial reasonableness. One of the perceived drawbacks of the rigid approach to enforcement still found in many domestic secured transactions laws is that, by way of balancing creditors' interests with the need to offer sufficient protection to debtors and third parties, they traditionally limit party autonomy *ex ante* and impose burdensome and lengthy procedural requirements. This runs against the goal of achieving a predictable, less costly and timely realisation of security rights, and represents the weakest and least efficient feature of such systems.<sup>36</sup> On the contrary, a more modern approach leaves greater room for parties' choices in their contractual agreement as to methods and manner of enforcement of creditor's rights, reduces formalities and provides short procedural timeframes overall, including in judicially authorised proceedings. In this context, rules protecting not only debtors but also qualified third parties (such as competing creditors) from abuse, are not absent. There are other mechanisms that can fulfil this balancing function, such as reliance on parties' agreement (the exercise of specific remedies may be subject to the contract expressly allowing them and sometimes to additional limitations and conditions); transparency provisions introducing information duties towards the debtor and qualified third parties; upholding the traditional principle of avoiding creditor's enrichment; and, last but not

<sup>30</sup> Thus, I will not address the specialised international instruments in the field of financial collateral, which refer to the parameter of 'commercial reasonableness' in relation to domestic law. These include harmonisation instruments, such as the EU Financial Collateral Directive (Directive 2002/47/EC of 6 June 2002 on Financial Collateral Arrangements [2002] L168/43, as amended by Directive 2009/44/EC [2009] OJ L146/37 and Directive 2014/59/EU [2014] OJ L173/190), which leaves the matter to national law: see Article 4(6) according to which there shall be no prejudice 'to any requirements under national law to the effect that the realisation or valuation of financial collateral and the calculation of the relevant financial obligations must be conducted in a commercially reasonable manner'. See also Michele Graziadei, 'Financial Collateral Arrangements: Directive 2002/47/EC and the Many Faces of Reasonableness' (2012) 17 Unif L Rev 497; Laura M Franciosi, 'Commercial Reasonableness in Financial Collateral Contracts: A Comparative Overview' (2012) 17 Unif L Rev 483. For a similar approach see the most recent 2017 UNIDROIT Legislative Guide on Intermediated Securities, which, in implementing the 2012 UNIDROIT Convention on Substantive Rules for Intermediated Securities (Geneva Securities Convention), underlines that 'the concept of commercial reasonableness is key where securities need to be valued, notably in the context of enforcement', but specifies that it is 'up to the domestic lawmaker to determine whether a specification of this content is necessary in the context of securities markets'. See UNIDROIT, 'UNIDROIT Legislative Guide on Intermediated Securities' (2017) para 287 <[www.unidroit.org/instruments/capital-markets/legislative-guide](http://www.unidroit.org/instruments/capital-markets/legislative-guide)> accessed 27 March 2019.

<sup>31</sup> The general provision is now in UCC § 9-610 (b). See n 37 below.

<sup>32</sup> See, eg, Personal Property Security Act, R.S.O. 1990, c. P.10 ('Ontario PPSA'), s 63(2); The Personal Property Security Act 1993 ('Saskatchewan PPSA'), s 65(3). See also nn 38 and 40 and the accompanying text.

<sup>33</sup> Personal Property Securities Act 1999, No 126, 1999 ('New Zealand PPSA'), s 25(1). See also n 40 below.

<sup>34</sup> Personal Property Securities Act 2009, No. 130, 2009 ('Australian PPSA'), s 111. See also n 38 below.

<sup>35</sup> See n 6 above.

<sup>36</sup> On this point, with particular regard to the comparison between the CTC regime and national secured transactions laws, see Souchirou Kozuka, 'The Cape Town Convention and its Implementation in Domestic Law: Between Tradition and Innovation' in Souchirou Kozuka (ed), *Implementing the Cape Town Convention and the Domestic Laws on Secured Transactions* (Springer 2017) 18ff; 22ff.

least, the use of an ex post evaluation of the exercise of enforcement rights on the basis of a general flexible standard, such as the one of commercial reasonableness. The latter, when present, is a typical statutory 'variable provision', the meaning of which is not only determined by judicial interpretation, but is basically dependent on a factual assessment and on the concrete circumstances of the case. This is particularly true when the legislative provision lacks more precise guidance for the interpreter.

While the general policy underlying the reliance on the standard of commercial reasonableness in enforcement may be similar in different instruments, there are differences in the way national laws refer to 'commercial reasonableness'. One model, which is well represented by Article 9 of the UCC, refers to this standard in the specific context of enforcement of a security interest. For example, Section 9-610(b) of the UCC applies to disposition of repossessed collateral and states that every aspect of a disposition including the method, manner, time, place (and other terms) must be commercially reasonable. It is a flexible standard filled in by courts, which consider it as a question of fact.<sup>37</sup> This model – if not the exact wording – found its way into the Ontario PPSA<sup>38</sup> and is embodied also in the UNCITRAL Legislative Guide.<sup>39</sup> The other Canadian PPSAs follow a different approach: they impose an overarching obligation on all parties to act 'in good faith and in a commercially reasonable manner in the exercise of their rights, duties and obligations'.<sup>40</sup> In practice, however, of the two elements of this overarching general provision, the test of 'commercial reasonableness' is considered to be principally significant in the context of the enforcement regime.<sup>41</sup> A similar overarching provision is present also in the UNCITRAL Model Law.<sup>42</sup>

Domestic laws have by now a considerable body of judicial decisions that applied the standard of commercial reasonableness to the factual circumstances of a litigated case. These decisions, however, cover a variety of concrete situations, including those where parties have different bargaining power

<sup>37</sup> For a review of application by courts, see Steven L Harris and Charles W Mooney Jr, *Harris & Mooney's Security Interests in Personal Property: Cases, Problems, and Materials* (6<sup>th</sup> edn, Foundation Press 2015) 638ff. On the original text of Article 9 of the UCC regarding commercial reasonableness and its rationale, see Grant Gilmore, *Security Interests in Personal Property* (Little, Brown & Company 1965) para 43ff.

<sup>38</sup> Section 63(2) of the Ontario PPSA (n 32) obligates the secured party to exercise all its disposition rights in a commercially reasonable manner. The Australian PPSA (n 34) contains a more general provision in the part on enforcement in section 111: 'All rights, duties and obligations that arise under this Chapter must be exercised or discharged: (a) honestly; and (b) in a commercially reasonable manner.'

<sup>39</sup> See UNCITRAL Legislative Guide (n 6), Chapter VIII, *Enforcement of security rights*, para 15 and Recommendations 131ff.

<sup>40</sup> See for example Saskatchewan PPSA (n 32), s 65(3), which states: 'All rights, duties or obligations that arise pursuant to a security agreement, this Act or any other applicable law are to be exercised or discharged in good faith and in a commercially reasonable manner'. A similar language can be found in section 25(1) of the New Zealand PPSA (n 33): 'All rights, duties, or obligations that arise under a security agreement or this Act must be exercised or discharged in good faith and in accordance with reasonable standards of commercial practice.'

<sup>41</sup> Ronald CC Cuming, Catherine Walsh and Roderick J Wood, *Personal Property Security Law* (2<sup>nd</sup> edn, Irwin Law 2012) 54.

<sup>42</sup> See UNCITRAL Model Law (n 6), Article 4, which states: 'A person must exercise its rights and perform its obligations under this Law in good faith and in a commercially reasonable manner'. According to the UNCITRAL Guide to Enactment (n 7) 27-28:

[T]he concept of commercial reasonableness is not defined in the Model law but is generally understood to refer to actions that a reasonable person would take in circumstances similar to those encountered in a particular case by a person exercising its rights or performing an obligation under the Model Law. ... [I]t should be noted that satisfying a specific standard referred to in a provision of the Model Law ... should generally be sufficient to meet the general standards of conduct ...

and knowledge, making it difficult to identify a clear-cut standard commercial practice.<sup>43</sup> Moreover, the standard of commercial reasonableness has been criticised by the business community as being excessively vague and leading to unpredictable results.<sup>44</sup>

## V. Some conclusions on the interpretation of 'commercial reasonableness' under the CTC

There are two important elements that set the CTC apart from other legislation when it comes to interpreting the contours of commercial reasonableness. Firstly, as mentioned above,<sup>45</sup> it contains a more detailed language that explains what is meant by the general standard of conduct, offering guidance in its application and limiting its flexibility. Secondly, it is necessary to take into account its limited scope of application to highly professionalised markets and its nature as a treaty and to apply the Convention's own rules to interpretation and gap-filling of its provisions, including the reference to commercial reasonableness.

Regarding the first point, the more specific guidance contained in the CTC clearly indicates that this standard cannot be seen, without further consideration, as having a meaning equivalent to the analogous clauses found in national secured transaction laws. Under the CTC, commercial reasonableness is presumed if the remedies are exercised in line with parties' agreement, unless the contractual clause is 'manifestly unreasonable'. At the very least, this language implies that it is up to the debtor (or the third party challenging the creditor's conduct) to prove that a contractual provision covering the exercise of creditor's default remedies is unacceptable because of a manifest unreasonableness. The CTC's reliance on parties' self-regulation implies the assumption that parties under the CTC are knowledgeable professionals that conclude agreements in full awareness of their terms. Those terms should be enforced short of a clearly abusive provision that is so at variance with industry practice as to be manifestly unreasonable. The latter is purposely an exceptional circumstance to discourage litigation and enhance certainty and predictability of creditors' risks. Because of the sectorial approach followed by the CTC, reference is to the 'established commercial practice and accepted international practice, or industry standards and customary practice' in the financing of the specific high value equipment covered by the applicable Protocol.<sup>46</sup> Courts should not feel encouraged to 're-write' parties' agreement in the light of a possibly discretionary view of what market practice should look like.

The first step in determining the contours of commercial reasonableness is therefore the contractual agreement, including its interpretation (which is governed by the applicable law rules on the interpretation of contracts and, subject to such rules, any interpretation clause contained in the contract itself). It is always possible, however, for parties to shape the meaning of 'commercial reasonableness' by including detailed provisions on default remedies and their exercise in their agreement.<sup>47</sup>

<sup>43</sup> For reference to the wide variety of circumstances where the standard of commercial reasonableness of a disposition is applied see, eg, Harris and Mooney Jr (n 37) 639.

<sup>44</sup> For the comment that flexibility in the standards applied to the chargee's/mortgagee's conduct may lead to uncertainty in an area where certainty is important to those lending on security see, eg, Hugh Beale et al, *The Law of Security and Title-Based Financing* (2nd edn, OUP 2012) 577.

<sup>45</sup> See section III.

<sup>46</sup> See Donald Gray, Jason MacIntyre and Jeffrey Wool, 'The Interaction between Cape Town Convention Repossession Remedies and Local Procedural Law: A Civil Law Case Study' (2015) 4 Cape Town Convention Journal 17, 19.

<sup>47</sup> It should be noted that the articles in the Convention and its Protocols referring to commercial reasonableness are included in the limited number of mandatory rules that cannot be displaced by parties' agreement (cf Article 15 of the Convention). Parties cannot therefore exclude the application of this standard. They can, however, shape its content through specific contractual regulation, which should not be manifestly unreasonable in the light of industry practice.

It is actually advisable for creditors to do so to concretise the open-ended standard of conduct.<sup>48</sup> Any challenge to contractual clauses should demonstrate manifest unreasonableness in the light of the market practice for the financing of the specific high value equipment covered by the applicable Protocol, which is purposely a high threshold to reach. For example, if the price resulting from the sale of the collateral is significantly lower than the price usually obtained in selling that type of equipment (in the secondary market) but the creditor has acted in accordance with the contractual provisions as to the method, manner, place and time of sale, the creditor's conduct cannot be challenged unless the agreement contains manifestly unreasonable terms in the light of industry practice.<sup>49</sup>

In this respect, it has to be noted that in view of the two-tiered structure of the Convention and of the application of the Protocols to different types of equipment, the contours of commercial reasonableness will be dependent on the practice of the specific market covered by the relevant Protocol. As a consequence, the question arises whether 'established commercial practice' and 'industry standards' may be subject to more uncertainly and potentially different interpretations in those cases where the market, in contrast to what happens in the aviation sector, were less uniform in its standards and more varied as to the level of sophistication of its participants (such as might be the case for certain types of equipment covered by the MAC Protocol). On the other hand, it should be emphasized that obtaining a good price is in the creditor's own interest since it minimises the need to sue the debtor for any deficiency (which is risky and may be practically useless in the case of an insolvent debtor) and also disincentivises competing creditors from challenging the sale.<sup>50</sup>

What if the contract were silent on the manner of exercising one or more remedies or did not cover all aspects of creditor's conduct in enforcement, and it were not possible to fill this gap by applying the rules on construction of the contract? The CTC only refers to enforcing parties' agreement unless manifestly unreasonable. It is surmised here that the threshold should not change, and the outer limit of 'manifest unreasonableness' related to industry standards and customary practice in the financing of the specific type of equipment should be used to determine the acceptable or unacceptable nature of creditor's behaviour.<sup>51</sup>

In this respect, it is important to consider the special nature of the CTC as a treaty with its own underlying goals and principles that should inform the interpretation of its provisions. Article 5(1) states that the Convention should be interpreted by taking into account its purposes as set forth in the Preamble, its international character, as well as the need to promote uniformity and predictability in its application.<sup>52</sup> Article 5(2) establishes that the matters governed by the Convention but not expressly settled in it are to be settled in conformity with the general principles on which it is based

<sup>48</sup> See Franciosi (n 30), referring to meticulous drafting as a response of the business community to the application of the vague criterion of 'commercial reasonableness' by courts.

<sup>49</sup> See Goode (n 2) para 2.112, stating that the creditor 'on a sale must act in a commercially reasonable manner, though if so acting the creditor will be protected even if its efforts do not result in its obtaining the best price'.

<sup>50</sup> On this point see Saidova (n 28).

<sup>51</sup> According to Wool and Jonovic, the CTC 'must also imply terms regarding the standard for 'reasonable' action and timing, as set out in Article 8 of the Convention and Article IX(3) of the Aircraft Protocol, with deference to the other terms in those articles, and, beyond such terms, to contractually agreed standards', in line with the general principle that 'there should be a strong presumption on the enforceability of contract provisions even when the Convention is silent on a topic'. See Jeffrey Wool and Andrej Jonovic, 'The Relationship between Transnational Commercial Law Treaties and National Law: A Framework as Applied to the Cape Town Convention' (2013) 2 Cape Town Convention Journal 65, 74–75.

<sup>52</sup> While this is common practice in international instruments introducing uniform substantive rules in the commercial field (see, eg, Article 7(1) of the 1980 United Nations Convention on Contracts for the International Sale of Goods - CISG), the drafters of the CTC adapted the language of the 'standard' provision on interpretation to be found in other treaties to the overarching goal of ensuring predictability in creditors' *ex ante* risk assessment. Thus, the reference to 'good faith' as a parameter for statutory interpretation is substituted by 'predictability', thereby underlying the fundamental value of clear rules with predictable outcomes.

or, in the absence of such principles, in conformity with the applicable law. Thus, the provision on commercial reasonableness should be interpreted in the light of the general principles underlying enforcement, as well as the principles of uniformity and predictability in the application of the CTC.

At the same time, it is also important to note that, notwithstanding the requirement, and goal, of an autonomous and purposive interpretation of the Convention, the interaction with the applicable domestic law cannot be avoided. The CTC itself expressly refers back, in a number of provisions, to national law (using different connecting factors). One of such provisions is of direct application in the field of enforcement: Article 14 expressly states that 'any remedy provided by the Convention shall be exercised in conformity with the procedure prescribed by the law of the place where the remedy is to be exercised'. Determining the contours of the application of Article 14, as well as, generally, the interaction between treaty provisions and applicable national law is one of the most challenging (and possibly controversial) issues in the interpretation of the CTC. In relation to the question at hand, ie the requirement of commercial reasonableness, however, it can be safely said that the standard of commercial reasonableness, which, by virtue of an express provision of the Convention, is applicable also to the additional domestic law remedies allowed under Article 12, is not part of the 'procedure' mentioned in Article 14.