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Item No. 5 on the agenda: International Interests in Mobile Equipment

b) Preliminary draft Protocol to the Cape Town Convention on Matters Specific to Mining Agricultural and Construction Equipment

(prepared by the Secretariat)

<i>Summary</i>	<i>Progress report on the MAC Protocol project, including the second session of the MAC Protocol Committee of Governmental Experts</i>
<i>Action to be taken</i>	<i>Decide whether the preliminary draft MAC Protocol is sufficiently developed to warrant the convening of a Diplomatic Conference in 2019</i>
<i>Mandate</i>	<i>Work Programme 2017-2019</i>
<i>Priority level</i>	<i>High</i>
<i>Related documents</i>	<i>UNIDROIT 2017 - Study 72K - CGE2 - Report - Appendix III UNIDROIT 2017 - Study 72K - CGE2 - Report MAC Protocol Promotional Flyer</i>

I. INTRODUCTION

1. The purpose of this document is to update members of the Governing Council on the preparation of a fourth Protocol to the 2001 Cape Town Convention on International Interests in Mobile Equipment on Matters Specific to Mining, Agricultural and Construction Equipment (the "MAC Protocol"), in order to allow the Governing Council to decide whether a Diplomatic Conference should be convened in 2019 to conclude the Protocol.

2. The primary resources to assist the Council in its deliberations are the preliminary draft MAC Protocol ([UNIDROIT 2017 - Study 72K - CGE2 - Report - Appendix III](#)) as endorsed by the Committee of Governmental Experts at its second session (CGE2, Rome, 2-6 October 2017) and the Committee's Report from that session ([UNIDROIT 2017 - Study 72K - CGE2 - Report](#)). This document provides additional information on the expected economic impact of the MAC Protocol, details related to Diplomatic Conference and a summary of the Secretariat's current and future proposed activities in relation to the project.

II. BACKGROUND

3. The *Convention on International Interests in Mobile Equipment* was opened for signature on 16 November 2001. Article 2(3) of the Convention provides that the initial three protocols, adopted respectively in 2001, 2007 and 2012, should cover aircraft, railway rolling stock and space assets. Article 51(2) of the Convention specifically contemplates the possibility of adopting additional protocols, which cover other categories of equipment.

4. At its 84th session (Rome, 2005), the UNIDROIT Governing Council decided to include in the 2006–2008 Work Programme of the Institute the preparation of a fourth Protocol to the 2001 Cape Town Convention on International Interests in Mobile Equipment on matters specific to agricultural, construction and mining equipment (the 'MAC Protocol'). Between 2005 and 2012 a range of background research activities were conducted in relation to the project, including a questionnaire distributed to member States, consultations with private industry and a preliminary economic analysis (for further information on the background of the project, see document [UNIDROIT 2015 – C.D.\(94\) 5\(b\)](#)).

5. At its 93rd session (Rome, 2014) the Governing Council agreed to convene a Study Group entrusted with preparing a first draft of the MAC Protocol prior to its 95th session. Composed of various international experts¹ in secured transactions law, the Study Group met four times (15-17 December 2014, 8-9 April 2015, 19-21 October 2015 and 7-9 March 2016) to consider legal issues associated with the preparation of the MAC Protocol and to prepare a preliminary draft text. In addition to the members of the Study Group, the meetings were attended by observers from various international organisations and academic institutions, including the United Nations Commission on International Trade Law (UNCITRAL), the International Finance Corporation (IFC), the Food and Agriculture Organization of the United Nations (FAO), the International Fund for Agricultural Development (IFAD), the World Customs Organization (WCO) and the National Law Center for Inter-American Free Trade (NLCFT). Several out-of-session teleconferences were also held to further work on specific issues relating to the Protocol.

6. At the conclusion of the fourth Study Group meeting on 8 March 2016, the Study Group decided that the preliminary draft Protocol should be submitted to the Governing Council with a recommendation that a Committee of Governmental Experts be convened. At its 95th session (Rome, 18-20 May 2016), the Governing Council considered the draft text produced by the Study Group, and decided that it was sufficiently developed to warrant the convening of a Committee of Governmental Experts for the preparation of a draft Protocol to the Convention on International Interests in Mobile Equipment on Matters specific to Agricultural, Construction and Mining Equipment (the Committee of Governmental Experts).

7. The first session of the UNIDROIT Committee of Governmental Experts was held at the Headquarters of the Food and Agriculture Organization of the United Nations (FAO) in Rome, from 20 to 24 March 2017. The session was attended by 126 representatives from 48 Governments (30 UNIDROIT member States and 18 non-member States), six regional and intergovernmental organisations and four international non-governmental organisations.

8. The Committee made good progress in reviewing the preliminary draft text provided by the Study Group. Several issues were subject to particularly rigorous consideration: (i) the scope of the Protocol in relation to MAC equipment; (ii) how the Protocol should address interests arising out of

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the association of MAC equipment with immovable property; and (iii) the amendment procedure for the Protocol, with particular regard to the Harmonized System codes (HS codes) contained in the Annexes to the preliminary draft Protocol. Majority of the text proposed by the Study Group was adopted by the Committee. On most of the challenging issues, there was consensus on many aspects. For example, the Committee agreed that the scope of the Protocol should be defined through the use of HS codes listed in the Annexes to the Protocol. The Committee also agreed with the general formulation of the three Alternatives in relation to the treatment of immovable property rights.

9. During the first session, a Working Group was established to give further consideration to the process for amending the Protocol. The Working Group proposed a new Article XXXII governing the amendment process, which was considered by the Drafting Committee and subsequently adopted by the Plenary. The Report for the meeting, which includes information on the deliberations of the Committee in relation to each Article, the Report of the Drafting Committee, the amended text to the preliminary draft Protocol and the list of participants is available on the UNIDROIT website and at this [link](#).

10. During the intersessional period, the Secretariat supported the operation of the Intersessional Working Group on Registration Criteria and prepared additional legal analysis for consideration by the Committee of Governmental Experts.

III. SECOND SESSION OF THE COMMITTEE OF GOVERNMENTAL EXPERTS

11. The second session of the Committee of Governmental Experts (CGE2) was held at the FAO headquarters in Rome from 2-6 October 2017. 126 representatives from 51 Governments, six regional and intergovernmental organisations and three international non-governmental organisations registered to attend the meeting. The sustained high numbers of participating States at CGE2 reflect the considerable interest the MAC Protocol project continues to generate in the international community. The MAC Working Group also attended the second session, and reiterated that the MAC Protocol continued to enjoy strong support from the private sector manufacturers, financiers and end-users of MAC equipment.

12. Negotiations proceeded smoothly during the second session. As consistent with the Committee's deliberations during its first session, vast majority of the preliminary draft MAC Protocol was subject to unanimous support and approval. The Committee retained its policy approach of maintaining consistency with the existing Protocols to the Cape Town Convention where possible.

13. However, the Committee made several substantive changes to the preliminary draft Protocol prepared at the first session. In particular:

(a) Alternative A of Article VII was redrafted to clarify and simplify its operation, and an additional limitation was added to prevent the removal of MAC equipment in circumstances where it would have a detrimental effect on the immovable. The exact formulation of the limitation was deferred to the Secretariat to provide different drafting options.

(b) A new Article XII was inserted to allow Contracting States to opt out of the MAC Protocol's application to inventory financing, in order to avoid unduly compromising well-functioning inventory financing laws.

(c) The Committee adopted amendments to Articles XVI [XVII in the current preliminary draft MAC Protocol] and XVII [XVIII] as proposed by the Intersessional Working Group on Registration Criteria, which provided that the primary registration criterion in the MAC Protocol should be the manufacturer-issued serial number, as supplemented by additional

information to ensure uniqueness (to be set out in the regulations of the International Registry).

(d) The Committee reaffirmed that Article XXXII [XXXIII] required further consideration, to ensure that it balanced the ability of Contracting States to control the content of the treaty, while allowing a flexible mechanism for amending the Annexes to the Protocol in relation to technical changes made to the Harmonised System itself and ensuring that the scope of the Protocol would be clear and predictable. The Committee tasked the Secretariat to develop an alternative text that was likely to attract wide support from negotiating States.

(e) The Committee amended the HS codes contained in the Annexes to ensure consistency with the 2017 edition of the Harmonized System.

14. At the conclusion of the session, the Committee decided that given majority of the open legal issues had been resolved, it appeared unnecessary to convene a third session. The Committee made a recommendation to the UNIDROIT Governing Council that a Diplomatic Conference be convened to finalise and adopt the MAC Protocol.

IV. ECONOMIC ASSESSMENT OF THE MAC PROTOCOL

15. At the first session, several participating States suggested that a revised *ex ante* economic impact assessment should be conducted for the MAC Protocol. As a result, the Committee requested that the Secretariat commission such an economic assessment. The Secretariat conducted a competitive closed tender process to select an independent entity to undertake the economic impact assessment. Following the process, the Secretariat commissioned Warwick Economics and Associates to carry out the project. The economic assessment project was funded through the UNIDROIT Foundation and supported financially by the MAC Working Group.

16. Due to the brief period between the first and second sessions of the Committee of Governmental Experts, it was not possible for a full and comprehensive economic assessment to be completed in advance of the second session. Instead, a preliminary economic assessment was prepared for the consideration by the Committee. The key findings of the preliminary economic assessment are summarised below.

17. Ken Warwick and Associates developed a theory of change model to explain the interaction between the product market (MAC equipment) and the credit market (finance to acquire MAC equipment). The model analysed how a given reduction in exposure to credit risk may feed through to a reduction in the cost of credit and an increase in its supply. By taking account of real world constraints and highlighting critical issues in the channels of impact, it helps inform an assessment of the impact.

18. The preliminary economic assessment found that the Mining, Agriculture and Construction (MAC) equipment markets were hugely important, accounting for over USD 100 billion a year of world trade. It noted that the MAC sectors are significant employers, sources of profit and earners of foreign exchange. Further, the MAC sectors enable economic growth and development in critical sectors of the world economy.

19. The preliminary economic assessment further explained that the MAC sectors operated with less capital equipment in countries with poorer access to credit, constraining productivity, profits and economic growth. It noted that the MAC Protocol would address the problem by increasing the supply of secured finance for MAC equipment in Contracting States.

20. Applying the theory of change model to the first study on the projected economic impact of the MAC Protocol undertaken by the Centre for the Economic Analysis of Law (CEAL) in 2013, Warwick Economics found that the MAC Protocol would deliver USD 32–48 billion annually for developing countries and USD 36–60 for developed countries. It concluded that given the low implementation costs, the net positive economic impact of the MAC Protocol would be substantial.

21. Warwick Economics and Associates delivered the preliminary economic assessment results during a presentation at CGE2 which was well received by participating States. The full economic assessment is currently being finalised by Warwick Economics, and will be made available by July 2018.

V. THE DIPLOMATIC CONFERENCE

22. In advance of the Governing Council's consideration of the MAC Protocol, the Secretariat has undertaken consultations with UNIDROIT member States that have expressed an informal interest in hosting the MAC Protocol. To assist States in their consideration, in January 2018 the Secretariat prepared and distributed an informational guide on the hosting the Diplomatic Conference to interested States.

23. Should the Governing Council approve the convening of a Diplomatic Conference, it is anticipated that the Conference would be scheduled for a two-week period between May and October 2019.

VI. PROPOSED SECRETARIAT ACTIVITIES IN ADVANCE OF THE DIPLOMATIC CONFERENCE

24. In preparation for the MAC Protocol Diplomatic Conference, the Secretariat prepared a strategic plan with three key objectives:

- (i) Allow for the conclusion of a text of the MAC Protocol that is supported by both negotiating States and the private sector.
- (ii) Maximise State attendance and States signing the MAC Protocol at the Diplomatic Conference.
- (iii) Minimise the time between conclusion of the MAC Protocol at the Diplomatic Conference and entry into force.

25. To achieve its key objectives, the Secretariat is undertaking the following tasks in advance of the Diplomatic Conference:

- (i) Prepare high quality analysis on both the MAC Protocol and the relevant HS System codes in order to resolve outstanding issues through broadly acceptable solutions.
- (ii) Promote the project globally through both bilateral, regional and multilateral fora involving both the public and private sectors.
- (iii) Conclude arrangements with the host State and efficiently organise logistical arrangements well in advance of the Diplomatic Conference.
- (iv) Identify an entity that is willing to perform the Supervisory Authority role in advance of the Diplomatic Conference.

- (v) Assist Sir Roy Goode in preparing the Official Commentary to the MAC Protocol and assist in coordinating the process of updating the existing Cape Town Convention Official Commentaries.
- (vi) Prepare initial documentation for the future regulations.

26. Over the last six months the Secretariat has undertaken promotional bilateral and regional consultations in Australia, Egypt, Hungary, Mexico and Papua New Guinea. Further consultations are under consideration for later in 2018 in China, Ireland, Japan, Paraguay, South Africa and the United Kingdom. In addition, the Secretariat was contacted by other interested States and provided information upon request.

27. Utilising existing international fora provides the Secretariat with efficient and cost-effective opportunities to engage large groups of diverse States. In this regard, the Secretariat is working with relevant international and regional organisations to promote the MAC Protocol, including the World Bank Group, the International Finance Corporation, Asia Pacific Economic Cooperation, the United Nations Commission on International Trade Law, the Visegrad Group, the Arab League, the African Union and the European Union.

VII. ACTION TO BE TAKEN

28. *The Governing Council is invited to consider whether the preliminary draft MAC Protocol as approved by the Committee of Governmental Experts at its second session in October 2017 is sufficiently developed to warrant the convening of a Diplomatic Conference in 2019 to conclude the Protocol.*