UNCITRAL DRAFT CONVENTION ON ASSIGNMENT OF RECEIVABLES IN INTERNATIONAL TRADE

Lowering the Cost of Credit: The Promise in the Future UNCITRAL Convention on Assignment of Receivables in International Trade

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The UNCITRAL Convention on Assignment of Receivables in International Trade is about to be finalized by UNCITRAL this year. The Convention will apply to international assignments and to assignments of international receivables. Internationality is based on the location of parties and location is defined by reference to the place of business and, in the case of multiple places of business of the assignor and the assignee, their place of central administration. For the Convention to apply, the assignor needs to be located in a State party to the Convention.

The Convention deals with outright transfers of receivables, including outright transfers for security purposes. It also deals with the creation of security rights in receivables. Receivable is defined broadly to include payment rights arising from any contract. Included are trade receivables, consumer receivables and sovereign receivables. Excluded are receivables arising from financial contracts or instruments e.g. swaps, derivatives etc.) deposit accounts and letters of credit. The Convention deals mainly with property issues (effectiveness and priority). It also deals with some contractual issues (representation etc.) by way of default rules applicable in the absence of an agreement between the parties.

In particular, the Convention validates assignments of future receivables and bulk assignments. It also validates assignments made despite anti-assignment clauses without defeating the contractual effect of the anti-assignment agreement as between the assignor and the debtor of the assigned receivable. Furthermore, the Convention refers priority to the law of the assignor's place of central administration, i.e., to a single and easily determinable jurisdiction and to one that is most likely to be the place of the main insolvency proceeding with respect to the assignor. In an optional annex, the Convention also contains substantive law priority rules for States that wish to modernize their laws in this regard to chose from. The Convention contains also independent conflict-of-laws rules that are applicable irrespective of whether the assignor or the debtor is located in a State party to the Convention.

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I. INTRODUCTION

A. The Problem

It has become self-evident that, in a modern economy, a claim for the payment of money (receivable) needs to be, with few exceptions, freely transferable. Mobilizing receivables for financing purposes is inevitable since receivables are often the main or the only asset a company may have at its disposal. In addition, future receivables, the future cash flow of a business, often provide the most inexpensive basis for financing. In view of this reality, any difficulties in transferring receivables may negatively impact the availability and cost of credit, the ability of a company to compete in the global marketplace, and, ultimately, the movement of goods and services across national borders.

In spite of the clear need for unified regulation of receivables, the law relating to the transfer and creation of security rights in receivables is outdated or insufficient. In many civil law countries where only a few general principles are codified, the courts must apply these principles to resolve issues arising in sophisticated financing contracts.[1] In several common law countries, uncertainty prevails because of a lack of "any uniform policy or set of rules" regarding security interests.[2] These common law jurisdictions also recognize that the law often needs to be "adjusted" by courts to address modern problems.[3]

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1. *See, e.g.*, Entscheidungen des Bundesgerichtshofs in Zivilsachen, [BGHZ] [Supreme Court], 149, 90 (F.R.G.); BGHZ 72, 94; BGHZ 257, 94; BGHZ 97, 86.

2. *See* ROY M. GOODE, COMMERCIAL LAW 728 (2d ed. 1995); *see also* FIDELIS ODITAH, LEGAL ASPECTS OF RECEIVABLES FINANCING 177 (1991).

3. *See generally* Jeremy Goldring, *It Floats*, 7 BUTTERWORTHS J. INT'L BANKING & FIN. L. 330 (1996).

At the international level, such problems are compounded.[4] An assignment, which is valid and effective when concluded in country *A*, may be unenforceable against the debtor in country *B*, because the notification requirements set forth by the law in country *B* were not followed. The assignment may also be of no value if challenged by the creditors of the assignor in country *C* because the requirements of the law of that country for the assignment to be effective as against creditors of the assignor may not have been followed.[5] Parties, therefore, may be dissuaded or prohibited from engaging in such assignment transactions because of the considerable time and cost involved in meeting the requirements of the law of a number of countries. The situation may be further complicated because the identity of the debtor or the assignor's creditors may not be known at the time of the assignment.

B. The Solution

National law reform could address a number of these problems. However, any national law, no matter how developed, has its limitations regarding the transfer of property rights in an international context.[6] Such transfers of property rights may be set aside if they conflict with mandatory law or public policy provisions of the forum. This is a particular concern where the borrower becomes insolvent. Following the borrower's bankruptcy filing, the secured lender's rights may be in conflict with the rights attached to unpaid taxes, employee compensation, or the rights of other secured or unsecured lenders protected under the law of the forum. This problem is compounded when the secured lender cannot anticipate the location of the forum at the time of the conclusion of the financing contract.

These problems may be effectively addressed by an international law that provides uniform solutions for all states enacting the law. The Convention on Assignment of Receivables in International Trade[7] (the Convention) prepared by the UN Commission on International Trade

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4. On the inherent limitations on the applicability of revised UCC article 9 to international transactions, see Neil B. Cohen & Edwin E. Smith, *International Secured Transactions and Revised Article 9 UCC*, 74 CHI.-KENT L. REV. 1191 (1999).

5. For the purposes of the Convention, the assignor is the old creditor of the assigned receivable (the borrower in the financing transaction; the debtor in article 9 UCC terminology), the assignee is the new creditor (the lender) and the debtor is the person who owes payment of the assigned receivable (the account debtor in article 9 UCC terminology).

6. *See* Annex Draft Convention on Assignment of Receivables in International Trade, U.N. Doc. A/CN.9/486.

7. UNCITRAL is the core legal body of the UN system in the field of International Trade Law and has the mandate of "furthering the progressive harmonization and unification of the law of International Trade." G.A. Res. 2102, U.N. GAOR, 20th Sess., Supp. No. 14, at 91, U.N. Doc. A/6014 (1965).

Law (UNCITRAL or the Commission) attempts to address this problem. The purpose of this Article is to present the various solutions offered in the Convention and to make a tentative evaluation of their effectiveness.

In Part II, this Article describes the background and the status of the Convention. Part III discusses the general principles underlying the Convention. Part IV deals with issues relating to the scope of application of the Convention. Part V deals with the creation of rights in receivables and issues relating to the effectiveness of an assignment. Parts VI, VII and VIII deal respectively with the relationship between the assignor and the assignee, effects of the assignment as against the debtor, and effects as against third parties. Part IX deals with conflict-of-laws issues and Part X deals with certain issues arising in the context of the final clauses of the Convention. Part XI attempts a tentative evaluation of the Convention.

II. BACKGROUND

UNCITRAL is no stranger in the field of secured transactions.[8] In 1993, the Commission decided to undertake work in the field of assignment of receivables in response to suggestions made at the 1992 UNCITRAL Congress.[9] At its twenty-sixth to twenty-eighth sessions (from 1993 to 1995), the Commission discussed three reports prepared by the Secretariat concerning certain legal problems in the area of assignment of receivables.[10] Having reviewed those reports at its twenty-eighth session, the Commission decided to undertake the preparation of a uniform law.[11] The purpose of this law was to remove legal obstacles to financing transactions by eliminating uncertainty as to the validity of international assignments or assignments of international receivables. The Working Group on International Contract Practices was

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8. For UNCITRAL's earlier work, see Spiros V. Bazinas, *UNCITRAL's Work in the Field of Secured Transactions*, *in* EMERGING FINANCIAL MARKETS AND SECURED TRANSACTIONS, 211-18 (J.J. Norton & M. Andenas eds., 1998).

9. *See Uniform Commercial Law in the Twenty-first Century, Proceedings of the Congress of the United Nations Commission on International Trade Law*, New York, May 18-22, 1992, U.N., GAOR Comm. Int'l Trade L., 25th Sess., at 271, U.N. Doc. A/CN.9/SER.D./1 (1992).

10. Those reports are contained in 24 U.N. Comm'n on Int'l Trade L.-Y.B. (1993), U.N. Doc. A/CN.9/378/Add.3; 25 U.N. Comm'n on Int'l Trade L.-Y.B. (1994), U.N. Doc. A/CN.9/397; and 26 U.N. Comm'n on Int'l Trade L.-Y.B. (1995), U.N. Doc. A/CN.9/412.

11. The discussion of those reports in the Commission is reflected respectively in 24 U.N. Comm'n on Int'l Trade L.-Y.B., ¶¶ 297-301 (1993), U.N. Doc. A/48/17; 25 U.N. Comm'n on Int'l Trade L.-Y.B., ¶¶ 208-14 (1994), U.N. Doc. A/49/17; 26 U.N. Comm'n on Int'l Trade L.-Y.B., ¶¶ 374-81 (1995), U.N. Doc. A/50/17; 27 U.N. Comm'n on Int'l Trade L.-Y.B., ¶¶ 231-34 (1996), U.N. Doc A/51/17; 28 U.N. Comm'n on Int'l Trade L.-Y.B., ¶¶ 252-56 (1997), U.N. Doc. A/52/17; 29 U.N. Comm'n on Int'l Trade L.-Y.B., ¶¶ 222-31 (1998), U.N. Doc. A/53/17; 30 U.N. Comm'n on Int'l Trade L.-Y.B., 319-30 (1999), U.N. Doc. A/54/17.

entrusted with the task. The Working Group completed its work in eight sessions beginning in November 1995 and ending in October 1999. The text prepared by the Working Group was considered by the Commission at its thirty-third session in 2000. At that session, the Commission adopted articles 1 to 17 of the Convention.[12] Articles 18 to 44 and the Annex were referred back to the Working Group so that the text could be advanced before the next annual session of the Commission in 2001.[13] The Working Group completed consideration of the Convention in December 2000.[14] The Convention is expected to be finalized by the Commission at its thirty-fourth session, which is scheduled to take place in Vienna from June 25 to July 13, 2001. One of the issues to be addressed by the Commission at that session is whether the Convention will be concluded at the end of 2001 by the General Assembly of the United Nations or later at a diplomatic conference to be convened by the General Assembly.[15]

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12. Annex I to the report of the Commission on the work of its 33rd session (A/55/17). The version of the Convention as considered by the Commission appears in annex I to the report of the Working Group on the work of its *thirty-first session* 2000 Yearbook 31 U.N. Comm'n on Int'l Trade L.-Y.B. (2000), U.N. Doc. (A/CN.9/466).

13. The reports of the eight sessions of the Working Group are contained in documents: 31 U.N. Comm'n on Int'l Trade L.-Y.B. (2000); U.N. Doc. A/CN.9/466; 27 U.N. Comm'n on Int'l Trade L.-Y.B. (1996), U.N. Doc. A/CN.9/420; 28 U.N. Comm'n on Int'l Trade L.-Y.B. (1997); U.N. Doc. A/CN.9/432 and A/CN.9/434; 29 U.N. Comm'n on Int'l Trade L.-Y.B. (1998), U.N. Doc. A/CN.9/455 and A/CN.9/447; and 30 U.N. Comm'n on Int'l Trade L.-Y.B. (1999), U.N. Doc. A/CN.9/455 and A/CN.9/456. Previous versions of the Working Group are included in working documents: U.N. Doc. A/CN.9/412; 28 U.N. Comm'n on Int'l Trade L.-Y.B. (1997), U.N. Docs. A/CN.9/WG.II/WP.87 and A/CN.9/WG.II/WP.89; 29 U.N. Comm'n on Int'l Trade L.-Y.B. (1998), U.N. Docs. A/CN.9/WG.II/WP.93 and A/CN.9/WG.II/WP.96; 30 U.N. Comm'n on Int'l Trade L.-Y.B. (1999), U.N. Docs. A/CN.9/WG.II/WP.98 and A/CN.9/WGII/WP.102; 31 U.N. Comm'n on Int'l Trade L.-Y.B. (2000), U.N. Doc. A/CN.9/WG.104. The first version of the commentary to the Convention appears in documents: 31 U.N. Comm'n on Int'l Trade L.-Y.B. (2000), U.N. Doc. A/CN.9/WG.II/WP.105 and 106. The second version of the commentary appears in 31 U.N. Comm'n on Int'l Trade L.-Y.B. (2000), U.N. Doc. A/CN.9/470. All reports and working papers are available through the homepage of the UNCITRAL secretariat in the World Wide Web, *at* http:\\www.uncitral.org.

14. The report of the Working Group is not available at the time of the issuance of this volume. However, the full text of the Convention as it was adopted by the Working Group in December 2000 is annexed to this Article. *See* U.N. Convention on Assignment in Receivables Financing, U.N. Doc. A/CN.9/486 (2000) [hereinafter Convention].

15. For a discussion of the background of the Convention, see Spiros V. Bazinas, *An International Legal Regime for Receivables Financing: UNCITRAL's Contribution*, DUKE J. COMP. & INT'L L. 315-58 (1998).

III. GENERAL PRINCIPLES OF THE CONVENTION

A. Facilitation of Access to Lower-Cost Credit

The facilitation of increased access to credit at more affordable rates is key to understanding the Convention.[16] In the realm of significant transactions, such as factoring, the Convention permits businesses to obtain credit or credit-related services on the strength of their records and not necessarily on the strength of their assets. As a result, the availability of credit may increase while costs may become lower than the cost of commercial credit.[17] In other transactions, such as securitization, the structure of the transactions results in a reduction of the risk of insolvency of the assignor which threatens that the assignee will lose the whole pool of the assigned receivables. The pooling of a large number of receivables may also have a positive impact on the availability and the cost of credit in that it creates a different and safer collateral by spreading the risk of debtor default. Furthermore, by obtaining access to international financial markets, business parties may have increased access to credit at lower interest rates.[18]

Such transactions typically involve a bulk assignment of all present and future receivables. The effectiveness of such assignments, however, is not recognized in all legal systems. Protecting the assignor from excessive limitations on its economic activity, addressed by requirements for a specific description of the assigned receivable, are at the core of such limitations. The Convention sets aside such limitations on assignment by clearly validating bulk assignments of present and future receivables. The Convention also recognizes that contractual limitations on assignment can defeat some transactions in which it is not possible for a potential assignee to determine the existence of such limitation—as is the case with future receivables—or can raise the cost of other transactions in which a potential assignee must examine a multiplicity of contracts to determine whether the assignability of the receivables is limited as is the case with bulk assignments without affecting any right the debtor may have against the assignor for breach of contract. The

16. For a more detailed discussion of the general principles of the Convention and its effect on domestic law, see Spiros V. Bazinas, *Le projet de Convention de la CNUDCI, Ses objectifs et ses effets sur les autres lois*, 171-82; Spiros V. Bazinas, *Die Arbeit von UNCITRAL im Bereich der Forderungsabtretung zur Kreditfinanzierung*, *in* DIE FORDERUNGSABTRETUNG, INSBESONDERE ZUR KREDITSICHERUNG 99-132 (W. Hadding & U. Schneider eds., 1999).

17. FREDDY SALINGER, FACTORING LAW AND PRACTICE (2d ed. 1995).

18. *See generally* Stephen L. Schwarcz, *The Alchemy of Asset Securitization*, 1 STANFORD J. BUS. L. & FIN. 133 (1994); INTERNATIONAL ASSET SECURITIZATION 3 (J.J. Norton et al. eds., 1995).

Convention recognizes the effectiveness of an assignment made despite a contractual limitation.

Uncertainty as to payment by the debtor is another factor that may defeat or raise the cost of a transaction. The Convention sets a clear, objective criterion for triggering a change in the way the debtor discharges its obligation without dealing with the payment obligation as such. Perhaps the key problem in transactions involving bulk assignments arises in the case of insolvency of the assignor, where the entire pool of receivables may be effectively lost to the assignee. The Convention does not provide a substantive law rule dealing with the effectiveness of an assignment as against third parties. It does, however, provide a conflict-of-laws rule which refers priority issues to the law of a single and easily determinable jurisdiction which is most likely to be the jurisdiction where the main insolvency proceedings with respect to the assignor will be opened.

B. Debtor Protection

The second main pillar of the Convention is the principle of debtor protection. The principle of debtor protection is reflected in the Preamble. It is also enshrined in article 17 as a kind of a universal principle. Furthermore, this principle underlies a number of provisions dealing with the debtor's rights and obligations.[19]

Facilitation of lower cost credit available to the assignor will likely result in better credit terms offered to debtors. The Convention recognizes the need to provide additional concrete protection to debtors. Therefore, debtors are given a clear discharge rule based on objective criteria[20] while the defences and rights of set-off of debtors are preserved.[21] Furthermore, contracting states may exclude the application of the provision dealing with contractual limitations on assignment with respect to sovereign debtors.

C. Party Autonomy

The Convention recognizes the right of parties to structure their transactions to meet their needs.[22] At the same time, the Convention recognizes that assignments involve the rights of third parties by necessity and that it would go beyond any acceptable notion of party autonomy to allow parties to a transaction to affect the legal position of

19. *See* Convention, *supra* note 14, art. 20-22.
20. *See id.* art. 19.
21. *See id.* art. 20.
22. *See id.* art. 7.

third parties. Accordingly, the assignor and the assignee, or the assignor or the assignee and the debtor, may modify the provisions dealing with their rights and obligations.[23] However, they may not modify those provisions that deal with the rights and obligations of a third party.

D. Good Faith

Article 8 provides for the application of the principle of good faith in the context of the interpretation of the Convention. Good faith is not intended to apply to the relationship between the assignor and the assignee or the assignor or the assignee and the debtor. In any case, the principle of good faith could not apply with respect to the effects of assignment as against third parties, such as the assignee-debtor or assignee-third party relationship, without leading to results that are inconsistent with the general principles of the Convention. For example, if the principle of good faith prevailing in the forum state were to apply to the assignee-debtor, a debtor, who pays the assignee after notification may have to pay again if the debtor knew about a previous, unnotified assignment. If that principle applied to the assignee-third party relationship, the law applicable under article 24 might be disregarded if it does not respect the principle of good faith as it is understood in the forum state.

IV. SCOPE OF APPLICATION

A. "Assignment" and "Receivable"

Unlike other UNCITRAL texts, the Convention mainly deals with property rights rather than with contractual rights. However, while the Convention's primary focus is on assignment as a transfer of property rights in receivables,[24] aspects of the contract of assignment, such as representations and the right of the assignee to notify the debtor and demand payment, are dealt with by default rules applicable in the absence of a contrary agreement by the parties.

The Convention recognizes the distinction between the assignment and the contract of assignment or the financing contract between the assignor and the assignee. However, the Convention does not address the relationship between the assignment and the contract of assignment, which is treated differently from system to system.[25]

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23. The Convention does not affect agreements between the assignee and the debtor. *See id.* art. 21 (debtor and assignor can enter into agreement not to raise defences on rights of set-off).

24. *See id.* art. 2.

25. *See* Hein Kötz, *Rights of Third Parties—Third Party Beneficiaries and Assignment*, 7 INT'L ENCYCLOPEDIA OF COMP. L., ch. 13, § 66 (1992).

The Convention is intended to apply only to contractual assignments. Assignments by operation of law are left to law applicable outside the Convention. Assignments are covered whether they are outright assignments (even if only for security purposes) or security assignments. The provision of financing is not necessary. Thus, the Convention recognizes the important practices in which a service is offered, such as collection, bookkeeping, or protection against bad debts, but not financing. Since assignment is broadly defined,[26] the Convention should apply to any transaction creating a property right in receivables, including pledges and contractual subrogations.

Receivables are defined as "the assignor's contractual right to payment of a monetary sum."[27] Therefore, the assignment of nonmonetary performance rights is excluded. Also excluded is the assignment of noncontractual receivables, such as tax and judgment receivables, receivables arising from unjust enrichment, or tort receivables, unless confirmed in a settlement agreement.

The Convention also covers assignments of trade receivables,[28] consumer receivables,[29] and sovereign receivables,[30] unless their assignment is prohibited by law, as is often the case with personal receivables such as wages and pensions.[31]

B. Practices Not Covered

The assignment of a consumer receivable is excluded if it is made to a consumer for consumer purposes.[32] There is no market for such assignments. The Convention also excludes assignments made by delivery and endorsement or by mere delivery of a negotiable instrument.[33] Such transfers are well regulated by national and international law and are distinct from assignments.[34] If, however, the same receivable arising under a contract exists in the form of a

26. *See* Convention, *supra* note 14, art. 2.

27. *See id.* art. 2(a).

28. Trade receivables are those receivables arising from the supply of goods, construction, or services assigned in factoring transactions.

29. Consumer receivables are those receivables arising from transactions made for personal, family, or household purposes and assigned in cases such as securitization transactions.

30. Sovereign receivables are those receivables owned by a governmental or other public entity and assigned in cases such as project financing transactions.

31. See Convention, *supra* note 14, art. 9.3.

32. *See id.* art. 4.1(a).

33. *See id.* art. 4.1(b).

34. There is no requirement for the notification of a transfer. If the debtor pays a transferee who is not the holder, the debtor is still liable to the holder. A person who takes the instrument for value and without knowledge of any hidden defences against the transferor is not subject to those defences.

negotiable instrument, only the transfer of the negotiable instrument is excluded and not of the receivable in its contractual form.[35] The Convention also excludes assignments made in the context of the sale of a business as a going concern, if made from the seller to the buyer.[36] Such assignments are excluded since they are normally regulated differently by national laws dealing with corporate buyouts and are not of a financing nature. However, assignments made to an institution financing the sale are not excluded.

As already mentioned, the assignment of sovereign receivables is covered by the Convention, unless prohibited by law. States that do not protect themselves through statutory limitations may exclude the application of article 11, which validates an assignment despite the existence of an antiassignment clause.[37] Whether a state may exclude the application of article 11 to public entities involved in commercial activities is left to each state to determine in a declaration deposited with the Secretary-General of the United Nations.[38] In order to enhance predictability, states may list in a declaration the types of entities intended to be excluded from article 11.

The Convention also excludes assignments of receivables arising under transactions on a regulated exchange, financial contracts governed by netting agreements, bank deposits, inter-bank payment systems, letters of credit, and transactions relating to securities.[39] The assignment of such "financial receivables" is excluded by the Convention primarily because they are already well regulated and some of the provisions of the Convention were considered to be unsuitable.[40] For example, these practices could be excluded from the scope of article 11, making an assignment valid and left to be governed by a law applicable outside of the Convention, chosen by the parties, despite the presence of an antiassignment clause. Then, if the assignment was invalid, the Convention would not apply. Such an approach would have preserved the benefits of the Convention for the relevant financial practices, leaving the parties to decide whether they want the Convention to apply.

The Commission also expressed the need to avoid reducing the acceptability of the Convention to the financial industry as another

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35. The text of article 4.1(b) may need to be revised to better reflect that intended result.

36. *See* Convention, supra note 14, art. 4.1(c).

37. *See id.* art. 40.

38. *See id.* In practical terms, this is the Treaties Section of the UN Office of Legal Affairs in New York.

39. *See id.* art. 1.2.

40. *See id.* art. 11 (validating an assignment despite an antiassignment). *See also id.* art. 24 (giving priority to the law of the assignor's location).

reason for excluding the assignment of financial receivables.[41] Unfortunately, the relevant financial industry was not involved in the process long enough for it to appreciate the benefits of the Convention. Lack of familiarity with the process and the text of the Convention may have been more the source of the industry's apprehension than the possibility that the Convention was not suitable to practices involving the assignment of financial receivables.

The Convention does not exclude the assignment of receivables arising from the sale or lease of real estate. However, the Convention does not grant to the holder of a right in real estate a right in a receivable related to the real estate.[42] Likewise, the Convention does not determine the priority of such a right or permit the acquisition of rights in real estate where not allowed by law.[43]

Article 4.3(a) is unnecessary because the Convention is not intended to address the question of whether the holder of a right in real estate acquires a right in the receivable. To the contrary, article 24 refers the question of the existence and the priority of the right of an assignee or other creditors of the assignor with respect to the proceeds that are assigned receivables to the law of the assignor's location.[44] The existence of a right in money-like proceeds other than receivables is left to the law governing the proceeds. A different approach would interfere with the legitimate expectations of creditors of the assignors in the countries where proceeds might be found. If proceeds are in the form of real estate, any priority conflict between the holder of a right in real estate and a right in the assigned real estate-related receivable should be referred to the law of the location of the real estate. This issue should be addressed in article 24 and not in article 4.3(a).

The Convention allows states to exclude further practices when they adopt the Convention or at any time thereafter.[45] The intention is for states to exclude practices that might develop in the future for which the Convention might be unsuitable.[46]

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41. *See id.*

42. From a substantive point of view, the reason cited by the commission is less than convincing. With some minor modifications, the Convention would be perfectly suitable to assignments of financial receivables. *See id.* art. 4.3.

43. *See id.*

44. Article 4.3(b) is also unnecessary, since in principle, the Convention does not deal with the acquisition of rights in real estate. Under article 13, the assignee may acquire a right in real estate securing the assigned receivable only to the extent that the assignment of real estate-related receivables is not prohibited by law. *See id.* art. 24, 9.3.

45. *See id.* art. 41.

46. *See id.* art. 47.

C. Internationality

For an assignment to be covered, it must be international or relate to an international receivable.[47] Domestic assignments of domestic receivables are not affected unless the assignment is part of a chain of subsequent assignments.[48] Conflicts of priority between a domestic and an international assignment of domestic receivables are covered by the Convention.[49]

Internationality is based on the location of a person.[50] Location refers to the place of business of a person. In the case of more than one place of business, the assignor and the assignee are deemed to be located in the place where they have their central administration[51] and the debtor is deemed to be located in the place which has the closest connection with the original contract.[52] If a person has no place of business, reference is to be made to his or her habitual residence.[53]

D. Territorial Connection

With the exception of the provisions dealing with the rights and obligations of the debtor, for the Convention to apply, only the assignor needs to be located in a contracting state.[54] For the provisions dealing with the rights and obligations of the debtor, the debtor must also be located in, or the law governing the receivable needs to be the law of, a contracting state.[55] This approach to the territorial scope of application of the Convention reflects the need for the Convention to be applicable to all situations relating to enforcement against the assignor and against the debtor. By requiring different parties to be located in a contracting state to trigger application of the Convention, a clear distinction arises

47. *See id.* art. 1.1.
48. *See id.* art. 1.1(b).
49. *See id.* art. 5(m)(i), 24.1(a).
50. *See id.* art. 47.
51. The place of central administration is akin to the centre of main interests (a term used in the *UNCITRAL Model Law on Cross-Border Insolvency*, 36 I.L.M. 1386 (1997)), chief executive office, or principal place of business. All of those terms are understood as denoting the centre of management and control, the real business centre, from which in fact, not as a matter of form, the important activities of an entity are controlled, ultimate decisions at the highest level are actually made (without regard to the place where most assets are located or books and records are kept), rather than the day-to-day management of the affairs and operations of such an entity.
52. *See* Convention, *supra* note 14, art. 5(h).
53. *See id.* art. 6(i).
54. *See id.* art. 1.1.
55. *See id.* art. 1.2.

between debtor-related issues, such as the discharge of the debtor, and other issues, such as priority issues.[56]

V. CREATION OF RIGHTS IN RECEIVABLES

A. Formal Validity

Under the Convention, a receivable is assigned by agreement between the assignor and the assignee. The Convention does not contain a substantive law provision as to form or even a pure conflict-of-laws provision as to formal validity because the Commission could not reach agreement on this matter.[57] The Convention contains instead a safe harbour rule, under which it is sufficient for the assignor to meet the form requirements of the law of the assignor's location or any other applicable law. While it is regrettable that the Commission could not agree on a substantive law provision on form, this safe harbour rule is an improvement when compared with the present situation, since it gives assignors a single, easily determinable law to obtain a formally valid assignment. Presently, in view of the uncertainty prevailing as to the law applicable to formal validity, assignors must meet the form requirements of more than one country to ensure that they obtain a valid assignment and may still not be fully protected because they may be unable to determine which countries laws must be complied with. However, the provision may need to be revised to refer to the law of the assignor's location only. Such an approach would be more in line with the approach followed in article 24, which refers the property effects of an assignment on third parties to the law of the assignor's location.

B. Material Validity/Effectiveness v. Priority

The term "effectiveness" is used in the Convention, since it better reflects the proprietary effects of an assignment than the term "validity." However, the Convention draws clear distinctions between effectiveness between the assignor and the assignee, effectiveness as against the debtor, and effectiveness or priority as against third parties. Article 9 covers material effectiveness between the assignor and the assignee, as against the debtor (subject to the debtor-protection articles). Since this distinction between effectiveness and priority may be unknown in some legal systems, article 9.4 provides that the material validity of an assignment is not left to laws outside the Convention. For the same

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56. This is why subjecting priority issues to a different law than the law governing debtor-related issues does not adversely affect the debtor's legal position. *See* Convention, *supra* note 14, art. 30, 31.

57. *See* 31 U.N. Comm'n on Int'l Trade L.-Y.B., § 127 (2000), U.N. Doc. A/55/17.

reason, article 24, referring priority issues to the law of the assignor's location, also provides that it does not apply to matters covered in other provisions of the Convention.

C. Future Receivables and Bulk Assignments

Recognizing the importance of practices involving assignments of receivables not existing at the time of the assignment (future receivables), bulk assignments,[58] and the need to reduce the risk arising with respect to the validity of such assignments in several legal systems, the Convention validates such assignments as of the time of the assignment.[59] There are two limitations. First, the receivable must be identified as one to which the assignment relates at the time of the assignment or for future receivables, at the time of the conclusion of the original contract.[60] Second, the assignment must be valid without prejudice to the rights of third parties.[61]

D. Time of Transfer of Receivables

Existing receivables are transferred upon conclusion of the contract of assignment.[62] Future receivables that, by definition, do not exist at the time of the conclusion of the contract of assignment,[63] are deemed to be transferred at the time of the contract of assignment. This means that once they arise, their transfer is back-dated. Such a transfer is effective between the assignor and the assignee and as against the debtor. It is also the basis for obtaining priority against a competing third-party claimant, but it does not prejudge the resolution of a priority contest, which is left to the law of the assignor's location.[64] In line with the principle that parties are free to modify their legal position by agreement but not to interfere with third-party rights, article 10 of the Convention allows parties to agree on a time of transfer that is later than the time of the conclusion of the original contract. Parties are free, however, to back-date their mutual contractual rights and obligations. As this result may

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58. Bulk assignments are assignments of receivables that are not identified individually at the time of the assignment.

59. *See* Convention, *supra* note 14, arts. 9.1, 10.

60. *See id.* art. 9.1.

61. *See id.* art. 10.

62. Under article 5(b), a receivable is an "existing receivable," if it arises upon or before the conclusion of the contract of assignment. There is no need for the receivable to be due at the time it arises. Conditional and hypothetical receivables are treated in the same way as any other future receivables. *See id.* art. 10.

63. *See id.* art. 5(6).

64. *See id.* art. 24.

be obtained from article 6, and article 10 cannot affect the rights of third parties, its necessity is questionable.

E. Statutory Assignability

The Convention is not intended to deal with statutory assignability in a comprehensive way. Rather the Convention is aimed at setting aside statutory limitations with regard to assignment of receivables in general or of certain types of receivables that are of significance for modern financing practices, such as future receivables, parts of receivables, and receivables that are not identified specifically but are assigned in bulk, without affecting other statutory limitations.[65] Normally, such limitations are aimed at protecting the assignor from excessive limitations on its economic autonomy by assigning all its future receivables.[66] The Convention is intended to set aside such limitations to the extent that it recognizes their effectiveness between the assignor and the assignee and as against the debtor.[67] The Convention does not, however, unduly interfere with national policies because it does not give one assignee, such as a bank receiving a bulk assignment, priority over another, such as a supplier of goods on credit with a retention of title in the goods extending in their sales price. The Convention leaves this matter to other law.

F. Contractual Assignability

In an effort to strike a balance between the need to facilitate the assignment of receivables and the need to protect the debtor, the Convention provides that assignments made in violation of an antiassignment agreement and absent an antiassignment agreement are equally effective.[68] However, while the antiassignment agreement cannot produce effects against the assignee, except if the assignment constitutes a tort, the assignment produces certain effects against the debtor, such as altering the way in which the debtor may discharge its

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65. *See id.* art. 9.3.

66. There are, however, statutory limitations, aimed at protecting the debtor. For example, limitations exist in consumer-protection legislation and in partial assignments. While the Convention validates partial assignments to protect the debtor in the case of multiple notifications, it allows the debtor to pay the assignor or as instructed in the notifications. *See id.* art. 19.6.

67. Effectiveness is the basis for obtaining priority but does not in itself ensure that an assignee will have priority or obtain payment over a competing claimant. The Convention refers to the notion of "effectiveness" rather than "validity" in order to better reflect the proprietary effects of assignment.

68. *See id.* art. 11. However, confidentiality clauses are not affected. An assignment made in violation of such a clause is not validated by the Convention.

obligation as well as affecting the debtor's rights of set-off and modification of the original contract.

While this result appears to be imbalanced, it is justified by the fact that it is in the interest of all parties involved to facilitate assignments rather than to ensure that the debtor is not inconvenienced. If the assignee were deprived of the right to collect from the debtor, the availability and the cost of credit to the assignor, and ultimately to the debtor, would be negatively affected. In any case, the effect of article 11 is limited in a number of ways. First, the scope of article 11 is limited mainly to trade and consumer receivables, where it may be better for all parties involved to validate an assignment rather than to ensure that the debtor will not have to transact with a new creditor. If the assignor is able to mobilize its receivables for obtaining credit, it will most likely be able to produce more goods or services on credit and to offer better credit terms to debtors buying such goods or services. If effect is given to contractual limitations against the assignee, the value of all receivables assigned in bulk would be reduced, whether they contain contractual limitations or not, because parties would always have to conduct a due diligence test (which in the case of future receivables may not produce any safe results).

Article 11 should not affect a consumer's legal position because it does not affect any statutory limitations in consumer-protection legislation. Furthermore, consumers usually do not have the bargaining power to include antiassignment clauses in their contracts, while those consumer debtors who have such bargaining power may not be in need of statutory protection.[69] Likewise, article 11 should not affect the rights of sovereign debtors because such debtors are often explicitly protected by legislation.[70] Those sovereign debtors who are not protected by statutory limitations may be exempted from the scope of article 11 by way of declaration by the state in which such debtors are located.[71]

G. Transfer of Security Rights

The Convention recognizes that the value for an assignee often is not in the assigned receivable itself but in the right securing or supporting the assigned receivable, such as a pledge, a mortgage, a guarantee, or a letter of credit. Article 12, therefore, provides that a security or supporting right is transferred to the assignee, with or without

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69. Only assignments made to a consumer for his or her own personal, family, or household purposes are excluded. *See id.* art. 4(a).

70. *See id.* art. 9.3.

71. *See id.* art. 40. The scope of the exclusion is left to the discretion of the state making the declaration.

a separate act of transfer, depending on whether an independent or accessory right is involved.[72] Such a transfer is effective even if the transfer of the security or supporting right is restricted by way of contract. Any liability of the assignor for breach of contract that may exist under laws applicable outside the Convention remains unaffected. Any form requirements of the laws applicable for the transfer of security rights are also not affected.

VI. THE RELATIONSHIP BETWEEN THE ASSIGNOR AND THE ASSIGNEE

A. Party Autonomy

As already discussed, the Convention focuses on assignment as a transfer of property rights in receivables, and is not intended to limit the right of the parties to structure their relationship to meet their needs. However, the Convention does address certain issues arising in the context of the contractual relationship between the assignor and the assignee. The reason for this approach lies in the educative and risk-allocating value of default provisions dealing with matters related to the contract of assignment. Party autonomy is broadly recognized in this context. Trade usages and practices are also recognized as sources of contractual obligations.[73]

B. Representations of the Assignor

Article 14, dealing with representations of the assignor, is formulated as a default provision which is mainly intended to allocate risks between the assignor and the assignee in line with generally acceptable practice and with a view to reducing the cost of credit. For example, the risk of hidden defences of the debtor is placed on the assignor, since the assignor is in a better position to know whether the contract will be properly performed and will not give rise to defences by the debtor.[74] Placing this risk on the assignee can defeat a transaction if the risk could not be priced. Alternatively, if the risk can be priced, placing this risk on the assignee might raise the cost of credit.

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72. Priority with respect to the security right is settled in the Convention only if such a right constitutes a receivable, such as a third-party guarantee, or the proceeds of a receivable.

73. *See id.* art. 15.1.

74. *See id.* art. 14.

C. Right To Notify the Debtor

The assignee is given the right to notify the debtor and to request payment independently of the assignor.[75] The reason for this approach is that if the relationship between the assignor and the assignee is strained, the assignor may not be willing to cooperate with the assignee in notifying the debtor, and the assignee may have no other way to enforce its rights. In the case of insolvency, the assignor may not be able to cooperate in this regard or, prior to the commencement of the insolvency, the assignor may manipulate a priority contest by cooperating with one assignee to the detriment of another. The Convention also recognizes the need to protect the debtor in the case of a notification from a strange or dubious person. In such a case, the debtor may request additional information about the assignment, such as a writing from the assignor. If the requested information is not received within a reasonable time, during which the debtor's payment obligation is suspended, the debtor may discharge by paying the assignor.[76]

A notification given in breach of an agreement between the assignor and the assignee is sufficient to discharge the debtor but insufficient to cut off the debtor's independent rights of set-off arising from contracts other than the original contract between the assignor and the debtor, or to affect the way in which the original contract may be modified by agreement between the assignor and the debtor without the cooperation of the assignee.[77] This approach attempts to ensure that the debtor's discharge is not the result of knowledge of any arrangements between the assignor and the assignee, while ensuring that a person notifying in breach of an agreement is not allowed to unduly benefit from such a breach.

D. Right To Payment

As between the assignor and the assignee, the assignee is given an in rem right in any proceeds of the assigned receivable and proceeds of proceeds.[78] However, if payment is made to a third person, the assignee is entitled to retain any proceeds only if it has priority. In any case, the assignee may not retain more than the value of its right in the receivable. As between the assignor and the assignee, proceeds include any goods

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75. *See id.* art. 15.1. Payment by the debtor in accordance with a notification is sufficient to discharge the debtor. *See id.* art. 19.1.

76. *See id.* art. 19.5. It is interesting to compare this solution with draft article 12.303 of the European Contract Principles, which, in the case of notification by the assignee, requires the assignment to be in writing, and grants the debtor a right to examine the document.

77. *See id.* art. 15.2.

78. *See id.* art. 16.

returned, either because they are defective or because the test period for which they were given is over. However, as against third parties, such a right in proceeds does not include returned goods and is subject to the law of the assignor's location.[79] This approach reflects the need to protect the assignee, without creating any prejudice for third parties who might have acquired a property interest in returned goods.

VII. EFFECTS AS AGAINST THE DEBTOR

A. General

The assignment of the receivable may have various effects on the debtor, including inconvenience, additional cost, and a change in the debtor's legal position. The Convention attempts to limit those effects by incorporating the principle of debtor protection.[80]

B. The Principle of Debtor Protection

Debtor protection is set forth in the Preamble as one of the main principles of the Convention. Because article 7, which deals with the interpretation of the Convention, refers to the Preamble, debtor protection must be considered in the interpretation and the filling of gaps in the Convention. The latter result is particularly evident in article 17.1, which states that the Convention can have no effect on the debtor's legal position without the debtor's consent, unless explicitly stated by the Convention.[81] In the case of doubt, the Convention has no effect on the debtor without the debtor's consent.[82] For example, in the case of a partial assignment, if the debtor chooses to pay the assignees,[83] the debtor should have a right to be reimbursed for any additional costs.

The Convention recognizes the right of the assignor and the debtor to revise their rights and obligations by agreement. For example, the debtor may waive certain defences in return for a longer period for the repayment of the price or a lower interest rate. There exist two limitations to party autonomy aimed at protecting the debtor. The first exception under article 17.2 is that whatever the effect of the assignment on the debtor, the country and the currency of payment cannot be

79. *See id.* art. 5(j), 16, 24(d).

80. Article 17 deals with the principle of debtor protection generally, and articles 18-22 deal with this principle specifically. *See id.* art. 17-22.

81. *See id.* art. 17.1.

82. The Commission may have to further clarify that a consumer debtor may not vary or derogate from the original contract if such variation or derogation is not permitted by the applicable consumer-protection legislation. *See* Report of the Commission Mid-Annual Session, 33rd Sess., 31 U.N. Comm'n on Int'l Trade L.-Y.B., § 172 (2000); U.N. Doc. A/55/17.

83. *See id.* art. 19.6.

changed.[84] However, to recognize international factoring practices, in which factors accept payment in the debtor's country so as to facilitate payment, article 17.2 allows a change in the country of payment only if the new country of payment is the country where the debtor is located. The second exception is contained in article 21.2, under which the debtor may not waive defences arising from fraudulent acts of the assignor or based on the debtor's incapacity.[85]

The principle of debtor protection is also reflected in article 18 which requires a written notification, reasonable identification of the assigned receivables and the assignee,[86] in a language sufficient to inform the debtor, and receipt by the debtor. Similarly, the principle of debtor protection is reflected in articles 19, through 22. Article 19 provides that the debtor is discharged on the basis of notification of the assignment, irrespective of what the debtor knows or ought to know. Article 20 preserves the debtor's defences and rights of set-off, with the exception of independent rights of set-off arising from contracts unrelated to the original contract that are not available to the debtor at the time of notification. Article 21 requires a written agreement signed by the debtor for a waiver of defences. Article 22 allows the debtor to modify the original contract before notification; after notification, the assignee is bound by this notification if it gives actual or constructive consent of the assignee.

C. Notification of the Debtor

Written notification that reasonably identifies the assignee and the assigned receivables,[87] and is in a language reasonably expected to be understood by the debtor[88] is the only act that may trigger any change in the legal position of the debtor as a result of an assignment. In the absence of such a notification, the assignment under the Convention has no effect on the debtor, even if the debtor has knowledge of the assignment. If knowledge of an assignment on the part of the debtor is taken into account, when an assignee or other party argues that the debtor knows about an assignment, the discharge of the debtor would depend on subjective circumstances that would be difficult to establish. More

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84. *See id.* art. 17.2.

85. *See id.* art. 21.2.

86. Notification, however, does not need to contain a payment instruction. *See* Convention, *supra* note 14, art. 5(d). A payment instruction may be sent by the assignor or the assignee together with the notification or, after notification, only by the assignee. *See id*. arts. 15.1, 19.2.

87. *See id.* art. 5(d).

88. *See id.* art. 18.1.

importantly, in the case of competing claims, the debtor would need to ensure that it paid the right person to avoid paying twice. This approach would inappropriately place on the debtor the burden of determining who among the competing claimants is the rightful claimant. The Convention's approach is based on the assumption that debtor discharge and priority conflicts are two separate issues. The basic rule is that the debtor is discharged if it pays the claimant to notify the debtor first. Whether that claimant is the rightful creditor is a matter to be resolved among the various competing claimants.[89]

In line with the principle of debtor protection, article 18.1 provides that notification must be in a language that "is reasonably expected to inform the debtor" about its contents.[90] The test is subjective, since it refers not to whether the debtor was in fact informed but to the expectation of the person giving the notification. The reference to "reasonable" expectation is an attempt to introduce an objective standard that must to be determined according to the relevant circumstances. To avoid doubt and to give parties a concrete indication of what is meant, the second sentence of article 18.1 introduces a safe harbour rule, declaring it sufficient for the notification to be in the language of the original contract.[91]

D. Discharge of the Debtor By Payment

The Convention does not deal with the obligation of the debtor to pay or with discharge of the debtor in general. These matters are appropriately left to the original contract and to the law governing the contract. The Convention only deals with discharge of the debtor by way of payment and establishes a simple rule stating that before notification, the debtor may be discharged by paying the assignor. After notification, the debtor can be discharged only by paying the assignee or the person identified by the assignee.

As the assignment is effective as against the debtor as of the time it is made, the debtor may discharge its obligation by paying the assignee, even before notification. However, this may be risky, since if it later turns out that there was no effective assignment, the debtor may have to pay twice.

The Convention deals at some length with several situations in which multiple notifications or payment instructions are given to the

89. This distinction between debtor discharge and priority issues is important for understanding why the debtor's legal position is not prejudiced when the debtor discharge issues to the law of the assignor's location.

90. *See* Convention, *supra* note 14, art. 18.1.

91. *See id.*

debtor. In the case of multiple payment instructions given with respect to one and the same assignment involving a correction or other change of the payment instructions, the debtor is discharged if it pays in accordance with the last payment instruction received by the debtor before payment.[92] This means that a payment instruction may be changed or corrected until the debtor pays. After notification is given by the assignor or the assignee, only the assignee may give a new or revised payment instruction.[93] This approach is justified, since after notification it is clear to the debtor that the assignee is the owner of or the holder of a security right in the assigned receivables.

In the case of multiple notifications, the Convention draws a distinction between cases involving more than one assignment of the same receivables (duplicate assignments), cases involving one or more subsequent assignment, and cases involving partial assignments. In the case of multiple notifications relating to duplicate assignments, the debtor is discharged if payment is made in accordance with the first notification received by the debtor.[94] In the case of multiple notifications relating to subsequent assignments, the debtor is discharged if payment is made in accordance with the notification of the last assignment in a chain of subsequent assignments.[95] If the debtor receives notification of duplicate assignments (*A* assigns to *B* and *C*) and subsequent assignments (A assigns to *D*, *D* assigns to *E*), a combined application of articles 19.4 and 19.5 produces the correct result. Thus, if the debtor is notified by *C* and *E*, the debtor is discharged by paying the first to notify since both received the assignment from *A*, and whether a duplicate assignment would be involved is a matter falling within article 19.4. In the case of multiple notifications relating to a partial assignment, the debtor may choose to ignore the notification or to pay in accordance with the notification.[96]

In the case of doubt as to what type of assignment is involved, the debtor may request additional information. If that information is not provided within a reasonable period of time, the debtor is discharged by paying as if no notification was given.[97] This approach ensures that the debtor is protected without creating yet another hurdle for notification to take effect.

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92. *See id.* art. 19.3.
93. *See id.* art. 15.1.
94. *See id.* art. 19.4.
95. *See id.* art. 19.5.
96. *See id.* art. 19.6.
97. *See id.* art. 19.7.

E. Defences and Rights of Set-Off of the Debtor

The Convention does not specify the debtor's defences or rights of set-off. This issue is appropriately left to the original contract and the applicable law. The Convention does provide, however, that the debtor has, against the assignee, the same defences and rights of set-off that the debtor would have against the assignor. There are two exceptions to this rule. First, the debtor cannot raise rights of set-off arising after notification from contracts unrelated to the original contract. The rationale for this approach is that it would be unfair for the debtor to keep accumulating rights of set-off from transactions with the assignor that are unrelated to the original contract and of which the assignee has no knowledge.[98] The second exception relates to the rights of set-off of the debtor in the case of breach of an antiassignment agreement. If the debtor were able to raise such rights by way of set-off and defeat the assignee's claim for payment, a provision stating that the assignment is effective notwithstanding any antiassignment agreements would be meaningless.

Recognizing the importance of waivers of defences for the assignor in increasing the value of receivables and for the debtor in obtaining better credit terms, the Convention permits the assignor and the debtor to agree on such waiver of defences. However, to protect the debtor from unconscionable acts, article 21.1 requires a written agreement signed by the debtor.[99] Furthermore, to protect the debtor from any undue pressure, article 21.2 provides that defences arising from fraudulent acts of the assignor or based on the debtor's incapacity cannot be waived.[100] The Convention does not deal with, and therefore does not limit, waivers agreed upon between the assignee and the debtor.

F. Modification of the Original Contract

Often, a change in the circumstances under which a contract was concluded makes it necessary for the contract to be revised. In such cases, questions arise as to whether the assignee acquires the modified

98. Article 20.2 refers to rights of set-off that were "available" to the debtor at the time of notification without specifying the meaning of the term "available" (e.g., whether the right has to be actual and accrued). Recognizing the variety of sources of rights of set-off referred to in article 20.2 and the possibility that set-off may be treated as a procedural matter subject to the law of the forum, the Convention does not attempt to specify the law applicable to independent set-off. However, article 30 refers contractual set-off to the law governing the relevant contract. *See id.* art. 20.2, 30.

99. *See id.* art. 21.1.

100. *See id.* art. 21.3.

receivable and whether the modification is binding on the assignee in the sense that the debtor may be discharged by paying the debt as modified.

The Convention provides that the assignee's consent is not necessary for a modification of the original contract agreed upon between the assignor and the debtor before notification of the assignment. However, an actual or constructive consent of the assignee is necessary for any modification of the original contract which is agreed upon after notification.[101] This approach is in line with the principle that before notification the debtor may be discharged by paying the assignor, while after notification the debtor may be discharged only by payment to the assignee.

VIII. EFFECTS AS AGAINST THIRD PARTIES

A. Different Priority Systems

As a transfer of property rights, assignment may affect the rights of third parties extending credit to the assignor in reliance on the assignor's receivables. In the case of default or insolvency of the assignor, creditors will be competing as to who will obtain payment from the assignor's receivables. In the absence of a clear rule as to how such conflicts of priority will be resolved, the risk of the assignee being unable to obtain payment will be higher. If this risk cannot be evaluated, a financing transaction may not be concluded at all. If the risk can be evaluated, the transaction will take place but its cost will be higher to the assignor and ultimately to the debtor.

All legal systems recognize that he who has priority in time has priority in right (*prior tempore potior jure*).[102] However, legal systems differ as to what act should take place for a claimant to have priority.[103] Under German law, priority is determined on the basis of the time of assignment.[104] In the case of several assignments of the same receivables, the first assignee prevails.[105] The assignments to all other assignees are ineffective based on the rule that, after the first assignment, the assignor had no right to transfer (*nemo dat quod non habet).*[106] Case law has developed certain exceptions to protect suppliers of material on credit from banks obtaining a global assignment of all present and future receivables of the assignor. In these situations, the assignment to a bank

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101. *See id.* art. 22.2.
102. *See Kötz*, *supra* note 25, § 100.
103. *See id.*
104. *See* Bürgerliches Gesetzbuch [BGB] § 398 (F.R.G.).
105. *See id.*
106. *See id.* Good faith of the second assignee is irrelevant. *See* Kötz, *supra* note 25, at 541.

may be invalid as unconscionable or as against public policy on the assumption that the assignor committed a breach of contract or fraud against the supplier if it knows that the supplier will obtain nothing under the assignment. If the bank accepts an assignment, knowing that the assignor may not be able to continue its business without assigning the same receivables to suppliers, the bank either becomes an accessory to the assignor's breach of contract or fraud, or unduly limits the assignor's economic freedom.[107] In the case of the assignor's insolvency, the assigned receivables are not part of the insolvency estate if the assignment was made before the opening of the insolvency proceeding. If made within a certain period before the opening of the insolvency proceeding, the assignment could be challenged as a fraudulent or preferential transfer. However, a legitimate transaction would normally carry no such risk.

The main advantage to this approach lies in its simplicity. Its obvious disadvantage is that potential third-party creditors have no way of knowing whether certain receivables have been assigned. The conclusion that one may draw is that credit is either unavailable or is only available at a higher cost. This conclusion, however, is only partially correct because in a closed market, banks can still rely on borrowers' representations and gain knowledge about their clients' financial transactions. Furthermore, the penalty for double financing of receivables in these markets outweighs the potential benefits and, thus, the possibility of conflicts is minimized. On the other hand, this situation creates higher costs and impedes access to international financial markets.

Under English law, priority in the case of duplicate assignments is determined primarily on the basis of the time of notification of the debtor.[108] The first assignee to notify the debtor prevails. However, a conflict between an assignee and an insolvency administrator is resolved on the basis of the time of the contract of assignment.

In other legal systems, this conflict is resolved on the basis of the time notification is received by the debtor. If such notification is received before the opening of the insolvency proceeding with respect to the assets of the assignor, the assigned receivables are not part of the insolvency estate (in the case of an outright assignment), or are subject to a security interest (in the case of an assignment by way of security). The

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107. BGHZ 30, 149; BGHZ 55, 34. *See also* Kötz, *supra* note 25, at 545-51.

108. This is the *Dearle v. Hall* rule, the practical significance of which has been reduced by registration requirements of book debts under the Companies Act of 1985 and the Insolvency Act of 1986. *See* 38 E.R. 475, 492. For a critique of the rule and a detailed discussion, see GOODE, *supra* note 2, at 762-63.

advantage of this system is that it provides potential assignees a possibility of finding out from the debtor whether certain receivables have been assigned. This system is certainly possible and easy to apply in the case of existing, high value receivables, provided that the debtor is obligated to respond and responds accurately. However, in the case of future receivables or bulk assignments of present and future receivables where the identity of the debtor is unknown or there are multiple debtors, it is either not possible or very costly for potential third-party creditors to find out whether certain receivables have already been assigned.

Under article 9 of the U.S. Uniform Commercial Code and the Canadian Personal Property Security Acts, priority is determined on the basis of information filed in a public filing office.[109] This information is typically limited to the identification of the assignor and the assignee, and a general description of the assigned receivables.[110] The first assignee to file a notice (financing statement) prevails. If filing takes place before the opening of an insolvency proceeding, depending on whether an outright assignment or an assignment by way of security is involved, the receivables are not part of the insolvency estate nor are they subject to a security interest. The advantage of this system is that it provides both an objective basis for determining priority and notice to potential financiers that certain receivables may have been assigned.

However, UNCITRAL was not able to agree on a priority rule based on the time of filing, due to confidentiality, data protection, and competition issues. It was argued that introducing a filing system would harm nonnotification practices and would not provide sufficient assurance that a right actually existed.[111] Practical problems in establishing a registration system for assignments of receivables under the Convention may also have played a role.

While the Convention does not contain a single, substantive priority rule, it does contain conflict-of-laws priority rules. Furthermore, the Convention offers in an optional annex several priority rules for those states that wish to modernize or to adjust their laws to accommodate assignments under the Convention. The assumption of the Commission in offering options was that competition between the relevant systems should not be impeded and that, in the end, the best system would draw more credit at a lower cost.

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109. U.C.C. § 9-312(5) (2000). Common law in the United States includes the *Dearle v. Hall* rule, the *nemo dat* rule, and other variations of these rules. *See* Kötz, *supra* note 25, § 103.

110. *See* U.C.C. § 9-402.

111. *See* 27 U.N. Comm'n on Int'l Trade L.-Y.B., § 248 (1997), U.N. Doc. A/CN.9/434.

B. Priority Issues Under the Convention

The Convention's primary rule dealing with priority issues is a conflict-of-laws rule. It is true that a conflict-of-laws approach may not lead to uniformity of practical results. Parties will always have to meet the priority requirements of the applicable law, which will differ from country to country.[112] Such an approach may also have inherent limitations. Parties may not be able to predict whether a priority conflict will arise in a contracting state and, therefore, may not know whether the Convention will apply. In addition, parties will not know with certainty whether a particular priority rule will apply or be set aside as conflicting with public policy or mandatory law considerations of another forum state. However, a clear conflict-of-laws rule has economic value in that by informing potential parties to financing transactions about the applicable law it would allow parties to obtain priority. This would be a significant improvement compared with the present situation where parties often do not know which law applies to priority issues and, as a result, must meet the requirements of several jurisdictions.[113]

Departing from traditional conflict-of-laws approaches, subjecting priority issues to the law chosen by the parties or to the law governing the assigned receivable, the Convention breaks new ground in providing for the application of the law of the assignor's location.[114] As a result, priority conflicts are submitted to the law of a single and easily determinable jurisdiction. In the case of multiple places of business, the law of the assignor's central administration becomes the appropriate jurisdiction for the resolution of priority conflicts.[115] Furthermore, conflicts with the law governing insolvency are avoided to the extent that the law of the assignor's central administration governs the main insolvency proceeding with respect to the assets and affairs of the assignor. Fundamental policy decisions of the forum of a secondary insolvency proceeding are preserved, since the forum may set aside a rule of law applicable to priority if it is manifestly contrary to the public policy of the forum (however, the balance of the law governing priority will still apply).[116] Insolvency considerations of the forum are also

112. For this reason, the Convention contains substantive law priority rules for states to opt into if they so wish in an annex.

113. For a critical evaluation of the present status of the law and an analysis of the merits of a place-of-assignor-based solution, see Eva-Maria Kieninger, *Das Statut der Forderungsabtretung im Verhältnis zu Dritten*, RABELS ZEITSCHRIFT 62, 678 (1998); *see also* Teun H.D. Struycken, *The Proprietary Aspects of International Assignments of Debts and the Rome Convention Article 12*, 24 LLOYD'S MAR. COM. L.Q. 345 (1998).

114. *See* Convention, *supra* note 14, art. 24.

115. For the meaning of place of central administration, see *supra* note 51.

116. *See* Convention, *supra* note 14, art. 25(1).

preserved in that nonconsensual super-priority rights existing under the law of the forum are given priority over the rights of an assignee.[117]

The Convention deals with priority contests in a comprehensive way, ensuring certainty as to the rights of third parties. It covers contests, with respect to receivables and their proceeds (including proceeds of proceeds), between assignees of the same receivables from the same assignor, as well as contests between assignees and creditors of the assignor or the insolvency administrator. The Convention also covers contests between Convention and non-Convention assignees, which may arise if domestic receivables are assigned both to a domestic and a foreign assignee. Furthermore, it covers conflicts between persons with a security right in goods extending to their proceeds, such as an inventory assignee or an assignee with a retention of title and an assignee. All conflicts are referred to the law of the assignor's location.

C. Special Proceeds Rules

The law of the assignor's location also governs the characteristics (the personal or property nature of a right) and the priority of an assignee's right with respect to receivables or proceeds that are receivables.[118] The existence, characteristic, and priority of the right of a competing claimant[119] in certain types of proceeds is left to the law of the location of the proceeds.[120]

With a view to facilitating certain financing practices, such as securitization and undisclosed invoice discounting, article 26 attempts to ensure that an assignee with priority, with respect to the assigned receivables, will have a right in rem with respect to proceeds of the receivables and proceeds of the proceeds, if proceeds are received by the assignor on behalf of the assignee and are kept separate from the assets of the assignor.[121]

Article 26 introduces an additional rule, under which if payment is made to the assignee, the assignee has a right in rem if it has priority with respect to the assigned receivables.[122] Article 26 is a key provision in providing practice with a safe harbour in ensuring rights in proceeds.

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117. *See id.* art. 25(2).

118. *See id.* art. 24.1(a).

119. A competing claimant may include another assignee, a creditor of the assignor, or the administrator in the insolvency of the assignee.

120. *See* Convention, *supra* note 14, art. 24.1(b), (c). Article 24.1(b) and (c) appear within square brackets, since no agreement was reached on whether such a rule should be included in the Convention and, if included, whether the provision in its present formulation is appropriate.

121. *See id.* art. 26.

122. *See id.*

IX. CONFLICT OF LAWS

A. Scope

Because the Convention leaves a number of issues to outside law,[123] the Convention contains a number of conflict-of-laws rules in chapter V. These provisions are intended to apply to assignments with an international element under the Convention, irrespective of whether the assignor or the debtor is located in a Contracting State.[124] As a result, the provisions of chapter V may apply to transactions falling within the scope of the material law provisions of the Convention and to transactions falling outside the scope of those provisions (since no territorial connection is needed for the application of chapter V). Where the provisions of chapter V apply to transactions that are within the scope of the material law provisions of the Convention, they apply only to matters not settled in the other provisions of the Convention.[125] States that already have adequate conflict-of-laws rules on assignment have the right to opt out of chapter V.[126]

B. Law Applicable to the Relationship Between the Assignor and the Assignee

Article 29 codifies the generally accepted principle that the parties may choose (explicitly or implicitly) the law governing their mutual rights and obligations. Only the purely contractual aspects of the contract of assignment are governed by this principle.[127] However, article 28 does not cover the substantial validity aspects addressed in the Convention with respect to assignments falling within its ambit or other substantive validity aspects, such as capacity or authority to act. Article 28 likewise does not cover formal validity or the proprietary aspects of assignment.[128]

In the absence of a choice of law provision, the law governing the contractual aspects of the assignment is the law of the state with which the contract of assignment is most closely connected.

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123. For example: whether an outright assignment or an assignment by way of security is involved; whether a right securing the assigned receivable is accessory or independent; or whether the right of the assignee in the assigned receivable is in rem or in personam.

124. *See* Convention, *supra* note 14, art. 1.4.

125. *See id.* art. 28.

126. *See id.* art. 1.4.

127. Purely contractual aspects of the contract of assignment generally include its conclusion, and to some extent substantive validity, the interpretation of its terms, the assignee's obligation to pay the price or to render the promised credit, and the existence and effect of representations as to the validity and enforceability of the debt.

128. *See* Convention, *supra* note 14, art. 30.

C. Law Applicable to the Relationship Between the Assignee and the Debtor

The law governing the receivable governs the conditions under which the assignment can be invoked against the debtor, the debtor's discharge, contractual assignability, and transaction set-off. For example, the law governing the receivable would govern cross-claims arising out of the original contract, but not independent set-off arising from other, unrelated contracts.[129] Because the Convention covers only assignments of contractual receivables, the law governing the receivable will be the law of the original contract from which the receivable arises. The Convention avoids specifying how the proper law of the original contract should be determined. Elaborate rules are not necessary in a chapter which is intended to set forth general rules, without addressing all assignment-related conflict-of-laws law issues. In any case, it would be inappropriate to attempt to determine the law governing the wide variety of contracts that might be at the origin of a receivable, such as contracts of sale, insurance contracts, and contracts relating to financial markets operations. Article 30 does not refer consumer-protection issues to the law of the debtor's location.[130] Article 32, which gives a court the discretion to apply any mandatory rules of the forum or of a closely connected law,[131] should be sufficient in preserving the application of consumer protection law.

D. Law Applicable to the Effects of an Assignment on Third Parties

Article 31 repeats the rules in articles 24 and 25 to ensure that the rules will apply to situations that are not fully within the ambit of the Convention, such as where there is no territorial connection with a Contracting State.

X. FINAL CLAUSES

A. Conflicts With Other Texts

Under article 38, the Convention gives way to other conventions dealing with matters governed by it. The Convention prevails, however, over the Convention on International Factoring, Ottawa 1988 (Ottawa Convention).[132] This approach is intended to avoid introducing uncertainty as to which text would apply, for example, if the Convention

129. *See id.*
130. *See id.* art. 32.
131. *See id.* art. 32.2.
132. *See* Convention on International Factoring, Ottawa, 1988, 27 I.L.M. 943.

were to be set aside by virtue of article 38 and the application of the Ottawa Convention were excluded by the parties. Furthermore, this approach is designed to avoid creating doubt as to whether the Convention would be set aside even with respect to matters not settled in the Ottawa Convention, such as priority issues. If a different approach were followed, assuming that the Convention would apply to such matters in a factoring context, parties would have to first examine the Ottawa Convention to determine whether the Convention would apply.

No conflicts exist between the Convention and the Inter-American Convention on the Law Applicable to International Contracts,[133] which addresses the law applicable to contracts in a general way that is consistent with article 28 of the Convention. Any conflicts between article 12 of the Convention on the Law Applicable to Contractual Obligations[134] (Rome Convention) and articles 29 and 30 of the Convention are minimal because articles 29 and 30 of the Convention are substantially similar to article 12 of the Rome Convention. Furthermore, conflicts should not normally arise between article 12 of the Rome Convention and article 31 of the Convention, because, according to the prevailing view, article 12 of the Rome Convention does not address this matter.[135] However, a view expressed in literature and case law suggests that article 12 of the Rome Convention addresses issues of priority, either in paragraph (1) (the law chosen by the parties) or in paragraph (2) (the law governing the receivable).[136] The Commission, however, has taken the position that neither of those two laws is appropriate. In any case, in order to avoid any conflict with the Rome Convention, article 39 provides that a state may opt out of chapter V.[137] As a result, if all parties to the Rome Convention opt out of chapter V, no conflict would arise. However, states may not opt out of articles 24 through 26 of the Convention. Therefore, conflicts may arise between articles 24 through 26 of the Convention and article 12 of the Rome Convention. This issue is left to the principles of public international law, under which the more specific or the substantive law text (i.e., the Convention) would prevail.

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133. *See* Inter-American Convention on the Law, Mexico City, 1994, Applicable to International Contracts, 33 I.L.M. 730 (1980).

134. *See* Convention on the Law Applicable to Contractual Obligations [hereinafter Rome Convention], 19 I.L.N. 1492.

135. *See* Kieninger & Struycken, *supra* note 113.

136. *See* Koppenol-Laforce, *The Property Aspects of an International Assignment and Article 12 of the Rome Convention*, NETH. INT'L L. REV. 129-137 (1998).

137. *See* Convention, *supra* note 14, art. 39.

No conflicts arise between the Convention and the European Union Insolvency Regulation.[138] The notion of central administration is identical with the centre of main interests used in the draft Insolvency Regulation which does not affect rights in rem in a main insolvency proceeding. While the draft Insolvency Regulation might affect rights in rem in a secondary insolvency proceeding,[139] article 25 of the Convention would be sufficient to preserve, for example, super-priority rights. In any case, the Convention should not affect special insolvency rights.

Since the assignment of rights under independent guarantees or stand-by letters of credit is excluded from the Convention, no conflicts arise with the UN Convention in Independent Guarantees and Stand-by Letters of Credit.[140]

Conflicts may arise between the Convention and the preliminary draft Convention on International Interests in Mobile Equipment (IIME),[141] currently being prepared by a group of experts in the context of the International Civil Aviation Organization (ICAO), Unidroit, and other organizations. IIME is intended to apply to aircraft, spacecraft, and railway rolling stock.[142] IIME can enter into force only together with a protocol for each of those types of equipment.[143] The main characteristic of IIME with respect to an assignment of receivables is that it treats the principal obligation—the receivable arising from the sale or lease of mobile equipment—as an accessory right of the security right in mobile equipment. As a result, an assignee who registers its security right in the mobile equipment with the international equipment-specific register of IIME would automatically obtain the principal obligation. An assignee of the principal obligation without a security right in the mobile equipment could not register or obtain priority. Under article 38, conflicts between the Convention and IIME would be resolved in favour of the application of IIME.[144] The same result would be reached, even in the absence of article 38, since according to general principles of customary treaty law the more specific text prevails (*lex specialis derogat legi generali*).

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138. *See* Council Regulation 1346/2000 on Insolvency Proceedings, 2000 O.J. (L 160) 1 [hereinafter EU Insolvency Regulation].

139. *See id.* arts. 2(g), 4, 28.

140. *See* UN Convention on Independent Guarantees and Standby Letters of Credit, N.Y., 1996, 35 I.L.M. 735.

141. *See* Convention on International Interests in Mobile Equipment, *available at* http://www.unidroit.org.

142. *See id.* art. 2(3).

143. *See id.* art. 7.

144. *See* Convention, *supra* note 14, art. 38.

B. Transitional Application of the Convention

The Convention addresses three separate issues related to its transitional application. Under articles 43.5, 43.6, and 43.7, a declaration or withdrawal by a state does not affect rights acquired by parties to assignments made before the declaration or withdrawal takes effect.[145] Under article 43.3, the Convention applies to assignments made after the date when the Convention enters into force in the country where the assignor is located.[146] Under article 44.3, the Convention remains applicable to assignments made before a denunciation takes effect.[147] The rationale underlying all of these provisions is that, for the sake of certainty and fairness, acquired rights of parties should not be affected.

XI. TENTATIVE CONCLUSIONS

Transactions covered by the Convention already take place, to one extent or another, under current law. However, in view of the high risk involved, such transactions under the Convention are not as widespread as they could or should be, and take place at a considerable cost.[148] As a result, the cross-border movement of goods and services is impeded, particularly in countries where credit is not sufficient or is excessively expensive and, therefore, available only to those who can afford it. The choice of law and choice of forum clauses in financing contracts are as strong as the law governing them, and that law has limitations where mandatory or public policy considerations of the forum are involved. If such a clause or a court judgment based on it is challenged in a foreign court on grounds of public policy or mandatory law, the outcome may well be contrary to the expectations of the parties to the contract. In any case, it is reasonable to suggest that the uncertainty as to the outcome affects the cost of the transaction, if it does not defeat it altogether. By validating assignments of future receivables and bulk assignments, and by addressing priority issues, the Convention attempts to justify the legitimate expectations of the parties. However, the Convention may not automatically result in a windfall of credit being offered to parties all over the world. It would indeed be unrealistic and perhaps irresponsible to suggest that any law, irrespective of the general social and economic circumstances (including, in particular, law enforcement), may bring

145. *See id.* arts. 43.5-43.7.
146. *See id.* 43.3.
147. 29 I.L.M. 1492 (1980).
148. Michael Carsella, *UNCITRAL: First Step in the Globalization of Asset-Based Lending*, SECURED LENDER 108 (Nov.-Dec. 1998); *UNCITRAL Update: On Assignment in Receivables Financing*, SECURED LENDER 8 (June 1999).

about any economic result.[149] However, the Convention, like any other law with its inherent limitations, is a necessary condition to further certain financing practices.

The value of the provisions dealing with representations, the right to notify, and the right in proceeds lies in their likely effect of reducing the risks that the assignee has to bear and, ultimately the cost of the transaction. While the provision on representations codifies law which is generally acceptable, the provisions granting the assignee the right to notify the debtor independently of the assignor and the right in proceeds are novel provisions that have received wide acceptance by the member states participating in the UNCITRAL process.

With regard to contractual assignability, the Convention attempts to find a balance between party autonomy and the need to promote the free transferability of property in the form of receivables. It is reasonable to say that the Convention favours the unlimited transferability of receivables. As a general rule, the large benefits to the economy outweigh the need to avoid debtor discomfort. Where legitimate interests of the debtor are concerned, as in the case of debtors of financial and sovereign receivables, the Convention introduces exceptions.

Furthermore, the Convention introduces a high standard of debtor protection with a clear discharge rule based on objective factors, such as notification, rather than relying on what the debtor knows or ought to know. Admittedly, there is potential for tension with good faith notions of national law. However, such notions should be applied with caution. The debtor protection regime introduced by the Convention is part of a regime which facilitates assignment. It would be unfair for the debtor, to be exposed to a regime that favours assignment more than the law governing the receivable. On the other hand, to deprive the debtor of protection offered by the Convention and to keep good faith standards of the law governing the receivable would also be unfair. As to priority issues, it is certainly regrettable that they are only dealt with by conflict-of-laws rules. However, centralizing issues of priority to a single jurisdiction (the jurisdiction of the assignor's location), signifies progress in comparison with the present law and is more likely to have a positive impact on the cost and availability of credit.

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149. Analysing, however, the economic impact of a certain law under certain circumstances surrounding its application is useful for other legal systems, even if only to the extent the law and those circumstances may be reproduced. The point here is that the best law may be bad law if the conditions for its optimal application are not there. For an analysis of the economic impact of secured transactions laws, see Heywood W. Fleisig & Nuria de la Peña, *Guatemala: How Problems in the Framework for Secured Transactions Limit Access to Credit*, Nov. 1998, Center for the Economic Analysis of Law, *at* http://www.ceal.org.

In general, it is fair to say that work on assignment confirmed the merits of the view that law unification and harmonization does not progress in great leaps, but rather in small, steady steps. The Convention makes this small, but significant and steady step.[150] Building on notions that are, to a large extent, common ground in many legal systems and on generally acceptable good practice, the Convention attempts to address some core issues in financing practice that affect the development of international trade. The Convention does not aspire to be a comprehensive code. Such an unrealistic aspiration would probably lead to failure and harm the process. In this connection, the criticism that, in failing to produce comprehensive results, the process may lead to the unnecessary creation of several layers of law that may not be even compatible with each other is legitimate. However, this criticism would be constructive if it results in caution being exercised to avoid any undesirable side-effects of a uniform law. It would be destructive if it leads to the conclusion that a uniform law is not useful. After all, there are issues that national law, no matter how developed, cannot fully address, and lawyers, no matter how skilful, cannot contract out of.

150. This is generally recognized by commentators. *See* I. LOJENDIO OSBORNE, PROJECTO DE CONVENCIÓN INTERNACIONAL SOBRE CESIÓN DE CREDITOS, ESTUDIOS DE DERECHO MERCANTIL: HOMENAJE AL PROFESOR JUSTINO F. DUQUE, VALLADOLID 1251-63 (1998); D. Janzen, *Der UNCITRAL-Konventionsentwurf zum Recht der Internationalen Finanzierungsabtretung*, Symposium, *in* HAMBURG AM 18 UND 19 SEPTEMBER 1998, RABELS ZEITSCHRIFT 63, 368-77 (1999); S.L. Schwarcz, *A Perfection System for Cross-Border Receivables Financing*, U. PA. J. INT'L ECON. L. (1999); J. Stoufflet, *Cessions internationales de créances, Les contraintes juridiques actuelles* 75 REVUE DE DROIT BANCAIRE ET DE LA BOURSE 169-71 (1999); J.P. Mattout, *Cessions internationales de créances, Les besoins de la pratique*, 75 REVUE DE DROIT BANCAIRE ET DE LA BOURSE 165-69 (1999)