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The United Nations Convention on the Assignment of Receivables in International Trade and Small Businesses

Receivables Financing and the UN Convention

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A. Introduction

Receivables are important assets for small and medium-sized businesses. Their utilisation as collateral for credit has grown since the 1980s. Raising finance through assignment of receivables is a vital financing technique for small businesses and routinely used by companies in financing their businesses.[1] It has been pointed out that raising finance through assignment of receivables 'is simply bigger business than the financing of mobile goods'.[2] Receivables financing has seen considerable growth as 'receivables are self-liquidating and … [a] short-term source of cash'.[3] Studies conducted by the World Bank, however, have revealed that the use of receivables or intangibles as collateral has not reached its full potential, as banks in developing economies do not widely recognise receivables as acceptable collateral.[4] Divergence in the regulation of the law of assignment in national

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* Some of the arguments in this chapter are partly based on N.O. Akseli "*The Utility and Efficacy of the UN Convention on the Assignment of Receivables and the Facilitation of Credit"* in Availability of Credit and Secured Transactions in a Time of Crisis (N.O. Akseli ed.) (CUP, 2013).

[1] Law Commission Report on Company Security Interests No 296 (2005), para 4.1 ('Law Commission Report').

[2] NB Cohen, 'Harmonizing the Law Governing Secured Credit: The Next Frontier' (1998) 33 *Texas International Law Journal* 173, 185.

[3] S Schwarcz, 'Towards a Centralized Perfection System for Cross-Border Receivables Financing' (1999) 20 *University of Pennsylvania Journal of International Economic Law* 455, 456. For the significance of receivables financing, see also F Oditah, *Legal Aspects of Receivables Financing* (London, Sweet and Maxwell, 1991) 2.

[4] See, eg, M Safavian, 'Firm-level Evidence on Collateral and Access to Finance' in F Dahan and J Simpson (eds), *Secured Transactions Reform and Access to Credit* (Cheltenham, Edward Elgar, 2008) 110, 113 ff. M

systems causes uncertainty and increases the cost of credit in cross-border assignment of receivables contracts. Hence the need to have an international instrument that promotes cross-border flow of goods and services by facilitating access to credit as well as acting as an example for domestic law reform activities.

The majority of world trade relies on credit supplied by banks and other financial institutions to SMEs, which comprise 90 per cent of businesses and 50 per cent of employment globally.[5] It can be argued that the use of movable and intangible assets as collateral may have a positive impact on production and growth.[6] With the continuous effects of the credit crisis, the access to credit for businesses has become a significant problem in both developed and developing economies.[7]

While the United Nations Convention on the Assignment of Receivables in International Trade ('the Receivables Convention') has been signed by three countries and ratified by one,[8] feasibility studies as to the possibility of adoption of the Receivables

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Safavian, H Fleisig and J Steinbuks, 'Unlocking the Dead Capital' (2006) March, *View Point* Note Number 307); S Simavi, 'Making Finance Work for Africa: The Collateral Debate', *World Bank PDP Forum* (2007); 'Vietnam Increasing Access to Credit through Collateral (Secured Transactions) Reform' (IFC/MPDF, 2007); 'Reforming Collateral Laws and Registries: International Best Practices and the Case of China' (FIAS/IFC PEP China, March 2007).

5 www.ifc.org/wps/wcm/connect/a16f4f004f36e8539c3cde032730e94e/SM2015_IFCIssueBrief_SMEs.pdf?MOD=AJPERES and www.ifc.org/wps/wcm/connect/967d26804b7eee0986a5c6bbd578891b/IFC-SME-Factsheet2012.pdf?MOD=AJPERES.

6 H Fleisig, 'The Economics of Collateral and of Collateral Reform' in Dahan and Simpson (eds) (n 4) 81, 89 ff.

7 According to the Federation of Small and Medium Sized Businesses statistics, small businesses in the UK have serious problems in gaining access to credit. www.fsb.org.uk/ Report on *Number Crunching the Credit Crunch*.

8 www.uncitral.org/uncitral/uncitral_texts/security/2001Convention_receivables_status.html. Five actions (ratification, accession, approval, acceptance, succession) are necessary for entry into force. So far the Convention has received one ratification (Liberia) and three signatures (US, Luxembourg and Madagascar).

Convention have been underway in North American jurisdictions.[9] On 10 February 2016, the President of the United States Barack Obama sent the Convention to the US Senate for ratification.[10] It is believed that other countries will follow suit soon.[11] Recently, support for the Receivables Convention has also gained momentum with endorsements[12] from influential business and professional bodies including the International Factors Group[13] and the International Chamber of Commerce (ICC).[14] It is argued that the general principles of the Receivables Convention have been widely accepted in national laws.[15] Thus, it is fair to say that these general principles have become international customary law.

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[9] For calls urging the US to adopt the Receivables Convention see, eg, RM Kohn, *Convention to Bolster Exports and Jobs. UN Pact Would Increase Business Loans Based on Receivables*, *The Washington Times*, 6 March 2012. See, eg, Uniform Law Conference of Canada www.ulcc.ca/en/us/Assignment_Receivables_International_Trade_En.pdf. Particularly in the US the self-execution method of implementation may be chosen. See www.uncitral.org/pdf/english/colloquia/3rdSecTrans/Ed_Smith_Implementation.pdf.

[10] https://www.whitehouse.gov/the-press-office/2016/02/10/message-senate-un-convention-assignment-receivables-international-trade

[11] See generally S Bazinas, RM Kohn, LF del Duca, 'Facilitating a Cost-Free Path to Economic Recovery—Implementing a Global Uniform International Receivables Financing Law' (2012) 44 *Uniform Commercial Code Law Journal* 277. www.ulcc.ca/en/uniform-acts-new-order/current-uniform-acts/639-uncitral-assignment-of-receivables-international.

[12] The Convention has received endorsements from legal bodies as well such as the American Bar Association (www.americanbar.org/content/dam/aba/migrated/intlaw/policy/investment/receivablesconvention113C.authcheckdam.pdf).

[13] www.ifgroup.com/wp-content/uploads/2014/12/IFG-endorsement-for-the-UN-Convention-on-the-Assignment-of-Receivables-in-International-Trade.pdf.

[14] www.iccwbo.org/News/Articles/2014/ICC-endorses-UNCITRAL-Convention-on-the-Assignment-of-Receivables-in-International-Trade/.

[15] The general principles of the Receivables Convention, in addition to being settled in most civil and common law jurisdictions, have also been followed in the modernisation of secured transactions law in China, Colombia, Malawi, Mexico, Ghana, India, Japan and South Korea. For example, in Latin free assignability is called *Pactum de non cedendo*. Free assignability is generally recognised by some of the Roman law-influenced civil law systems, for instance the Swiss Code of Obligations (Art 164) and the Turkish Code of Obligations (Art 162(1)) and the PPSA and the UCC Article 9 regimes: see, eg, UCC §9-406(d) and UCC §9-408(a). In the UK, under the Small Business, Enterprise and Employment Act 2015 s 1, bans on assignment are nullified. For a

The central argument in this chapter will focus on three significant general principles of the Receivables Convention that may assist small businesses' access to finance. These are: Article 8, which recognises the validity of bulk assignments of receivables and assignment of future receivables; Article 9, which aims to override anti-assignment clauses; and the registration of security interests over receivables (Annex of the Receivables Convention). The chapter will first present the background of the Receivables Convention and its general principles. This will be followed by an evaluation of the provisions that aim to override anti-assignment clauses and those that enable the registration of security interests over receivables. Conclusions will summarise the arguments.

B. Background and General Principles of the Receivables Convention

The United Nations Commission on International Trade Law (UNCITRAL) drafted the Receivables Convention after almost a decade of careful work.[16] It was adopted in 2001.[17] The Receivables Convention has a dual purpose. First, the explicit purpose of the Receivables Convention is to harmonise the law of assignment of receivables in international trade. Secondly, its implicit purpose is to provide a model for the modernisation of domestic

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comparative work on the assignment of receivables see also H Sigman and E-M Kieninger, *Cross Border Security over Receivables* (Munich, Sellier, 2009). See also Chs 16, 17 and 19 on Germany, Italy and Belgium respectively.

[16] For the background of the project and its inception point, see Report of the Secretary General: Study on Security Interests (A/CN.9/131 and Annex). Previous attempts were a uniform conditional sales Act enacted by Norway, Sweden and Denmark between 1915 and 1917; Unidroit Draft provisions of 1939 and 1951 concerning the impact of reservation of title in the sale of certain goods; provisions regarding the effect of bankruptcy of reservation of title in the sale of goods in the draft EEC Bankruptcy Convention of 1970; and model reservation of title clauses contained in several General Conditions elaborated by the UN Economic Commission for Europe. HS Burman, 'The Commercial Challenge in Modernizing Secured Transactions Law' [2003] *Uniform Law Review* 347, 348–49.

[17] A/RES/56/81.

assignment laws. This is achieved by its general principles and key provisions, which may be taken as an example in domestic modernisation or reform activities. Therefore, with these two purposes, the Receivables Convention aims to facilitate increased access to low-cost credit by reducing legal obstacles. Reduction of legal obstacles provides greater certainty to lending transactions.

UNCITRAL observed that:

> [T]he diversity of national laws and the lack of standard transnational rules creates significant additional expenditure, delays and uncertainty [in] many international business transactions … [and] parties may be dissuaded from using receivables financing at all and are then forced to rely on … more expensive arrangements, such as overdraft facilities, letters of credit or export guarantees.[18]

There is divergence in the way national legal systems regulate taking security over, or sale of, receivables. These divergences are deeply rooted in the cultural, legal and historical traditions of nations. They have the tendency to increase the cost of credit in the global markets and affect the competitiveness of businesses. These divergences are felt in the creation, third-party effectiveness, priority and enforcement of a security right.[19] These differences relate to the proprietary effects of security.[20] Particularly, the role of possession in some civil law jurisdictions as the significant element in proprietary rights[21] is considered to be an obstacle

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[18] 'UN Investigates Receivables Financing', *International Trade Finance*, 3 June 1994; 213 ABI/INFORM Global, 4 ff.

[19] Report of the Secretary General: Study on Security Interests (A/CN.9/131 and Annex), reprinted in (1977) 8 *Yearbook of the United Nations Commission on International Trade Law*, 180 ff. For a similar view see also generally HL Buxbaum, 'Unification of the Law Governing Secured Transactions: Progress and Prospects for Reform' [2003] *Uniform Law Review* 322.

[20] For a comparative analysis of cross-border receivables financing, see, eg, Sigman and Kieninger (n 14).

[21] See generally R Goode, 'Reflections on the Harmonization of Commercial Law' in R Cranston and R Goode (eds), *Commercial and Consumer Law: National and International Dimensions* (Oxford, Clarendon Press,

to the development of receivables financing and its harmonisation. This aspect of the law is regarded as one of the reasons for the lack of recognition of the Receivables Convention. The reluctance of a country to adopt the Receivables Convention may be linked to the following two broad observations: adopting a different set of principles than the ones that have been well established, and the familiarity of the legal and financial community with this new set of principles.[22] However, the Receivables Convention provides a number of solutions that enable countries to modernise their laws in order to respond to the needs of small businesses. These include, particularly, promoting secured financing of receivables financing, overriding anti-assignment clauses and enabling the use of future receivables in assignment and the bulk assignment of receivables.

There is a link between the borrower's financial strength and the attraction to secured credit. It has been pointed out that 'borrowers exhibit an increasing tendency toward unsecured debt as their financial strength increases'.[23] Public companies usually borrow on an unsecured basis. The reasons for this are that they have sufficient credit strength and can spread their sources of finance. Large companies rather prefer to use negative pledge clauses in their contracts.[24] The Law Commission observed this tendency by reporting that 'well-established

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1993) 3, 12. For example, receivables are intangible assets which cannot be transferred using traditional methods of transfer or security.

[22] HD Gabriel, 'Commentary on the Availability of Credit and the Utility and Efficacy of UNCITRAL's Legislative Efforts in Secured Transactions' in O Akseli (ed), *Availability of Credit and Secured Transactions in a Time of Crisis* (Cambridge, Cambridge University Press, 2013) 217, 222–23.

[23] RJ Mann, 'Explaining the Pattern of Secured Credit' (1997) 110 *Harvard Law Review* 625, 674 where Mann concludes that secured credit '[enhances] the borrower's ability to give a credible commitment to refrain from excessive future borrowing and by limiting the borrower's ability to engage in conduct that lessens the likelihood of payment'.

[24] P Wood, *Law and Practice of International Finance* (London, Sweet and Maxwell, 2008) 253. Fleisig empirically provides that in the US one-third of credit is unsecured and about two-thirds is secured. HW Fleisig, 'The Economics of Collateral and of Collateral Reform' in Dahan and Simpson (eds) (n 4) 81, 88.

public companies are able to borrow readily on an unsecured basis, but for many smaller enterprises credit can be obtained on significantly better terms … if the borrower is able to offer security to the lender'.[25] This observation is supported by empirical studies which suggest that security is mainly used by small businesses that pose default risk.[26] Small businesses are mainly able to offer receivables owed to them as their only meaningful collateral. Thus, there is a policy reason to modernise secure credit laws to promote the availability of capital and make credit at affordable rates.[27] Professor Gabriel succinctly notes on this point as follows:

> [T]he [Receivables] Convention, by providing for a source of secured credit should favor smaller borrowers in less developed economies. Most importantly, by opening up new potential markets for capital, and thereby creating a wider number of potential borrowers in a greater number of jurisdictions, the Convention should serve the larger goal of providing a vehicle for capital to move toward its most efficient use by finding borrowers who can best use the resources.[28]

The general principles of the Convention aim to create simplicity in the law of assignment of receivables. By simplifying the rules on the assignment of receivables, the Convention, prevents complexity and achieves certainty and accessibility.[29] It recognises the validity of

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[25] Law Commission Report No 296 (2005) para 1.2.

[26] J Armour, 'The Law and Economics Debate About Secured Lending: Lessons For European Lawmaking?' in H Eidenmüller and E-M Kieninger (eds), *The Future of Secured Credit in Europe* (Munich, De Gruyter Recht, 2008) 3, 9; MA Lasfer 'Debt Structure, Agency Costs and Firm's Size: An Empirical Investigation', Working Paper, Cass Business School (2000) 18. Lasfer concludes that small firms hold more secured and less unsecured debt than larger companies.

[27] See, eg, the Preamble of the Receivables Convention '*Being of the opinion* that the adoption of uniform rules governing the assignment of receivables would promote the availability of capital and credit at more affordable rates …'.

[28] Gabriel (n 21) 222.

[29] For a similar argument in terms of an ideal law of security, see R Calnan, 'What Makes a Good Law of Security?' in F Dahan (ed), *Research Handbook on Secured Financing in Commercial Transactions* (Cheltenham, Edward Elgar, 2015) 451, 453 ff.

assignments of future receivables and bulk assignment of receivables.[30] The Convention also partially nullified contractual limitations to the assignment of receivables. Certainty is achieved with respect to the rights of the assignor and assignee, as well as with respect to the effectiveness of the assignment as against the debtor. The Receivables Convention establishes a conflict-of-laws provision on priority of competing claims. It also provides a substantive law regime as an optional annex governing priority between competing claims and offers a model for the registration of security interests for the purposes of obtaining priority,[31] as well as covering outright and security transfers of receivables.[32]

C. Assignment of Future Receivables and Bulk Assignment of Receivables

Eliminating restrictions on the use of receivables as collateral to obtain finance is important for small businesses. In this context, the Receivables Convention recognises the validity of bulk assignments of receivables and present assignments of future receivables as well as

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[30] Article 8.

[31] Article 42(4).

[32] On these issues see, eg, S Bazinas, 'Key Policy Issues of the United Nations Convention on the Assignment of Receivables in International Trade' (2003) 11 *Tulane Journal of International & Comparative Law* 275; S Bazinas, 'UNCITRAL's Work in the Field of Secured Transactions' (2004) 36 *Uniform Commercial Code Law Journal* 67; S Bazinas, 'An International Legal Regime For Receivables Financing: UNCITRAL's Contribution' (1998) 8 *Duke Journal of Comparative & International Law* 315; S Bazinas, 'Lowering the Cost of Credit: the Promise in the Future UNCITRAL Convention on Assignment of Receivables in International Trade' (2001) 9 *Tulane Journal of International & Comparative Law* 259; S Bazinas, 'UNCITRAL's Contribution to the Unification of Receivables Financing Law: The United Nations Convention on the Assignment of Receivables in International Trade' [2002] *Uniform Law Review* 49; F Ferrari, 'The UNCITRAL Draft Convention on Assignment in Receivables Financing: Applicability, General Provisions and the Conflict of Conventions' (2001) 1 *Melbourne Journal of International Law* 1; F Ferrari, 'The UNCITRAL Draft Convention on Assignment in Receivables Financing: Critical Remarks on Some Specific Issues' in J Basedow, I Meier, AK Schnyder, T Einhorn and D Girsberger (eds), *Private Law in the International Arena—Liber Amicorum Kurt Siehr* (The Hague, TMC Asser Press, 2000) 179; M Deschamps, 'The Priority Rules of the United Nations Receivables Convention' (2002) 12 *Duke Journal of Comparative & International Law* 389.

assignments of partial or undivided interests in receivables. These restrictions are generally known as *statutory limitations* as they are found in legislation dealing with assignment of receivables.

The Receivables Convention Article 8 aims to facilitate the flow of credit by eliminating statutory limitations in national laws. In this context, the Convention focuses on financing practices such as securitisation, project financing, factoring and asset-based financing by recognising the validity of the assignment of future receivables and bulk assignment of receivables. Certain legal systems restrict the assignment of future receivables and receivables assigned in bulk in order to protect the assignor from over-charging its assets.[33]

These restrictions tend to increase the cost of credit as every single receivable upon its creation has to be described and the debtor for every receivable needs to be notified. This activity requires administrative work to ensure an effective transfer. Costs associated with administering this process arise when the assignor and the assignee create new agreements each time a receivable comes into existence. Thus the Receivables Convention does not require each receivable to be described in the contract of assignment and does not require a new contract of assignment to be concluded when a future receivable is created.

Legal systems provide certain reasons for restricting these types of assignment. First, restriction protects 'the assignor from excessive limitations on its economic activity, addressed by requirements for a specific description of the assigned receivable'.[34] Second, concerns over bulk assignments and assignments of future receivables gather around the fact

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[33] For a similar assertion see Bazinas, 'Lowering the Cost of Credit' (n 32) 265.

[34] ibid 265.

that these types of financing practice may have an impact 'on the economic freedom of the assignor or related specificity concerns'.[35] The restriction of security over future receivables arises out of 'the desire to restrict security and … the desire to prevent future property being caught up as a security for pre-existing debt'.[36] Third, statutory prohibitions on bulk assignments have been justified with the 'concerns about the advantage gained by [large] financing institutions, obtaining a bulk assignment … and future receivables from their borrowers, over small suppliers, who are often protected by retention of title arrangements'.[37]

Specificity and publicity requirements limit the use of future receivables as collateral in traditional Napoleonic legal systems.[38] Otherwise, most legal systems recognise the assignability of future receivables. It can be argued that specificity and publicity doctrines may not be compatible with the requirements of modern finance. The specificity doctrine[39]

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[35] S Bazinas, 'Multi-Jurisdictional Receivables Financing: UNCITRAL's Impact on Securitization and Cross-Border Perfection' (2002) 12 *Duke Journal of Comparative & International Law* 365, 371.

[36] P Wood, *Comparative Law of Security and Guarantees* (London, Sweet & Maxwell, 1995) 41.

[37] Bazinas (n 35) 372.

[38] K Zweigert and H Kötz, *An Introduction to Comparative Law*, 3rd edn (Oxford, Clarendon Press, 1998) 445 ff; see also P Wood, 'World-Wide Security—Classification of Legal Jurisdictions' in J Norton and M Andenas (eds), *Emerging Financial Markets and Secured Transactions* (London, Kluwer, 1998) 39, 40 ff.

[39] This doctrine was abolished in England by *Tailby v Official Receiver* (1888) LR 13 App Cas 523 and *Holroyd v Marshall* (1861) 10 HLC 191, All ER Rep 414 [1861]–[1873]. The doctrine has three basics. First, one cannot transfer an asset unless the asset is identified. Secondly, if a security is created over a future asset at the present time to cover an existing debt, then this actually is a creation of security for pre-existing debt when the asset comes into existence and is treated as a potentially voidable preference. Thirdly, there may be a prejudice against debtors granting security over all of their future receivables and thereby either destroying their means of income or weakening the cushion available to unsecured creditors, see Wood (n 35) 40 ff.

requires the identification, specification and separation of the asset from the transferor's assets in order for the assignment to be valid.[40] Specification of the debtor and the information on the receivable are elements of separation. The specification requirement is based on the idea that the owner of assets needs to be known in order for a valid transfer. Publicity depends on specificity. This is because publicity may require some form of creditor's control or possession over the assets. In order to achieve creditor's control assets need to be specifically identified otherwise the transfer cannot be publicised.[41] Under the publicity requirement, if an assignment requires notification of the debtor, whose identity may not be known at the time of the contract of assignment, that may be considered as an obstacle to the assignment of future receivables. The critical problem with notification to underlying obligors is that it provides no means of constituting a present pledge of the future accounts of a business since there is no debtor to notify until the right to payment arises.[42]

The Receivables Convention Article 8(1) recognises the validity of assignment of future receivables and bulk assignment of receivables (receivables that are not identified individually). An assignment cannot be deemed as ineffective against the assignor, the assignee, and the debtor or a third party just because it is an assignment of future receivables

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[40] P Wood, *Maps of World Financial Law* (London, Allen & Overy LLP, 2005) 83.

[41] Wood (n 23) 258.

[42] See R Serick, *Securities in Movables in German Law: An Outline* (Deventer, Kluwer, 1990) 81–82 (where he argues that this sort of limitation as to future accounts rather than a desire to maintain secrecy is the main reason why pledges of intangibles are not generally used in German financing practice); see also J Rakob, 'Germany' in Sigman and Kieninger (eds) (n 14) 63 (noting that 'the creation of a pledge over receivables requires that notice of the pledge be sent to the third party debtor. This … made pledges unpopular—loss of possession deprives the pledgor of the chance to work with the collateral, notice to third party debtors of receivables may damage the reputation and credit of the pledgor or may confuse the debtor about who to pay to'. See Ch 16.

or a receivable that is not individually identified at the time of the assignment. The Receivables Convention sets a condition in Article 8(1)(a) and (b) that these receivables should be identified as receivables to which the assignment relates. The Convention does not require specific description of the receivables. The description can be general so long as the receivables may be identified to the contract of assignment. If the parties provide general descriptions in an assignment, this will be effective as long as receivables are described in such a manner that they can be identified as receivables to which the assignment relates, which means that the debtor and the amount owed should be identifiable in order for the assignments made in bulk to be valid.

Article 8(1)(b) provides that assignments of future receivables are to be recognised provided that the receivables can, at the time of the conclusion of the original contract, be identified as receivables to which the assignment relates. In relation to bulk assignments, receivables should be identifiable at the time of the assignment, if they cannot be identified individually by virtue of Article 8(1)(a). Identification of the exact moment at which the transfer becomes effective would clarify doubts in those legal systems where bulk assignments and assignments of future receivables are not recognised. Recognising the assignment of future receivables as of the time of the conclusion of the original contract does not compromise the rights of the assignee. This is because 'in practice credit was extended at the time when an actual transaction from which receivables might flow was concluded'.[43] This also makes sense as the assignor might assign the same receivable to another person; therefore the Convention protects the interests of the assignee.[44]

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[43] See A/CN.9/434, para 118.

[44] See generally B Markell, 'UNCITRAL's Receivables Convention: The First Step, But not the Last' (2002) 12 *Duke Journal of Comparative & International Law* 401. See also A/CN.9/445, para 224 (where it was noted that

Article 8(2) dispenses with the need for a new contract of assignment to be executed when there is an assignment of future receivables. The future receivable must arise or be created after and be identified to the contract of assignment. The rationale is that future receivables arise after the contract of assignment therefore there is no need to have a new assignment document covering that receivable. Article 10(1) supplements the position and provides that a personal or property right securing payment of the assigned receivable is transferred to the assignee without a new act of transfer.

D. Anti-assignment Clauses

One of the general principles of the Receivables Convention, under the Effects of Assignment chapter, is its recognition of an assignment made notwithstanding an anti-assignment clause. The Receivables Convention under Article 9(1) provides that an anti-assignment clause in a contract dealing with certain types of trade receivable is not enforceable against the assignee. However, the rights of the debtor against the assignor are not affected.[45] Trade receivables mentioned in this provision are trade receivables other than those arising from financial services, construction or real estate; receivables arising from intellectual property

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'There was general support for the principle that a future receivable should be deemed as having been transferred at the time of the contract of assignment. It was observed that, in view of the risk that, after the conclusion of the contract of assignment, the assignor might assign the same receivables to another assignee or become insolvent, it was essential to set the time of the transfer of the assigned receivables at the time of the conclusion of the contract of assignment ... in practice, the assignee would acquire rights in future receivables only when they arose, but in legal terms the time of transfer would be deemed to be the time of the contract of assignment'.

[45] For a more detailed treatment of anti-assignment clauses under the Receivables Convention see, eg, O Akseli, 'Contractual Prohibitions on Assignment of Receivables: An English and UN Perspective' (2009) 7 *Journal of Business Law* 650. In the US under the UCC Art 9 regime UCC §9-406(d) provides free alienability of rights to payment and that any agreement between an account debtor (*debtor*) and an assignor is ineffective.

transactions; credit card receivables; and receivables arising from multi-party netting agreements. The Convention's treatment of anti-assignment clauses also means that small businesses may be able to further utilise financing techniques such as factoring and securitisation in order to access finance.

Under the Convention's treatment, an assignment made notwithstanding an anti-assignment clause will be effective as against the debtor and third parties such as the creditors of the assignor and his trustee in bankruptcy. Recognising the effectiveness of an assignment made notwithstanding an anti-assignment clause poses a question at the juncture of freedom of contract and the ability to create security. The Receivables Convention, the UNCITRAL Legislative Guide on Secured Transactions, and common and civil law systems have recognised the effectiveness of an assignment made in violation of an anti-assignment clause.[46] Under English law an assignment made in violation of an anti-assignment clause is ineffective.[47] However, recently section 1 of the Small Business, Enterprise and Employment Act 2015 has nullified bans on invoice assignment clauses in order to facilitate small businesses' access to finance.[48] It is argued that in the refinement of the implementation of this provision, the Receivables Convention's approach could be helpful.

Recognising the effectiveness of an assignment made in violation of an anti-assignment clause would not adversely affect small debtors, as 'they do not have the

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[46] UCC Article 9 §9-406(d); Australian Personal Property Securities Act 2009 s 81; Swiss Code of Obligations Art 164; Turkish Code of Obligations Art 162(1); UNCITRAL Legislative Guide on Secured Transactions Recommendation 24.

[47] *Linden Gardens Trust v Lenesta Sludge Disposals* [1994] 1 AC 85.

[48] www.gov.uk/government/uploads/system/uploads/attachment_data/file/408130/bis-15-165-nullification-of-ban-on-invoice-assignment-clauses-summary-of-responses.pdf; www.gov.uk/government/uploads/system/uploads/attachment_data/file/392477/bis-14-1232-nullification-of-ban-on-invoice-assignment-clauses-consultation.pdf; for evidence supporting the nullification of bans on anti-assignment clauses www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/memo/sb76.htm; www.publications.parliament.uk/pa/cm201415/cmpublic/smallbusiness/memo/sb13.htm; see also Chs 2 and 15.

bargaining power to insert anti-assignment clauses in their contracts and … would continue paying the same bank account or post office box'.[49] This approach would not affect large debtors as they have sufficient bargaining power.[50] The Receivables Convention protects the assignee, under Article 9(2), by providing that the breach of an anti-assignment clause by the assignor is not in itself a sufficient reason for the avoidance of the original contract by the debtor. The liability of the assignor for breach of the anti-assignment clause is preserved under the Receivables Convention. However, the debtor may not terminate the agreement on the grounds of breach of an anti-assignment clause (Articles 9(2) and 10(3)). This prevents the debtor avoiding the contract and strengthening his bargaining power.[51] This approach also provides certainty to the assignee in relation to the outcome of the transaction. The assignor may be held liable for breach of contract of anti-assignment. However, the right to compensatory damages that the debtor may have under the applicable law has been left outside the Receivables Convention.[52] Article 9(2) aims to protect a person who is not party to an agreement between the assignor and the debtor on the sole ground that he had knowledge of the agreement. The knowledge by the assignee of the existence of the anti-assignment clause is irrelevant. The assignee cannot be held liable on the sole ground of knowledge of the anti-assignment clause. There must be additional grounds of knowledge in order for the assignee to be held liable as the third party. However, knowledge may be relevant in the case of tortious liability of the assignee such as for malicious interference with

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[49] A/CN.9/WG.II/WP.105, para 83; see also A/CN.9/489, para 103.

[50] A/CN.9/WG.II/WP.105, para 83. The Addendum to the Draft Legislative Guide on Secured Transactions para 230 clearly indicates that a debtor such as a consumer may protect itself through statutory prohibitions. A/CN.9/631/Add.1.

[51] Bazinas, 'Key Policy Issues' (n 32) 287.

[52] A/CN.9/489, para 99.

advantageous relations.[53] Article 18(3) does not allow the debtor to make a claim for breach of an anti-assignment clause against the assignee by way of set-off so as to defeat the assignee's demand for payment.

The Contracting States are not permitted to make a declaration to override the effectiveness of the provision of free assignability. A Contracting State is permitted to make a declaration as to whether an assignment of a receivable owed by a governmental debtor in that state will be excluded from the Convention's anti-assignment rules (Article 40). Article 9 will not be effective vis-à-vis a sovereign debtor who is located in a Contracting State if that state makes a declaration under Article 40. Article 9 does not apply to restrictions arising by statute or other rule of law.

E. Registration

The Convention also offers a model for the registration of security interests for the purposes of obtaining priority.[54] The Convention's optional annex contains substantive law priority rules, which the Contracting States may opt into if they 'wish to modernize or to adjust their laws to accommodate assignments under the Convention'.[55] The rules are based on Uniform Commercial Code Article 9 (*first registration in time*), English law (*Dearle v Hall*) and the civil law system (*first assignment in time*). The registration system proposed by the Convention under Article 42(4) is intended to modernise national laws. States may apply their own priority rules and they can still utilise the registration system. The rationale for preparing an optional annex is that some states may have no priority rules, or the existing

[53] A/CN.9/470, para 102; see also A/CN.9/WG.II/WP.105, para 85.

[54] Article 42(4).

[55] Bazinas (n 35) 380 ff.

rules may be outdated or not fully adequate in addressing modern financing techniques.[56] A general registry of security interests system that provides notice to potential financiers may present clear advantages to small businesses. Small businesses do not radiate information about their credit unlike large firms who release information through their access to stock market, financial statements, ratings conducted by the rating agencies or registration of earlier security interests by previous creditors.[57] Financiers or investors do not have credit data information.[58] Asymmetric information is a critical matter in small businesses' access to finance. It is also one of the reasons why small businesses are refused finance.[59] Investors incur transaction costs in due diligence, which leads to reduction in funding causing an 'equity gap'.[60] Clear information about the financial strength and the status of small business could encourage lending and reduce the financial vulnerability of lenders.[61] Financiers lend to small businesses provided there is clear information about their previous transactions with lenders. Although banks have their own reliable information systems (credit card information, exclusive and informal relationships with small businesses etc), it is important to reduce the effectiveness of information asymmetry as a ground for refusing finance to small businesses. One way to obtain clear and reliable information about incorporated and unincorporated businesses is to register security interests created by these businesses.

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[56] A/CN.9/489/Add 1, para 72.

[57] B Carruthers and L Ariovich, *Money and Credit: A Sociological Approach* (Cambridge, Polity, 2010) 85, 149 ff.

[58] For reform discussion in sharing credit data with alternative financiers, see, eg, www.gov.uk/government/consultations/competition-in-banking-improving-access-to-sme-credit-data; www.gov.uk/government/consultations/competition-in-banking-improving-access-to-sme-credit-data.

[59] *The SME Financing Gap Theory and Evidence*, v 1 (OECD Publishing, 2006) 19.

[60] JE Stiglitz, 'The Contributions of the Economics of Information to Twentieth-Century Economics' (2000) 115(4) *Quarterly Journal of Economics* 1441; JE Stiglitz and A Weiss, 'Credit Rationing in Markets with Imperfect Information' (1981) 71 American Economic Review 393.

[61] Carruthers and Ariovich (n 56) 155.

(i) Priority Rules Based on Registration

Optional Annex sections 1 and 2 provide priority rules based on registration. The rules detailed in these sections aim to provide notice to potential financiers that certain receivables may have been assigned. The rule on priority among several assignees (Section I, Article 1) is that the assignee who registers the information about the assignment first gains priority. If no such information is registered, priority will be determined by the order of conclusion of the respective contracts of assignment. The rationale underlying such registration is 'not to create or constitute evidence of property rights, but to protect third parties by putting them on notice about assignments made and to provide a basis for settling conflicts of priority between competing claims'.[62] The rationale for the priority between the assignee and the insolvency administrator or creditors of the assignor (Section I, Article 2) is that if registration takes place and the receivable is assigned before the commencement of insolvency proceedings in relation to the assets and affairs of the assignor, the assignee will have priority. Section II Article 3 details how a registration system should be established. This is an especially important guide for Contracting States that do not have a general registration system. The registry is open to any person for search of the records according to identification of the assignor and a search in writing can be obtained. The written search result issued by the registry is admissible as evidence and is proof of the registration of the data to which the search relates. The registration is proposed to be simple and inexpensive and requires a limited amount of data by virtue of Article 4, which establishes the basic characteristics for an efficient system and therefore an assignee and an assignor would not be required to register information that is too detailed. These basic characteristics are 'the public character of the registry, the type of data that need to be registered, the ways in which the registration-

[62] A/CN.9/489/Add 1, para 74.

related needs of modern financing practices may be accommodated and the time of effectiveness of registration'.[63]

(ii) Priority Rules Based on the Time of the Contract of Assignment

Articles 6 to 8 of the Optional Annex regulate priority rules based on the time of the contract of assignment. Article 6 deals with priority among several assignees based on the order of the conclusion of the respective contracts of assignment. Article 7 regulates priority between the assignee and the insolvency administrator or creditors of the assignor. The right of the assignee has priority over the right of an insolvency administrator and creditors, provided that the receivable is assigned before the commencement of insolvency proceedings. The time of the assignment may be established by any method of proof under Article 8.

The time of the assignment determines priority. Although under the *nemo dat* rule, after the first assignment the assignor cannot assign the same receivable to another assignee as he has no right to assign, there is a disadvantage to this approach. Third-party creditors may not be able to determine whether certain receivables have been assigned. This is because there is no registration system that they can check with. This may have a negative impact on the availability and the cost of credit. Third-party creditors would need to protect themselves against the risk of a previous assignment having taken place. On the other hand 'in a closed market, banks can still rely on borrowers' representations and gain knowledge about their clients' financial transactions [and] and the penalty for double financing of receivables in these markets outweighs the potential benefits'.[64]

(iii) Priority Rules Based on the Time of Notification of Assignment

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[63] A/CN.9/489/Add 1, para 78.

[64] Bazinas, 'Lowering the Cost of Credit' (n 32) 284.

In this approach, priority is determined by the order in which the debtor receives notifications of the respective assignments. However, the knowledge of a prior assignment by an assignee makes it impossible for that assignee to obtain priority over that prior assignment even if the subsequent assignee notified the debtor first. The priority between the assignee and the insolvency administrator or creditors of the assignor is governed by Article 10. According to Article 10, the assignee will have priority over the right of an insolvency administrator if the receivable was assigned and notification was received by the debtor before the commencement of such insolvency proceeding. It is possible that potential assignees may inquire from the debtor as to whether receivables have been assigned previously. In terms of bulk assignments and assignment of future receivables the system may not be ideal for assignees. This is because the identity of the debtor will be unknown or there will simply be multiple debtors. Thus it can be argued that this system may not be cost-effective for assignees.[65]

Under English law,[66] an assignment made by a company will only be registrable if it is an assignment by way of security (charge) over book debts of the company.[67] If it is an assignment by way of sale it is not registrable. On the other hand, all types of assignments (outright or for security purposes) by an individual are registrable.[68] The Law Commission in its Report recommended that sales of receivables by companies should also be registered.[69] Functionally, sale of receivables is similar to charge over receivables; it seems perfectly

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[65] For criticism of the rule in *Dearle v Hall* see, eg, J de Lacy, 'The Priority Rule of Dearle v Hall Restated' (1999) 63 *The Conveyancer* 311.

[66] For more information see Ch 2.

[67] Companies Act 2006 s 860(7)(f).

[68] Insolvency Act 1986 s 344.

[69] Law Commission Report No 296, paras 4.7 ff.

reasonable to make the sale of receivables registrable. Registration can, at least, be on a voluntary basis. Lack of registration causes certain problems such as subsequent creditors or assignees having to rely on the representations of the assignor and possibly not being informed of the existence of a functional equivalent of charge over receivables.[70] The rule in *Dearle v Hall*,[71] which regulates priority over receivables, is not suitable for modern financing techniques.[72] Failure to notify debtors will result in the loss of priority status in subsequent assignments under *Dearle v Hall* and in civil law jurisdictions the assignment could become void in the insolvency of the assignor.[73] According to Professor Oditah: 'bulk assignees of receivables, especially lenders as opposed to invoice discounters generally do not give notice of their bulk assignments until the assignor defaults and it is necessary for the assignee to collect the assigned receivables itself'.[74] In the assignment of future receivables this rule is not ideal either. It is not possible to notify debtors who are unknown at the time of conclusion of the contract of assignment. Even when the identities of future debtors are known and notice is given prior to the receivables coming into existence, this may not be sufficient to secure its priority. It is because a notice given to the debtor after the receivables have come into existence will have priority.[75]

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[70] ibid.

[71] *Dearle v Hall* (1828) 3 Russ I.

[72] Nevertheless, the rule also applies to assignment of bulk receivables *Compaq Computer Ltd v Abercorn Group Ltd* [1993] BCLC 602.

[73] For a similar assertion see F Oditah, 'Recurrent Issues in Receivables Financing' in J Armour and J Payne (eds), *Rationality in Company Law: Essays in Honour of DD Prentice* (Oxford, Hart Publishing, 2009) 321, 351. This is because formal validity and publicity requirements are considered as condition of priority and they have not been met.

[74] ibid.

[75] *Re Dallas* [1904] 2 Ch 385.

F. Conclusions

The Receivables Convention is a sophisticated piece of legislative work which has not yet received the praise it deserves. While it has not yet received sufficient ratifications and entered into force, its general principles, some of which have been further discussed in this chapter, have been incorporated in developed legal systems that support the facilitation of credit. The principles have also been incorporated into the UNCITRAL Legislative Guide on Secured Transactions and the UNCITRAL draft Model Law on Secured Transactions. Thus, it can be argued that it has perhaps achieved its mission.