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# DRAFT CONVENTION ON ASSIGNMENT [IN RECEIVABLES FINANCING] [OF RECEIVABLES IN INTERNATIONAL TRADE]

## Compilation of comments by Governments and international organizations

## Addendum

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States

JAPAN

[Original: English]

Japan believes that the unification of laws concerning assignment of receivables is important from the point of a view that it would prevent complications arising out of differences of laws of various countries and promote international receivable financing. We are continuing a careful study of the draft Convention with a special attention to pending issues, including the issues of location (article 6 (1) ), receivables other than trade receivables (article 5) and individual provisions concerning private international law. At this point, we would like to make brief comments on the issues as follows.

*Title and Preamble*

Japan is of the view that it is preferable that the words "receivables financing" remain in the title and the preamble, because the draft Convention contains rather detailed provisions as to obligations or defenses (Chapter IV, Sections I and II), which might not be always suitable for all kinds of assignment of receivables.

*Scope of chapter V (articles 1 (3) and 37)*

With a view to improving uniformity in the field of assignment law, it is preferable that the substantive priority rules in the annex do not apply through the private international law rules in chapter V. Therefore, Japan is of the opinion that article 1 (3) should be deleted and chapter V should have a provision stipulating explicitly that the chapter only supplements the draft Convention.

We prefer this chapter to be subject to an opt-in rather than to an opt-out clause (article 37 should be amended), because we understand that it is aimed at States that do not have such private international law rules.

*Debtor's discharge by payment (article 19)*

We would like to clarify article 19 (5), in particular with regard to the case in which A assigns a receivable to B, who assigns it to C subsequently, and the debtor requests C to provide adequate proof of the assignment.

One question is whether C needs to provide proof concerning the assignment only between B and C, or proof concerning both assignments so that C might be a true assignee. We believe that the latter might be proper considering that the debtor would not necessarily be notified of the assignment between A and B provided that article 18 (3) which states that notification of a subsequent assignment (in this case, between B and C) constitutes notification of any prior assignment (between A and B).

Another question is, if C fails to provide adequate proof of assignments, whether the debtor should pay A or B in order to be discharged.

UNITED STATES OF AMERICA

[Original: English]

## I. GENERAL COMMENTS

The report of the 31st session of the Working Group (A/CN.9/466) and the consolidated text of the draft Convention, set out in Annex I thereto, provide a well negotiated basis on which to conclude a final international text of a United Nations convention on modern commercial finance law relating to the assignment of receivables ("the draft Convention"). The benefits of global economics and trade have not yet been fully realized in many states, and the absence of adequate international commercial finance and credit in this important area is one of the obstacles for achievement of these goals. The draft Convention can substantially cover that gap and thus benefit countries at all levels of economic development and in all regions.

*Bulk assignments and assignments of future interests*

The development of modern commercial finance law relating to the assignment of receivables through the draft Convention and the ability to generate credit from capital markets through such laws offer an important opportunity to address these goals. A multilateral convention can achieve these ends by recognizing the validity of and supporting the use of assignments of receivables, especially for future interests and large volume assignments, which have become the backbone of new sources of credit in international capital markets.

*Commercial predictability as key to generating credits*

In addition to including substantive uniform rules for the assignment of receivables, the draft Convention provides States with options in order to adapt the draft Convention's provisions to their particular economic needs. On some other matters the draft Convention sets out rules to determine which national legal regime applies, which can also promote finance, provided that the rules reflect transactional practice, serve the needs of commercial efficiency and are not counterproductively premised on general notions of conflict of laws. The combination of these techniques in the draft Convention is aimed at assuring the necessary level of commercial certainty, which is critical to the willingness of capital markets to extend credit to areas previously under-served.

## II. SPECIFIC COMMENTS ON KEY ISSUES

*Scope of application (article 1)*

The draft Convention's standards on location of the assignor, the assignee and the debtor, and consistency of those standards with the equally important standards in articles 24 and 25, are critical to achieve benefits under the draft Convention. Financing parties in modern assignment practices must have ex-ante certainty of when the draft Convention applies, and cannot be left generally to a later analysis of facts and circumstances, or the benefits of the draft Convention will be lost. This is

especially the case with the major source of new credits through assignments which involve future interests, and bulk and syndicated assignments.

Article l (1) (b) needs to be aligned with article l (1) (a) so as to require for a subsequent assignment, like article l (1) (a) does for an initial assignment, that the assignor be located in a Contracting State. The rationale for the requirement in article l (1) (a) that the assignor be located in a Contracting State was that the rules of the draft Convention, especially those relating to third-party rights in part III of chapter IV, must apply to all third parties dealing with the assignor. This application could not be assured, particularly in the likely case of a dispute with a third party arising in a forum in the assignor's State, unless the assignor's State were a Contracting State. We see no policy reason to distinguish between initial assignments and subsequent assignments in requiring the assignor to be located in a Contracting State. We believe that the Working Group did not intend for there to be different treatment.

To align article 1 (1) (b) with article 1 (1) (a), we suggest that article 1 (1) (b) should read as follows:

> "(b) a subsequent assignment by an assignor located in a Contracting State at the time of the conclusion of the contract of assignment, provided that any prior assignment is governed by this Convention; and"

The assignment addressed in article 1 (1) (c) is not really a third type of assignment to which the draft Convention applies, as is suggested by the present wording, but rather this provision is a negation of a possible limitation that might otherwise have been made with respect to a type of assignment described in article 1 (1) (a). Therefore, this provision should be modified to be a new paragraph (2), reading as follows:

> "This Convention applies to a subsequent assignment that is described in paragraph (1) (a) of this article notwithstanding that this Convention did not apply to any prior assignment of the same receivable."

*Scope of application (article 2 (a))*

Article 2 (a) is in many ways a scope provision. This is because the definition of the term "receivable" in article 2 (a) - any contractual right to the payment of a monetary sum - is so broad that the draft Convention must address as a matter of scope, either by a rule in the draft Convention or by exclusion, a wide variety of financial practices that may involve the assignment or possible assignment of a receivable as so defined. The rules of the draft Convention generally work well, and are generally consistent with current commercial practices in many countries, when the receivable is a contractual right to payment arising out of the sale of goods or the provision of personal services.

The draft Convention does not work as easily in the case of other receivables, such as those arising out of deposit accounts, securities accounts, commodity accounts, swaps and other derivatives, repos, letters of credit, independent guaranties and the leasing of real estate. To increase the opportunity of the draft Convention to gain broad acceptance, certain rules may possibly need to be adjusted, or specific exclusions provided, for those cases. It would be our hope that this goal could be achieved at the Commission meeting in June of 2000.

*Excluded transactions (articles 4 and 5)*

We continue to believe that proposals for exclusion of certain transactions or entities or negotiation of special provisions to accommodate those sectors, raised at the previous meeting of the Working Group, remain an important cross-cutting issue. Our proposal with respect to certain commercial sectors set forth at the last meeting of the Working Group in variant A of article 5 has been subsumed in our comments on article 2 (a) above. We continue our efforts to confer with industry groups to seek the appropriate solutions in this area.

*"Location" (article 6 (i))*

We are continuing to consult with industry groups in various countries and governmental regulatory authorities as to whether the rules for determining the location of an assignor in article 6 (i) should be modified for branches of banks. It is important to consider whether the location rule should take into account the common practice of banks to expand their foreign operations through branch banking. The separate regulatory scheme that many States have devised for branches of foreign banks operating in their States, and current debt syndication and trading markets in which banks and other parties, in dealing with each other, regard a regulated branch of a foreign bank much like a separate legal entity operating domestically in the State in which the branch is located *(for an initial proposal which the Working Group did not have time to consider, see A/CN.9/466, paras. 98 and 99)*. A similar treatment may be desirable for branch offices of foreign insurance companies where like regulatory considerations may be implicated.

*Effectiveness and time of assignment (articles 9 and 10)*

There are three situations in which these articles might be read to bring about a result different from that intended by the Working Group. First, despite the clear policy choice in article 9 to validate individual or bulk assignments of future receivables, article 24 might be interpreted so as to override the effect of that policy choice. Second, despite the clear policy in article 24 (a) (iii) of deference to the insolvency law of the state in which the assignor is located, articles 9 and 10 could be read to override that domestic insolvency law regarding priorities with respect to certain receivables arising after the commencement of the insolvency proceeding or earned after the commencement of the insolvency proceeding by the use of unencumbered assets of the insolvency estate. Third, despite the Working Group's clear intention to have no Convention rule that would override statutory limitations on assignment, article 9 might be interpreted to override an applicable statutory limitation on assignment of a receivable.

We offer a further explanation of our concerns and suggested language in the appendix hereto.

*Priority in proceeds (article 26)*

The text of article 26 should clarify that the assignee's proceeds interest is not superior to the interest of another assignee in the proceeds themselves if that other assignee's interest in the proceeds (in contrast to its interest in the receivable out of which the proceeds arose) would be superior under

the law of the assignor's jurisdiction. To achieve this clarification, we would suggest adding to article 26 the following:

> "(3) Paragraphs (1) and (2) of this article do not affect the priority of the right of another assignee in the proceeds themselves if the other assignee's right in the proceeds would have priority under the law of the State in which the assignor is located."

*Reservation as to sovereign debtors (article 38)*

Insert "..., or any specified public entities or agencies," after "A State may declare at any time that it...". Because a complete exclusion would significantly limit the benefits of the Convention, it is important to allow States narrowly to tailor the proposed exclusion, if that is in their economic interest, rather than permit only an "all or nothing" choice of a complete exclusion. In some States, public entities are involved in a broad area of transactions.

*Annex (sections I and II)*

Transparency, a particularly important factor in modern capital markets, is implemented in some countries through the use of publicly accessible notice filing (registry) systems, which enable any financing party to be on notice of certain prior rights, and which generally establish priorities between certain claimants. This technique has proven to be a significant factor in expanding credit and lowering rates in those countries where it has been employed. The draft Convention appropriately does not require this technique to be adopted, but rather provides in Annex I, Sections I and II a fully optional approach, which any State can opt into at any time in order to obtain its benefits.

## III. SPECIFIC COMMENTS ON OTHER ISSUES

*Title*

We recommend that the title be "Convention on Assignment of Receivables". The discussions at the Working Group have led us to the view that the term "financing" should be avoided so as to preclude arguments as to scope of application based on which transactions fall within the draft Convention solely because of the differing usages of that term.

*Preamble*

In order to reflect in the principles embodied by the preamble the purposes of this work as often discussed by the Working Group, we recommend that the language of the third paragraph be restated as follows:

> "Desiring to establish principles and adopt rules relating to the assignment of receivables that would create certainty and transparency and promote modernization of law relating to assignments of receivables, including but not limited to assignments used in

factoring, forfaiting, securitization, project financing, and refinancing, and that would facilitate the development of new practices without disrupting existing practices,...",

and that the following sentence be substituted for the fifth paragraph:

"Being of the opinion that the adoption of uniform rules governing assignments of receivables would facilitate the development of international trade and promote the availability of capital and credit at more affordable rates,..."

*Application of the Annex (article 1 (4))*

The language should be clarified to reflect the intention of the Working Group that "applies in" refers to the substantive law of the State whose law is being applied, rather than the law of a forum State in which an action may happen to be maintained.

*"Location" (article 6 (i) (ii))*

The commentary should clarify that "place of central administration" means the chief executive office, i.e. place from which the assignor or assignee manages its affairs, and not a place where books and records are kept or where assets are located. It is to be determined with a view to providing maximum certainty and predictability for those dealing with the assignor or assignee under the draft Convention.

*Gap-filling (article 8 (2))*

The last clause should be amended, or commentary added that clarifies that under this provision, the law applicable as determined by the draft Convention is first applied, and then as necessary the law applicable through general conflicts rules of that jurisdiction.

*Effectiveness of assignment (article 9 (2))*

In order to carry out the purposes of the article, the phrase "at the time a future receivable arises" should be substituted for "at the time of the conclusion of the original contract", which may have been inadvertently carried over from an earlier draft.

*Liability for violation of contractual limitations (articles 11 (2) and 12 (3))*

It is important to clarify the effect of the (identical) second sentences of each article, or alternatively restate them. Both provisions provide a rule negating liability in a specified circumstance. It is very important to make clear that: the draft Convention itself does not create or provide a basis for liability of a person not a party to an anti-assignment agreement; the existence *vel non* of liability of such a person is left to national law; and the purpose, and the sole effect, of these

provisions is to negate liability based solely on the ground of knowledge of the agreement, should that be a sufficient ground for liability under the applicable national law.

*Security and supporting rights (article 12)*

Article 12 refers in four instances to a right "securing" payment. This reference is intended to include personal rights such as a guarantee. Indeed, this is the type of personal right most likely to be the object of this provision. In some States, however, such as the U. S, a guarantee is not a form of security, as it is not a form of right in property; rather, it is, in such systems, a claim properly characterized as a "supporting" obligation. This point can be adequately dealt with by the commentary, making clear the inclusion of such personal rights within the meaning of the article, and, thus, that no change to the text of the draft Convention is required.

*Notification of the assignment (article 19 and other appropriate articles)*

The term "notification of the assignment" is a defined term and refers to a writing that satisfies certain requirements. As a result of differing interpretations by reviewers, references in the official commentary or a textual mark to indicate a defined term should be used to signal that reference is made to the defined term, and not to a general concept of notification, which could otherwise be misunderstood as meaning simply when the debtor learns of the assignment.

*Debtor's discharge (article 19 (2))*

Replace "notification of" with "notifications of assignment indicating to the debtor that". In view of the fact that the rule refers to the first notification received, it applies only when the debtor has received more than one notification.

*Modification of the original contract (article 22 (3))*

The article refers only to modifications agreed between the assignor and the debtor. Thus, there is no way an assignee can incur liability for such conduct. The article should be restated so as to be consistent with that.

*Recovery of payments (article 23)*

The reference to "and the debtor's rights under article 20" is unclear, and could lead to an erroneous interpretation. Article 23 refers to affirmative recovery while article 20 refers only to defenses and rights of set-off. The two provisions are, therefore, incompatible, and the "without prejudice" clause is potentially misleading. The phrase should be deleted. If, however, some reference is nevertheless deemed necessary, an explanation in the commentary would be better. If the text is for some reason deemed necessary, a separate sentence to the following effect would be appropriate: "The debtor's inability to obtain an affirmative recovery under this article does not preclude the debtor's

assertion of a defense or set-off in such amount if the debtor is otherwise entitled to do so under article 20."

*Priority in proceeds (article 26 (2))*

This provision should be revised to make clear that each competitor stands on its own footing. The present wording suggests that an assignee loses to each type of competitor unless it has priority over not only that type but also over all other types. The rewording should make explicit the relevant date for determining whether the condition has been met.

The commentary should make clear that the instructions referred to paragraph (2) (a) of article 26 may be given: at any time, whether at the inception of the assignment transaction or at a later time, such as the assignor's default; as part of the contract of assignment or in a separate document; in specific terms or in general language; and in writing, electronically or in any other manner that is capable of proof.

*Law applicable to the relationship between the assignor and the assignee (article 28)*

Subject to how this chapter finally reads, the bracketed language is important to avoid it being construed as an opening for an override of other provisions of the draft Convention, outside of chapter V, which determine applicable law.

*Relationship with other texts (article 36)*

If the bracketed language is retained, a separate exclusion may be necessary for those aircraft financing transactions in which the receivables are identified with and bound to particular aircraft or engines, in view of industry practices and special laws applicable to aircraft transactions in some States.

*Additional exclusions (article 39)*

This provision should be retained in order to permit adjustments necessary for States to implement the draft Convention's terms. Unnecessary use of this provision would adversely affect the credit ratings of parties within any State, so use of this provision is expected to be self-limiting.

*Application of the annex (article 40)*

In paragraph (1) (a), the term "will" should be replaced by "may", in line with the approach that use of the registration system is optional even for States that choose sections I and II, as indicated in paragraph (1) (b). States may wish to, and would be able to under this formulation, establish their own or use alternative registries. Registries that do not operate efficiently and reliably will not draw credit, so this mechanism while preserving options is also self-correcting.

*Transitional application issues (articles 41 (5), 43(3) and 44 (3))*

The transition provisions are very important, and need to be further tested as to their effect on common paradigms of receivables practice. Commercial lenders need certainty that prior rights will be unaffected, and certainty as to at what point of time new transactions are covered by the draft Convention.

*Registration-based priority provisions (Annex, articles 1 and 2)*

This section should also be amended so as to permit States to provide by declaration further adjustments to articles 1 and 2 as to the manner in which such a notice-filing system is effected as to them.

*Establishment of registry (Annex, article 3)*

We are prepared to work informally at the Commission session or at any subsequent time with other States that are considering joining the new registration regime, in order to prepare the groundwork for internationally-linked notice-filing systems. We would at the same time oppose any provision which would unnecessarily raise costs of and make setting up such system(s) much more difficult, by requiring a diplomatic or other process unsuited to establishing a technical computer-based system. The experience of other international bodies is instructive in this regard. The preliminary draft Unidroit Convention, which will have as an integral part of its structure such a computer-based notice system, will include some brief guidelines, but will leave the establishment of the system to the contracting states after the preliminary draft Unidroit Convention is adopted. Further, as noted in comments to article 40 above, participation in any registry system is wholly optional, and would permit any State to substitute its own registry system, should it so choose.

*Appendix*

*Explanation of comments on articles 9 and 10*

*Bulk and future assignments.* Article 24 might be interpreted to override article 9's validation of bulk and future assignments. This could occur in cases in which the domestic law of the State in which the assignor is located does not recognize such an assignment and, thus, would find the assignment ineffective as against the claim of a competing party or would subordinate the rights of the assignee as against such a party. In those cases, the reference in article 24 to the law of the assignor's State to resolve competing rights of other parties might lead a court to apply that domestic law to reach the conclusion that the assignee of the future receivables has no rights with respect to such parties or is subordinate to them.

To avoid this possible interpretation, we suggest that article 9 be amended by adding the following language:

"(3) A transfer of a receivable is effective, as between the assignor and the assignee, at the time of transfer.

(4) A transfer of a receivable is not ineffective against and may not be subordinated to, a person described in paragraph (1) (a) (i) to (iii) of article 24, solely because law other than this Convention does not generally recognize an assignment described in paragraph (1) or (2)."

The Commentary could make clear that the word "generally" in proposed paragraph (4) is intended to refer to the general provisions of the commercial law of the assignor's country that does not recognize bulk assignments or assignments (whether individual or in bulk) of future receivables, and that the word "generally" is not intended to refer to more specific laws of the assignor's country that, for manifest policy reasons, prohibit the assignments of certain more narrow types or categories of receivables. For example, law prohibiting assignments of future wage receivables as a specific category of receivables would not be law that "generally" does not recognize present assignments of future receivables, because the law relates to only a specific type of category of receivables, not to receivables generically.

*Domestic insolvency law on priorities for post-insolvency receivables.* Articles 9 and 10 could be read to override the domestic insolvency law of the assignor's jurisdiction regarding priorities with respect to receivables arising after the commencement of the insolvency proceeding or earned after the commencement of the insolvency proceeding by the use of unencumbered assets of the insolvency estate. This interpretation could result from applying article 24's deference to matters settled elsewhere in the draft Convention to reach the conclusion that the time-of-transfer rules of article 10 override domestic insolvency laws addressing post-insolvency receivables. We do not believe that this interpretation was the intention of the Working Group. Rather, we believe that the intention of the Working Group, as generally indicated in article 24, was to defer to national insolvency law on the question of to what extent an assigned receivable arising after the commencement of the insolvency proceeding, or earned after the commencement of the insolvency proceeding by the use of unencumbered assets of the insolvency estate, could be set aside by or be subject to the interest of the insolvency administrator.

To avoid this interpretation, we suggest that article 9 be amended by adding the following language:

(_) Whether the transfer of a receivable affects the rights of a person described in paragraph (1) (a) (i) to (iii) of article 24 is determined in accordance with section III of chapter IV.

*Statutory prohibitions on assignment.* Article 9 might be interpreted to abrogate an applicable statute that limits assignment of a receivable by contract. This is because article 9 appears to render *all* contractual assignments "effective".

Addition of the following language to article 9 would preserve applicable statutory prohibitions on assignment without affecting the provisions of articles 11 and 12 addressing contractual prohibitions on assignments:

(_) This article is subject to any applicable statute that prohibits or limits the assignment of a receivable for a reason other than the existence of a contractual prohibition or limitation of such assignment.

*Consolidated text.* We offer the following language as a way to interrelate all three of our text suggestions with one another. The language accomplishing the interrelation is in italics.

Article 9. Effectiveness of bulk assignments, assignments of future receivables, and partial assignments

(3) A transfer of a receivable is effective, as between the assignor and the assignee, at the time of transfer.

(4) A transfer of a receivable is not ineffective against, and may not be subordinated to, a person described in paragraph (1) (a) (i) to (iii) of article 24, solely because law other than this Convention does not generally recognize an assignment described in paragraph (1) or (2).

(5) This article is subject to any applicable statute, other than a statute of the type described in paragraph (4), that prohibits or limits the assignment of a receivable for a reason other than the existence of a contractual prohibition or limitation of such assignment.

(6) *Except as otherwise provided in this article*, whether the transfer of a receivable affects the rights of a person described in paragraph (1) (a) (i) to (iii) of article 24 is determined in accordance with section III of chapter IV.

The italicized language is necessary to except (a) from the clause preserving any statutory prohibitions on assignment, a statute that generally prohibits individual or bulk assignments of future receivables, (b) from the clause requiring priority to be determined under section III of chapter IV, any law that, for purposes of priority, does not generally recognize individual or bulk assignments of future receivables, and (c) from the clause requiring priority to be determined under section III of chapter IV, the effect of any applicable statute that does not permit the assignment by contract of a specific type or category of receivable.

International organizations

INTERNATIONAL SWAPS AND DERIVATIVES ASSOCIATION (ISDA)

[Original: English]

ISDA (International Swaps and Derivatives Association, Inc.)1/ and TBMA (The Bond Market Association)2/ give their support to the arguments set out in the comments of the EBF (European

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1/ ISDA is a global trade association representing more than 450 participants in the privately negotiated derivatives industry, a business which includes swaps, futures and options and combinations of these products relating to a variety of underlying financial and other risks, including interest rates and currency risks. A report of the Bank for International Settlements estimated the total outstanding notional value of four main categories of derivative transaction as at end December 1998 to be US$ 80 trillion and that these transactions had a gross market value at that time of US$ 3.2 trillion. For further information, see ISDA's website (www.isda.org).

2/ TBMA represents securities firms and banks that underwrite, distribute and trade fixed income securities domestically and internationally. These debt securities and related investments include:

Banking Federation) and the FMLG (Financial Markets Lawyers Group). 3/ ISDA and TBMA join the EBF and the FMLG in supporting the aims of the draft Convention. We are concerned, however, about the impact of certain aspects of the draft Convention on certain financial transactions and the contractual provisions underlying those transactions. These concerns are addressed in detail in the comments of the EBF. We support the proposals made by the EBF, with the additional point that we believe it would be appropriate to further narrow the definition of "trade receivable" in article 5, variant B of the EBF's proposed changes to exclude regular securities accounts, such as margin accounts, and debt securities generally.

The purpose of the draft Convention is to lower costs of borrowing and increase access to credit by reducing legal risks. It is important, however, that this goal be accomplished without adversely affecting existing, widely accepted contractual arrangements for certain categories of financial transactions, such as derivatives, repurchase agreements and securities lending arrangements. These transactions are a vital risk reduction tool for financial institutions, companies, governmental entities and other users. These transactions are most often documented under agreements sponsored or co-sponsored by ISDA or the TBMA. These agreements establish a means by which exposures under transactions are effectively netted on close-out. Anything that runs the risk of undermining the enforceability of netting under these agreements is a source of concern to ISDA, TBMA and our members.

ISDA and TBMA are grateful for the opportunity to comment on the draft Convention and are willing to assist UNCITRAL by commenting on any specific provisions as and when drafting is proposed by UNCITRAL.

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Repurchase agreements; U.S. Treasury securities; Federal Agency securities; Mortgage and other asset-backed securities, Corporate Debt securities; Municipal bonds; and Money Market instruments. Further information concerning the Association may be obtained from TBMA's website (www.bondmarkets.com).

3/ See A/CN.9/472/Add.1.