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U n i d r o i t

INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW

STUDY GROUP FOR THE PREPARATION OF UNIFORM RULES
ON THE FACTORING CONTRACT

Working papers considered by the Study Group
during its third session held in Rome from 19 to 21 April 1982

Rome, April 1982

Factoring Group
3rd session
Misc. 1
(Original: English)

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INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW

STUDY GROUP FOR THE PREPARATION OF UNIFORM RULES ON THE
FACTORING CONTRACT

Third session: Rome, 19-21 April 1982

Observations

of Mr Ebbe SUENSON (Denmark), member of the Legal Committee
of Factors Chain International, on the preliminary draft
uniform rules on the factoring contract approved at the
second session of the Study Group

Rome, April 1982

Re: Unidroit's Proposal for Uniform Rules on the Factoring Contract

As a member of the Legal Committee I have studied the above-mentioned proposal and have given my comments below as I would presume this letter is to be distributed to the other members of the Committee.

.....

On page 15, in point 60 it is stated that

"In the opinion of one member of the Group, the text constituted not so much a draft Convention on factoring contracts as one on the validity of assignments of debts and relations with third parties, since scarcely any trace was to be found in the draft of the relations between the two parties to the contract, the supplier and the factor; these were touched on only in Article 1, which is concerned with definitions, and nowhere else. He wondered whether there was not a case for widening the scope of the draft by adding articles dealing with the mutual rights and duties of the parties and by providing answers to the questions of who must give notice to the debtor, when must such notice be given and what happens if it is not given".

This is obviously quite correct and presumably it is connected with the fact that agreements between the two parties to the contract, the supplier and the factor, are made individually and adjusted to the special requirements of the parties, and consequently difficult to force into a uniform international legislation.

The same applies to the agreements between factors in international relations where such agreements are either made individually or generally, as in IFC supplemented by individual interfactor agreements, see also pp. 11-12, points 42 and 43.

Thus the proposal deals exclusively with rules intended to regulate the relations towards a third party, in most cases the debtor, these relations at present being covered by a wide spectrum of national and international rules.

Those who are engaged in international factoring business between members of the FCI and are familiar with the IFC which regulate the relationship between members will soon realize that although everyday practical activities are smoothly settled numerous cases will give cause for many cases of doubt, which may be difficult to solve because of different rules of law prevailing in the member countries.

When the Legal Committee of the FCI starts dealing with a problem it nearly always turns out to entail new problems. A proposal for international rules will therefore have to be either very detailed and presuppose extensive changes in national legislation, changes which will constitute radical breaks with well established national rules of law, or a very generally described proposal the practical effect of which may be said to be limited.

The Study Group has chosen the last-mentioned principle.

Art. 1 describes the activities to be covered by a factoring contract, as e.g. collection of receivables providing that supplier the assign to the factor..... by way of sale or security receivables, see page 6, point 12.

If the factor is only to collect receivables, but not to offer any financing nor assume any credit risk it seems hard to establish the assignment as sale or security.

Art. 3 mentions "the validity of the factoring contract".

What is meant by this?

Is it between the parties or in relation to the debtor, or in relation to the parties' creditors? It could not be taken for granted that the same requirements in respect of validity could be made in all cases.

Art. 4 is important in the sense that it sets aside the debtor's prohibition against assignment of a receivable account, but also in this case the question arises concerning the interpretation of "the assignment shall be effective". Can the debtor be sentenced to pay to the factor? Can the debtor be sentenced to pay again, if he paid to the supplier after he had received notice of the assignment, Art. 6 sect. 2?

Art. 5 deals with "reserving title to the supplier". As it will appear from Art. 10 this means the title to the goods sold.

This seems a very general rule because the rules of law in several countries require more than an assignment of receivables to transfer the title to the goods sold to the factor.

Art. 7, sect. 2 ends with the words "to the extent" It would seem rather obvious that the debtor cannot set-off claims against a third party, but can the debtor set-off claims against the factor, and if so, without regard to the origin of such claims?

In Art. 8 reference is made to Art. 7 which seems misleading as Art. 7 does not mention the cases where the debtor has, in fact, paid.

Concerning Art. 9 I find it reasonable that the Group has considered it preferable to defer any decision, since a conflict between the factor and a third party may be entirely independent of the relations with the supplier. In such a case it would seem unreasonable to apply the law of the place of the supplier.

Art. 10, sect. 1 seems reasonable but is presumably in contravention of the EEC proposed Directive on Products Liability.

Factoring Group
3rd session
Misc. 2
(English only)

U n i d r o i t

INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW

STUDY GROUP FOR THE PREPARATION OF UNIFORM RULES ON THE
FACTORING CONTRACT

Third session: Rome, 19-21 April 1982

REPORT

OF MEETING WITH LEGAL COMMITTEE OF FACTORS CHAIN INTERNATIONAL AT
THE OFFICES OF DISKONT UND KREDIT AG, COUVENSTRASSE 6, DUSSELDORF,
ON MONDAY 7th SEPTEMBER, 1981

Rome, April 1982

REPORT OF MEETING WITH LEGAL COMMITTEE
OF FACTORS CHAIN INTERNATIONAL AT THE
OFFICES OF DISKONT UND KREDIT AG,
COUVENSTRASSE 6, DUSSELDORF, ON
MONDAY 7TH SEPTEMBER, 1981

Present: Roy Goode (representing Unidroit)

Jeroen Kohnstamm

Marco Loni

Peter Moore

Bob Niehorster

Ebbe Suenson

Krister Svedberg

Heinrich Sommer

This proved to be a very useful meeting. Initially, the members of the Committee seemed rather sceptical of the value of the work, but as the discussion progressed they became interested, and appeared to regard several of the provisions of the draft Uniform Rules as potentially helpful in international factoring transactions.

Some constructive criticisms were made of the draft which I promised to refer to the Study Group and which seem to me to merit serious consideration.

Art. 1

In order to make it clear that the services referred to in paragraph 1 are not exhaustive (for example, factors also offer advisory services), the words "(inter alia)" should be inserted in line 3 after "factor of."

In sub-paragraph (b), it was suggested that the word "ordinarily" be inserted before "to be made" so as to allow some flexibility.

The Committee suggested that sub-paragraph (c) be omitted, because in some systems the debtor is told that he can pay the supplier until notice to the contrary.

Art. 3

This was particularly welcomed by the Italian member. Nevertheless, Article 3 contains certain weaknesses which need to be eliminated.

- (1) It should be made clear that the article is concerned solely with relations between the factor and the supplier. This might be done by inserting the words "As between the supplier and the factor" at the beginning of the article.

- (2) The article deals only with the validity of the agreement as a contract, not with its effect as a transfer of rights. Under some systems, a contract to assign future receivables has no proprietary effects, and a separate transfer is necessary after the receivables have come into existence. This, I understand, is the position in Dutch law. On the other hand, English law usually treats a binding obligation to transfer a future asset as if it were a transfer, so that upon the assignor acquiring the asset, the interest in it passes to the assignee by virtue of the agreement, without the need for any new act of transfer. We shall need to consider whether we wish to import this latter principle into the Uniform Rules or whether, on the other hand, we leave it to national law restricting the scope of Article 3 to the contractual effect of the factorin agreement.
- (3) It was also felt that Article 3 should be elaborated so as to make it clear that it validated transfers of receivables to secure an indebtedness of the supplier to the factor not yet in being.

Art. 4

Insert at the beginning of this article: "Subject to compliance with the requirements of paragraph 2 of Article 6".

Art. 6

It was felt desirable to make it clear that a single notification to the debtor in advance stating that all future receivables payable by him to the supplier had been assigned to the factor, without further specification, was not to be considered effective notice of assignment for the purpose of the article.

R.M. Goode

April 1982

Factoring Group
3rd session
Misc. 3
(English only)

U n i d r o i t

INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW

STUDY GROUP FOR THE PREPARATION OF UNIFORM RULES ON THE
FACTORING CONTRACT

Third session: Rome, 19-21 April 1982

UNIDROIT 1981 Draft on International Factoring :

Observations and Proposals by

Mme Bianca CASSANDRO SULPASSO

Istituto di Diritto Commerciale e Industriale della
Università Statale di Milano

Rome, April 1982

Additions and modifications of the articles of the 1981 Preliminary draft

Article 2, paragraph 2 : instead of "at or about the time of sale"
"on the same invoice".

Article 3. I suggest the addition of a 2nd paragraph as follows:

"Future receivables will be ascertainable in particular by the determination in the factoring agreement: a) of the lines of goods or services whose sales are included in the contract, b) of the countries of the customers and, where possible, c) of a list of usual customers the parties have agreed upon".

Article 6.

"For the effectiveness of the assignment against the debtor it is sufficient to give him a written notice by way of registered letter with receipt of the general assignment from the supplier to the factor of the existing and future debts he owes or will owe to that customer. The notice should expressly state that payment has to be made to the factor, who is because of the assignment (or, in the case of a general proxy) the only person entitled to give proper discharge. The same statement will be written on each invoice".

Article 9.

In cases where there is a dispute between the factor and any third party claiming rights on the receivables, priority shall be given to the person who has served notice first to the debtor.

Article 12.

The factoring contract, the interfactors agreement, the notice to the debtor of the general assignment of existing and future debts and each invoice shall state clearly that the assignment will be ruled by the Unidroit Uniform Rules on International Factoring.

1. From a general point of view I would like to stress that the purpose of this project is the preparation of uniform rules on the factoring contract, in particular on international factoring.

We have therefore to bear in mind that it will be necessary in certain cases to introduce into the legislation of one or more of the countries involved in this project, special rules, in particular in respect of the assignment of the receivables to the factor.

This however has been done very rarely up to now, especially because of the fear that a certain modification would not be acceptable in a particular country.

2. In fact the only example of the introduction of a rule which is new for the legislation in some countries, is Article 4. This article provides that assignment of accounts receivables will be effective notwithstanding any provision in the contract of sale prohibiting such assignment.

This is indeed a very important point in the project and the awareness of its innovation in respect of some of the legal systems involved is stressed by the provision of the second paragraph of Article 6. This is the only case in which notice of assignment to the debtor has to contain a specific statement that the assignment will be governed by the Unidroit Uniform Rules.

In my view a general provision for this specific indication should be contained in a separate article and should be referred to not only in the notice to the debtor, but also in the factoring agreement, in the interfactors agreement and on each invoice (see art. 12).

3. There are however, other aspects which require more coordination or, more specifically, the preparation of uniform substantive rules. These rules might in some ways be different from those generally applied in some of the countries involved, but they should be considered in relation to the particular situation of the factoring contract.

Factoring agreements provide indeed for a continuing relationship and for a global assignment of existing and future debts, at least in respect to some specific customers the parties (factor and supplier) have agreed upon. In fact it is common practice in the factoring business to factor all accounts receivables, which the supplier has acquired from the same customer, although factors may limit their assumption of credit risk to a certain amount.

This has direct consequences in solving the following problems:
a) ascertainability of future receivables, b) effectiveness of the assignment in respect to the debtor, c) effectiveness of the assignment in respect of third parties.

A) Ascertainability of future receivables

Future receivables will be ascertainable primarily on the basis of the lines of goods or services sold by the supplier and covered by the factoring agreement and of the countries where the supplier exports his products or services.

However, as in most of the cases future receivables will arise from a continuing relationship between supplier and customers, who have been previously identified, the reference to specific customers in the factoring agreement will help in the ascertainability of future receivables and will be a further ground for the validity of future receivables (1).

B) Effectiveness of the assignment in respect of the debtor

One written notice to the debtor of the general assignment of existing and future debts he owes or will owe to the supplier (possibly by way of registered letter with receipt) will be sufficient to avoid all defences by the debtor based on alleged ignorance of the assignment. It will therefore not be necessary to give notice of the assignment for each receivable. It will in fact be possible to consider valid against the debtor a notice in which it is stated that he has to pay the factor (i.e. the import factor). A legend stamp on each invoice will remind the debtor each time of the continuing existence of the factoring contract.

After the notification of the general assignment the debtor cannot validly pay the supplier. If he does so, he will also be obliged to pay the factor.

B") Effectiveness of the assignment in respect of third parties

It is possible to provide a better protection of factor's rights in respect of third parties claiming rights in the same receivables. In most of the countries involved, problems of priority between assignee and third parties are solved by considering the first notice of assignment to the debtor provided that entitlement to priority can be proved.

(1) See, on this specific problem, E. Cassandro, *Il Factoring in Europa* Giuffrè, Milano 1981, pp. 67 ss.

It is consistent with this premise that Article 6, which deals with notice to the debtor, should include as far as possible all conditions which may entitle the factor to claim priority over third parties including a trustee in bankruptcy or a liquidator.

The modification I suggest for Article 6 follows what is already a common practice of the factoring companies: a) notification of the factoring contract to the debtor with the precise indication of the related consequences on the obligation of the debtor to pay, b) legend stamp on each invoice.

It will be necessary however for notice to the debtor to have a certified date in order to allow the ascertaining of the moment from which: a) the debtor cannot pay the supplier and get proper discharge, b) the factor will take priority over third parties who claim rights in the same receivables on the basis of a subsequent title or a subsequent notice.

For both these purposes notice of the general assignment will be deemed to have been served once it has been sent by registered post with receipt, the date of the receipt being decisive for ascertaining the debtor's bad faith and factor's priority.

Factoring Group
3rd session
Misc. 4
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U n i d r o i t

INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW

STUDY GROUP FOR THE PREPARATION OF UNIFORM RULES ON THE
FACTORING CONTRACT

Third session: Rome, 19-21 April 1982

Proposals by Professor Goode (Rapporteur)
for the revision of Articles 3 and 6
of the preliminary draft articles

Rome, 20 April 1982 (morning)

Article 3

1. As between the supplier and the factor:

- (a) it is sufficient for the validity of the factoring contract that there be an express agreement providing for the assignment by the supplier of existing and future receivables, even though the contract does not specify them individually;
- (b) a provision in the factoring contract by which future receivables are assigned shall have effect according to its terms without the need for any new act of transfer by the supplier after the receivables have come into existence.

2. Subject to paragraph 1, the validity of an assignment of receivables as between the supplier and the factor shall be determined by the law of the State in which the supplier has his principal place of business.

Article 6

1. The assignment shall be effective against the debtor if notice of the assignment to the debtor:

- (a) is given in writing and indicates sufficiently clearly the receivables which have been assigned and the person to whom the debtor is required to make payment; or
- (b) complies with trade usage or with the requirements of the law of the State in which the debtor has his place of business within the meaning of paragraph 1 of Article 2.

2. In the case of an assignment prohibited by the contract of sale, such notice must be in writing and must contain the statement that the assignment is governed by these rules.

3. VARIANT I

A notice of assignment does not comply with the requirements of paragraph 1 (a) of this article unless the receivable to which it relates arises under a contract which is in existence at the time the notice is given.

VARIANT II

A notice of assignment does not comply with the requirements of paragraph 1 (a) of this article unless it identifies the contract under which the receivable to which the notice relates arises.

4. If the debtor in good faith and without notice of any other person's right to payment of a receivable makes payment to the factor pursuant to a notice of assignment given by the supplier or by the factor with the supplier's actual or apparent authority, the payment shall be effective to discharge the debtor's liability pro tanto even if :

(a) the receivable had not been validly assigned by the supplier to the factor; or

(b) the right to payment of the receivable was vested in a third party.

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3rd session
Misc. 5
(Original: English)

U n i d r o i t

INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW

STUDY GROUP FOR THE PREPARATION OF UNIFORM RULES ON THE
FACTORING CONTRACT

Third session: Rome, 19-21 April 1982

Proposals by the Drafting Committee

Rome, 21 April 1982 (morning)

Provisional text of preliminary draft uniform rules on certain
aspects of international factoring

Article 1

1. For the purpose of the present rules, "factoring contract" means a contract concluded between one party (the supplier) and another party (the factor) by which the factor is to provide one or more of the services specified in paragraph 2 and the supplier is to assign to the factor on a continuing basis, by way of sale or security, receivables arising from the sale of goods.

2. The services referred to in paragraph 1 are finance, the maintenance of accounts, the collection of receivables and protection against credit risks.

3. In these rules references to "sale of goods" and "sale" shall, except as otherwise indicated, include the supply of services.

Article 2

1. The present rules shall apply in relation to international factoring contracts, that is to say, factoring contracts relating, wholly or in part, to receivables arising from a contract for the sale of goods between parties whose places of business are situated in different States. Where a party has more than one place of business, his place of business for the purpose of this article shall be that having the closest relationship to the contract of sale and its performance.

2. The present rules shall apply only in relation to factoring contracts pursuant to which:

(a) the receivables to be assigned arise from the sale of goods to trade or professional debtors, and

(b) notice of assignment of the receivables is to be given to debtors.

Article 3

As between the supplier and the factor:

- (a) a contractual provision for the assignment by the supplier of existing or future receivables shall be valid, even though the contract does not specify them individually, if they are so described that at the time when they come into existence they can be identified as falling within the contract;
- (b) a provision in the factoring contract by which future receivables are assigned shall have effect according to its terms without the need for any new act of transfer by the supplier after the receivables have come into existence.

Article 4

The assignment of a receivable by the supplier to the factor shall be effective notwithstanding any provision in the contract of sale prohibiting such assignment.

Article 5

The factoring contract or an assignment made pursuant to it may validly provide for the transfer, automatic or otherwise, to the factor of all or any of the supplier's rights under the contract of sale, including any provision in such contract reserving to the supplier the title to the goods.

Article 6

1. Subject to paragraph 2 of this article, the assignment shall be effective against the debtor if notice of the assignment to the debtor:

- (a) complies with the requirements of the law of the State in which the debtor has his place of business within the meaning of paragraph 1 of Article 2; and
- (b) states that the assignment is governed by these rules.

2. A notice of assignment shall be effective for the purpose of paragraph 1 of this article only in relation to a receivable arising under a contract which has been concluded at or before the time the notice is given.

Article 7

If the debtor in good faith and without having reason to know of any other person's right to payment of a receivable makes payment to the factor pursuant to a notice of assignment given by the supplier or by the factor with the supplier's actual or apparent authority, the payment shall be effective to discharge the debtor's liability pro tanto even if :

- (a) the receivable had not been validly assigned by the supplier to the factor; or
- (b) the right to payment of the receivable was vested in a third party.

Article 8

1. Subject to Article 4, in a claim by the factor against the debtor for payment of a receivable arising under a contract of sale the debtor may set up against the factor all defences of which the debtor could have availed himself under that contract if such claim had been made by the supplier.

2. The debtor may also exercise against the factor any right of set-off in respect of claims existing and available to the debtor against the supplier at the time the debtor received notice of the assignment.

Article 9

Non-performance or defective or late performance of the contract of sale by the supplier shall not entitle the debtor to recover, otherwise than as permitted by Article 8, money paid by the debtor to the factor.

Article 10

1. The factor shall not, by reason only of transfer of title to goods to the factor as provided by Article 5, incur liability to a third party for loss, injury or damage caused by the goods.

2. Nothing in this article shall affect the liability of the factor where he sells or otherwise disposes of the goods to a third party who is not the supplier or another factor.

Article 11

The present rules shall also apply to subsequent assignments of the receivables by the factor to another factor as if the first factor were the supplier, whether the establishments of the factors are situated in the same State or in different States.