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INTERNATIONAL INSTITUTE FOR THE UNIFICATION OF PRIVATE LAW

COMMITTEE OF GOVERNMENTAL EXPERTS FOR THE PREPARATION OF A DRAFT  
CONVENTION ON CERTAIN ASPECTS OF INTERNATIONAL FACTORING

Commentary prepared by the Secretariat on the text of the preliminary  
draft Convention on certain aspects of international factoring drawn  
up by the committee of governmental experts at its first session held  
in Rome from 22 to 25 April 1985

Rome, July 1985

## BACKGROUND TO THE PRELIMINARY DRAFT CONVENTION

1. At its 53<sup>rd</sup> session, held in Rome from 4 to 7 February 1974, the Governing Council of Unidroit decided on the basis of a memorandum submitted by the Secretariat to include in the Work Programme for the triennial period 1975 to 1977 the subject of the assignment of debts in general and more particularly that of the contract of factoring. It also asked the Secretariat to present a preliminary study on the contract which would give the Council the possibility to take a decision on the order of priority to be accorded to this topic with a view to the elaboration of uniform rules. (1)

2. The Governing Council was seized of the preliminary report prepared by the Secretariat (2) at its 55<sup>th</sup> session, held in Rome on 16 and 17 September 1976, on which occasion it authorised a wider distribution of the report and accompanying questionnaire, especially to practitioners (3) so that a decision might be taken at its 56<sup>th</sup> session on whether steps should be taken towards the convening of a study group or a committee of governmental experts to work out uniform rules on the contract of factoring. At that session, held in Rome on 19 and 20 May 1977, it decided to set up a restricted group of members of the Governing Council, perhaps assisted by one or more experts on factoring, to examine an analysis of the replies (4) to the questionnaire. (5) The restricted group concluded, inter alia, that it would be desirable to elaborate uniform rules on factoring given the significance of factoring as a new method of financing international trade which is capable of responding to needs which other financing techniques fail to meet to the same extent, and also considered that the uniform rules should, initially at least, be restricted to international factoring although it was suggested that rules on international factoring would not fail to influence the various domestic laws. (6)

3. The detailed conclusions of the group were brought to the attention of the Governing Council at its 57<sup>th</sup> session, held in Rome from 5 to 7 April 1978 (7), and in accordance with the powers conferred upon him by the Council the President of the Institute constituted a study group for

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- (1) Minutes of the 53<sup>rd</sup> session of the Governing Council, p. 20.
  - (2) UNIDROIT 1976, Study LVIII - Doc. 1.
  - (3) Minutes of the 55<sup>th</sup> session of the Governing Council, p. 44.
  - (4) UNIDROIT 1977, Study LVIII - Doc. 3.
  - (5) Minutes of the 56<sup>th</sup> session of the Governing Council, p. 33.
  - (6) See UNIDROIT 1978, Study LVIII - Doc. 4 for the report on the session.
  - (7) Minutes of the 57<sup>th</sup> session of the Governing Council, pp. 20-23.

the preparation of uniform rules on the factoring contract. The study group held three sessions in Rome, the first on 5 and 6 February 1979, the second from 27 to 29 April 1981 and the third from 19 to 21 April 1982 (8). At the conclusion of that session the study group adopted the preliminary draft uniform rules on certain aspects of international factoring.

4. At its 62<sup>nd</sup> session, held in Rome from 4 to 7 May 1983, the Governing Council approved the draft rules and decided to communicate the text of the preliminary draft, together with an explanatory report prepared by the Secretariat (10), to the Governments of the member States, with a request for observations so as to permit the Council to take a decision as to whether a committee of governmental experts should be convened to continue work on the subject (9). In the light of the observations received from seven Governments the Governing Council decided at its 63<sup>rd</sup> session, held from 2 to 4 May 1984, to set up a committee of governmental experts for the preparation of a draft Convention on certain aspects of international factoring. (11).

5. The first session of the committee was held in Rome at the seat of the Institute from 22 to 25 April 1985. It was attended by representatives of 20 member States of the Institute, one non-member State, one intergovernmental organisation and four non-governmental international organisations. (12) After electing as its Chairman Mr Royston M. GOODE (United Kingdom), the committee proceeded to the first reading of the preliminary draft rules on certain aspects of international factoring. A drafting committee, composed of the Chairman of the committee of governmental experts and of the French and Swedish representatives, adapted the text to take account of the amendments made to it by the committee during the first reading and the revised version was considered in the course of a second reading which the committee completed during the session. The new text of the preliminary draft Convention on certain aspects of international factoring, prepared by the Secretariat on the basis of the decisions taken by the committee of governmental experts on the occasion of the second reading of the preliminary draft rules, is contained in the Annex to this commentary.

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(8) The reports on the three sessions are contained in UNIDROIT 1979, Study LVIII - Doc. 7, UNIDROIT 1981, Study LVIII - Doc. 10 and UNIDROIT 1982, Study LVIII - Doc. 13 respectively.

(9) Minutes of the 62<sup>nd</sup> session of the Governing Council, p. 12.

(10) UNIDROIT 1983, Study LVIII - Doc. 16 for the text of the preliminary draft rules adopted by the study group and the explanatory report.

(11) Minutes of the 63<sup>rd</sup> session of the Governing Council, p. 39.

(12) UNIDROIT 1985, Study LVIII - Doc. 19 for the list of participants.

## II

### GENERAL CONSIDERATIONS

6. Although it has a long history in the United States of America, factoring as it is understood today is a comparatively recent phenomenon outside North America and especially in those countries which do not have a Common Law tradition. In these circumstances a few introductory remarks explaining the nature of factoring operations and their spectacular growth over the last twenty years or so would seem to be in order. (13)

7. Factoring is without doubt today one of the most effective ways for a small or medium size business selling raw materials or consumer goods or providing services to finance the trade credit it grants to its customers. True, it may rely on its own resources or on credit provided by the bank or on that available from its own suppliers but inflation coupled with high interest rates and the current low supply of risk capital have led many businessmen to seek alternative forms of financing such as factoring, with the many services which it offers.

8. The concept of factoring, it has been pointed out, is simple in that it is a continuing arrangement whereby a finance company, the factor, purchases or takes a security over the trade debts of a merchant, manufacturer or provider of services, the supplier, and in most cases undertakes to recover the debts from the latter's customers. Usually notice of the transfer of the debts (receivables) which is in most countries accomplished by their assignment, will be given to the customers of the supplier on the invoice together with instructions to pay the factor. Again it is frequent for the factor to make no provision for recourse against the supplier in the event of the insolvency of the customer, subject to his approval of the latter's credit standing, and it is also usual for the factor to relieve the supplier of the burden of keeping the accounts. In addition to the supplier's paying the factor for these services a fee which ranges from a fraction of 1% to some 2% of the face value of the invoice representing each debt, the supplier may also pay the factor a discounting charge, in return for which he obtains a substantial part of the receivables arising from each debt

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(13) Paragraphs 7 to 10 owe much to a paper by Mr Frederick R. Salinger, Director of Anglo-Factoring Services, Ltd., which appears as Chapter 26 in the present edition of Sheldon and Fidler's "Practice and Law of Banking".

as soon as the goods have been sold and delivered, the remainder (usually some 20%) being retained by the factor until the customer pays or until a date calculated by reference to the average period of credit taken by the supplier's customers. The amount retained by the factor may be set off by him against his rights in regard to disputes or claims raised by customers.

9. As a rule, the factoring contract concluded between the supplier and the factor, whereby the supplier undertakes to assign or actually assigns his trade debts to the factor, will be of a duration of at least one year. The factor will decide whether he will purchase the debts of a given customer as well as determining any credit limit he may establish in respect of such a customer. As stated above, the supplier's invoice will in the case of notification factoring give notice to the customer of the assignment to the factor with instructions to pay him. Copies of the invoice will be sent to the factor who will credit the supplier with the value of the invoices (less his charges) and debit the accounts of the customers, the supplier being free to draw on the credit in his account subject to the arrangements with the factor.

10. Finally in this brief exposé of the rudiments of factoring, it should be recalled that while the factor will normally accept responsibility for payment of debts arising from the insolvency of a customer, always provided that the supplier has not exceeded his credit limit or that the supplier is not in breach of his undertaking that the receivables accepted by him are free from rights of set-off by his customers, the factor will not accept responsibility for any breach of contract by the supplier against his customer, for example by non-performance, defective or late performance, or for the accuracy of any invoices and credit notes which have been issued.

11. If the mechanics of factoring operations are relatively straightforward, the converse is true in many countries of the law applicable to them. As is the case with leasing, in respect of which a draft Convention is ~~also~~ under preparation within Unidroit, it has often been necessary to adapt the development of factoring to conform to a preexisting legal framework which was not designed to accommodate it. The attendant difficulties in the various legal systems are still further exacerbated in international factoring, not only by the wide variations in national law but also by the frequent uncertainty as to which law will apply.

12. It is in these circumstances that the committee of governmental experts fully endorsed the opinion of the study group that it would be desirable to work out uniform rules on factoring. It also agreed with the proposal of the study group to restrict the scope of application of the rules to international factoring, that is to say to cases where the contract for the sale of goods or the supply of services under which the receivables to be factored arise is concluded between parties with places of business in different States. It considered in effect that such a limitation would be conducive to the acceptance of the uniform rules by a greater number of States for while it might be desirable in theory to contemplate the preparation of uniform rules on factoring at national as well as international level, there would well be a strong reluctance on the part of many States to accept changes to well-established principles of law which are of much more general application than simply to factoring operations.

13. As a result of the decision to limit the scope of application to international factoring, the committee decided to cast the uniform rules in the form of a convention: it was emphasized that this would not exclude its influence as a model law and that those States which so wished might take the principles contained in the international rules as a basis for the regulation of domestic transactions. However, with a view to encouraging States to apply the provisions of the Convention to purely national relations, reference was made to the possibility of including in the final clauses a provision along the lines of Article 30 of the 1983 Convention on agency in the international sale of goods, paragraph 1 of which provides that a Contracting State may at any time declare that it will apply the provisions of the Convention to specified cases falling outside its sphere of application. Finally, the choice of the form of a convention has entailed the inclusion of a preamble, as well as of draft final clauses which will be prepared by the Secretariat; on the other hand, the territorial scope of application has been amended and the two criteria determining the applicability of the draft Convention now refer to Contracting States.

14. A further observation should be made concerning the general purpose of the Convention under preparation, namely that the rules seek to interfere as little as possible with the contractual relations of suppliers and factors and of factors inter se. Generally speaking it was acknowledged that the regulation of these relations is best left to the parties, between whom many practices and customs have grown up, a large number of which have been embodied in general conditions to be found in the agreements concluded between suppliers and factors and in the arrangements concluded between factors themselves. Moreover the rules do not attempt to regulate the validity of the factoring contract itself, which should be determined by the applicable law, that is to say usually by the law of the State where the

supplier and the factor (in international transactions normally the export factor) have their places of business. What is on the other hand contemplated is the specific question of the assignment of receivables in the context of factoring transactions with a view to encouraging the development of factoring as an instrument for the promotion of international trade, while having due regard to the interests of the parties. The scope of application is regulated in the first two articles of the draft Convention: first the substantive scope with the definition of the factoring contract whose characteristics are set out in the introductory language of Article 2, and then the territorial scope dealt with in the two sub-paragraphs of that article.

15. The first point dealt with in the draft Convention relates to the validity of assignments of receivables between the supplier and the factor: Article 3 removes certain obstacles to the validity of assignments of future receivables and dispenses with the need for a new act of transfer in respect of such receivables after they have come into existence, as distinct from provisions in the factoring contract assigning them, while Article 4, which is a highly controversial provision and whose retention is still open to question, affirms the possibility of the receivables being assigned notwithstanding an agreement between the supplier and the debtor prohibiting such assignment. Article 5 makes provision for the validity of the transfer of the supplier's rights deriving from the sale of goods, including the benefit of any reservation of title clause, whether that transfer be made with or without a new act of transfer.

16. The second matter regulated is the extent to which the assignment will be effective against the debtor and concerns therefore the relations between the factor and the debtor following such assignment. Paragraph 1 of Article 6 sets out the formalities which must be satisfied if the notification of the assignment to the debtor is to be effective; paragraph 2 lays down the conditions for the validity of the payment by the debtor while Article 7 determines the extent to which the debtor may set up against the factor defences which he had against the supplier. Article 8 also concerns the effects of the assignment but only in relation to the factor and it governs the special situation where the factor acquires ownership of goods as a result of the transfer of a reservation of title clause: in such cases, and on condition that he does not dispose of the goods or that he is not liable under an international agreement, it is provided that he will not incur liability to a third party for damage caused by the goods.

17. Finally Article 9, which the committee agreed to be in need of redrafting so as to ensure its compatibility with the other provisions of the draft, is concerned with the case where the parties to the factoring contract are no longer the supplier and the export factor but two factors.

The final articles of the draft Convention, Articles 10 and 11, relate respectively to the question of which provisions of the draft are to be regarded as mandatory and to the rules of interpretation of the provisions of the Convention under preparation.

18. In conclusion it should be recalled that the study group had discussed at length the question of whether the rules should also include provisions dealing with cases of conflicting claims of the factor and third parties over receivables. In this connection it had noted that there exist wide discrepancies in approach from one country to another, some systems granting priority to the first assignee of a receivable, others to the first assignment to be notified to, or accepted by, the debtor, or alternatively to the first of which the debtor receives notice, and yet others to the first to be filed in a public register. In addition, the possibility of laying down an acceptable uniform rule of a substantive character in this connection would seem to be even less likely if one bore in mind the variety of situations in which priority questions could arise and therefore the only prospect of success seemed to lie in solving the problem on the basis of a conflicts of law rule. Here again however insuperable problems were encountered in the elaboration of a uniform rule, given the difficulties in determining the connecting factor as the priority question might, according to the circumstances, be characterized as one relating to the law of contract, tort law, the law of property, quasi-contract, equitable rights, restitution etc. In these circumstances the study group had decided that it would regrettably have to leave the whole problem of priorities between the factor and third parties to be decided in accordance with whatever might be the applicable national law and this approach was endorsed by the committee of governmental experts.



III

COMMENTARY ON THE PROVISIONS OF THE PRELIMINARY DRAFT CONVENTION ON

CERTAIN ASPECTS OF INTERNATIONAL FACTORING

19. As regards the title of the rules under preparation, it will be seen that the term "Convention" has replaced that of "uniform rules" in accordance with the decision of the committee of experts regarding the final form to be given to the instrument (see above, paragraph 13). In addition, a change has been made in the language of the French text with a view to avoiding the use of English terminology where there exists a well established French translation. However, since the technique of financing in the process of regulation is better known under the name of "factoring", this word is included in parenthesis after the term "affacturage" in the preamble. On the other hand, the word "factor" which appears in Article 1 has no strict equivalent in French and after due consideration the French delegation proposed that it be translated by the words "l'entreprise d'affacturage" which, for reasons of convenience, is designated by the term "cessionnaire" in the articles of the draft Convention. (14)

20. The committee considered it appropriate at this stage to include a draft preamble, the first two paragraphs of which have been taken over from the preamble to the draft Convention on international leasing which is also under preparation within Unidroit. The declared aims are to provide a legal framework to facilitate international factoring while maintaining a fair balance of interests between the different parties involved in factoring transactions. The last paragraph reproduces almost word for word the corresponding provision of the preamble to the 1980 United Nations Convention on contracts for the international sale of goods (hereafter referred to as the "Vienna Sales Convention") which was also included in the 1983 Convention on agency in the international sale of goods and which refers to the development of international trade while taking account of the different social, economic and legal systems.

Article 1

21. As has already been indicated above in the general considerations, one of the primary concerns of the study group and subsequently the committee of governmental experts was to permit the free growth of factoring as a technique for financing international trade. In the absence of a defini-

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(14) In the French version of the commentary, reference will be made without distinction to "factoring" and to "affacturage", and to the "factor" and to the "entreprise d'affacturage" or to the "cessionnaire".

tion of factoring in national laws, as wide a definition as possible has been sought in the Convention so as not to hinder the expansion of activities which already are, or may be, regarded as factoring in certain countries. Thus the possibility of limiting the application of the rules to recourse factoring or of fixing a maximum time-limit for the credit granted to the buyer under the sales contract to which the receivables relate was ultimately rejected. The definition in Article 1 attempts therefore to identify what may be considered to be the lowest common denominator in factoring contracts and after indicating the parties to the factoring contract, namely the supplier on the one hand and the factor on the other, paragraph 1 sets out the respective duties of the parties in their contractual relations and lays down the condition that the assignment of the receivables must be notified to the debtor.

22. Sub-paragraph (a) indicates the obligation of the supplier towards the factor, namely the assignment of the receivables in respect of which three conditions must be satisfied. The first concerns the nature of the assignment which must be effected by way of sale or security, that is to say that there must either be an outright sale of the receivables or a loan of money on the security of the receivables. The two other conditions relate to the receivables themselves, and it may perhaps be useful to mention that Article 2, which determines the international character of factoring transactions, and Article 3 which is concerned with the validity of the assignment of existing and future receivables, also deal with certain questions regarding the receivables. In the first place the receivables assigned must arise from contracts for the sale of goods and in accordance with paragraph 2 of Article 1 these include also, where appropriate, contracts for the supply of services. Furthermore, the contracts which give rise to the receivables must be concluded between the supplier and his customers in the course of business. The intention of this language is to exclude the application of the rules to the factoring of receivables arising from consumer sales and the new wording of this provision is designed to indicate clearly that the commercial character of the parties to the sales contract is not sufficient and that the latter must be concluded in the exercise of their commercial activity. Finally, two remarks should be made concerning the terminology employed in the English text: the term "customer" to denote the debtor in the underlying contract of sale was chosen so as to avoid any doubts arising in the minds of United States lawyers for whom the word "debtor" normally signifies the supplier as the debtor of the factor under his contract with the latter, the supplier's customer most often being referred to as an "accounts debtor". On the other hand, it was suggested that the term "receivables" might cause problems as the expression "accounts receivable" was more familiar in certain countries, and a proposal was made to include a definition of what is meant by "receivable", perhaps by taking over that to be found in the United States Uniform Commercial Code.

23. The effect of sub-paragraph (b) of Article 1, paragraph 1 is to exclude from the field of application of the future Convention non-notification factoring, a technique often preferred by suppliers who do not wish their customers to know that they have assigned the receivables: this important restriction which derogates from the declared principle of embracing the most diverse forms of factoring is justified, according to some, by the fact that non-notification factoring is in effect rather a form of "invoice discounting", and in any event on account of the different problems which arise according to whether or not the assignment has been notified, especially in connection with the rights of the debtor. This provision, which in Article 1 lays down an indispensable element of the factoring contract for the purposes of the draft Convention, is completed in Article 6 which determines the method of giving notice and, together with Article 7, its effects.

24. Sub-paragraph (a) having set out the supplier's obligation to the factor, sub-paragraph (c) of Article 1, paragraph 1 deals with the duties of the factor. In practice, factors provide a series of widely differing services; however it seemed that only four of the services to be found most frequently in factoring transactions needed to be mentioned, namely finance, maintenance of accounts, collection of receivables and protection against credit risks. For the contract between the supplier and the factor to be considered to be a factoring contract for the purposes of the future Convention, at least two of these services must be provided: in fact since none of them taken individually is characteristic of factoring transactions, each may be absent from a factoring contract. It has been pointed out that the provision contained in sub-paragraph (c) would have the effect of excluding from the scope of the rules certain "bulk factoring" operations under which the factor is required to give notice to the debtor of the assignment to him of receivables by the supplier but is only responsible for financing. As to the different services mentioned, the question was raised in the committee of governmental experts of whether the collection of receivables by the factor did not naturally follow from the fact that the receivables had been transferred to him by way of ownership or security. Furthermore, it was observed that if the two services provided were collection and the maintenance of accounts, it might be open to question whether the operation could indeed be considered to be a factoring transaction. To this it was replied that the requirement under sub-paragraph (c) was additional to that in sub-paragraph (a) that the receivables have been assigned by way of sale or security, sub-paragraphs (a), (b) and (c) laying down cumulative conditions, and that the situation contemplated was not rare in practice.

25. Finally, in connection with Article 1, it should be indicated that the text submitted to the committee of governmental experts provided that the assignment by the supplier to the factor should be "on a continuing basis". Those words have now been deleted by the committee which was

of the opinion that the continuing relationship resulted impliedly from the services provided by the factor as well as from the formulation of subparagraph (a) which refers to "contracts... made". Furthermore, the committee was concerned to allow a maximum of flexibility so as not to exclude certain transactions which a strict interpretation of the words "on a continuing basis" would have left outside the scope of application of the draft Convention.

## Article 2

26. Article 2, the structure of which is based on that of Article 1, paragraph 1 of the Vienna Sales Convention, contains two kinds of provisions. The first determines the substantive scope of application which Article 1 had limited to factoring contracts: thereafter, the introductory words of Article 2 restrict the scope of application of the future Convention to the factoring of international receivables. This approach was decided on by the committee as it facilitates the application of the rules in the draft to domestic transactions for those States which might wish to incorporate its provisions in their national law. On the other hand, Article 2 includes provisions which are intended to determine the territorial scope of application of the future Convention and sets out the connecting factors for its application.

27. The introduction to Article 2 provides that the Convention applies to a factoring contract in so far as it relates to receivables arising from a contract of sale of goods between a supplier and a debtor whose places of business are in different States. Since one of the principal aims of the proposed Convention is the facilitation of factoring as a technique of financing international trade, it is the commercial relationship giving rise to the factoring contract to which regard is had when determining the international character of the transaction governed by the rules, independently of the place of business of the factor: in practice the latter will, when he is the export factor, most frequently be in the same country as the supplier and in that of the debtor when he is the import factor. The definition of the international character of the contract of sale of goods (or where appropriate the supply of services) is taken over from Article 1, paragraph 1 of the Vienna Sales Convention: it must however be emphasized that the elements pointing to the existence of an international contract of sale are not intended to constitute a definition of an international contract of sale but merely to reflect the mechanics of international factoring as understood by factors themselves in their activities. Finally, some explanation should be given of the words "in so far as" which the committee substituted for the previous formulation so as to make it clear that the future Convention will apply only to receivables arising from international transactions which are assigned to the factor in the context of a factoring contract and not to receivables deriving from domestic transactions which might be assigned under the same contract.

28. The determination of the connecting factors for the purpose of the application of the Convention is a consequence of the form chosen for the rules under preparation and gave rise to lengthy discussion in the committee. The complicated nature of this question results in part from the fact that it is intended to deal only with international transactions but above all from the complexity of the situation under consideration which involves two contractual relationships. In fact, the "foreign" aspect of the factoring contract, which is itself most often purely national in character, is to be found in the contract of sale. Furthermore, the draft Convention contains provisions governing certain effects of the sales contract on the factor and others which concern the effects of the assignment on the debtor. Moreover, the committee was concerned that while the Convention should have as extensive a scope of application as possible so as to cover a wide range of transactions, this should not cause any prejudice to the legitimate interests of the parties involved. These various considerations finally led to the committee adopting the solution contained in the two sub-paragraphs of Article 2: sub-paragraph (a) lays down the objective criteria of the place of business of the parties so as to confer on the Convention an autonomous scope of application, which is evidently desirable for an instrument unifying rules of substantive law. The committee emphasized that an objective connecting factor would ensure greater security and speed in commercial transactions, two prerequisites for international factoring. Sub-paragraph (a) therefore provides that the Convention will apply to the assignment of international receivables when the supplier, the debtor and the factor have their places of business in Contracting States: this solution seemed to be the one which guaranteed the best protection of the interests of each of the parties concerned in factoring transactions and in particular of the debtor who, although not a party to the factoring contract, might find his position altered by the assignment and who must in consequence know which law will be applicable. Sub-paragraph (b) on the other hand provides an alternative ground for the application of the Convention based on conflicts rules: thus when the conditions laid down in sub-paragraph (a) are not met, the Convention will still apply when the rules of private international law lead to the application to the factoring contract and to the contract of sale of goods of the law of a Contracting State. The considerations which militated in favour of the choice of the two contracts are the same as those which led the committee to retain the place of business of the debtor among the relevant criteria set out in sub-paragraph (a).

29. It should be noted that the text submitted to the committee of experts contained a provision indicating the place of business to which regard should be had for the transaction in question in respect of parties with more than one place of business. The solution adopted by the committee on first reading was that contained in the corresponding provision

of the Vienna Sales Convention. It was, however, decided to reconsider the wording of this rule once the principle concerning the sphere of application had been settled. In the absence of any further discussion within the committee the text drawn up subsequent to the session of the committee of governmental experts contains no provision covering cases where one of the parties to the contract of sale or to the factoring contract has more than one place of business. The final remark concerning Article 2 relates to its drafting: whereas the English version provides that "This Convention applies in relation to a factoring contract", the French text states that "La présente Convention s'applique à un contrat d'affacturage"; although the drafting committee which met during the first session of the committee of governmental experts noted that the two versions were not identical and that this might give rise to confusion as regards the scope of application of the future Convention, it was decided to come back to the point later.

### Article 3

30. Article 3 completes the provisions of sub-paragraph (a) of Article 1, paragraph 1 as regards the questions of the manner and validity of the assignment of receivables by the supplier to the factor: in effect, after affirming the validity of a clause in a factoring contract making provision for a global assignment of receivables (provided that they are sufficiently identified), it indicates the effects of such a clause, namely the transfer of the receivables as from the time when they come into existence. This article, as adopted by the committee of governmental experts at its first session, shows only slight changes from the version prepared by the study group: some amendments, essentially of a drafting nature were introduced so as to bring out more clearly the guiding principles underlying these provisions.

31. The introductory wording limits the scope of the rules which follow to relations between the parties to the factoring contract: this formulation was preferred to an express designation of those parties so as to avoid any ambiguity as to the scope of the article in certain legal systems where the term "supplier" might be understood as possibly including a trustee in bankruptcy carrying on the supplier's business. In consequence, and in accordance with the decision of the committee to leave outside the rules under preparation any questions touching upon the problem of priorities between the factor and third parties with regard to the receivables, Article 3 is concerned exclusively with the relations inter partes.

32. Sub-paragraph (a) seeks to overcome the difficulties existing in some legal systems regarding the possibility of assigning future receivables since an agreement to assign such receivables, let alone their effective

assignment, might not be valid on account of the absence of any indication of their subject matter by a sufficient identification of the receivables. As it stands, the sub-paragraph states that a contractual provision for the assignment of existing or future receivables is valid, even though the contract does not specify them individually, if at the time when they come into existence they can be identified as falling within the contract. So as to leave the provision as flexible as possible with a view to facilitating international factoring transactions, the committee preferred not to lay down criteria governing the question of whether the required condition has been satisfied which is in consequence left to the appreciation of the judge in each individual case. It was however suggested by way of example that considerations which might be relevant in deciding whether future receivables can, in accordance with Article 3 (a), be identified from the time they come into existence as falling within the factoring contract, are the line of goods or services whose sale is included in the contract, the countries of the customers or, possibly, a list of usual customers the supplier and the factor have agreed upon. It is however clear that under no circumstances does the provision permit the assignment of receivables which are uncertain.

33. It should be noted with regard to sub-paragraph (b) that it constitutes a considerable advance over certain national laws in the direction of stimulating factoring by establishing the rule that a provision in the factoring contract by which future receivables are assigned operates to transfer the receivables to the factor when they come into existence without the need for any new act of transfer. While this provision reflects the law of a certain number of States, even though in some of them it is not uncommon for a new assignment to be made purely for evidentiary purposes so as to avoid the need for the whole factoring contract to be exhibited in court, in other legal systems an act of assignment relating to specifically designated receivables distinct from the factoring contract itself is necessary for an effective assignment of the receivables to the factor. It was for those legal systems which do not recognize the global assignment of future receivables that the committee considered that it would be desirable to clarify the moment at which the transfer becomes operative so as to permit the determination, always independently of the question of priorities, of the time as from which the factor will become entitled to certain rights. It should moreover be recalled that in accordance with the general scope of application of the future Convention the rule laid down in Article 3 does not affect the rules of national law relating to assignments of receivables arising out of domestic operations. Finally, it should be borne in mind that Article 3 is not concerned with the formal requirements for an assignment in the sense of what is necessary to make a valid assignment under national law. These questions will continue to be regulated by the law applicable to the assignment between

the supplier and the export factor, or between the export and the import factor in the event of a second assignment.

#### Article 4

34. The text of Article 4 as submitted in the preliminary draft to the committee of governmental experts had been the subject of lengthy discussion in the study group where some opposition had been encountered in its regard but the group had nevertheless adopted it, recognizing that it was one of the most important and novel provisions of the draft. This article provides that the assignment of a receivable by the supplier to the factor may be effective notwithstanding any agreement between the supplier and the debtor prohibiting such assignment. For its part, the committee of governmental experts was divided on the question of whether the provision should be retained: a slender majority of representatives who were certainly prepared to recognize the value of a provision of this kind in a Convention aimed at the development of international factoring transactions emphasized however that it constituted a derogation from the principle of party autonomy and that it was in consequence unacceptable even if its application were limited to international transactions; moreover they pointed out that it would be to the advantage of the factor while there might be good reasons for the debtor to prohibit assignment. On the other hand, the provision was supported by a certain number of delegates who, it should be noted, represented either countries which already had such a provision in their law (in particular the United States of America) or which applied the contrary rule to domestic transactions by giving effect to the prohibition on assignment, but who could accept the provisions of Article 4 in respect of international relations. They observed that the article was of the utmost importance for the promotion of international factoring and that it would increase the certainty of operations as the factor would not have to devote a large amount of time to consulting the sales contracts; they further laid stress on the fact that the rule would facilitate the provision of credit to the supplier, insisting also that at present some large companies often take advantage of their position to impose their standard contracts containing such a prohibition on small suppliers who, by reason of their limited financial capacity, are normally those who have the greatest need of the services offered by factoring companies. They furthermore recognized that this provision was in the interest of the factor but they believed that, unlike the assignment of debts, the assignment of receivables would cause no prejudice to the debtor: the latter was in any event protected by Article 7 since he could set up against the factor any defences deriving from the contract of sale and exercise any right of set-off in relation to rights existing at the time he received notice of the assignment. In conclusion, they recalled that the rule would in no way prevent the debtor recovering against the supplier for any damage he might sustain



as a consequence of the supplier's breach of the contractual prohibition, whether it be contained in an individual contract of sale or a term of a master contract regulating future transactions between them.

35. These conflicting positions led the experts to consider intermediate solutions which might provide a basis for compromise: the first consisted in stating that the assignment of a receivable by the supplier to the factor could be effective notwithstanding any agreement between the supplier and the debtor prohibiting such an assignment, unless the debtor within (X) number of days after notice of assignment sent written notice to the factor invoking such agreement; the committee agreed that this solution, if adopted, would have to be completed by a provision indicating the method of calculating the time limit. The second formula proposed was to provide that a stipulation in the contract of sale prohibiting the assignment of a receivable shall be effective against the factor only if specifically accepted in writing by the supplier. The general view was that this solution would be difficult to operate in practice. Another possibility, not far removed from the last proposal, was to indicate that the assignment of a receivable by the supplier to the factor may be effective notwithstanding any agreement prohibiting the assignment contained in a standard form contract. A number of representatives objected however that the distinction between standard form and negotiated contracts did not exist in the law of their countries and that the formula would give rise to difficulties. Finally, the possibility was canvassed of combining the first and second solutions mentioned above.

36. At the conclusion of a wide-ranging debate, the committee came to the conclusion that none of the compromise proposals constituted a satisfactory solution. Independently of the various objections which could be levelled at each of them, the representatives whose legal systems contained a solution of the kind to be found in Article 4 indicated that all things considered they would prefer the future Convention to contain no rule at all on the question and to leave it to national law to determine the effect to be given to a stipulation in a contract of sale prohibiting assignment: any intermediate solution of a mandatory character would represent a step backwards in relation to the law of their countries on the matter. The committee decided that two solutions remained open: either to retain Article 4 in its original form or to delete it, and it is for this reason that it has been placed in square brackets. Finally it should be noted that the possibility was mentioned of retaining Article 4 with a reservation clause which would allow those States which so wished not to apply the provision; it was however pointed out that such a solution would amount to a failure to achieve unification or harmonisation on this question. The committee will therefore take a decision on this article at its next session.

Article 5

37. Article 5 plays a role similar to that of Article 3. In effect, in some legal systems not only is the validity of a clause providing for the assignment of future receivables or the effectiveness of such a clause not recognized, but the transfer of rights deriving from future contracts of sale and therefore not yet in existence cannot be effected. Moreover, while Article 3 concerns the assignment of receivables, Article 5 governs the assignment of rights deriving from the sale of goods and although it differs in structure and drafting it regulates the two questions dealt with in Article 3; indeed a suggestion was made to amalgamate the provisions relating to the assignment of receivables and the transfer of rights in a single article.

38. The provision therefore establishes the principle of the validity of a stipulation in a factoring contract providing for the transfer to the factor of all or any of the supplier's rights deriving from the sale of goods. So as to indicate clearly that ~~the provision~~ is not intended to deal with problems concerning the effectiveness of such a transfer against third parties it is stated, as in Article 3, that only the relations between the parties are governed. Moreover, Article 5 indicates the method of transfer, which may be effected directly, that is to say without a new act of transfer, which corresponds to the form already indicated in the rules on assignment of receivables, although the parties may agree that the transfer will take place once a new act for the purpose has been concluded. Article 5 therefore provides an option on this point, as it might not be in the interest of one of the parties to provide for an automatic transfer of rights.

39. It should be mentioned that the committee of experts gave lengthy consideration to the question of what precisely was meant by the term "rights": in the version adopted by the study group, Article 5 included the benefit of provisions in a contract of sale reserving title to the goods to the supplier. It goes without saying that this rule, which has been maintained in the present draft, in no way seeks to confer validity upon any provision for the reservation of title in the contract between the supplier and the customer not to regulate questions associated with the recognition or enforceability of such clauses. At the request of one representative however a further indication has been added to cover those situations where the supplier's security assumes a different character, and especially in North America that of a security interest. Thus, under the terms of Article 5, the benefit of any provision in the contract of sale of goods conferring a security interest on the supplier may be transferred. Furthermore, a representative of the factoring profession considered that the rights should also include those concerning the contract of

sale itself, such as the right to terminate the contract and to retake possession of the goods. Finally, it should be emphasized that the rights in question are not simply those created under the contract of sale but all those deriving from the sale of goods, including therefore rights conferred on the seller by the applicable law even though not stipulated in the contract.

#### Article 6

40. In the version adopted by the committee of governmental experts as redrafted by the Secretariat, Article 6 is the consequence of the amalgamation and amendment of Articles 6 and 7 of the text approved by the study group. Paragraph 1 sets out the conditions which must be met by the notice of the assignment to the debtor for his resulting obligation to pay the factor, a formulation preferred by the committee to the former language which provided that the assignment was effective against the debtor. Paragraph 2 is concerned with the validity of the payment by the debtor to the factor as a consequence of the notice received by him.

41. Paragraph 1, sub-paragraph (a) lays down the first condition which the notice must satisfy, namely that it must be in writing. While it is true that in a number of legal systems oral notice may be sufficient, it seemed preferable in the interests of the certainty of the transactions governed by the future Convention to require written notice. It should however be pointed out that oral notice, even though not sufficient under the terms of the draft Convention to place an obligation on the debtor to pay the factor, could nevertheless have the effect of imputing bad faith to the debtor if he pays the supplier, with the consequence that he would be required to pay twice over. The second condition, contained in the former Article 7, relates to the question of who must give notice; this may in the first place be the supplier since he is the original creditor and the contracting partner of the debtor. However the factor has a legitimate interest in the debtor's receiving notice of the assignment as it is to him that payment must be made and in those legal systems where the creditor's rank is determined by the order in which notice is given he will usually be more diligent than the supplier. In consequence the committee decided that the factor may give notice of the assignment, on condition however that he acts with the supplier's authority. The committee of experts also decided to delete the words "actual or apparent" which touched on complex questions relating to agency and to apparent authority, and given its intention simply to indicate that the debtor must have reasonable grounds for believing in the existence of the factor's authority, where appropriate by seeking information from the supplier, the committee agreed that questions regarding the form of the authority should be settled by the applicable law. Similarly, the possibility for notice to be given by other persons acting in the name of the supplier or of the factor will be governed by the appli-

cable law.

42. It should at this juncture be recalled that the text of Article 6 as submitted to the committee of governmental experts contained a sub-paragraph (b) including the condition that the notice should state that the assignment was governed by the rules in the course of preparation. This provision gave rise to a lengthy debate and the committee was divided on the question of the usefulness of its retention. The reasons which had led to its inclusion, which were strongly supported by one representative, were that the debtor must be informed of the regime governing the assignment and of its effects in his regard, and this in the name of equity and of the need to ensure clarity in commercial relations; such knowledge on the part of the debtor would be all the more necessary in cases where he had stipulated a prohibition on assignment in the contract of sale concluded with the supplier, so as to inform him that the Convention was applicable and that the clause prohibiting the assignment would be rendered ineffective by Article 4: it was indeed in the framework of that article that the rule had originally been introduced. There was however a very considerable majority against the maintenance of the provision: among the arguments advanced were the drawback that the Convention would be disapplied merely by the absence of the statement required in the notice, whose insertion might for example have simply been overlooked, as well as the fact that while the application of an instrument such as a Convention may be excluded by the exercise of party autonomy, its application should not on the other hand be determined by the inclusion in the contract of a stipulation of the kind contemplated. The committee as a whole recognized that the interest of the provision in question was bound up with Articles 2 and 4. It should be pointed out that those two articles were the subject of further discussion at the end of the first session of the committee of experts and that the implications of the decisions taken in connection with them were not themselves considered in any detail. It may be added that the decision which was finally taken to delete the former sub-paragraph (b) of Article 6, paragraph 1 in accordance with the wishes of a large majority of representatives is all the more justified, and this independently of the fate of Article 4, the principle of which has been contested, by the fact that under Article 2, as now worded, the debtor no longer runs the risk of a surprise application of the Convention.

43. Sub-paragraph (b) of Article 6, paragraph 1 provides that, in addition to the conditions set out in sub-paragraph (a), the notice must reasonably identify the receivables which have been assigned and the factor to whom or for whose account the debtor is required to make payment. The first part of this provision is therefore concerned with the scope of the debtor's obligations to the factor and it should be noted that a further condition regarding the receivables is to be found in sub-paragraph (c).

As to the person to whom the debtor must make payment, one representative expressed the wish that the provision specifically indicate that that person is a factor, having regard above all to the deletion of the requirement that the notice indicate that the assignment is governed by the Convention, so that the debtor will know that the assignment is not subject to the rules normally applicable to the assignment of receivables. This proposal met with strong opposition as it would impose a requirement which does not exist in the domestic law of a large majority of States and which would render the notice ineffective if the requirement were not satisfied. On the other hand, the committee was prepared to admit the possibility of the factor's receiving payment in a bank account and likewise an indication that the notice must mention "the factor to whom or for whose account the debtor is required to make payment". It was emphasized that this new formulation did not establish the condition that the assignee's acting as a factor be apparent and after considering, without adopting, the idea of including a reservation clause on this point in the draft Convention, the committee decided, for the present, to adopt the language mentioned above.

44. The effect of sub-paragraph (c) of Article 6, paragraph 1 is to provide that notice of the assignment given before the conclusion of the sales contract is not effective, thus covering the situation where notice is given by the supplier or the factor of a general assignment under a factoring contract and no subsequent notice is given to the debtor; in other words while the assignment of a future receivable may be effective between the supplier and the debtor under Article 3, notice of the assignment of a receivable which will arise under a future contract of sale will not, under the terms of Article 6, paragraph 1(c), be effective against the debtor.

45. Paragraph 2 of Article 6 relates to the conditions of the validity of the payment by the debtor to the factor when notice has been given in the form required by paragraph 1. The provision states that the debtor's liability will be discharged pro tanto provided that he makes the payment in good faith, and without knowledge of any other person's claim to payment of the receivables. The former version read "without having reason to know of any other person's right to payment...". The committee sought to provide a greater degree of security to the debtor who, under the new drafting, will not have to conduct research into the possible existence of creditors other than the factor and of the well-foundedness of their claims: if another person claims a right to payment of the receivable and if the debtor knew of the existence of such a claim then payment will not discharge the debtor who may have to make payment a second time. The problem was however raised as to whether, in the event of the contract of sale containing a prohibition on assignment, the supplier or the general body of creditors of a bankrupt supplier could not invoke the bad faith of the debtor who had paid the factor. Since the reply to this question depended

on the solution to be adopted in connection with Article 4, the committee agreed to return to the matter at its next session.

46. Lastly as regards Article 6, it should be noted that the committee of governmental experts decided to delete two provisions contained in Article 7 of the version adopted by the study group and which set out rules in force in most legal systems whereby payment to a factor by a debtor acting in good faith who had no knowledge of the existence of a third party claim over the receivable would discharge the debtor of liability irrespective of the validity of the assignment between the parties to the factoring contract, or of the right to payment of the receivable being vested in a third party. However one member of the committee of experts pointed out that this would not always be the case in his own country's legal system; the solution favoured by the majority of the committee admittedly militated in favour of the security of the debtor and of the development of international factoring but it could on the other hand prejudice the legitimate interests of third parties and he suggested that priority questions relating to the payment of receivables should be determined by national law. The view was expressed that the problem raised would be solved by rules concerning priorities which were not dealt with by the draft Convention but with a view to reaching a generally acceptable solution the committee agreed to retain the general principle set out in paragraph 2 of the former Article 7 (now contained in Article 6, paragraph 2) and to delete sub-paragraphs (a) and (b) which had been included therein. Finally, the possibility of adding a provision to deal with cases where the factor has been paid notwithstanding the existence of the superior right of a third party was rejected on the ground that here again the question of priorities arose.

#### Article 7

47. Article 7 completes paragraph 2 of Article 6 in the sense that it sets out the rights of the debtor following the giving of notice in accordance with paragraph 1 of Article 6. It is concerned with the extent to which the debtor may set up against the factor defences relating to the receivable on the one hand, and on the other defences not connected with it based on his relations with the supplier.

Paragraph 1 embodies the rule common to virtually all legal systems that an assignment cannot place the debtor in a worse position vis-à-vis the assignee than he would have been in in relation to the assignor. It provides therefore that the debtor may, if a claim is brought against him by a factor for payment of a receivable arising under a contract of sale, set up all defences against the factor of which the debtor could have availed himself under the contract if such claim had been made by the supplier. It is only the prohibition of the assignment stipulated in the

contract of sale between the supplier and the debtor which may be not be set up against the factor, subject however to Article 4 ultimately being retained by the committee of experts; it is for this reason that the introductory words of the provision read "subject to Article 4", which are at present placed in square brackets.

48. Paragraph 2 of Article 7 deals with the related but distinct question of the debtor's exercise against the factor of rights of set-off he may have against the supplier. Such rights may be exercised against the factor subject to certain conditions, the first of which is that they are not merely contingent. In other words they must exist and be available to the debtor at the time he receives notice of the assignment, for otherwise it would be possible for the supplier and the debtor subsequently to erode the position of the factor by the conclusion of new contracts giving rise to a set-off of which the factor was unaware. In addition, the set-off pleaded by the debtor against the factor must have arisen in respect of claims against the supplier in whose favour ~~the receivable~~ arose so as to avoid the possibility of a debtor asserting a right of set-off in respect of claims against a different supplier regarding the receivables which had been assigned to the same factor.

49. The text of the draft articles submitted to the committee of governmental experts contained a provision (former Article 9) to the effect that without prejudice to the debtor's rights under Article 8 (now renumbered Article 7) non-performance or defective or late performance of the contract of sale by the supplier should not entitle the debtor to recover money paid by him to the factor. This provision dealt therefore with the situation where it is the debtor who is seeking to recover from the factor and was justified on the ground that the factor does not guarantee performance of the contract of sale by the supplier: the debtor must accordingly content himself with a recourse action against the supplier unless he is in a position to exercise his rights under the present Article 7. The representatives of a number of States expressed strong reservations concerning this rule which, in their opinion, placed the debtor at a disadvantage by depriving him of any recourse, for example in the case where the supplier became bankrupt before performing his obligations and where the factor to whom payment had been made knew of the defect in performance. It was moreover observed that it seemed somewhat unjust and indeed illogical not to permit the debtor to recover money paid to the factor before receiving or examining the goods, when he would have been entitled to invoke the provisions of Article 7, paragraph 1 in cases where payment should have been made after performance by the supplier; even if the factor had not been enriched because he would have paid the supplier, the debtor should not find himself in a position which he had had no part in bringing about. In the light of these objections the committee agreed to delete the whole of the former Article 9 of the draft Convention and to leave the question to be determined by the applicable national law.

Article 8

50. The question dealt with in Article 8 (former Article 10) relates to the effects, in regard to third party liability for damage caused by the goods, of the transfer of ownership of such goods to the factor when the factoring contract has so provided (such a clause in the factoring contract being effective in accordance with Article 5). As regards the usefulness of regulating this question in the Convention under preparation, the representatives of the factoring associations have indicated that to their knowledge goods affected by factoring transactions have never caused damage but that the problem could arise with the diversification of the products concerned. They added that the period during which the factor may be owner of the goods in consequence of the transfer to him of the benefits of a reservation of title clause is, it is true, in general shorter than that in the case of leasing, but that this consideration did not deprive the rule of its importance. Finally, they pointed out that in the absence of the protection afforded to factors by the principle contained in this provision, the latter would be obliged to take out insurance and that the increased costs would in turn fall on suppliers.

51. A majority in ~~the committee of governmental experts~~ was of the opinion that the factor's rôle was a strictly economic one: while he might become owner of the goods because the benefit of the reservation of title clause had been transferred to him at the same time as the receivable, he would not on the other hand have the animus possesendi as ownership served only as security for the receivable. The conclusion of this reasoning was the solution contained in the corresponding article of the text adopted by the study group which sought, in such cases, to exonerate the factor from third party liability for damage to property or persons caused by the goods. If, on the other hand, the factor was not simply the economic owner of the goods but exercised the attributes of ownership by selling or otherwise disposing of the goods to a person not connected with the factoring transaction, then the principle that he should be relieved of liability would be displaced.

52. The other approach suggested was to make the factor responsible for all the consequences of ownership resulting from his acquisition of the goods and the representatives endorsing this view were reluctant to introduce into the field of factoring transactions a liability regime which would derogate from the principles of various national laws and international instruments which impose a presumption of liability on the owner. It was moreover observed that in those countries where there exists a presumption of liability on the owner, a provision such as that under discussion would create a precedent and that other agencies which provide



credit against receivables to which a reservation of title clause is attached would also ask for relief from civil liability.

53. With a view to achieving a compromise solution, the committee agreed to amend the former Article 10: the basic principle contained in paragraph 1 of the new article remains unchanged, namely the exoneration of the factor for liability to third parties for damage caused by the goods of which the factor has become owner in the circumstances contemplated by Article 5, that is to say following the transfer to him of the benefit of a reservation of title clause under the factoring contract. It should be noted that this drafting does not settle the question of whether the same rule should apply if, under the applicable law, the benefit of a reservation of title clause passes to the factor independently of a contractual stipulation to that effect. However, two exceptions have been made to the Principle: the first, contained in the draft of the study group, is to be found in paragraph 2 which establishes the liability of the factor when in the exercise of ownership he disposes of the goods to any other person and not only, as under the earlier version, to a person who is not the supplier, another factor or the debtor. Paragraph 3 affirms the primacy of the provisions of any other international agreement which has already been or may be entered into and which imposes liability founded on ownership of the goods.

#### Article 9

54. At the present stage of the elaboration of the draft, Article 9 reproduces the corresponding provision of the draft adopted by the study group. Its underlying principle recognizes the fact that in international factoring the original assignment by the supplier to the factor may be followed by one or more assignments between export and ~~import factors~~ and it provides that any such assignments must comply with the rules, the positions of the assignor and assignee factors being equated mutatis mutandis to those of the supplier and the original factor. Likewise, the places of business of the factors involved in subsequent assignments are no more relevant than those of the parties to the original assignment in determining the international character of the factoring operations for the purpose of the uniform rules, which is established by the introductory language of Article 2. However, the committee of governmental experts observed that this provision, as formulated, raised difficulties of application in respect of certain articles: in effect, although the assignment is made

in such cases between two factors, the underlying relationship created by the contract of sale between the supplier and his customer is relevant to a certain number of provisions of the draft Convention. In consequence the committee requested the Secretariat to prepare a redraft of Article 9 which should be communicated to Governments, together with the present commentary.

55. With a view to considering the possibility of redrafting Article 9, the Secretariat has proceeded to an article by article examination of the draft Convention in the light of the situation where an assignment is made between two factors. Various formulations have been considered, in particular that of introducing a provision according to which, unless the Convention provides otherwise, any mention of "the factor" is to be taken as referring to the second factor in the event of a subsequent assignment: this solution would require a number of drafting amendments to certain articles (in particular those where a reference is made to the supplier in the context of the factoring contract since, in the case of a subsequent assignment, he has been replaced as assignor by the first factor), as well as the inclusion of some additional provisions. Another possibility considered was that of designating the parties by different terms according to their position in the legal relation contemplated: thus the term "supplier" would be retained when he is considered as a party to the contract of sale; the term "assignor" would be introduced to indicate either the supplier in the context of the factoring contract or the export factor in the event of a subsequent assignment: the "factor" would, according to the circumstances, be either the export or the import factor and when the rules contained in the draft Convention necessitate a distinction being drawn between the two types of assignment, clarification would be needed as to whether reference was being made to the first or the second factor. Such a formula would certainly complicate the understanding of the provisions of the draft and would also entail changes to the present text (in particular as regards the definition, and the substitution where appropriate of the names, of the parties, in application of the principle mentioned above).

56. The Secretariat has however attempted to find a means of rendering applicable to the subsequent assignment the provisions of the draft as discussed and provisionally adopted at the first session of the committee of governmental experts without amending the text of the articles of the draft Convention which precede Article 9. In any event, the mechanism of substitution as proposed in Article 11 of the draft adopted

by the study group has been abandoned and one could imagine a broad formulation which would permit the application to successive assignments of the principles contained in the Convention, with provisions governing certain special situations where, in the case of the subsequent factor, the rule would complete or perhaps modify the corresponding provision concerning the assignment between the supplier and the factor.

57. The three possible avenues proposed above seek only to resolve the technical problems of drafting; however when considering an appropriate formulation and the implementation of the proposed principles in respect of each article, the Secretariat ran up against certain difficulties of a substantive character relating to successive assignments which call for consideration and for the making of certain choices by the members of the committee. The Secretariat proposes therefore at this stage to indicate the points at issue and to formulate subsequently the drafting alternatives in the light of the observations and suggestions which will be made on this commentary.

58. For reasons of simplicity and clarity, the problems which have arisen are set out below in the form of questions, without any commentary:

- 1 - Must the application of the Convention to the first assignment (between the parties to the factoring contract mentioned in Article 1) be a condition for the possible application of the Convention to a successive assignment?
- 2 -
  - a) Must the subsequent contract of assignment necessarily satisfy all the criteria set out in sub-paragraphs (a), (b) and (c) of paragraph 1 of Article 1, if it is itself to be governed by the Convention?
  - b) If all the criteria set out in paragraphs (a), (b) and (c) need not necessarily be satisfied in the event of a subsequent assignment, can a contract for such an assignment nevertheless be characterized as a "factoring contract"?
  - c) Must the assignee in the subsequent assignment be a factor?

- 3 - Without prejudice to the answer to question 1. (which will determine whether the supplier must have his place of business in a Contracting State or whether his place of business is irrelevant), is it necessary for the application of the Convention to successive assignments that not only the debtor and the factor but also the subsequent assignee has his place of business in a Contracting State?
- 4 - As regards the provisions of Article 6, paragraph 1(a), is it necessary to make provision for an assignee under a subsequent assignment to be able to give notice of that assignment to the debtor when duly authorised to do so?
- 5 - As regards the debtor's rights of set-off against the second assignee, must they relate to claims existing against the supplier and available to the debtor at the time the debtor received notice of the /first/ assignment, or may they also relate to claims existing against the first assignee which the debtor may invoke at the time the debtor received notice of the /second/ assignment?

The Secretariat would be grateful for any observations on the points raised above or on any other aspect not specifically mentioned, so as to permit it to submit drafting proposals relating to Article 9 before the next session of the committee of governmental experts.

#### Article 10

59. The intention of Article 10, which was introduced by the committee of governmental experts at its first session, is to leave the parties free to choose the rules applicable to their contractual relations. This provision corresponds to a principle generally to be found in international commercial law conventions and indeed takes over the text of the corresponding article of the Unidroit draft Convention on international leasing. It should be noted that this possibility for the exercise of the autonomy of the parties on the one hand concerns only their mutual relations and on the other exists to the extent only that the Convention does not provide otherwise. This latter restriction on party autonomy was introduced at the request of a number of representatives, having regard to Articles 1 and 2 but above all in connection with Article 4 in respect of which it was pointed out that if its provisions were to be maintained, they would lose all their interest if their application could be systematically excluded by the parties. Although it was argued that Article 4 could not be excluded by the parties to the contract of sale by virtue of Article 10 for the reason that it did not concern exclusively the relations between the supplier and the debtor, it seemed preferable, in the interests

of clarity, to include the introductory language of Article 10 and to place it in square brackets pending further consideration by the committee at its next session with a view to determining which provisions of the Convention should be mandatory, in particular in the light of the final decision regarding Article 4.

#### Article 11

60. Article 11 concerns the rules of interpretation to be applied to the Convention under preparation. This article takes over almost word for word the corresponding provision of the Vienna Sales Convention, namely Article 7, which has been incorporated in several international trade law conventions. Paragraph 1 lays stress on the promotion of uniformity in the application of the Convention, having regard to its international character, so as to avoid the attempt at harmonisation at legislative level being defeated by different or piecemeal approaches at the stage of implementation by judges or arbitrators; the paragraph also refers to the observance of good faith in international trade. Paragraph 2 supplements the first part of paragraph 1 in that it is directed not to the interpretation of the provisions of the Convention but to the principles to be applied to matters governed by the Convention which are not settled by it: for such cases mention is made of the general principles on which the Convention itself is based and, moreover, of the law applicable by virtue of the rules of private international law.

Preliminary draft Convention on certain aspects of  
international factoring

PREAMBLE

THE STATES PARTIES TO THIS CONVENTION,

CONSCIOUS of the importance of providing a legal framework that will facilitate international factoring, while maintaining a fair balance of interests between the different parties involved in factoring transactions,

AWARE of the need to make international factoring more available to developing countries,

RECOGNIZING therefore that the adoption of uniform rules which govern certain aspects of international factoring and take into account the different social, economic and legal systems would contribute to the removal of legal barriers in international trade and promote the development of international trade,

HAVE DECIDED to conclude a Convention for this purpose and have thereto agreed as follows:

Article 1

1. For the purpose of the present Convention, "factoring contract" means a contract concluded between one party (the supplier) and another party (the factor) pursuant to which:

- (a) the supplier is to assign to the factor, by way of sale or security, receivables arising from contracts of sale of goods made between the supplier and his customers (debtors) in the course of business;
- (b) notice of the assignment of the receivables is to be given to debtors; and
- (c) the factor is to provide at least two of the following services, namely finance, maintenance of accounts, collection of receivables and protection against credit risks.

2. In this Convention references to "sale of goods" shall, where appropriate, include the supply of services.

## Article 2

This Convention applies in relation to a factoring contract so far as it relates to receivables arising from a contract of sale of goods between a supplier and a debtor whose places of business are in different States:

- (a) when the supplier, the debtor and the factor have their places of business in Contracting States; or
- (b) when the rules of private international law lead to the application to the factoring contract and to the contract of sale of goods of the law of a Contracting State.

## Article 3

As between the parties to the factoring contract:

- (a) a contractual provision for the assignment of existing or future receivables shall be valid, even though the contract does not specify them individually, if 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 operates to transfer the receivables to the factor when they come into existence without the need for any new act of transfer.

## Article 4

The assignment of a receivable by the supplier to the factor shall be effective notwithstanding any agreement between the supplier and the debtor prohibiting such assignment.

## Article 5

A factoring contract may validly provide as between the parties thereto for the transfer, with or without a new act of transfer, of all or any of the supplier's rights deriving from the sale of goods, including the benefit of any provision in the contract of sale of goods reserving to the supplier title to the goods or creating any security interest.

Article 6

1. The debtor is under a duty to pay the factor if notice of the assignment :

- (a) is given to the debtor in writing by the supplier or by the factor with the supplier's authority;
- (b) reasonably identifies the receivables which have been assigned and the factor to whom or for whose account the debtor is required to make payment; and
- (c) relates to receivables arising under a contract of sale of goods made at or before the time the notice is given.

2. Payment to the factor by the debtor in accordance with paragraph 1 of this article shall be effective to discharge his liability pro tanto provided that he makes the payment in good faith and without knowledge of any other person's claim to payment of the receivable.

Article 7

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 of goods 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 against the supplier in whose favour the receivable arose, and available to the debtor at the time the debtor received notice of the assignment.

Article 8

1. The factor shall not, by reason only of his acquisition of ownership of the goods in the circumstances contemplated 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.



3. Nothing in this article shall affect the liability of the factor under any other international agreement which has already been or may be entered into.

#### Article 9

This Convention shall also apply to subsequent assignments of the receivables by the factor to another factor as if the first factor were the supplier and the other factor were the initial factor, whether the places of business of the factors are situated in the same State or in different States. (1)

#### Article 10

/Except as otherwise provided by this Convention (2), / the parties may, in their relations with each other, exclude the application of this Convention or derogate from or vary the effect of any of its provisions.

#### Article 11

1. In the interpretation of this Convention, regard is to be had to its international character and to the need to promote uniformity in its application and the observance of good faith in international trade.

2. Questions concerning matters governed by this Convention which are not expressly settled in it are to be settled in conformity with the general principles on which it is based and in conformity with the law applicable by virtue of the rules of private international law.

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- (1) The Secretariat will attempt to produce a redraft of Article 9 which will be communicated to Governments together with the commentary on the revised text of the draft Convention as a whole.
  - (2) It was agreed to leave to a later stage any decision as to which provisions of the Convention are to be regarded as mandatory.