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DRAFT CONVENTION  
ON INTERNATIONAL FACTORING

as adopted by a Unidroit committee  
of governmental experts  
on 24 April 1987

with

EXPLANATORY REPORT

prepared by  
the Unidroit Secretariat

Rome, September 1987

DRAFT CONVENTION ON INTERNATIONAL FACTORING

as adopted by a Unidroit committee of governmental experts  
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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 AGREED as follows:

*Article 1*

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

(a) the supplier may or will assign to the factor receivables arising from contracts of sale of goods made between the supplier and his customers (debtors) other than those for the sale of goods bought for their personal, family or household use;

(b) the factor is to perform at least two of the following functions:

- finance for the supplier, including loans and advance payments;
- maintenance of accounts (ledgering);
- collection of receivables;
- protection against default in payment by debtors;

(c) notice of the assignment of the receivables is to be given in writing to debtors.

2. - In this Convention references to "goods" and "sale of goods" shall include services and the supply of services.

3. - In this Convention "writing" includes any form of writing, whether or not signed.

## *Article 2*

1. - This Convention applies whenever the receivables assigned pursuant to a factoring contract arise 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 both the contract of sale of goods and the factoring contract are governed by the law of a Contracting State.

2. - For the purpose of this Convention, if a party to the contract of sale of goods or the factoring contract has more than one place of business, the place of business is that which has the closest relationship to the contract and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that contract.

## *Article 3*

1. - The parties to the factoring contract may exclude the application of this Convention.

2. - The parties to the contract of sale of goods may exclude the application of this Convention only in respect of receivables arising at or after the time when the factor has received notice in writing of such exclusion.

3. - Where the application of this Convention is excluded in accordance with the preceding paragraphs of this article, such exclusion may be made only as regards the Convention as a whole.

## *Article 4*

As between the parties to the factoring contract:

(a) a contractual provision for the assignment of existing or future receivables shall not be rendered invalid by the fact that the contract does not specify them individually, if at the time of conclusion of the contract or when they come into existence they can be identified to 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 5

1. - 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.

2. - However, such an assignment shall not be effective against the debtor when he has his place of business in a Contracting State which has made a declaration under Article X of this Convention.

#### Article 6

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 7

1. - The debtor is under a duty to pay the factor if, and only if, the debtor does not have knowledge of any other person's superior right to payment and 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. - Irrespective of any other ground on which payment by the debtor to the factor discharges the debtor from liability, payment shall be effective to discharge his liability *pro tanto* if made in accordance with paragraph 1 of this article.

#### Article 8

1. - 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 assert against the factor any other defences, including 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 a notice of assignment conforming to Article 7 of this Convention.

#### *Article 9*

1. - Without prejudice to the debtor's rights under Article 8 of this Convention, non-performance or defective or late performance of the contract of sale of goods by the supplier shall not alone entitle the debtor to recover money paid by the debtor to the factor if the debtor has a claim against the supplier for recovery of the price.

2. - The debtor who has such a claim against the supplier shall nevertheless be entitled to recover money paid to the factor:

(a) to the extent that the factor has not paid the purchase price of the receivable to the supplier; or

(b) where at the time the factor paid such purchase price he knew of the supplier's non-performance as regards the goods to which the debtor's payment relates.

#### *Article 10*

1. - Where a receivable is assigned by a supplier to a factor pursuant to a factoring contract governed by this Convention:

(a) the rules set out in Articles 3 to 9 of this Convention shall, subject to paragraph (b) of this article, apply to any subsequent assignment of the receivable by the factor or by a subsequent assignee;

(b) the provisions of Articles 7 and 8 of this Convention shall apply as if the subsequent assignee were the factor.

2. - Notice to the debtor of the subsequent assignment may also constitute notice of the assignment to the factor.

3. - This Convention shall not apply to an assignment which is prohibited by the terms of the factoring contract.

*Article 11*

1. - In the interpretation of this Convention, regard is to be had to its object and purpose as set forth in the Preamble, 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.

*Article X*

A Contracting State may at any time make a declaration in accordance with Article 5, paragraph 2 of this Convention that an assignment under Article 5, paragraph 1 shall not be effective against the debtor when he has his place of business in that State.

EXPLANATORY REPORT ON THE  
UNIDROIT DRAFT CONVENTION ON INTERNATIONAL FACTORING

prepared by the Unidroit Secretariat



I

BACKGROUND TO THE DRAFT CONVENTION

1. - The origins of the work on this draft Convention date back to a decision taken on the basis of a Secretariat memorandum by the Unidroit Governing Council at its 53<sup>rd</sup> session, held in Rome in February 1974, 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 factoring contracts. The Council also requested the Secretariat to prepare a preliminary study on such contracts which would permit the Council to take a decision on the order of priority to be accorded to the item with a view to the elaboration of uniform rules <sup>(1)</sup>.

2. - The Governing Council was seized of a preliminary report submitted by the Secretariat at its 55<sup>th</sup> session, held in Rome in September 1976, on which occasion it authorised a wider distribution of the report and accompanying questionnaire, especially to practitioners; at its 56<sup>th</sup> session it decided to set up a restricted group of members of the Governing Council, assisted by one or more experts on factoring, to examine an analysis of the replies to the questionnaire. The detailed conclusions of the group <sup>(2)</sup> were brought to the attention of the Governing Council at its 57<sup>th</sup> session, held in Rome in April 1978, and in accordance with the powers conferred upon him by the Council the President of Unidroit constituted a study group for 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 <sup>(3)</sup>. At the conclusion of that session the study group adopted the preliminary draft uniform rules on certain aspects of international factoring.

3. - At its 62<sup>nd</sup> session, held in Rome in May 1983 <sup>(4)</sup>, 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 <sup>(5)</sup>, to the Governments of the member States of Unidroit,

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(1) Report on the 53<sup>rd</sup> session of the Governing Council, p. 20.

(2) For the report on the session of the restricted group, see Study LVIII - Doc. 4.

(3) The reports on the three sessions are contained in Study LVIII - Doc. 7, Study LVIII - Doc. 10 and Study LVIII - Doc. 13 respectively.

(4) Report on the 62nd session of the Governing Council, p. 12.

(5) Study LVIII - Doc. 16.

with a request for observations. In the light of the observations received, the Governing Council decided at its 63<sup>rd</sup> session in May 1984 to set up a committee of governmental experts for the preparation of draft uniform rules on certain aspects of international factoring<sup>(6)</sup> (hereinafter referred to as "the committee").

4. - The text of the preliminary draft uniform rules was considered and revised at three sessions of the committee, held in Rome from 22 to 25 April 1985, from 21 to 23 April 1986 and from 22 to 24 April 1987 respectively<sup>(7)</sup>. At its second and third sessions the committee also considered a set of draft final provisions prepared by the Secretariat<sup>(8)</sup>. Mr Royston M. Goode chaired the committee throughout, as also the drafting committee which met on the occasion of each session to take account of the amendments made in plenary. In all, 33 member States of Unidroit, four non-member States, three intergovernmental organisations and two non-governmental international organisations, as well as three international and three national professional associations took part in the work of the committee<sup>(9)</sup>.

5. - At the close of its third session, the committee completed its work with the adoption of the text of a draft Convention on international factoring<sup>(10)</sup> which was now ready for submission to a diplomatic Conference for adoption. At the closing session of the third and final session of the Unidroit committee of governmental experts for the preparation of a draft Convention on international financial leasing, which was held immediately after the session of the committee of governmental experts for the preparation of a draft Convention on certain aspects of international factoring, the Canadian representative announced that his Government would host a diplomatic Conference for the adoption of the two draft Conventions. The Conference will be held in Ottawa from 9 to 28 May 1988.

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(6) Report on the 63<sup>rd</sup> session of the Governing Council, p. 39.

(7) The Secretariat prepared a commentary on the text of the preliminary draft Convention drawn up by the committee at its first session (Study LVIII - Doc. 20), as well as a revised commentary on the text of the preliminary draft Convention drawn up by the committee at its second session (Study LVIII - Doc. 25) and a summary report on the third session of the committee (Study LVIII - Doc. 32).

(8) For the revised version of the draft final provisions, see Study LVIII - Doc. 34.

(9) For the full list of participants, see the APPENDIX hereto.

(10) For the text of the draft Convention, see above.

## II

### GENERAL CONSIDERATIONS

6. - Although the origins of factoring <sup>(11)</sup> are to be found in antiquity, and the institution underwent a new development in the nineteenth century in the relations between Great Britain and the United States of America, it was only after the First World War that its characteristics became clear, first in Common law countries, then in other Western countries and finally in the world at large. Since the nineteen-sixties, its considerable and uninterrupted growth, including its expansion into ever more diversified fields of activity and an increasing number of countries, bear witness to the adaptation of this means of financing to meet the needs of contemporary commercial activity. A brief explanation of the economic role of factoring and of the legal mechanisms adopted to regulate it at national level will permit a better understanding of the reasons which influenced the choices made by the authors of the draft Convention in their attempt to provide a suitable legal framework at international level for a device forged and employed with success by the commercial and financial worlds.

7. - Recourse to factoring by a small or medium-sized manufacturer or supplier of services who sells on credit terms to his professional or commercial customers is the result of a decision to rationalise his business: it frees him from a certain number of concerns of a financial character which are assumed by a professional who offers a wide range of services characterised by the efficiency and low cost permitted by specialisation. The services offered by the factor may be summarised as four: in the first place he may assume the risk of the insolvency of the supplier's debtors; after enquiring into the creditworthiness of each debtor, the factor will, when he judges it appropriate, establish a credit limit calculated principally by reference to the turnover in respect of the debtor and to the average term for payment, and he will assume the risk of non-payment resulting from the debtor's insolvency up to the limit of the credit granted. According to whether or not this service is provided, the factoring transaction will be designated "recourse" or "non-recourse" factoring. Moreover, factoring may serve the purpose of financing debts (receivables), the factor advancing to the supplier an amount proportional to the value of the receivables, payment of which by the debtor will only be made later at the time stipulated. The two other services traditionally offered by factors are, on the one hand, the handling of the supplier's

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(11) This note concerns the French version only.

accounts with his debtors, which implies their maintenance, the conduct of correspondence and the soliciting of payment by debtors, with the aid of the most advanced technical methods of management, and on the other the recovery of receivables from debtors, the latter making payment directly to the factor who pays over the sums in question to the supplier in accordance with the arrangements they have agreed upon. When the factor is authorised to accept payment of the receivables, he will also take the necessary steps for their recovery. The supplier may agree with the factor, on the basis of both commercial and legal considerations, whether or not to give notice to the debtor that he is bound by a factoring contract. In particular, when the recovery of receivables is included among the services for which provision is made, the debtor is by such notice informed that he can obtain discharge only by paying the factor.

8. - The factor obtains payment for his services in the form of the commission he receives from the supplier, which may amount to up to two percent of the value of each receivable, calculated in accordance with the services provided and their cost in each case. Whenever he agrees to make advance payments against the receivables the factor takes the benefit of the corresponding interest. It will readily be appreciated that factoring transactions can only be based on a continuing relationship between the supplier and the debtors in question and this on account both of the nature of the services which characterise factoring and of the primordial importance for the factor to amortise his investment. It is precisely for these reasons that the factor will require the supplier to grant him the exclusive right to factor the receivables or certain categories of receivables which arise out of the supplier's commercial dealings with his customers.

9. - It is apparent from this brief description of factoring that it presents many economic advantages; as has been seen, it provides financial liquidity, the certainty of payment and the handling and recovery of receivables, the choice of the combination of the services being left to the parties. In each system, legal means have been sought to ensure the development of this relatively recent technique of financing in the most satisfactory manner possible, in terms not only of facilitation and flexibility, but also of certainty and cost, and this explains the fact that while in most countries it is the assignment of receivables which provides the underlying legal basis for factoring transactions, the procedures whereby such assignments are effected and the rules which govern the different aspects of them differ considerably. In consequence, when the supplier has commercial dealings with foreign buyers, the problem of distance and the difficulties facing the former in obtaining information as to the financial position of the latter, language barriers and frequently ignorance of the applicable foreign law make the services offered by

factors all the more attractive. It is nevertheless true that the divergencies in national law and the frequent uncertainty as to the law applicable to a given transaction or to one or another aspect of it create problems which the factoring industry must constantly face and which it seeks to overcome by passing on to suppliers the increased cost of its services.

10. - It is in these circumstances that the Unidroit committee of governmental experts, endorsing the conclusions of the study group, recognized that trade would be encouraged by facilitating factoring and that it would therefore be desirable to draw up uniform rules in this connection. It also agreed however to limit the attempt at unification to international factoring, considering that such a restriction 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 could 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 transactions. While the committee opted, as regards the form of the future instrument, in favour of a Convention, it emphasized on a number of occasions in the course of its work that this choice would leave it open to those States which wished to do so to draw on the international rules when preparing national legislation directed to domestic transactions. As to the general approach followed in the elaboration of the draft Convention, the committee decided to limit the scope of its work of unification to what may be considered the keystone of factoring transactions, namely the specific question of assignments, and to lay down basic minimum principles concerning a restricted number of aspects raising particular problems. Furthermore, it should be pointed out that the rules governing the mechanics of assignments are limited to the relations between the three parties directly interested - the assignor, the assignee and the debtor - to the exclusion of situations involving third parties, and this is one of the reasons for the deletion of a provision which had initially been included concerning the liability of the factor towards third parties for damage caused by goods of which he has become owner as a result of the transfer of the benefit of a reservation of title clause. As regards on the other hand the problems relating to priorities between the rights of the factor and those of third parties in the receivables, it is on account of their extreme complexity that the committee decided not to deal with them, by way either of a substantive rule of law or of a conflicts rule, and this notwithstanding the widely expressed regret that the Convention failed to regulate an aspect of the question which created very great difficulties at international level.

11. - Before embarking on a commentary on each of the provisions of the draft Convention, reference should be made to the committee's concern to take account as far as possible of the 1980 United Nations Convention on contracts for the international sale of goods (hereinafter referred to as "the Vienna Convention"), since the transactions governed by the future Convention on international factoring most often follow an international sale transaction which may therefore be subject to the Vienna Convention. This concern is evidenced in a number of ways: firstly in the general structure of the draft (in particular the order of the articles), sometimes in the provisions of a given article and finally, whenever possible and desirable, in the terminology employed with a view to seeking harmonisation of the concepts to be found in various recent international instruments dealing with related matters. Although the committee did not consider the possibility of grouping the articles together under general chapter headings, as is the case with other international trade law Conventions, several parts may be identified as follows. The first concerns the scope of application, both substantive and territorial, and the possibility for the parties to exclude the application of the Convention (Articles 1 to 3); one could also include within this chapter Article 10, which broadens the scope of application of the Convention by applying the principles set out in it to assignments made subsequent to those effected under a factoring contract governed by the Convention. The second would contain the rules removing certain obstacles which may exist under national law to the validity of the assignment of receivables or of the transfer of rights accessory to the receivables between the parties to the factoring contract (Articles 4 and 6). A third part would be that concerned with certain effects of the assignment on the debtor (Articles 7 to 9), whereas Article 5 concerns both the question of the validity of the assignment *inter partes* and that of its effects on the debtor. Finally, Article 11 contains general provisions relating to the interpretation of the rules of the Convention.

### III

#### COMMENTARY ON THE PROVISIONS OF THE DRAFT CONVENTION

12. - The *title* of the draft Convention was slightly modified in the course of the committee's work, originally reading "Preliminary draft Convention on certain aspects of international factoring" so as to indicate from the outset the limited scope of the work in hand. The committee preferred however to simplify the title of the future Convention by stating its purpose in general terms, although it was agreed to maintain in the Preamble an express reference to the fact that only certain aspects of the matter are dealt with.

#### *Preamble*

13. - The second and third paragraphs, the source of which is to be found in the provisions proposed for inclusion in the Preamble of the Unidroit preliminary draft Convention on international financial leasing, set out the aims of the instrument, namely the provision of a legal framework that will facilitate international factoring while maintaining a fair balance of interests between the different parties involved in such transactions and making international factoring more available to developing countries. The last two paragraphs take over almost word for word the corresponding provisions of the Preamble to the Vienna Convention and lay stress on the development of international trade while respecting the differences between social, economic and legal systems.

#### *Article 1*

14. - As indicated above in the general considerations, and as is apparent from the provisions of the Preamble itself, the aim which guided the work on the draft Convention was that of facilitating factoring as a means of assisting the development of international commercial exchanges. Given the variety of forms which factoring has assumed in practice and the legal frameworks within which it has been accommodated or to which it has been adapted in different countries, as broad 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, assimilated to this technique of financing 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 sale contract to which the receivables relate was ultimately rejected. An important derogation

from this principle is constituted by the decision to restrict the scope of application to transactions in which debtors are to be given written notice of the assignment. The definition in Article 1 seeks therefore to identify what may be considered to be the lowest common denominator in notification factoring 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.

15. - *Sub-paragraph (a)* defines the supplier's obligation to the factor, namely the assignment of receivables arising from a contract: this is the legal basis for factoring as a financing technique. The language agreed by the committee: "*the supplier may or will assign ...*" reflects factoring practice in the sense of the supplier's undertaking to assign receivables which will arise thereafter, although it may also constitute the act under which existing receivables are assigned; finally, the supplier may in many cases be free to assign, or not to assign, certain kinds of receivables, in accordance with agreements concluded with the factor. It should be noted that the provision is silent as to the procedures for the assignment for while at an earlier stage of the work it was required that it should be made "on a continuing basis" and "by way of sale or security", the committee considered as to the first point that the continuing relationship between the parties to the factoring contract was implicit in the functions performed by the factor and in the wording of Article 1, and was more generally of the opinion that a strict interpretation of those expressions in the light of the concepts and characterisations of national law could run the risk of excluding the application of the Convention in certain cases.

16. - *Sub-paragraph (a)* also lays down a number of conditions regarding the contracts which give rise to the receivables assigned. In the first place, they must be contracts for the sale of goods or for the supply of services (Article 1, paragraph 2), and they must moreover be concluded between the supplier and his customers in the course of their business, the intention being essentially to exclude consumer transactions on account of the special regime governing such transactions under the law of a number of countries. The language finally adopted is that of the negatively framed definition contained in Article 2(a) of the Vienna Convention, which excludes contracts between the supplier and his customers "*for the sale of goods bought for their personal, family or household use*". It should also be stressed that the assignment of receivables arising out of contracts concluded with public bodies or enterprises of a non-profit making character will be subject to the provisions of the Convention on international factoring, as also will be the assignment of receivables relating to other categories of sales excluded from the application of the Vienna



Convention under Article 2(b) to (f) thereof. As to the question of whether the prospective Convention should apply to the assignment of receivables arising from sale contracts concluded orally, the committee agreed that this was a matter which should be left to be decided by the law applicable to the contract as there was no intention here of imposing any condition as to the form of the contract of sale.

17. - Sub-paragraph (a) having set out the supplier's duty to the factor, *sub-paragraph (b)* of Article 1, paragraph 1 deals with the obligations of the factor. In practice, factors perform a series of widely differing functions; it seemed however that only four of those most frequently found in factoring transactions needed to be mentioned, namely: finance, which usually assumes the form of a loan or advance payment; the maintenance of accounts (ledgering); the collection of receivables and protection against default in payment by debtors, this latter expression referring to the factor's assumption of the risk of the insolvency of the supplier's customers and not to the case of the debtor's refusal to make payment as a consequence of his disputing his obligation to pay. For a contract of assignment to be considered as a factoring contract for the purposes of the future Convention, the factor must agree thereunder to perform at least two of these functions for indeed since none of them when taken alone is characteristic of factoring, each of them may be absent from a factoring contract. It should also be underlined that the requirement in sub-paragraph (b) and the conditions set out in sub-paragraphs (a) and (c) are cumulative, with the consequence that if the contract provides that the receivables are to be assigned by the supplier to the factor and that the debtor must receive notice of the assignment, then even if the two functions performed by the factor are the collection of receivables and the maintenance of accounts the contract will be a factoring contract for the purposes of the Convention.

18. - The last element which, under *sub-paragraph (c)*, characterises as a factoring contract one meeting the conditions set out in sub-paragraphs (a) and (b) is that it provides that notice of assignment of the receivables will be given to debtors (in writing). This important restriction, which derogates from the declared principle of embracing the most diverse forms of factoring, has from the very outset been retained as a criterion for the definition of the factoring contract for the purposes of the Convention; among the considerations which led to this decision was a concern that the inclusion of non-notification factoring could result in the Convention applying to a large number of transactions, in particular international banking operations where the receivable is used as security, transactions which might moreover assume forms of factoring unknown to some legal systems, and the fact that in any event the problems raised by assignments were totally different in respect of the rights of debtors

according to whether the assignment was or was not notified to them. It should be noted that when the parties to the factoring contract choose the form of notification factoring (which will necessarily be the case if the future Convention is to apply) the function of recovery of the receivables will almost always be performed by the factor: in that event, the requirement of notice in Article 1, paragraph 1 (c) is completed by the conditions set out in Article 7, paragraph 1 concerning in particular the manner of the notification, which gives rise to the debtor's duty to pay the factor.

19. - The other two paragraphs of Article 1 contain definitions. While *paragraph 2* provides that "... references to *"goods"* and *"sale of goods"* shall include services and the supply of services", in accordance with the decision of the committee concerning the contracts which may give rise to receivables assigned under a factoring contract, *paragraph 3* is intended to clarify what is meant by "writing", a term which concerns the form of the notice referred to in Article 3, paragraph 2 as well as notice to the debtor; in the latter case the committee was of the belief that it was important for the parties to know with certainty whether a stamp or sticker affixed on an invoice issued to the debtor would be deemed to be a "written" communication in the absence of any signature. The provision reads: *"In this Convention "writing" includes any form of writing, whether or not signed"*; the committee was however at the conclusion of its work conscious of the unsatisfactory nature of this wording which failed to mention modern means of communication, and it requested the Unidroit Secretariat to prepare for the Conference another formulation which could be based on definitions contained in other international texts, some of them still at the drafting stage, or in national law.

## Article 2

20. - *Paragraph 1*, whose structure is based on that of Article 1, paragraph 1 of the Vienna Convention, contains two kinds of provisions. The first determine the substantive scope of application which Article 1 has limited to factoring contracts, restricting it to the factoring of international receivables. This approach was decided on by the committee as it facilitates the application of the rules of the future Convention to domestic transactions for those States which wish to do so. Paragraph 1 establishes on the other hand the territorial scope of application of the Convention by indicating the connecting factors leading to its application.

21. - The *introductory language* of paragraph 1 provides that *"This Convention applies whenever the receivables assigned pursuant to a factoring contract arise from a contract of sale of goods between a*

supplier and a debtor whose places of business are in different States." Whereas Article 1 gives the definition of "factoring" for the purposes of the Convention, this provision of Article 2 defines "international" factoring. Since the principal aim of the proposed Convention is to facilitate factoring as an instrument for the promotion of international trade, it is easy to understand that the international character of factoring transactions should be determined by the international character of the contract of sale. This is moreover the one and only relevant factor as attempts to identify an independent international character of factoring contracts have shown that it would be undesirable for a receivable arising from a domestic sale relationship to be submitted to a different legal regime according to whether it is assigned to a factor in the same country or abroad, or yet again successively to two different regimes, the first of which might be internal law and the other the international Convention. The criterion selected for the purpose of qualifying the contract of sale of goods as international is that traditionally employed in recent international trade law conventions and in particular the Vienna Convention, Article 1, paragraph 1 of which provides that the parties to the contract must have their places of business in different States; in consequence, the place of business of the factor has no bearing on the question. It should finally be noted that the introductory language of paragraph 1 is intended to make it quite clear that, when a factoring contract makes provision for the assignment of both national and international receivables, only transactions relating to the latter will be subject to the regime established by the Convention.

22. - The determination of the territorial scope of application of the future Convention proved to be an extremely complex matter, principally on account of the two "layers" of contractual relations present in the transaction under consideration. In effect, as stated in the preceding paragraph, 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 sale contract on the factor and others which relate to 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 the committee to adopt the solution contained in the two sub-paragraphs of paragraph 1 of Article 2. *Sub-paragraph (a)* 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*". The committee considered that it was particularly desirable that the Convention should have an autonomous scope of application based on objective connect-

ing factors which would provide the certainty and speed indispensable for international factoring transactions and this solution seemed to be the one which best guaranteed the protection of the interests of each of the parties concerned, in particular those 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 even when the conditions laid down in sub-paragraph (a) are not met, the Convention will nevertheless apply "*when both the contract of sale of goods and the factoring contract are governed by the law of a Contracting State*", this formula being intended to cover those cases where the rules of private international law lead to the application of the law of a Contracting State to each of the two contracts, including those where the parties have chosen the law of a Contracting State to govern their respective contractual relationships. The reasons which led to the two contracts being taken into consideration were the same as those which dictated the choice of the places of business of the three parties in sub-paragraph (a); it should moreover be noted that the two contracts may both be governed by the law of the same Contracting State or each by the law of a different Contracting State. There was, however, some criticism within the committee of the introduction of a connecting factor based on conflicts rules in this Convention on the ground that it would cause serious difficulties in its practical application as the parties would, notwithstanding the large number of transactions and the speed with which they must be handled, have to undertake complicated and costly enquiries to ascertain whether the conditions laid down in Article 2(1) (b) had been satisfied. With a view to giving the future instrument a wide scope of application and so as to avoid departing from a solution contained in many recent international trade law conventions, the committee ultimately decided to maintain the rule, although it should be recalled that Article F of the draft final provisions<sup>(12)</sup> permits States to make a declaration that they will not be bound by Article 2, paragraph 1 (b).

23. - Since, as in other modern international trade law conventions, it is the place of business of the parties which serves to determine the international character of the contract of sale of goods and therefore of the factoring contract as well as the conditions for the application of the Convention under paragraph 1 (a), a factor which is moreover decisive for the application of Article 5, paragraph 1, it was essential to include a provision indicating the relevant place of business when one or more of the three parties involved has more than one place of business. The committee

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(12) See Study LVIII - Doc. 34, p.7.

took over, subject to the adaptations which were necessary having regard to the two contractual relationships relevant to factoring transactions, the formulation of the corresponding provision of the Vienna Convention (Article 10 (a)). Article 2, *paragraph 2* reads as follows: "For the purpose of this Convention, if a party to the contract of sale of goods or the factoring contract has more than one place of business, the place of business is that which has the closest relationship to the contract and its performance, having regard to the circumstances known to or contemplated by the parties at any time before or at the conclusion of that contract". The word "contract" in the third line of this provision should be understood as that corresponding to the legal relationship contemplated.

### Article 3

24. - Article 3 determines the extent to which the parties involved in factoring transactions may exclude the application of the prospective Convention and the circumstances in which such exclusions are operative. It should be recalled that in the course of the committee's work a view was expressed by some participants to the effect that the whole of the Convention could be of mandatory application, principally for the reason that it would be unlikely that the factor would wish to exclude rules which were designed to facilitate international factoring and that this aim would be frustrated if the parties to the contract of sale were to be free to choose another law to govern the assignment; a majority however declared itself to be firmly attached to the principle of party autonomy, all the more so as the subject fell within the domain of international trade law, and it stressed the fact that the choice of a mandatory regime could be detrimental to the success of the prospective Convention whereas many States would on the other hand be prepared to accept an instrument from whose provisions the parties could derogate.

25. - The principle which originally guided the thinking of the committee was that the parties might, in their relations with each other, exclude the application of the Convention. It seemed that the supplier and the factor could have a legitimate interest in submitting their relations to a law other than the Convention and that such freedom should be accorded to them, the debtor in any case not being a party to such an agreement; the rule is thus laid down in Article 3, *paragraph 1* that: "*The parties to the factoring contract may exclude the application of this Convention*".

26. - *Paragraph 2* is concerned with those situations where it is the supplier and the debtor who stipulate in the contract of sale or in a separate instrument that the Convention on international factoring shall not apply in the event of the assignment of the receivables arising under

that contract. Notwithstanding some doubts as to the desirability of allowing the parties to another contract (in this case the sale contract) to determine indirectly the law applicable to the contract governed by the future Convention (namely the factoring contract), the prevailing view was that the legitimate interests of the debtor, whose position was to a certain extent affected by the assignment, to exclude the application of the prospective rules should also be recognized. With a view however to protecting the factor who, on account of the need for certainty and speed in conducting the transactions with which he deals, must be able to proceed on the assumption that the Convention will govern the assignment, the committee agreed that he must be given notice, and not simply by means of the contract of sale, of the decision of the parties to that contract that the Convention shall not apply to assignments of receivables arising after the giving of such notice to the factor. In consequence, paragraph 2 provides that: *"The parties to the contract of sale of goods may exclude the application of this Convention only in respect of receivables arising at or after the time when the factor has received notice in writing of such exclusion"*. It should be noted that the term "writing" is to be understood in the light of the definition contained in Article 1, paragraph 3 of the future Convention.

27. - Finally, *paragraph 3* of Article 3 provides that: *"Where the application of this Convention is excluded in accordance with the preceding paragraphs of this article, such exclusion may be made only as regards the Convention as a whole"*. Although special agreements may sometimes be concluded between the debtor and the factor, in particular in connection with the rights dealt with in Article 8, the general view within the committee was that the future instrument should be seen as a whole which could not be split up or modified without disturbing the balance which it was sought to achieve between the rights and obligations of the parties involved in factoring transactions.

#### *Article 4*

28. - It has been seen from the commentary thereon that Article 1 contains a number of elements permitting a characterisation of a "factoring contract", one of which is that the supplier undertakes to assign or directly assigns receivables to the factor. Article 4 for its part provides a sound legal basis for the factoring contract effectively to assign the supplier's receivables to the factor, certain legal systems in effect not recognizing the global assignment of receivables, in particular future receivables. After affirming the validity as between the parties to the factoring contract of a clause in that contract under which existing or future receivables are to be assigned (subject to sufficient identification

of them), it indicates the time at which the transfer of the future receivables takes place.

29. - *The introductory language* 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 the parties so as to avoid any ambiguity as regards the scope of the article in those legal systems where the term "supplier" might be understood as possibly including a trustee in bankruptcy carrying on the supplier's business, an interpretation which would run counter to the committee's decision not to deal with the problem of the effectiveness of the assignment against third parties (including the trustee in bankruptcy or any other creditor of the supplier), certain effects of the assignment on the debtor being dealt with in Articles 7 to 9 of the Convention. *Sub-paragraph (a)* seeks to overcome the difficulties existing in some legal systems caused by the fact that an agreement to assign receivables may not be valid on account of the absence of any precise indication of the subject-matter of the assignment. It should be noted that it was not the committee's intention to establish a general rule governing the validity of the contract independently of other grounds of invalidity recognized by the applicable national law, a consideration which led it to clarify the English text as follows: "*a contractual provision ... shall not be rendered invalid by the fact that ...*", a refinement absent from the French text ("*une clause du contrat ... est valable, même si ...*") as in the opinion of the French-speaking representatives its wording could be open to no other interpretation than that intended by the committee. The only condition imposed by sub-paragraph (a) as regards the rule of limited validity enunciated by it is that the receivables must be described in such terms by the factoring contract that those subject to the assignment can be determined without difficulty, the time at which a given receivable may be identified to the contract being the conclusion of that contract as regards receivables already in existence and, in respect of future receivables, the time when they come into existence. Although the committee preferred not to lay down criteria governing the identifiability of receivables so as to leave a wide measure of appreciation to the judge, considerations which may be relevant are, for example, the designation by the contract of the line of goods or services contemplated, the countries from which the supplier's customers come or, possibly, a list of regular customers agreed by the parties to the factoring contract.

30. - Following the statement of principle as to the validity of global assignments, *sub-paragraph (b)* of Article 4 deals with the recognition of the effects of such a clause, namely the effective transfer not only of existing receivables, which goes without saying, but also of future receivables, the assignment being operative in such cases at the

very moment at which the receivable arises. While this rule reflects the law of a certain number of States, even though the parties sometimes choose to make a new assignment 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.

#### *Article 5*

31. - Article 5 attempts to settle a particularly thorny problem in the field of international factoring caused by the radically different solutions to be found in national law concerning the question of the validity of assignments to the factor when the supplier has acted in breach of an undertaking to his customer not to factor the receivables arising from their contract. The main interest of the debtor is to guard himself against a change in his creditor and to be certain that he will obtain discharge by making payment to the supplier, thus being free from any concern as to third party claims. As regards the supplier however, the factoring of receivables subject to a prohibition on assignment may sometimes be a source of financing necessary for the conduct of his business. Independently of priority questions involving third parties, the factor will, according to whether or not national law gives effect to the prohibition on assignment, either enjoy no rights in the receivable or acquire rights over it in accordance with the terms of the assignment stipulated by the parties to the factoring contract, a problem which is particularly acute in the event of the insolvency of the supplier.

32. - From the outset of the work on the draft, there was a feeling that such an important matter could not be left aside without seriously compromising the value of the future Convention as a whole. The underlying aim of facilitating international factoring would seem to lead to upholding the validity of the transfer, an approach initially followed in the draft rules. Some members of the committee supported this solution, which they saw as providing a degree of security in international factoring transactions, either because it reflected the position in their national law or, even though it constituted a departure from that law, was nevertheless acceptable in the context of international transactions; other representatives however were firmly opposed to a provision which ran counter to



the fundamental principle of the respect of party autonomy. The question was the subject of lengthy and detailed debate at various sessions of the committee, at which the supporters and the opponents of the original rule adduced a number of arguments which need not be repeated here <sup>(13)</sup>. The committee considered compromise solutions, none of which however, after careful examination, provided full satisfaction. The possibility was then studied of combining a provision dealing with the validity of an assignment effected in violation of a prohibition thereon stipulated between the parties to the contract of sale with a reservation clause which, while it would not offer a uniform solution to this controversial question, would at least have the merit of opening the way to a certain measure of harmonisation.

33. - The first attempt to settle the problem by way of the proposed new approach consisted in the affirmation of a basic principle ("The assignment ... shall be effective"), combined with a rule displacing the principle ("The provisions of the preceding paragraph shall not apply ...") when the debtor has his place of business in a Contracting State which has made a declaration to that effect. This solution was based on a similar approach adopted in the Vienna Convention (Articles 11, 12 and 96) and was intended, whenever the condition concerning the debtor's place of business was satisfied, to give free play to the rules of private international law to determine the applicable law for the purpose of resolving the question of the validity of the assignment. Serious objections were however raised in relation to this formula, the actual effects of which did not seem to be clear, and which was also criticized on the ground that it could in effect lead to the same result as that which some were seeking to avoid, all the more so as it was probable that the law applicable to the assignment would most often be that of the seller's place of business, and in consequence that of the factor, a solution which would hold out scant prospects of protection to the debtor.

34 - Moreover, on the basis of an earlier decision to limit the principle of the validity of the assignment of the receivable to the right to payment (following the model of the Uniform Customs and Practices for Documentary Credits), with the consequence that the debtor could never, unlike the case of other rights over the receivable, contest such a transfer, the committee came to the conclusion that it must distinguish the

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(13) See Study LVIII - Doc. 26, p. 13 et seq.

validity *inter partes* of the assignment from the question of its effectiveness against the debtor. Given the agreement reached within the committee on this important point, it decided to accept the principle of a reservation of a substantive character which would in any event have the merit of guaranteeing certainty. The rule finally adopted may be set out as follows: the general principle to be found in *paragraph 1* that "*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 agreement*" means on the one hand that the prohibition on assignment agreed by the parties to the contract of sale has no effect on the validity of the assignment of the receivable as between the parties to the factoring contract <sup>(14)</sup> and on the other that it does not prevent such an assignment having effects on the debtor. The exception to this rule, which applies by virtue of *paragraph 2* when the debtor has his place of business in a State which avails itself of the declaration for which provision will be made in the final clauses (see at present Article X of the text of the draft), will have no incidence on the validity of the assignments as between the parties to the factoring contract but will on the other hand protect the debtor from any effects of the assignment on him when he has stipulated a prohibition on assignment with the supplier. It follows that the factor cannot, in cases contemplated by Article 5, paragraph 2, rely on the provisions of the future Convention dealing with the position of the debtor subsequent to the assignment, namely Articles 7 to 9.

#### *Article 6*

35. - Article 6 performs a similar function to Article 4 in that after providing in its introductory language that the only relations dealt with are those between the parties to the factoring contract, it affirms the validity and effectiveness of a clause in a factoring contract providing for the transfer to the factor not only of the receivables but also of the rights of the supplier in the receivables assigned: what is intended here is to ensure that rights deriving from future sales may be transferred, thereby removing an obstacle existing in some legal systems, although it is to be understood that this article also applies to the transfer of rights already in existence.

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(14) Attention should be drawn to the fact that, like Article 4, Article 5, paragraph 1 does not seek to establish a general rule on validity but is intended only to remove the obstacle which could be created by the prohibition on the assignment.

36. - Apart from establishing the principle of the validity of the transfer of rights Article 6 indicates the method of transfer: the parties may agree that the assignment of the receivable will automatically carry with it any corresponding securities or alternatively that the rights in question can only be transferred by a special instrument to that effect. When the parties are silent on this point the matter will fall to be decided by the applicable national law, but it is in any event clear that whatever the choice of the parties as regards the method of transfer, it remains subject to the rules as to form or public notice of the applicable law to the extent that they seek to make the transfer effective against third parties.

37. - It should finally be mentioned in connection with the words "*the supplier's rights deriving from the sale of goods*" that the committee intended to cover securities (to be understood in the broadest sense so as to embrace the different forms existing under national law) which guarantee the assigned receivables in particular or, more generally, the performance of the contract of sale as a whole; moreover, both contractual and legal securities are contemplated. The committee considered it useful to cite by way of example the reservation of title. It need scarcely be added that this provision in no way affects questions concerning the validity and possible recognition abroad of such guarantees.

#### Article 7

38. - After laying down a number of rules relating to the validity of the assignment between the parties to the factoring contract, the draft Convention contemplates in Articles 7 to 9 the position of the debtor subsequent to the assignment (subject naturally to the provisions of Article 5, paragraph 2). It should be recalled that the committee chose from the outset of its work to dissociate the two aspects - validity *inter partes* and effects of the assignment on the debtor - so as to avoid placing the latter under a duty to make enquiries, possibly difficult ones, which could entail the most serious consequences for him.

39 - Whenever the factoring contract provides that the factor shall recover the receivables (or in the converse case, if the factor has good reason to require payment directly by the debtor), the debtor is under a duty in accordance with *paragraph 1* of Article 7 to make payment to the factor, an obligation which derives from the notice given in the manner prescribed in sub-paragraphs (a) to (c). Moreover, a condition additional to that of notice is one that the debtor did not have knowledge of any other person's superior right to payment of the receivable. This requirement, which the committee saw as being bound up with the concept of

good faith, seems however to place a certain burden on the debtor, for although he has no obligation to conduct research into the possible existence of creditors other than the factor, on the other hand whenever the debtor has knowledge of another person's claim to payment of the receivable, the present language of the provision may be taken as obliging him to make enquiries as to the merits of the claim and, if it does exist, as to whether it constitutes a superior right to payment. It should in conclusion be made clear that the two conditions (absence of knowledge of a superior right and notice given in accordance with sub-paragraphs (a), (b) and (c)) are both necessary and sufficient to create the debtor's obligation to pay the factor, which cannot therefore arise, in the context of a factoring transaction governed by the prospective Convention, from any rules of the applicable national law, whether more or less strict.

40. - *Sub-paragraph (a)* recalls in the first instance the requirement already referred to in Article 1, paragraph 1 (c) that notice must be given in writing, a notion to be understood in the light of the definition to be found in Article 1, paragraph 3. On the other hand this provision indicates the person who must give notice: this may first of all be the supplier on the ground that he is the original creditor who has concluded a contract with the debtor; the factor has however 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 priority among creditors is determined by the order in which notice is given, he will in most cases be more diligent than the supplier. Consequently, the committee considered that the factor should himself be capable of giving notice of the assignment, on condition however that he acts with the supplier's authority, this formula simply indicating that the debtor must have reasonable grounds for believing in the existence of the factor's authority, if appropriate by making enquiries of the supplier, although questions regarding the form of the authority and the possibility for notice to be given by other persons acting in the name of the supplier or of the factor are left to the applicable law.

41. - *Sub-paragraph (b)* provides that the notice must reasonably identify the beneficiary under the assignment to whom the debtor must make payment: this may be the factor himself and the committee agreed that the notice need not necessarily indicate that the assignee was indeed a factor, or a bank receiving payment on behalf of a factor. The notice must moreover reasonably identify the receivables so that the debtor may be informed of the precise subject matter of the assignment while, under *sub-paragraph (c)*, it must relate only to receivables arising under a contract made at or before the time the notice is given. In consequence, although a clause in the factoring contract effectively transfers all future receivables from the supplier to the factor pursuant to Article 4 of the draft Convention,

notice of the assignment of a future receivable will only place the debtor under an obligation to pay if the contract under which the receivable arose was made at or before the time notice was given.

42. - *Paragraph 2* of Article 7 provides in the first instance that payment by the debtor to the factor discharges the debtor's liability *pro tanto* if made in accordance with the provisions of paragraph 1. On the other hand, while the committee agreed that the debtor's obligation to make payment under the future Convention could only arise in cases where the conditions set out in paragraph 1 were met, it was nevertheless of the opinion that the debtor should be entitled to make payment and thereby to discharge his liability when such payment would have that effect under the applicable national law. Given the committee's unwillingness to refer to the applicable law without indicating how it should be determined, and its preference not to lay down a connecting factor in an instrument establishing uniform rules of substantive law, the paragraph provides that payment by the debtor in accordance with paragraph 1 shall discharge him from liability "*irrespective of any other ground on which payment by the debtor to the factor discharges the debtor from liability*".

#### Article 8

43. - This article is concerned with the extent to which the debtor may set up certain defences against the factor at the time of payment. *Paragraph 1* deals with defences relating to the receivable assigned and provides that the debtor may set up against the factor all defences of which the debtor could have availed himself under the same contract if such claim had been made by the supplier. *Paragraph 2* relates to defences available to the debtor against the supplier not connected with the receivable. The rule which has been adopted, and which is moreover to be found in many legal systems, is that the rights and claims on which the debtor may rely against the other party to the contract at the time he received notice of the assignment may be asserted against the factor. This solution is to be explained by a concern to protect the factor's position in respect of contracts concluded between the supplier and the debtor which subsequently give rise to rights of set-off of which the factor had no knowledge.

44. - It may be noted that Article 8 limits itself to laying down two fundamental principles concerning the debtor's rights as against the factor, many aspects of the question thus being left to national law, especially those falling under the complicated law of set-off. In particular the committee deemed it preferable not to indicate whether the rights "*available to the debtor*" are those due for payment or simply those in

existence at the time notice is received. Furthermore, while the provision confirms the debtor's right of set-off in relation to rights or claims *"existing against the supplier in whose favour the receivable arose"*, it leaves open the question of the effectiveness of rights of set-off arising out of any earlier dealings between the debtor and the factor, or of dealings with other suppliers of the debtor who assign their receivables to the same factor. Likewise, Article 8, paragraph 2 provides that the notice which serves to limit the defences is that given in accordance with Article 7 of the Convention. It is in consequence to be understood that the effects of different forms of notice which will not therefore be effective under the future Convention will be determined by the applicable national law. Finally, some legal systems provide that in certain cases the debtor will lose the benefit of defences, in particular his right of set-off (in some systems when the debtor accepts the assignment), and the committee recalled that in conformity with Article 11, paragraph 2 the absence of any rule on this matter in the Convention would in any event mean that the question would be determined by the applicable national law.

#### *Article 9*

45. - The case contemplated by Article 9 is that where the debtor has already fulfilled his obligation to make payment but has not received consideration in that the supplier has failed to perform his obligations under their contract. The special feature of this situation following the assignment of the receivable is that, when looked at from the debtor's point of view, there is a dissociation of the person who receives payment from the one who supplies the goods or services. In the case of a continuing relationship the debtor may certainly, in accordance with Article 8, paragraph 2, subsequently set-off against the factor his rights against the supplier (recourse by the factor against the supplier being dealt with in the factoring contract); however the problem here is that of deciding whether the factor is obliged to return to the debtor money received from him.

46. - A certain number of arguments were adduced in the committee in favour either of denying the debtor's right to recover money paid to the factor or of leaving the problem to be decided by the applicable law. The committee as a whole was however in agreement as regards the general approach which would determine the solution to be adopted, namely that the debtor's position should be neither improved nor worsened as a result of the assignment. In particular there was thus no reason, in the event for instance of the supplier's bankruptcy, for the debtor to recover a sum from the factor when he might not have been able to do so had no factoring contract been concluded. On the other hand, in those legal systems where

the debtor loses his right to claim recovery of the price from the supplier because it is the factor who has received payment, it did not seem fair to deprive the debtor of the possibility of recovery from the factor. *Paragraph 1* reflects a concern not substantially to alter the debtor's existing situation, by providing that the supplier's failure to perform shall not alone entitle the debtor to recover money paid to the factor (any other grounds of recovery which may exist under national law therefore being unaffected). The application of this rule is however restricted by the last part of the provision to those cases where, under the applicable national law, the debtor has not been deprived by the assignment of his claim against the supplier for recovery of the price.

47. - The committee considered it desirable to state in *paragraph 2* two exceptions to the general rule intended to protect the factor (exceptions applicable on condition that the debtor has a claim against the supplier for recovery of the price), which are, independently of the position of the debtor, justified by the financial role of the factor in the transaction. *Sub-paragraph (a)* provides that the debtor may recover money paid to the factor to the extent that the latter has not paid the purchase price of the receivable to the supplier, the situation contemplated being that of the unjust enrichment of the factor when the sum paid by the debtor has remained in the hands of the factor, either because the latter ought already to have paid the supplier or because he has not yet done so. For its part, *sub-paragraph (b)* is concerned with the case where the factor has already paid the supplier the purchase price of the receivable although he knew at the time of such payment that the supplier had not yet performed his own obligations towards the debtor. The committee considered that in such circumstances it was the factor and not the debtor who should subsequently assume the financial risk deriving from non-performance or defective or late performance by the supplier, all the more so as it is customary for factors to include in the factoring contract guarantees as to performance and to retain part of the advance with a view to securing their position against the supplier.

#### Article 10

48. - In conformity with Article 1, the articles of the draft Convention preceding Article 10 have been concerned with the situation where it is one and the same factor to whom the supplier assigns the receivable and to whom payment is made by the debtor. Although this system is well known in international factoring, it is more often the case that, for reasons of practicality, a second factor enters on the scene: the supplier assigns the receivable pursuant to a factoring contract concluded with a factor who is usually located in the same country and the latter in his turn assigns the

receivable to another factor who acts as his correspondent in the debtor's State, the two factors being respectively designated by practice as "the export factor" and "the import factor". It is evident that from the outset of the work it was understood that this kind of factoring should fall within the rules to be contained in the future instrument, the position of the subsequent factor to whom the assignment is made being assimilated, *mutatis mutandis*, to that of the other party to the factoring contract concluded by the supplier, not only as regards the provisions concerning the validity of the assignment of the receivable but also the conditions under which the assignment may be effective against the debtor. While the committee entertained no doubts as to the usefulness of applying the Convention to assignments as between factors, on the other hand the drafting of this article caused a number of difficulties <sup>(15)</sup> arising principally from the fact that although the relations between the parties to the contract for the subsequent assignment may be assimilated to those between the parties to the factoring contract, the underlying sale relationship retains its relevance in a number of respects. The present wording of Article 10, paragraph 1 is a combination of two approaches to the transposition to subsequent assignments of the rules of the Convention previously examined by the committee; at its final session however it considered that the drafting called for improvement, in particular in the light of a detailed examination of the way in which the transposition mechanism would operate in connection with each of the provisions of the future Convention.

49. - Article 10 contains provisions relating to the future Convention's scope of application as well as substantive rules of law. The *introductory language* of *paragraph 1* determines the connecting factor according to which the Convention will apply to subsequent assignments of the receivable by the factor or by a subsequent assignee. The committee rejected a number of criteria such as the particular characteristics of the contract for the subsequent assignment of the receivables or the character of the parties to that contract; nor did it consider it desirable to establish a connecting factor based on the subsequent assignee's place of business or on an alternative conflicts rule modelled on Article 2, paragraph 1 (b), principally because the subsequent assignee is most often in practice a factor with his place of business in the same State as the debtor. The only condition required for the rules of the Convention to apply - in accordance with sub-paragraphs (a) and (b) - to a subsequent assignment of a receivable is that the latter has previously been "... assigned by a supplier to a factor pursuant to a factoring contract governed by this Convention".

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(15) See Study LVIII - Doc. 23, p. 5 et seq., which also sets out the drafting proposals made by the Secretariat.



50. - The two sub-paragraphs of paragraph 1 contain the very principle on which the extension of the scope of application of the Convention rests. *Sub-paragraph (a)* provides that the rules laid down in Articles 3 to 9 (with the exception of Articles 7 and 8 which are dealt with in sub-paragraph (b)) apply to any subsequent assignment of the receivable by the factor or by a subsequent assignee. The term "subsequent assignment" is to be understood as referring to the transfer of the receivable by the person to whom it has been assigned and not, of course, to a second fraudulent assignment by the same assignor. In this connection it may be recalled that a proposal was made at the second session of the committee for the inclusion of a separate article laying down a limited priorities rule which would apply in such cases; given however the difficulty of reaching agreement on a criterion acceptable to all legal systems and of the restricted scope which such a rule would enjoy in practice, this proposal was rejected by the committee. Moreover, if a series of transactions takes place following the first assignment, all of those assignments will be governed by the Convention provided that that assignment was itself governed by the rules of the Convention and, as indicated above, this will be the case whatever the form or the characteristics of the subsequent assignment or assignments and the status or places of business of the subsequent assignees. The committee considered that the flexible formulation of the rule contained in sub-paragraph (a) would permit those called upon to interpret it to apply to any subsequent assignment of the receivable the principles governing an assignment made pursuant to a factoring contract. Those principles may briefly be recalled here, in the context of subsequent assignments, in respect of each of the articles in question. In the first place Article 3, which permits the parties to exclude the application of the Convention, has been included among those referred to by Article 10 as a consequence of the changes in the order and numbering of its provisions; in the event of it being decided to allow the parties to a subsequent assignment to exclude the application of the Convention to their transaction, it would be preferable to indicate in detail the operation and effects of such a rule, in particular in regard to its implications for the debtor. By virtue of the combination of Articles 10 and 4, a subsequent assignor may validly make a global assignment of future receivables and he may also transfer rights deriving from the sale of goods (Article 6). In conformity with Article 5, a prohibition on assignment agreed upon by a supplier and a debtor who has his place of business in a Contracting State which has made the declaration for which provision is made in the corresponding article (at present entitled Article X), will not prevent a subsequent assignment of the receivable which has already been validly assigned pursuant to a factoring contract, although the debtor will continue to be protected from the effects of such assignments. Finally, the circumstances in which the debtor may recover payments made to a factor which are set out in Article 9 may without

difficulty be transposed so as to apply to a subsequent assignment as it is obvious that the debtor will only pay once, either to the assignee of the supplier when there is only one factor, or to the last assignee in the event of successive assignments, especially when the factoring transaction is performed by two factors.

51. - As regards Articles 7 and 8, the committee considered it useful to reconsider at its final session the fiction contained in *sub-paragraph (b)* of Article 10, paragraph 1 whereby the subsequent assignee is, as regards the debtor, placed in the position of the factor: for the same reasons as those set out in relation to Article 9, the debtor is, in the case of a subsequent assignment, required to pay only the subsequent assignee, subject to the requirements of Article 7, paragraph 1 being met, and he is discharged from liability in accordance with paragraph 2 of that article. Similarly, the debtor may set up against the subsequent assignee any of the defences under the contract of sale and rights of set-off existing against the supplier referred to in Article 8. It may therefore be noted that in these circumstances the draft Convention is silent as to the rights of set-off available to the debtor against the last assignee arising out of his relations with the factor or any earlier assignee, a matter which will in consequence fall to be determined by the applicable national law.

52. - When notice of the subsequent assignment is not given to the debtor, the latter is informed only of the first assignment made pursuant to the factoring contract and thus in such cases the rules contained in Articles 4 to 6 will govern the corresponding aspects of the validity of both the first and the second assignments, although the provisions of Articles 7 to 9 will be of relevance only to the first assignment. As a general rule however, in international factoring transactions, the supplier gives notice to the debtor that he must make payment to a person who is in fact the subsequent assignee, no notice having been given of the first assignment. Since only notification factoring is dealt with by the future instrument, pursuant to Article 1, paragraph 1 (c), it was important to ensure that the absence of notice regarding the first assignment would not have the effect of excluding it from the application of the Convention (and in consequence all subsequent assignments) and for this reason it was decided to include a provision such as *paragraph 2* of Article 10 by virtue of which "*Notice to the debtor of the subsequent assignment may also constitute notice of the assignment to the factor*".

53. - *Paragraph 3*, which provides that "*This Convention shall not apply to an assignment which is prohibited by the terms of the factoring contract*" was introduced at the request of one delegation which recalled that its law did not allow a receivable which had already been assigned to

be assigned a second time and that factoring contracts contained a clause whereby the factor undertook not to reassign the receivable; in the context of international transactions the supplier directly assigned the receivables to an import factor in the same State as that in which the debtor had his place of business. It may however be noted that doubts were expressed within the committee as to the need for such a provision; in any event it does not seem that the possible application of the Convention to a subsequent assignment made in violation of a prohibition contained in the factoring contract would validate such an assignment (Articles 4 to 6 in effect doing no more than laying down rules of limited validity), this question being determined by the applicable national law, which is indeed the result to which paragraph 3 leads. Furthermore, as regards the effects on the debtor, he would not, unless the supplier himself had given notice to the debtor of the subsequent assignment made in contravention of his own obligation in the factoring contract, be under a duty to pay the subsequent assignee pursuant to Article 7 since the latter would have no authority from the supplier to give notice of the assignment.

#### *Article 11*

54. - Article 11 concerns the rules of interpretation to be applied in respect of the future Convention. The language of *paragraph 1* is based on that of the corresponding provision of the Vienna Convention, namely Article 7, which has been incorporated in a number of international trade law conventions and 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. Furthermore, a new consideration, not to be found in the precedents for the wording of this article, has been added to those designed to aid in the interpretation of the Convention, namely its object and purpose as set forth in the Preamble, so as to ensure that the Convention will be applied in accordance with the intention of its authors and with the declared objectives of States when they become Parties to it. Finally, *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. It should be noted that unlike the Vienna Convention (Article 7) and the Geneva Agency Convention (Article 6) which contemplate reference to the applicable law only in the absence of general

principles on which the Convention is based, such principles and the applicable law are here placed on the same footing.

LIST OF THE REPRESENTATIVES OF GOVERNMENTS, INTERNATIONAL ORGANISATIONS AND PROFESSIONAL ASSOCIATIONS WHO ATTENDED ONE OR MORE (\*) OF THE SESSIONS OF THE UNIDROIT COMMITTEE OF GOVERNMENTAL EXPERTS FOR THE PREPARATION OF A DRAFT CONVENTION ON CERTAIN ASPECTS OF INTERNATIONAL FACTORING (\*\*)

LISTE DES REPRESENTANTS DES GOUVERNEMENTS, DES ORGANISATIONS INTERNATIONALES ET DES ASSOCIATIONS PROFESSIONNELLES QUI ONT PARTICIPE A UNE OU PLUSIEURS (\*) SESSIONS DU COMITE D'UNIDROIT D'EXPERTS GOUVERNEMENTAUX CHARGE D'ELABORER UN PROJET DE CONVENTION SUR CERTAINS ASPECTS DU FACTORING INTERNATIONAL (\*\*)

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Le numéro (1) porté après le nom et l'adresse d'une personne indique que celle-ci a participé à la première session du comité; (2) qu'elle a participé à la deuxième session; (3) qu'elle a participé à la troisième session.

(\*\*) The committee held three sessions, all at the seat of Unidroit in Rome. The first ran from 22 to 25 April 1985, the second from 21 to 23 April 1986 and the third from 22 to 24 April 1987.

Le comité a tenu trois sessions, au siège d'Unidroit à Rome; la première du 22 au 25 avril 1985, la deuxième du 21 au 23 avril 1986 et la troisième du 22 au 24 avril 1987.

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