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Factoring Model Law Working Group

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PRELIMINARY DRAFTING SUGGESTIONS FOR THE MODEL LAW ON FACTORING

1. This document provides preliminary drafting suggestions for the future Model Law on Factoring. At this stage, this document contains preliminary versions of three possible chapters:
 - a. Chapter I – Scope and general provisions (Page 3)
 - b. Chapter II – Transfers of receivables (Page 9)
 - c. Chapter III – Making a transfer of a receivable effective against third parties (Page 12).
2. The drafting follows the UNICITRAL Model Law on Secured Transactions (MLST) as a starting point, as the MLST is the most recent example of a model law developed by an intergovernmental organisation in this area and reflects current thinking on best practices. This methodology is also consistent with the definition and scope of the project as included in our Work Programme ([C.D. \(98\) 14 rev. 2](#)).
3. The tables in each of the chapters on the following pages include proposed text for articles to be included in the future Model Law on Factoring, their corresponding articles in the MLST, as well as items for discussion. The Working Group is also invited to consider issues of numbering, structure, etc, as the present draft is of a preliminary nature. Many of the articles prepared are based on consensus or discussion which took place during the first session of the Working Group. Where possible, the relevant sections of the [Summary Report of the First Session \(Study LVIII A – W.G.1 – Doc. 4 rev. 1\)](#) have been referenced accordingly.
4. The Secretariat is grateful to Working Group Members Mr Bruce Whittaker (University of Melbourne) and Mr Marek Dubovec (Kozolchyk National Law Center (NatLaw)) for their assistance in the preparation of this document.

MODEL LAW ON FACTORING

DRAFTING SUGGESTIONS FOR CHAPTER I – SCOPE AND GENERAL PROVISIONS

Art.	Suggested text	Corresponding Article in MLST	Discussion
	Article I – Scope of application		
1.	This Law applies to [transfers] of receivables.	1(1)	The Working Group may wish to consider whether the Model Law on Factoring should use the term “transfer” or “assignment” (or something else entirely).
2.	Despite paragraph 1, this Law does not apply to:	1(3)	It may be worth giving further consideration to whether it is desirable to exclude certain types of transfers of receivables from the scope of the Model Law on Factoring, for at least two reasons: <ul style="list-style-type: none"> - While the primary focus of the Model Law on Factoring is to facilitate the transfer of receivables as a capital-raising tool, there is no <i>a priori</i> reason why it should not facilitate transfers of receivables in other contexts. - If a receivable is covered by the Model Law on Factoring but some dealings in it are not, then difficult priority issues can arise if there is a competition between a transfer that is covered by the law, and one that is not.
(a)	[a transfer of a receivable as part of the sale or change in ownership status of the business out of which the assigned receivable arose]; or		This language is taken from the 2001 United Nations Convention on the Assignment of Receivables in International Trade (Assignment Convention) (Article 4(1)(b)). There is no equivalent provision in the MLST. The Working Group may wish to consider whether this should be retained, both for the reasons set out above, and for a number of additional reasons: <ul style="list-style-type: none"> - there is no equivalent provision in the MLST; - the UCC and PPSAs contain a similar exclusion; and - the meaning of some of the text is unclear (eg “change in ownership status”).¹
(b)	[a transfer of a receivable for collection].		It was suggested at the first meeting of the Working Group that the law should perhaps exclude transfers for collection. The

¹ See summary of this issue in Paragraph 66 of the Summary Report of the First Session of the Working Group (Study LVIII A – W.G.1 – Doc. 4 rev. 1)

Art.	Suggested text	Corresponding Article in MLST	Discussion
			consensus was that they should not necessarily be excluded for all purposes. If that is agreed, then para (b) would come out. Note that this text does not appear in either the Assignment Convention or the MLST. Furthermore, some specific provisions might be needed to clarify the aspects of the FML that would not apply to such transfers (e.g., registration). ²
3.	[<i>Application to proceeds – to be discussed.</i>]	1(4)	
4.	Nothing in this Law affects the rights and obligations of a transferor or a debtor of a receivable under other laws governing the protection of parties to transactions made for personal, family or household purposes.	1(5)	This concept was discussed in principle at the first meeting of the Working Group, but no conclusion was reached on how it should be formulated. ³
5.	Nothing in this Law overrides a provision of any other law that limits the transfer of specific types of receivable, with the exception of a provision that limits the transfer of a receivable on the sole ground that it is a future receivable, or a part of or an undivided interest in a receivable.	1(6)	The Working Group only generally discussed “statutory bars” on transfers, and is yet to reach a conclusion. If those bars were not to be overridden, this provision will be retained. ⁴
	Article 2. Definitions		The corresponding heading in the MLST says “Definitions and rules of interpretation”, but appears to contain only definitions.
	For the purposes of this Law:		
(-)	“Debtor” of a receivable means a person who owes payment of the receivable, including a guarantor or other person secondarily liable for payment of the receivable.	1(i)	This is a slightly simplified version of the definition “debtor of the receivable” in the MLST.
(-)	“Receivable” means a [contractual] right to payment of a sum of money, other than:	2(dd)	The MLST uses the expression “right to payment of a monetary obligation”. That is arguably a slightly jumbled formulation, as one technically holds either a right to <i>discharge</i> of a monetary

² See summary of this issue in Paragraph 56 of the Summary Report of the First Session of the Working Group (Study LVIII A – W.G.1 – Doc. 4 rev. 1)

³ See summary of this issue in Paragraph 120 of the Summary Report of the First Session of the Working Group (Study LVIII A – W.G.1 – Doc. 4 rev. 1)

⁴ See summary of this issue in Paragraph 162 of the Summary Report of the First Session of the Working Group (Study LVIII A – W.G.1 – Doc. 4 rev. 1)

Art.	Suggested text	Corresponding Article in MLST	Discussion
			<p>obligation, or a right to <i>payment</i> of a sum of money. The proposed language is also closer to the corresponding text in the Assignment Convention (Article 2(a)). It does however use the term “money”, which may raise questions about exactly this means (e.g. does it include cryptocurrencies?).</p> <p>The Working Group decided at its first meeting that the concept of receivable should apply to contractual rights, but that the exact meaning of that term needed further consideration. The Working Group did not form a view on whether the Law should extend to non-contractual payment rights (and if so, which ones).⁵</p>
	(i) a right to payment under a negotiable instrument;	2(dd)	<p>The Assignment Convention states that nothing in the Convention “affects the rights and obligations of any person under the law governing negotiable instruments” (Article 4(3)). The MLST approach distinguishes receivables and instruments through a set of definitions.</p> <p>The Working Group was did not make a decision in relation to the treatment of different types of negotiable instruments in the Model Law on Factoring.⁶</p>
	(ii) a right to payment of funds credited to a bank account;	2(dd)	<p>Similar to the previous paragraph, the Assignment Convention does not exclude bank accounts from the definition of “receivable”, but instead says that the Convention “does not apply” to an assignment of a receivable arising from bank deposits (Article 4(2)(f)).</p>
	(iii) a right to payment under a security;	1(3)(c), 2(dd)	
	(iv) a right to payment under an independent guarantee or letter of credit;	1(3)(a)	<p>The MLST put this exclusion into Article 1, rather than as an exclusion to the definition of receivable in Article 2(dd), because it wanted to exclude letters of credit etc from the whole law, not just from the concept of a receivable. As the Model Law on Factoring is only about receivables, we can achieve the same effect by simply excluding it from the definition of receivable. The</p>

⁵ See summary of this issue in Paragraph 28 of the Summary Report of the First Session of the Working Group (Study LVIII A – W.G.1 – Doc. 4 rev. 1)

⁶ See summary of this issue in Paragraph 49 of the Summary Report of the First Session of the Working Group (Study LVIII A – W.G.1 – Doc. 4 rev. 1)

Art.	Suggested text	Corresponding Article in MLST	Discussion
			Assignment Convention adopts a different drafting technique in Article 4(2)(g), but with substantially the same result.
	(v) a right to payment arising under or from financial contracts governed by netting agreements, except a payment right arising upon the termination of all outstanding transactions; or	1(3)(d)	Same point as for the preceding paragraph.
	(vi) [others?].		Other potential exclusions to be discussed. See for example Article 4(2) of the Assignment Convention. Whether there is a need for additional exclusions (or indeed for the exclusions listed in subparas (i) to (v)) will depend on whether the primary definition of "receivable" is left very broad. For example, they may not be needed if the primary definition is limited to classical factoring arrangements, i.e. receivables from the sale of goods or provision of services, similarly to the UNIDROIT Factoring Convention
(-)	"Security" means: [(i)] An obligation of an issuer or any share or similar right of participation in an issuer or in the enterprise of an issuer that: (A) Is one of a class or series, or by its terms is divisible into a class or series; [and] (B) Is of a type dealt in or traded on a recognized market, or is issued as a medium for investment; [and (ii) The enacting State to specify any additional rights that should qualify as securities even if they do not satisfy the requirements expressed in subparagraphs (i)(A) and (B).;]	2(hh)	The term "security" is used in an exclusion from the definition of "receivable" (subpara (iii)). This definition does however add complexity to the Model Law on Factoring. Similarly, if other exclusions from the definition of "receivable" (e.g. the exclusion of netting agreements) necessitate additional detailed definitions then this will detract from the Model Law on Factoring as a whole, as it will become cluttered with definitions that have no relevance to factoring.
(-)	"Transfer" of a receivable means:	2(kk)	The Working Group may wish to consider whether this text should be retained here or moved to Article. 1(1).
	(i) an [absolute/outright] transfer of the receivable by agreement; and	2(kk)	This is to exclude transfers by operation of law. It covers both outright transfers, and transfers by way of security. See also the

Art.	Suggested text	Corresponding Article in MLST	Discussion
			Discussion related to the definition of “receivable” with respect to non-contractual rights to payment. ⁷
	(ii) [A transfer/An assignment] of the receivable by agreement, or the creation of an interest in the receivable by agreement, in either case to secure payment or other performance of an obligation, regardless of the way in which the parties have described the transaction, the status of the transferor or the nature of the secured obligation.	2(kk)	<p>This captures the creation of an interest in a receivable by way of. This was not discussed at the first meeting, at least not in depth. The text is included as a prompt for further discussion.</p> <p>The corresponding definition in the MLST (of “security right”) divides the subject matter up differently, by dealing first with in-substance security rights (whether or not by way of transfer), and then with outright transfers of receivables. That reflects the fact that the primary focus of the MLST is on security rights, not transfers. For the Model Law on Factoring, however, the primary focus is on outright transfers, not on security rights <i>per se</i>. The proposed drafting here reflects this.</p>
(-)	“Transfer agreement” means an agreement made in accordance with Article 6(4) that provides for the transfer of a receivable.	2(jj)	<p>The corresponding definition in the MLST (of “security agreement”) repeats the substance of the subparagraphs of the definition of “security right”, i.e. the express inclusion in the law of outright transfers of receivables, in addition to in-substance security rights. Given the way in which we define “transfer” of a receivable, it is not clear that this is necessary.</p> <p>The proposed text also cross-refers to the requirements for a transfer agreement that are set out in Article 6(4). The MLST does not do this in the corresponding definition of security agreement, but instead simply says in its Article 6(3) that a security agreement “must” comply with the requirements set out in the Article. The intention behind Article 6(3) of the MLST no doubt is that an agreement can only be a security agreement for the purposes of the MLST if it complies with those requirements, but the drafting leaves this less than completely clear. The proposed drafting of the definition of transfer agreement removes the uncertainty.</p>
(-)	“Transferee” means a person to whom or in whose favour a receivable is transferred.	2(ff)	The dichotomy of having both “to whom” and “in whose favour” is intended to capture both limbs of the definition of transfer (i.e.

⁷ See discussion of this issue in Paragraphs 11-28 of the Summary Report of the First Session of the Working Group (Study LVIII A – W.G.1 – Doc. 4 rev. 1)

Art.	Suggested text	Corresponding Article in MLST	Discussion
			<i>transfer</i> of a receivable to a transferee, or <i>creation</i> of a security right <i>in favour of</i> a transferee).
(-)	"Transferor" means a person who transfers a receivable.	2(o)	
	Article 3. Party autonomy		The proposed text for this Article is materially identical to the corresponding provisions in the MLST.
1.	With the exception of Articles [...], the provisions of this Law may be derogated from or varied by agreement.	3(1)	
2.	An agreement referred to in paragraph 1 does not affect the rights or obligations of any person who is not a party to the agreement.	3(2)	
3.	[Nothing in this Law affects any agreement to use alternative dispute resolution, including arbitration, mediation, conciliation and online dispute resolution.]	3(3)	The Working Group may wish to consider whether it wants to include this in the Model Law on Factoring, even though it is in the MLST that has a broader scope covering transactions where these mechanisms are important.
	Article 4. General standards of conduct		The proposed text for this Article is identical to the corresponding provision in the MLST.
	A person must exercise its rights and perform its obligations under this Law in good faith and in a commercially reasonable manner.	4	During the drafting of MLST, One suggestion was that the word "commercially" qualifying the words "reasonable manner" in paragraph 1 should be deleted or revised as, in many jurisdictions, the concept of "commercial reasonableness" was not known and its use might inadvertently result in uncertainty and increased litigation. While some support was expressed, that suggestion was adopted. It was stated that the concept of "commercial reasonableness" referred to the commercial context and to best business practices, and was universally known. It was widely felt, however, that the Guide to Enactment could usefully elaborate on that concept. The Working Group may wish to consider this matter.

Art.	Suggested text	Corresponding Article in MLST	Discussion
	Article 5. International origin and general principles		<p>The proposed text for this Article is identical to the corresponding provisions in the MLST.</p> <p>It also reflects Article 4 of the UNIDROIT Model Leasing Law, so its inclusion would be consistent with the model law drafting conventions of UNIDROIT.</p>
1.	In the interpretation of this Law, regard is to be had to its international origin and the need to promote uniformity in its application and the observance of good faith.	5(1)	
2.	Questions concerning matters governed by this Law that are not expressly settled in it are to be settled in conformity with the general principles on which this Law is based.	5(2)	

MODEL LAW ON FACTORING**DRAFTING SUGGESTIONS FOR CHAPTER II – TRANSFERS OF RECEIVABLES**

Art.	Suggested text	Corresponding Article in MLST	Discussion
	Article 6. Requirements for the transfer of a receivable		
1.	A receivable may be transferred by a transfer agreement, provided that the transferor has rights in the receivable or the power to transfer it.	6(1)	
2.	A transferor may transfer:		Article 8 of the MLST also contains Article 8(a), which says that a security right may encumber “any type of movable asset”. As this law deals only with receivables, it did not seem necessary to include an equivalent provision here. Compare also with Article 8(1) of the Assignment Convention that uses a different drafting technique.
	(a) a part of or an undivided interest in receivables;	8(b)	The Working Group may wish to consider whether the Model Law needs to refer to both “parts” of a receivable and “undivided interest” in receivables”– and if so, whether they should be covered in the same or different paragraphs.
	(b) a generic category of receivables; and	8(c)	The Working Group may wish to consider whether this is necessary, or whether the fact that a person can transfer all of their receivables makes it sufficiently clear that a person can transfer something less, like a category.
	(c) all of a transferor’s receivables.	8(d)	
3.	A transfer agreement may provide for the transfer of a future receivable, but the transfer occurs only when the transferor acquires rights in the receivable or the power to transfer it.	6(2)	
4.	A transfer agreement must be [in/evidenced by] a writing that is signed by the transferor and:	6(3)	Article 6(3) of the MLST also contains two paragraphs that set out how the security agreement should identify the obligation that is secured. As the principal focus of this law is on transfers of receivables rather than secured credit, it may overly complicate the Model Law on Factoring with marginally-relevant text if we were to include similar provisions here as well.

Art.	Suggested text	Corresponding Article in MLST	Discussion
			<p>This draft also does not include an equivalent of Article 7 of the MLST, for the same reason.</p> <p>The Working Group should discuss whether any additional text is needed to ensure that the State does not impose some formalities, like notarisation.</p>
	(a) identifies the transferor and the transferee; and	6(3)(a)	
	(b) describes the receivables as provided in paragraph 5.	6(3)(c)	
5.	A transfer agreement must describe the receivables in a manner that reasonably allows their identification. This includes a description that indicates that the receivables consist of all of the transferor's receivables, or all of the transferor's receivables within a generic category.	9(1) and (2)	
	Article 7 - proceeds	10	
1.	A transfer of a receivable extends to its identifiable proceeds.	10(1)	The Working Group discussed this topic at its first meeting, but without coming to a view on how it should be handled. This text is included as a starting point for further discussion. ⁸
	Article 8 – Contractual limitations on the transfer of receivables		The suggested text for Article 8 is materially identical to the corresponding text in the MLST. It is provided as a starting point for discussion.
1.	A transfer of a receivable is effective notwithstanding any agreement between the initial or any subsequent transferor and the debtor or any transferee limiting in any way the transferor's right to transfer the receivable.	13(1)	
2.	Neither a transferor nor a transferee is liable to any person for breach by the transferor of an agreement referred to in paragraph 1, and the other party to the agreement may not avoid the contract giving rise to the	13(2)	The Working Group decided at its first meeting that a debtor should not be able to sue a transferor at all for breaching an anti-assignment clause. That goes beyond the language of Article 13(2) of the MLST. ⁹

⁸ See discussion of this issue in Paragraphs 214-219 of the Summary Report of the First Session of the Working Group (Study LVIII A – W.G.1 – Doc. 4 rev. 1)

⁹ See summary of this issue in Paragraph 162 of the Summary Report of the First Session of the Working Group (Study LVIII A – W.G.1 – Doc. 4 rev. 1)

Art.	Suggested text	Corresponding Article in MLST	Discussion
	receivable or the transfer agreement on the sole ground of the breach of that agreement. A person that is not a party to the agreement referred to in paragraph 1 is not liable for the transferor's breach of the agreement on the sole ground that it had knowledge of the agreement.		As a result of this change in approach from the MLST, it may be that the final sentence of this paragraph is no longer needed.
3.	This Article applies only to receivables:		The Working Group did not decide at its first meeting how to describe the types of receivables to which this Article should apply. The application of this Article would also depend on the types of receivables within the scope of the Model Law on Factoring that the Working Group is yet to settle on. The text from the MLST is provided as a starting point for discussion.
	(a) arising from a contract that is a contract for the supply or lease of goods or services other than financial services, a construction contract or a contract for the sale or lease of immovable property;	13(3)(a)	
	(b) arising from a contract for the sale, lease or licence of industrial or other intellectual property or of proprietary information;	13(3)(b)	
	(c) representing the payment obligation for a credit card transaction; or	13(3)(c)	
	(d) arising upon net settlement of payments due pursuant to a netting agreement involving more than two parties.	13(3)(d)	
	Article 9. Personal or property rights securing or supporting payment of a receivable		
	A transferee of a receivable has the benefit of any personal or property right that secures or supports payment of the receivable without a new act of transfer. If that right is transferable under the law governing it only with a new act of transfer, the transferor is obliged to transfer the benefit of that right to the transferee.	14	This is a topic that has not yet been considered by the group. The suggested text is materially the same as the corresponding provision in the MLST and is provided here as a starting point for discussion. ¹⁰

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See Paragraph 30-31 of the Issues Paper for the Second Session of the Working Group (Study LVIII A – W.G.2 – Doc. 2)

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DRAFTING SUGGESTIONS FOR CHAPTER III – MAKING A TRANSFER OF A RECEIVABLE EFFECTIVE AGAINST THIRD PARTIES

Art.	Suggested text	Corresponding Article in MLST	Discussion
	Article 10. Registration		
1.	A transfer of a receivable is only effective against third parties if a notice with respect to the transfer is registered in the Registry.	18(1)	For some aspects of registration, see Part I of the Issues Paper for the Second Session of the Working Group (Study LVIII A – W.G.2 – Doc. 2)
2.	If the third-party effectiveness of a transfer lapses, third-party effectiveness may be re-established in accordance with paragraph 1, but the transfer is effective against third parties only as of that time.	21	This provision may not be necessary, and the consequence of a lapse may be explained in a commentary.
	Article 11. Proceeds	19	
	<i>[To be discussed.]</i>		
	Article 12. Continuity in third-party effectiveness upon a change of the applicable law to this Law	23	This topic is being considered by the conflict-of-laws subgroup.