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Item No. 5 on the agenda: Ongoing legislative activities

(a) Development of a Model Law on Factoring

(prepared by the Secretariat)

<i>Summary</i>	<i>Report on the Model Law on Factoring project.</i>
<i>Action to be taken</i>	<i>Note the progress made by the Model Law on Factoring Working Group, decide whether the draft Model Law is sufficiently developed to undertake public consultations.</i>
<i>Mandate</i>	<i>Work Programme 2020-2022</i>
<i>Priority level</i>	<i>High</i>
<i>Related documents</i>	<u>Study LVIII A – W.G.4 – Doc. 6</u>

I. INTRODUCTION

1. The purpose of this document is to provide Members of the Governing Council with additional information on the Model Law on Factoring, in order to allow the Governing Council to assess the draft instrument and determine whether it's sufficiently developed to undertake public consultations.

II. BACKGROUND

2. In December 2018, as a proposal for the UNIDROIT Work Programme 2020-2022, the World Bank suggested that UNIDROIT develop a Model Law on Factoring (MLF).¹ At its 98th session in May 2019, the UNIDROIT Governing Council approved the project for the 2020-2022 Triennial Work Programme as a high priority project.²

3. The purpose of the Model Law is to provide an instrument for States that want to introduce a new factoring law or update their existing laws but are not yet in a position to undertake a comprehensive secured transactions law reform based on the instruments developed by the United Nations Commission on International Trade Law (UNCITRAL). The instrument will consist of a set of black letter rules, that may eventually be accompanied by a text (in the form of a commentary

¹ [UNIDROIT 2019 C.D. \(98\) 14 rev.2](#), p.17.

² [UNIDROIT 2019 C.D. \(98\) 17](#), p. 36.

following each article, or of a separate guide) offering guidance as to how the rules are to be implemented and explaining some of the core concepts, their origin and context, as well as their possible use.

III. DEVELOPMENT OF THE MODEL LAW ON FACTORING

4. As consistent with the Institute's established working methodology, the MLF is being developed by a Working Group composed of international legal experts representing different legal systems.³ The Working Group is chaired by Governing Council member Professor Henry Gabriel. In addition, several international, regional and private organisations with expertise in factoring are participating in the Working Group as observers.⁴ The Working Group has held five sessions. The first session took place via videoconference between 1 and 3 July 2020 and was attended by 32 participants.⁵ The second session took place via videoconference between 14 and 16 December 2020 and was attended by 30 participants.⁶ The third session took place via videoconference between 26 and 28 May 2021 and was attended by 32 participants.⁷ The fourth session took place in hybrid format between 1 and 3 December 2021 and was attended by 30 participants.⁸ The fifth session took place in hybrid format between 16 and 18 May 2022 and was attended by 35 participants.⁹

5. The Working Group has also held a number of intersessional and informal meetings and created several subgroups to work on specific legal issues.¹⁰

6. At the close of its fifth session, the Working Group decided that the draft MLF was sufficiently developed to undertake public consultations and referred the draft instrument to the Governing Council for consideration at its 101st session.

IV. THE DRAFT MODEL LAW

7. In preparing the MLF, the Working Group has adopted a policy of adherence to the UNCITRAL Model Law on Secured Transactions (2016) and the United Nations Convention on the Assignment of

³ The Working Group is composed of the following experts: (i) Henry Gabriel (Chair) (United States), (ii) Giuliano Castellano (Italy), (iii) Neil Cohen (United States), (iv) Michel Deschamps (Canada), (v) Marek Dubovec (Slovakia), (vi) Alejandro Garro (Argentina), (vii) Louise Gullifer (United Kingdom), (viii) Megumi Hara (Japan), (ix) Cathy Walsh (Canada) and (x) Bruce Whittaker (Australia).

⁴ The following organisations are observing the MLF Working Group: (i) The World Bank Group, (ii) UNCITRAL, (iii) the Kozolchyk National Law Centre (NatLaw), (iv) the European Bank for Reconstruction and Development (EBRD), (v) the Organization of American States (OAS), (vi) the African Export-Import Bank (AFREXIMBANK) (vii), the Organisation for the Harmonisation of Business Law in Africa (OHADA) and (viii) several Industry Groups; (a) Factors Chain International (FCI), (b) World of Open Account (WOA), (c) Secured Finance Network (SFN) and (d) the International Chamber of Commerce Banking Commission (ICC).

⁵ The report from the Working Group's first session is available at: [Study LVIII A – W.G.1 – Doc. 4.](#)

⁶ The report from the Working Group's second session is available: [Study LVIII A – W.G.2 – Doc. 4.](#)

⁷ The report from the Working Group's third session is available: [Study LVIII A – W.G.3 – Doc. 4.](#)

⁸ The report from the Working Group's fourth session is available: [Study LVIII A – W.G.4 – Doc. 6.](#)

⁹ The report from the Working Group's fifth session is not yet available.

¹⁰ On 11 February 2020, in the margins of the International Secured Transactions Coordination Conference in Cartagena, Colombia, UNIDROIT held a short planning meeting for the Working Group. During the planning meeting, the Working Group identified an initial list of issues for discussion at the first Working Group meeting. During its first session, the Working Group established a subgroup to consider issues relating to conflicts of laws, which met several times in 2020. At its third session, the Working Group established a subgroup to develop the MLF's registry rules and an additional subgroup to consider transition issues. Both the registration subgroup and the transition subgroup met several times during 2021 and reported back to the Working Group at its fourth session. Finally, the Working Group held an intersessional meeting on 20 September 2021 to further define the scope of the MLF.

Receivables in International Trade (2001), unless deviation from these instruments is strictly necessary. The Working Group adopted this policy of adherence to ensure that the MLF will (i) be consistent with international best practice as represented in the UNCITRAL instruments, and (ii) serve as an initial step towards broader secured transactions reform in implementing States.

8. The Working Group is making good progress in preparing the MLF. The draft MLF currently consists of 54 Articles and 25 Registry Clauses and follows the structure of the UNCITRAL Model Law on Secured Transactions:

- Chapter I – Scope and general provisions
- Chapter II – Transfers of receivables
- Chapter III – Making a transfer of a receivable effective against third parties
- Chapter IV – The registration system
- Chapter V – Priority of a transfer
- Chapter VI – Rights and Obligations of the Parties
- Chapter VII – Collection and Enforcement
- Chapter VIII – Conflict of Laws
- Chapter IX - Transition
- Annexe A – Registry Provisions

Scope of the MLF

9. The MLF will apply to factoring, reverse factoring and invoice discounting and will apply to both outright transfers of receivables as well as security interests in receivables. The MLF will also apply to both domestic factoring and international factoring and apply to future receivables. As such, the scope of the instrument is broader than the traditional notion of factoring in the 1988 UNIDROIT Convention on International Factoring. This expansion was necessary to ensure that the instrument will appropriately apply to the various financing methods that have become more common since the UNIDROIT Factoring Convention was adopted.

10. While the MLF will have a broader scope than the UNIDROIT Factoring Convention, the Working Group has ensured that the draft MLF has a clear and limited scope. The MLF will apply to receivables (i) arising from contracts for the supply or lease of goods and services, (ii) arising from contracts for the licence or assignment of intellectual property and (iii) representing the payment obligation for a credit card transaction. By adopting a clear and limited scope, the MLF will not apply to receivables arising from contracts for the sale or lease of immovable property and receivables arising from various financial transactions, such as financial contracts governed by netting agreements, receivables arising from foreign exchange transactions and receivables arising from inter-bank payment systems. The MLF will also not apply to negotiable instruments (except to the extent they are proceeds of a receivable).

Priority and registration rules

11. As consistent with the UNCITRAL Model Law on Secured Transactions, the MLF will provide for a debtor-based registry for the registration of both outright transfers and security interests related to factoring transactions. Priority between competing transfers is determined by order of registration. Unlike the UNCITRAL Model Law on Secured Transactions, the rules relating to registrations and searches of the registry are set out in the 25 Clauses contained in Annexe A. The Working Group adopted this decision in order to streamline the text of the instrument, while still ensuring that implementing States will have the model rules required to establish a functional registry.

Anti-assignment clauses

12. The MLF will provide for a complete override of anti-assignment clauses. In a rare departure from the UNCITRAL Model Law on Secured Transactions and the Receivables Convention, the MLF will not preserve the right of a debtor to claim damages from the transferor for breach of contract in relation to an anti-assignment clause. The anti-assignment clause override will be limited to transactions within the scope of the MLF and apply to any restriction on transfers of supporting rights.

V. PUBLIC CONSULTATIONS AND FUTURE STEPS

13. Should the Governing Council decide that the draft MLF is sufficiently developed to initiate public consultations, the Secretariat will undertake a three-month consultation campaign between July and September 2022. The public consultation will have three aspects:

- i. UNIDROIT stakeholders, including Member States, Governing Council Members the UNIDROIT Correspondents
- ii. Project stakeholders, including UNCITRAL, the World Bank Group, the European bank for Reconstruction and Development and the International Chamber of Commerce.
- iii. Industry stakeholders. In particular, the Secretariat will work with private sector organisations such as Factor Chain International (FCI), World of Open Account (WOA) and the Secured Finance Network in order to allow private sector experts to provide input on the draft instrument and thereby ensure that it meets the needs of industry.

14. The Secretariat will organise one or more online consultation events to discuss the content of the draft instrument with a broad range of stakeholders.

15. At its future sixth session in November 2022, the Working Group will consider all comments received on the draft MLF. The draft MLF will be submitted to the Governing Council at its 102nd session in 2023 for final evaluation and adoption. The instrument will then be published later in 2023.

16. Further information regarding the MLF project and all documents from the Working Group meetings are available on the UNIDROIT website at <https://www.unidroit.org/work-in-progress/factoring-model-law>.

VI. ACTION TO BE TAKEN

17. *The Governing Council is invited to discuss the draft Model Law on Factoring and consider whether it is sufficiently developed to initiate public consultations on the draft instrument.*