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DRAFT GUIDE TO ENACTMENT
TO THE UNIDROIT MODEL LAW ON FACTORING

Introduction

1. This document contains the draft Guide to Enactment (Guide) to the UNIDROIT Model Law on Factoring (MLF), for consideration by the Working Group at its third session. The draft Guide was updated intersessionally between the Working Group's second and third sessions (January – March 2025), based on the Working Group's discussions at its second session.

2. The draft Guide was developed in consistency with the working methodology and drafting approach adopted by the Working Group at its first session.[1] The sections were prepared in consistency with the draft Guide outline, and the content is based on the section summaries prepared in March 2024,[2] as amended by the WG during its first and second sessions.

3. In reviewing the draft Guide for discussion at the third session, the Working Group is invited to take note of the following matters:

4. Intersessional revisions: The draft Guide was revised intersessionally primarily to (i) incorporate the Working Group's comments from its second session and (ii) complete the drafting of sections that were previously incomplete or drafted in shorthand. As such, the draft Guide should now be considered as substantively complete. There have been some refinements in relation to style, consistent use of terminology and other matters (e.g. the naming of parties in examples). However, further proofing will be required in relation to style, drafting, consistent use of terms and other issues (cross-references, use of quotation market etc). To assist Working Group members in identifying the intersessional changes made to the draft Guide, Study LVIII B – W.G.3 – Doc. 3 provides a "tracked changes" version of the draft Guide which sets out the changes made to the document between the second and third sessions.

[1] See UNIDROIT 2024 – Study LVIII B – W.G.1 – Doc. 2, available https://www.unidroit.org/wp-content/uploads/2024/03/Study-LVIII-B-%E2%80%93-W.G.1-%E2%80%93-Doc.-2-Development-of-the-MLF-Guide-to-Enactment.pdf.

[2] See UNIDROIT 2024 – Study LVIII B – W.G.1 – Doc. 3, available https://www.unidroit.org/wp-content/uploads/2024/04/Study-LVIII-B-%E2%80%93-W.G.1-%E2%80%93-Doc.-3-GtE-section-summaries.pdf.

5. Comments and footnotes: To make the document easier to use and as consistent with the previous version of the draft Guide considered at WG2, Working Group member comments on the draft Guide have been incorporated into the footnotes of the document, with an * and the initials of the expert making the comment.[3] Footnotes without an * are intended to be included in the actual Guide.

6. Policy objectives and core concepts: Additional references to reinforce the importance of the MLF's policy objectives an core concepts have been made throughout the draft Guide (particularly in Chapter IV). The Working Group may wish to discuss at WG3 whether further references to policy objectives and core concepts should be added.

7. Terminology: The draft Guide has tried to adopt consistent terminology in describing the relationship between the MLF and the enacting State's "other law". The terms used are explained below. The Working Gorup may wish to discuss whether this consistent use of terminology is useful, and whether the intended meaning of "interact", "adapt", "amend", "coordinate" an "align" should be explained in the Guide.

i. Interact: there is likely to be a relationship between the MLF and the enacting State's "other" law. The enacting State will need to review their own general law to determine the degree of "interaction".

ii. Adapt: "Adapt" should be used where the Guide is recommending that States make a change to either the MLF or their general law (and the Guide should, to the extent possible, specify which one should be changed). "Amend" can be used instead of "adapt" where the Guide is specifically suggesting that the enacting State will likely need to change a piece of legislation to give way to the MLF.

   1. The MLF rule should be changed to give way to the general law, or

   2. The general law should be changed to give way to the MLF.

iii. Coordinate: there may or may not be the need to adapt either the rules in the MLF or the general law. The Guide should use "coordinate" where it is not possible to give the enacting State guidance on what might need to be changed, and whether the MLF rules should give way to the enacting State's other law, or vice versa.

iv. Align: Align is generally not used, aside from in relation to describing the relationship between the MLF and regulatory rules.

8. Internal cross-references: There are over 100 internal cross-reference in the document, which will eventually be hyperlinked to assist readers use the electronic version. Most cross-references have not yet been updated from the WG2 draft (as denoted by "WG3" in the cross-reference), as they are likely to change further several times before the Guide is finalised. All cross-references will need to be updated and checked once the draft Guide is further revised following WG3.

9. External cross-references to the UNIDROIT Best Practices for Effective Enforcement: Several footnotes reference the need for the Guide to cross-reference the UNIDROIT Best Practices for Effective Enforcement. This instrument is still in the process of finalisation, so these cross-references will need to be added after WG3.

[3] LG = Louise Gullifer, MD = Marek Dubovec, NC = Neil Cohen, GC = Giuliano Castellano, AG = Alejandro Garro, CW = Cathy Walsh, Megumi Hara = MH, MDE = Michel Deschamps, Bruce Whittaker = BW.

10. The Secretariat is particularly grateful to the following experts that assisted in revising the draft Guide:

a. Louise Gullifer for revising Part I(4), Part II(1) paragraphs 62 - 79, and Part IV(1 – 6).

b. Marek Dubovec for revising Part II(3), Part III(1) and the Digital Economy Supplement.

c. Giuliano Castellano for revising Part III(2).

d. Neil Cohen for revising Part IV(7 – 9).

e. Bruce Whittaker for revising Part IV Annexe A (Registry Provisions).

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UNIDROIT MODEL LAW ON FACTORING

DRAFT GUIDE TO ENACTMENT

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PART I

PURPOSE AND OVERVIEW

SECTION 1 - INTRODUCTION TO THE MLF GUIDE TO ENACTMENT

1. The purpose of this Guide to Enactment is to assist States to understand, interpret and implement the UNIDROIT Model Law on Factoring (MLF). The Guide to Enactment (Guide) seeks to explain both the purpose and objectives of the MLF, as well as the operation of its provisions.

2. The primary audience for this Guide is government officials in States considering implementing the MLF. However, this Guide might also assist companies, regulatory authorities, legal practitioners and judges to interpret the MLF.

3. Part I of this Guide introduces the MLF by providing (i) a description of the types factoring transactions that are facilitated by the MLF, (ii) an explanation of the development, policy objectives and core concepts (iii) a broad overview of the MLF itself, and (iv) advice on how the MLF should be coordinated with other relevant international instruments.

4. Part II explains (i) how the MLF can be implemented in States with different legal traditions, alongside broader general law and within existing legal frameworks for factoring, receivables finance and secured transactions, (ii) different methods of implementation, and (iii) how common implementation issues can be resolved.

5. Part III (i) outlines how the MLF interacts with the digital economy, and (ii) describes how the MLF should be coordinated with regulatory frameworks for factoring.

6. Part IV provides an article-by-article commentary on the 54 Articles and 25 Registry Clauses in the MLF.

7. The electronic version of this Guide also includes a Digital Economy Supplement, which provides additional guidance on how the MLF can be coordinated with emerging technologies that facilitate finance and access to credit. The Digital Economy Supplement is designed to be updated periodically, in order to be able to address new technological developments. The Digital Economy Supplement is also available on the UNIDROIT website.

8. This Guide was prepared under the auspices of the International Institute for the Unification of Private Law (UNIDROIT) by a Working Group of international legal experts from different geographic regions and diverse legal traditions, with participation from representatives of relevant international and intergovernmental organisations, private sector associations and academia (a full list of participants in the MLF Guide to Enactment Working Group is available in Annexe [1]). The Guide was negotiated over a period of three formal sessions and several intersessional meetings between January 2024 and April 2025, and was adopted by the UNIDROIT Governing Council in [date in 2025].

SECTION 2 - FACILITATING ACCESS TO CREDIT THROUGH FACTORING

Introduction to factoring

9. Factoring is a type of financial transaction where businesses (transferor/seller) can raise finance (e.g. for working capital purposes) by transferring (assigning/selling) their receivables (contractual right to payment) to a financial institution (FI) (transferee/factor). The FI in turn can be repaid by collecting payment for the receivables from the transferor's customer/purchaser of the goods or services (debtor/buyer). Factoring allows for a high degree of control of the cash flow from the debtor to the FI by ensuring payment is made to the FI's account by way of notification to the debtor that payment is to be made to the FI,[1] collection of the receivable if and when the account becomes past due, and the payment reconciliation process to offset the matching invoice(s) and pay down the advance made to the transferor. The payment by the debtor acts as a form of repayment of the advance made to the transferor.

Global importance of factoring[2]

10. Factoring is designed to increase the opportunity of access to debt capital to companies of all types. Access to finance is a great challenge in any market, but especially when the company is a Micro, Small or Medium sized business (MSME). MSMEs are the most important contributor to global growth and development, accounting for 90% of businesses, 70% of employment, and 50% of GDP worldwide.[3]

11. It is estimated that the trade finance gap, which is the gulf between requests made and approvals provided to support the financing of imports and exports exceeds $2.5 Trillion United States Dollars (USD).[4] This widening gap is particularly evident in developing States. The principal reason is due to a lack of financial products supporting MSMEs. Most forms of credit in developing States is done via commercial loans from FIs, typically requiring some form of collateral, by way of a security interest in fixed assets of the proprietor, which can be a residential house, commercial building, land, equipment, as well as financial assets like stocks and bonds. However, such assets typically cannot be provided by a proprietor of a small business, either because they do not own such assets or they may be already encumbered. Factoring addresses the trade finance gap by allowing MSMEs to access finance by transferring or creating a security interest over their accounts receivable.[5]

12. Historical data indicates that factoring is a particularly important tool to increase access to finance following global crises, due to the fact that commercial banks tend be become more conservative during such periods. During the period immediately after every economic and financial

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[1] *Secretariat: At WG2, CW made the point that the MLF covers both notification and non-notification factoring, whereas this description of factoring here covers notification factoring. Is this ok, or does the WG think this might be misleading to leave as drafted?

[2] *Secretariat: At WG2 it was suggested that this sub-section be moved up from the end of Part I Section 2. The WG might want to confirm this restructuring has improved the flow of this section.

[3] United Nations, "Mirco, Small and Medium-sized Enterprises Day 2024", available: https://www.un.org/en/observances/micro-small-medium-businesses-day.

[4] Asian Development Bank's (ADB), "2023 Trade Finance Gaps, Growth and Jobs Survey", September 2023, available https://www.adb.org/publications/2023-trade-finance-gaps-growth-jobs-survey.

[5] The term "accounts receivable" is an accounting term for money owed to a business for goods or services that it has delivered but not yet been paid by the account debtor. Accounts receivable is listed on a company's balance sheet as a current asset, meaning it is short-term and liquid by nature. Receivables refer to monies owed to a company by its customers for goods or services sold to them provided on credit, recorded as assets on the seller's balance sheet at the time of the issuance of the commercial invoice. The term "credit" means that the seller has agreed to sell the goods or services on "open account" or extended payment terms, meaning the company has delivered the product or service but is awaiting payment from their customer. Accounts receivable can be considered an extension of credit by a company, where payment is due at a certain point of time in the future. These receivables typically lie dormant on the seller's balance sheet, due to the lack of an adequate legal and regulatory framework or a lack of understanding of how the receivables could be transferred to obtain finance.

crisis since the Great Depression, the factoring industry experienced double digit growth. Between 1935 and 1948 in the US, the factoring industry grew by an unprecedented 13% compound annual growth rate (CAGR), a five-fold increase during this 13-year period. In the period following the Great Recession between 2009-2019, global factoring volume increased from 1.28 trillion euros to 2.977 trillion euros, representing a two-fold increase and a 9% CAGR. During the COVID-19 inspired Global Recession 2020-2023, factoring once again witnessed an increase from EUR 2.726 Trillion in 2020 to EUR 3.791 Trillion in 2023, a 11.6% CAGR. These historical trends demonstrate the need to ensure a robust global legal framework for factoring, in order to minimise the damage caused by limitations in access to credit resulting from future global economic crises.

Financing arrangements facilitated by factoring

13. While the meaning of the term "factoring" has changed over time[6], the MLF is designed to enable a broad range of receivable financing arrangements whereby receivables are used as collateral. FIs have developed a variety of different financial products that utilise factoring to facilitate global Supply Chain Finance (SCF). These financial products include not only "traditional" notions of factoring (sometimes also known as invoice discounting or debtor finance), but also payables finance (sometimes also known as reverse factoring, confirming, buyer-led supply chain finance, supplier finance and vendor pre-pay).[7] The term "factoring" encompasses the outright transfer of receivables, transfer of receivables by way of security, recourse and non-recourse factoring, as well as notification and non-notification factoring and the transfer of receivables for collection. In this sense, the term "factoring" should be understood to cover the broad range of receivables financing arrangements within the scope of the MLF.

14. Outright transfers and transfers by way of security: In principle, factors purchase the receivables from their clients (transferors) through a transfer of the receivable to the factor (outright transfer), who thereby becomes the principal owner. Factors can also take a security interest over receivables in order to provide receivables finance (transfer by way of security). As such, factoring covers not only the "traditional" buying and selling of receivables, but also the financing of receivables by businesses taking a security interest in them.

15. Recourse: Factoring transactions can be undertaken with or without recourse for the factor. Recourse factoring is the most common used historically, which requires that the risk of recourse remains with the transferor in the case when the factor is unable to collect payment from the debtor as repayment against the advances made to the transferor. This means that the transferor is ultimately responsible for non-payment of the invoices. Non-recourse factoring means the factor assumes most of the risk of non-payment by the debtor. The risk that the factor assumes is the commercial risk of the debtor, or their inability to pay the invoice at due date due to the filing of bankruptcy protection or their commercial default. However, non-recourse factoring does not necessarily protect the transferor from all risks. There are stipulations associated with non-recourse factoring, whereby the factor can demand recourse against the transferor. Such risks include dilution

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[6] In the 1988 UNIDROIT Convention on International Factoring, "factoring" was narrowly understood to apply to the outright transfer of receivables to a factor that would perform several specific functions (finance for the supplier, including loans and advance payments; maintenance of accounts (ledgering) relating to the receivables; collection of receivables; and/or protection against default in payment by debtors). While "factoring" is not defined in the UNIDROIT Model Law on Factoring, it is intended to enable a broad range of transactions, as explained in this section.

[7] *Secretariat: These terms are taken from the Global Supply Chain Finance Forum's terminology. However, it is suggested we don't necessarily cross-reference the GSCFF's work, as their definition of "factoring" remains limited to outright sales of receivables. See http://supplychainfinanceforum.org/.

risk, which is the risk of disputes raised by the debtor. The other is transferor (seller) fraud. In both cases, the factor has the right of repayment from the transferor.[8]

16. Notification: There are also two approaches to offer factoring to the client: notification and non-notification (also referred to as non-disclosure factoring). For example, "notification factoring" means the debtor is informed that their invoice has been sold to a factor, while "non-notification factoring" means the debtor remains unaware of the factoring arrangement and continues to pay the original transferor, who then forwards the payment to the factor; essentially, the debtor is not notified that the invoice(s) from their supplier has been sold to a third party. This involves a notification of assignment where the factor notifies the debtor that going forward, they will be required to remit all payments pertaining to the invoices issued from the transferor directly to the factor. Non-notification factoring carries a higher risk, as the factor may relinquish their right to a dispute of nonpayment, payment mistakenly made directly to the transferor, or factoring fraud brought on by collusion between the transferor and debtor.

17. Payables finance (reverse factoring): Payables finance is a type of factoring whereby the anchor buyer (typically a large investment rated company) offers early payment terms to their suppliers based on approved invoices by the buyer. This would then require the buyer to pay the invoice on a certain date and in a certain currency. Suppliers of the anchor buyer, who agree to participate in a reverse factoring program can request early payment against invoices, the financing typically provided by a commercial bank or other finance provider, with the buyer sending payment to the factor at maturity of the invoice. Buyers ultimately reduce the risk of disruptions within their supply chains and strengthen the supplier relationships, while also improving their own working capital position, as typically payment due date is further extended. While payables finance is sometimes referred to as reverse factoring or buyer-led supply chain finance, it is one of many services that that form a part of global Supply Chain Finance (SCF). Technological innovation has facilitated the growth of SCF through the creation of virtual platforms that automate transactions and track invoice approval and settlement processes.

18. Receivables may be transferred for financing purposes in transactions outside of factoring transactions, including through securitisation. Receivables can be securitised to create publicly tradable and investible securities, or privately through the factor establishing a Special Purpose Vehicle (see next paragraph). While the MLF does not inhibit the securitisation of receivables, it is not written with them specifically in mind.[9]

19. Factoring has the additional benefit of facilitating off-balance sheet financing, withs allows businesses to access credit while keeping debt-to-equity levels low. For the transferor, selling a receivable to a factor allows the business to access funds efficiently without taking on a loan which might affect their balance sheet. For a factor, a receivable that has been transferred to them can be further transferred to a trust or a Special Purpose Vehicle (SPV) as part of securitisation or getting a loan secured with those receivables, which allows the factor to keep the receivable off their own balance sheet.

20. The MLF is designed to reduce the legal risks associated with factoring by providing clear legal rules that facilitate the transfer of receivables and their collection when due. It balances However, it cannot eliminate commercial risks in factoring transactions. Factors should ensure that

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8 In non-recourse factoring the factor also provides protection against bad debts ("default protection") so payment by the factor is made even if the debtor of the receivable is unable to pay or becomes insolvent. Ledgering and maintenance of accounts often is provided by the factor as a service, and so is dunning and collection. While large ticket factoring is often based on a non-notification policy, it is common in MSME factoring to notify the debtor of the transfer of the receivable, and request payment on due date directly to the factor.

9 *Secretariat: This is an alternative drafting of the paragraph on securitisation partially suggested by BW.

they implement strong underwriting procedures and operational controls in order to minimise commercial risks.[10]

[10] *Secretariat: This is an alternative drafting of the paragraph on control and risks, as partially suggested by BW.

SECTION 3 - INTRODUCTION TO THE MLF

Development of the Model Law on Factoring

21. Many States around the world do not have effective legal frameworks for factoring that facilitate a broad range of receivable finance products. Often, legal regimes do not provide sufficient certainty in relation to what constitutes a receivable, whether receivables can be transferred, what formalities are required to transfer receivables, priority between competing transfers, as well as different treatment of outright transfers (sales) of receivables and security interests over receivables. This legal uncertainty often means that financiers are less willing to provide finance to companies for whom receivables are their most important asset. As a result, many MSMEs are either unable to access credit, thereby preventing them from accepting new orders, increasing output and participating in local, regional and global supply chains.

22. The MLF was designed to address the legal uncertainty arising from weak legal frameworks for factoring. Adopted in May 2023 by the International Institute for the Unification of Private Law (UNIDROIT), the MLF was the result of a legislative project proposed by the World Bank Group in 2018. The World Bank's proposal to develop the MLF was based on three elements: (i) the importance of factoring as a mechanism to increase finance for MSMEs (ii) ongoing constraints in access to credit for MSMEs in developing States; and (iii) the existing gap in the international legal framework in relation to factoring.

23. International instruments prepared by UNIDROIT and other international standard setting bodies are held in high esteem primarily because of the robust, inclusive and consultative negotiation process required for their adoption. The methodological process is technical, rigorous, and comprehensive. The MLF was prepared over a period of three and half years and involved several hundred hours of negotiations between dozens of legal experts and key stakeholders, the preparation of hundreds of pages of legal analysis, draft instruments and reports, and finally consultations with thousands of stakeholders.[11]

24. The MLF has been recognised as the leading international standard establishing a private law legal framework to facilitate factoring. The MLF has been recognised as the key legislative pillar of the "Financial Inclusion in Trade Roadmap" (FIT) as adopted by the World Trade Board. [12] The FIT is a framework designed to increase the participation of micro, small and medium-sized enterprises (MSMEs) in international trade. The MLF has also been recognised in the "New Finance Support" report published by the European Bank for Reconstruction and Development (EBRD) as the international legal standard for receivables finance which supports access to credit for MSMEs in States that implement the Model Law.[13] The MLF has also been acknowledged as the international best practice private law framework for factoring in Part I of the "Knowledge Guide on Factoring Regulation and Supervision" published by the International Financial Corporation of the World Bank Group.[14]

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[11] Further information on the preparation of the Model Law on Factoring is available on the UNIDROIT website at: https://www.unidroit.org/instruments/factoring/model-law-on-factoring/preparatory-works/.

[12] Financial Inclusion Trade Roadmap: https://www.baft.org/wp-content/uploads/2023/04/FinancialInclusion-in-Trade-Roadmap-202326.pdf).

[13] See ERBD New Finance Report: https://www.ebrd.com/what-we-do/sectors/legal-reform/access-tofinance.html.

[14] See IFC Knowledge Guide on Factoring Regulation and Supervision: https://www.ifc.org/content/dam/ifc/doc/2024/knowledge-guide-on-factoring-regulation-and-supervision-ifc-2024.pdf. Further information on the factoring regulation is available in Part III (2) of this Guide.

Policy objectives and core concepts of the Model Law on Factoring

25. The rules of the MLF are designed to achieve a number of policy objectives to be achieved through a set of core concepts[15]. The policy objectives are a set of broad principles that will be achieved by a State effectively implementing the MLF. The core concepts are specific aspects of the MLF that ensure the instrument's broader policy objectives.

26. The MLF's ultimate objective is to facilitate factoring. This ultimate objective is achieved through the cumulative effect of the following [five] policy objectives:

i. Transparency, predictability and certainty. The MLF provides a set of clear and comprehensive legal rules that provides certainty, predictability and transparency for parties involved in factoring.

ii. Transactional efficiency. The MLF provides a simplified set of rules that in many States will make it easier to transfer or secure a receivable.

iii. Balanced rules for parties. The MLF carefully balances the rights and obligations of the debtor, transferor and transferee to ensure that no party is unfairly disadvantaged by the implementation of the law.

iv. Flexibility in facilitating a variety of different financing arrangements. The MLF is designed to flexibly apply to a variety of different receivable finance arrangements encompassing both the outright transfer of receivables and transfer of receivables by way of security.

v. International harmonisation. The MLF provides a set of rules that, where uniformly implemented, will create a harmonised legal framework for both domestic and cross-border factoring.

27. The MLF is built around [seven] core concepts that are designed to achieve the five policy objectives noted above:

a. Application to both outright transfers and security transfers.
b. Simple legal requirements for the transfer or grant of security in receivables.
c. Clear scope in defining receivables.[16]
d. [Complete override of anti-assignment clauses.][17]
e. Registration of a public notice in order to achieve third party effectiveness and priority of a transfer.
f. Efficient enforcement rules.[18]
g. Inclusion of conflict of law rules [based on the location of the debtor][19].

28. While it is recommended for States to implement the entire MLF, in certain circumstances States may choose not to implement certain rules or core concepts. As a soft law instrument, such an approach is permissible. In many States, partial implementation of the MLF will still provide a

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15 *Secretariat: At WG2 BW suggested to the Secretariat that "core concept" sounds too academic and that "key feature" might be more practical. The Working Group may wish to further discuss this at WG3.

16 *Secretariat: This replaces "application to proceeds of receivables", as agreed at WG3.

17 *Secretariat: This was suggested by MH at WG, although it appears no conclusion was reached. The Secretariat is supportive of its inclusion, and invites the WG to further consider the matter at WG3.

18 *Secretariat: This replaces "enforcement rules that can also apply in insolvency". NC had suggested during WG2 that "rules that endure even if the key parties become insolvent" might be worth including. NC had also queried whether "efficient enforcement rules" should be balanced with a reference to debtor protection. These matters may warrant further discussion at WG3.

19 *Secretariat: At WG2 it was decided to retain conflict of law rules and remove transition rules, MD suggested we be a little more specific (noting that some laws reference the GRIF as a conflict of law rule). It is suggested that the WG confirm this point at WG3.

significant improvement of the legal framework and facilitate additional factoring transactions. However, in identifying and explaining the MLF's core concepts and related policy objectives, this Guide is designed to inform implementing States of the potential disadvantages of diverging from the core concepts. As such, throughout this Guide, the purpose and objectives of certain articles or approaches will be explained with reference to the MLF's core concepts and policy objectives.

SECTION 4 - OVERVIEW OF THE MLF

29. The MLF is divided into a number of chapters, and this overview largely follows the order of the chapters. However, provisions relating to the operation of the Registry are found in Annexe A to the MLF. These are in a separate annexe as a State may want to incorporate them into legislation relating to an existing registry system. However, these provisions are summarised in this overview as part of chapter 4.

30. The MLF addresses the private law relating to factoring transactions, and does not address regulatory law. Regulation is, however, a very important part of the law in this area and a State may want to include some regulatory provisions in the legislation implementing the MLF. The interaction with regulation is further discussed at part III(2).[20]

31. The scope of the MLF is dealt with in Chapter I and is clearly delineated by definitions of many terms used within it. It applies (and only applies) to transfers of receivables. A transfer of a receivable is defined widely as either an outright transfer or a security transfer (a term which can include security transactions that are not, under domestic law, transfers) in each case by agreement. If a receivable is transferred, the transferee also obtains a right to the proceeds of that receivable.

32. The scope, however, is limited by the definition of 'receivable' which, very broadly speaking, is limited to 'trade receivables'. A receivable is a contractual right to payment of money arising from the supply of things supplied in the course of trade, such as goods, services, data (or data processing) and intellectual property. Thus, for example, receivables arising from the making of loans and other financial transactions are not included, nor are rights to payment in instruments such as negotiable instruments and letter of credit. Policy based domestic law rules, such as those in consumer protection law and those limiting the transfer of specific types of receivables, are not affected by the Law.

33. Many of the provisions in the Law relating to the relationship between two parties can be varied by the agreement of those parties, while those affecting third parties (such as the provisions about third party effectiveness, priority and conflict of laws) cannot. The rights and obligations under the Law must be exercised or performed in good faith and in a commercially reasonable manner.

34. Under Chapter II, receivables can be transferred by an agreement between the transferor and the transferee. The formal requirements for an agreement are minimal. It can describe the transferred receivables generically: it is not necessary to identify specifically every receivable transferred. Future receivables can be included in a transfer agreement, with transfer taking place when they arise. For example, the agreement can cover all the transferor's present and future receivables.

35. Moreover, even if the debtor and the transferor agree that the transferor's right to transfer it is completely or partially limited, a receivable can still be transferred effectively and the agreed limitation is completely ineffective.

36. Under Chapter III, a transfer of receivables will only be effective against third parties if a notice relating to it is registered in the registry. There is no other way under the MLF to make a transfer effective against third parties. Without registration the transfer only takes effect as between the transferor and the transferee. A transfer that is effective against third parties remains effective if the transferor enters into insolvency proceedings.

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[20] *LG: MD suggesting taking this out but I think cross-references are important so I have left it in (we could do it in a footnote or maybe an embedded link if we prefer).

37. The MLF provides detailed rules for the establishment and operation of the registry which are found in Annexe A. The registry is a notice filing system: a notice relating to one or more transfers can be registered either before or after the actual transfers have taken place, and is designed to inform anyone searching the registry that a transfer may have taken place. It will then be up to the person searching to make further enquiries as to whether the transfer has actually taken place, and as to the details of the transfer.

38. A notice contains quite minimal information: identification of the transferor and the transferee, plus a description of the transferred receivables that allows them to be identified. The main search criterion is the identifier of the transferor. Registration of a notice is effective from the time that its information is accessible to searchers; as will be seen below, that time is the priority point for the transfer(s) included in the notice. Under the electronic registration system, once a registrant submits the relevant information for a notice, the registration of a notice containing that information takes place automatically [without any act by the Registrar.][21]

39. Chapter V contains the priority rules. There is one simple rule for priority between transfers: a 'first to file' rule. This means that the order of priority between competing transfers is the order in which notices relating to transfers are registered, and this priority rule also applies to the proceeds of transferred receivables. This priority rule applies even if a notice is registered before a transfer actually takes place. It also applies irrespective of any knowledge of any competing transfer. The order of priority outside the insolvency of the transferor largely survives within insolvency proceedings relating to the transferor.

40. Chapter VI deals with the rights and obligation of the transferor, transferee and debtor as between themselves. The relationship between a transferor and transferee is largely governed by the agreement between them, but the MLF provides for certain rights and obligations which exist unless varied by the parties' agreement. For example, it provides that the transferor makes certain representations to the transferee about the transfer and the receivable, but does not represent that the debtor can pay the receivable.

41. The MLF provides various rules governing the protection of the debtor when a transfer takes place, which reflect the balancing of interests between the interest of the debtor (that its position vis a vis the receivable does not change) and that of the transferee (that it has an unrestricted right to the receivable and its proceeds). The balance is carefully constructed so that, while consent of the debtor to a transfer is not required for an effective transfer, the debtor's position only changes once it has been given relevant information about the transfer and who it needs to pay to obtain a discharge of the receivable.

42. It is possible under the MLF for a debtor not to be notified of a transfer at all (non-notification factoring), in which case the debtor is discharged by paying the transferor, and the transferor must then pay the proceeds to the transferee.

43. A debtor can be given information by a notification of a transfer and/or by a payment instruction, either of which must be in writing. If a debtor is notified of a transfer, it must, to be discharged, pay the identified transferee or, if different, as instructed in a payment instruction. The Law provides more detailed rules about who the debtor must pay to be discharged in various situations where a receivable has been transferred more than once.

44. The MLF also sets out which dealings between the debtor and the transferor affect the transferee. For example, the debtor is able to assert defences or set-offs against the transferee,

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[21] *LG: I'm still not sure whether to take this out or not. I raised the query in the footnote, and MD seemed to support taking it out at WG2. However, I do wonder whether it is rather meaningless to say that registration takes place automatically without explaining what the alternative would be be, ie that a registrar had to do something before registration takes place.

except those that are unconnected with the receivable and that arose after the debtor was notified of the transfer. Similarly, any modification of the contract giving rise to the receivable made before the debtor is notified of the transfer binds the transferee.

45. Under Chapter VII, an outright transferee can collect a receivable once it is due, subject to the operation of the debtor protection rules, for example, if the debtor has a set-off that is effective against the transferee. The rules in the MLF in relation to enforcement of a security transfer are more complicated, since the security right only extends to the amount of the secured obligation, and so rules are required to protect the transferor or anyone else interested in any surplus value in the receivable.

46. Chapter VIII provides rules identifying the applicable law in relation to various issues. There are two main situations in which such issues are likely to arise. The first is where the receivable being transferred is an international receivable, that is, where the debtor and the transferor are located in different jurisdictions. The second is where there is an international transfer, that is, where the transferor and the transferee are located in different jurisdictions. The rules include identification of the applicable law to the mutual rights and obligations of the transferor, transferee and debtor, the effectiveness and priority of transfer and the enforcement of transfers. A national court or arbitral tribunal can still apply mandatory provisions or public policy of a State other than that of the applicable law.

47. Chapter IX includes transitional provisions, which are required to deal with the situation where a transaction concerning receivables is entered into under the law in force before the MLF comes into force but the transaction continues after the MLF comes into force. These provisions cover the third party effectiveness and priority of transfers during the transitional period related to the entry into force of the new law based on the MLF.

SECTION 5 - COORDINATION OF THE MLF WITH OTHER INTERNATIONAL INSTRUMENTS

48. The UNIDROIT Model Law on Factoring is the most recent instrument negotiated by an intergovernmental organisations responsible for creating international private law standards in the field of factoring. As the most recent instrument, the MLF reflects international best practice and should be the primary instrument used by States that are considering reforming their domestic factoring laws. However, it's important to note that the MLF is built upon the foundations of a long history of earlier international instruments, produced by both UNIDROIT and UNCITRAL in the field of factoring, receivables finance and secured transactions law.[22]

49. The first international instruments in the field took the form of treaties. In 1988 UNIDROIT adopted the Convention on International Factoring (Factoring Convention) and in 2001 UNCITRAL adopted the United Nations Convention on the Assignment of Receivables in International Trade (Receivables Convention). Both treaties were designed to provide legal rules for international transactions between parties located in different States.

50. Following the Factoring Convention and Receivables Convention, UNCITRAL Working Group VI negotiated a number of instruments, which culminated in the adoption of the UNCITRAL Model Law on Secured Transactions (MLST) in 2016. Utilising a functional approach in conceptualising secured transactions, the MLST provides a comprehensive legal framework for security interests in all types of tangible and intangible movable property.

51. The MLST provides a clear set of rules for the assignment of receivables, which are well designed to fit within a broader comprehensive secured transactions framework. It is important to note that the text of the MLF is based upon and broadly consistent with the text of the MLST. This is to ensure that States which implement the MLF can later implement the broader MLST should they wish to do so, without having to make significant changes to their factoring law. As such, there are three important recommendations for States considering legal reform:

a. States that intend to undertake a specific factoring reform are advised to implement the MLF.
b. States that intend to undertake a comprehensive secured transactions reform (which includes receivables) are advised to implement the MLST.
c. States that have already established a registry for notice of security rights should not establish a separate registry for notices relating to the transfer of receivables (this matter is discussed more in Part XXX).[23]

52. The MLF represents an evolution of these earlier international standards, which were based on similar policy objectives and core concepts. For example, the Factoring Convention, Receivables Convention and MLST all contained a limited override of anti-assignment clauses, which has been strengthened under the MLF. Similarly, the Receivables Convention included priority rules based on registration of data about assignments as one of several approaches to establishing priority, and the MLST established registration as the only way to establish priority of a security interest. The MLF

[22] UNIDROIT, UNCITRAL and the HCCH have jointly published a document that provides a comparative analysis of the major features of international instruments relating to secured transactions (available https://uncitral.un.org/sites/uncitral.un.org/files/media-documents/uncitral/en/uncitral-hcch-unidroit-e.pdf). As the comparative analysis was published in 2012, it does not cover the UNCITRAL Model Law on Secured Transactions, nor the UNIDROIT Model Law on Factoring. It should also be noted that the MLF is generally consistent with many of the broader international best practice standards in the field of commercial law, including the Unidroit Principles of International Commercial Contracts.

[23] *Secretariat: This addition was suggested by WB, EBRD and CW at WG2, to flag this issue here and explain it in detail later.

goes further be requiring the creation of a an electronic registry for the registration of notices of transfers of receivables to establish priority.

53. Over the last few decades, several regional and non-governmental organisations have also prepared a number of standards on secured transactions and factoring.[24] While the MLF shares a degree of complementarity with these earlier instruments, it is advised that States use the MLF when undertaking factoring reforms on the basis that (i) the MLF was negotiated through a robust, inclusive and consultative process, (ii) the MLF provides a modern, best-practice standard that has improved on earlier instruments, and (iii) the MLF provides a global standard which establishes a uniform international framework for factoring to support both regional and global supply chains.

[24] These standards include the 2002 Model Inter-American Law on Secured Transactions prepared by the Organisation of American States (OAS), the 2010 Model Law on Secured Transactions prepared by the European Bank for Reconstruction and development (EBRD), the 2014 Model Factoring Law prepared by the Global Representative Body for Factoring and Financing of Open Account Domestic and International Trade Receivables (FCI), and the 2016 Model Law on Factoring prepared by the African Trade Finance Bank (AFREXIMBANK).

PART II

IMPLEMENTATION OF THE MODEL LAW ON FACTORING

54. The MLF provides an instrument for States seeking to modernise and optimise their legal framework governing the transfers of receivables. The MLF was designed so that it can be implemented in States with a wide variety of legal systems and traditions. However, it is not anticipated that the text of the MLF will necessarily be enacted verbatim. While States will need to tailor the implementation of the MLF to suit their legal culture and existing legal framework, this Guide has two general recommendations for States that are implementing the MLF:

a. Implement the entirety of the content of the MLF: The MLF is designed to be implemented as a refined, yet complete legal framework. Each article was carefully designed to perform a specific function and properly interact with the entire instrument. As such, it is recommended that States implement all articles of the MLF. A decision to change the content or omit a certain article should be carefully considered, as doing so may have knock-on effects throughout the law.
b. Implement the core concepts: As introduced in [Part I Section 4], the policy objectives of the MLF are underpinned by a set of core concepts. While a State may decide to adapt the form, terminology and drafting of the MLF to suit their individual domestic context, States should to the greatest extent possible attempt to retain the instrument's core concepts. A decision to not implement a core concept may undermine the MLF's policy objectives, and impede the use of factoring.

55. Adherence to these two general implementation recommendations will not only establish a best-practice legal framework for domestic receivables finance in implementing States, it will also facilitate international financing arrangements through cross-border legal harmonisation. Because receivables, as intangible assets, can be traded across state borders at little cost, it is beneficial to efficient commerce in receivables (and to the parties that benefit from that efficiency) for the legal structure governing that commerce to be the same or similar in the relevant states. As such, if a region or group of States implement the MLF consistently, it will facilitate more efficient cross-border factoring arrangements between parties in those States. The adoption of the MLF's conflict-of-law rules (MLF Articles 36 - 46), particularly those on third-party effectiveness and those determining who is entitled to receive payment as between the transferee and a competing claimant (including creditors of the transferor, another transferee, or the transferor's insolvency administrator), go a long way in addressing legal barriers to the collection of receivables from foreign debtors.[25]

56. Part II Section 1 provides guidance in relation to (i) adapting the MLF to a State's legal traditions, (ii) adapting the MLF to a State's general law and (iii) adapting the MLF to a State's existing legal framework for factoring and secured transactions. Part II Section 2 provides further information on different methods of implementation. Throughout Part II and the rest of this Guide, the word "transfer" is used as consistent with its meaning in the MLF itself, and thus covers both (i) the outright transfer of receivables by agreement, and (ii) the transfer of receivables by way of

[25] *Secretariat: During WG2, it was suggested that the recommendations be reordered, which has been adopted. BW noted that the "cross-border harmonisation" recommendation (now para 55) was more of a benefit from following the other recommendations than a separate recommendation itself, so this subsection has been restructured to better reflect this.

security (security transfer).[26] Users of this Guide are reminded to keep this dual meaning of "transfer" in mind.[27]

The MLF implementation process[28]

57. Successful implementation of the MLF requires more than legislative reform and establishment of a registry. While each State will have their own individual law reform process, implementation of the MLF usually requires at least three phases:

i. Pre-implementation assessment phase: Before legislation is prepared, an assessment/diagnostic of existing law is undertaken to evaluate (i) how well the existing legal regime for factoring works, (ii) how the existing legal regime compares to international best practice (as reflected in the MLF), and (iii) whether the private law rules and regulatory rules for factoring work well together. During this first phase, it can be useful to analyse court cases that interpret the existing law. Existing case law often proves valuable in identifying how the existing substantive law might need to be adapted to better reflect the MLF.[29]

ii. Legislative phase: During this phase, legislation is developed to implement the MLF. States will often have different approaches to how they implement the substantive content of the MLF (see Part II Section 1), as well the method of legislative implementation (see Part II Section 2). The legislative adoption of the MLF should also be accompanied by thorough commentaries explaining the origins and purposes of the MLF, supplemented by academic writings providing illustrations how the law can and should work in practice.

iii. Capacity building phase: Following the legislative implementation phase, a promotion and education process regarding the law will have to delivered to build the capacity of different groups of stakeholders. Business people and financiers will need to be educated on how the new law operates, the types of financing arrangements it facilitates and how to use the Registry. Lawyers, arbitrators and judges will need to be taught how to properly apply the new law. In particular, judges should be encouraged to interpret the new law in the context of the MLF's purpose, objectives and general principles (as explained in this Guide), which will ensure that the new law is being applied consistently with international best practices.[30] A reliable case-law reporting system also supports the development of a consistent interpretation of the MLF. Finally, Regulators will need to also to be educated on how the new law operates in order to ensure that the regulatory and private law regimes governing factoring are properly coordinated.

Pre-implementation interpretation of the MLF by regulatory and judicial authorities

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[26] Articles 2(i) provides that a "security transfer" is any transfer of a receivable by agreement, or creation of a right in a receivable by agreement, 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 transferee or the nature of the secured obligation. See further the commentary on Article 2(i) in Part VI paragraphs [XXX].

[27] *Secretariat: At WG2, the WG decided to explain at a prominent point in the Guide that the concept of transfers in the MLF covers both outright and transfers by way of security (security transfers), and that references to transfers through the Guide should be generally understood to cover both outright transfers and security transfers. The Working Group further agreed that this point could be re-emphasised at points in the Guide through a footnote, where the context particularly warranted it. The WG may wish to discuss at WG3 whether this is a good location in the Guide to make this point.

[28] *Secretariat: This was adapted from the text previously in paragraphs 91 and 92 of Part II Section 2. It was been expanded and relocated, based on suggestions made at WG2.

[29] *Secretariat: This was a point made by the EBRD at WG2, that might be worth including in the Guide.

[30] *Secretariat: This is a point that AG made at WG2.

58. As explained in this part of the Guide, the MLF can only be implemented through a legislative reform that enacts the instrument's substantive rules and provides for the establishment of a registry for the registration of notices of transfers of receivables. However, before a legislative reform process is undertaken (pre-implementation phase), in some circumstances it can be useful for a regulatory authorities to issue regulatory guidance (such as prudential regulation) in relation to the interpretation of existing law, which could coordinate regulatory rules with concepts in the MLF. This regulatory guidance is often a first step that allows for a full legislative reform of the MLF. In some States, judicial authorities also have the power to issue guiding cases that can effectively reform existing laws to better adapt them to the MLF. Similarly to regulatory guidance, judicial interpretation can have the effect of familiarising a State with the MLF, as an initial step towards a subsequent legislative reform.[31]

[31] *Secretariat: This section has been redrafted intersessionally based on feedback at WG2.

SECTION 1 - IMPLEMENTATION OF THE MODEL LAW ON FACTORING WITHIN THE EXISTING LEGAL FRAMEWORK

Adapting the MLF to a State's legal traditions

59. Every State has a unique legal system which is a product of their history, development, culture and legal tradition. A State's approach to implementing the MLF will depend on its legal system and traditions. Implementation will differ depending on whether the implementing State has a common law, civil law, Islamic law or mixed legal tradition. Implementation is also likely to differ between States within the same legal traditions. A State's legal tradition will affect both the extent and manner in which the State implements the substantive content of the MLF (as set out in this section), as well the method of legislative implementation (Part II Section 2).

60. In relation to implementing the content of the MLF, enacting States will take care to craft their implementing legislation so as to be consistent with fundamental precepts of their legal systems. Such precepts may be based on a written or unwritten constitution or similar basic law. Such precepts may also follow from binding religious precepts such as Shari'ah, where rules concerning *riba* and *gharar*, among others, may be relevant to transactions in receivables. Some of the provisions of the MLF on the effects *inter partes* of the transfer of a receivable (MLF Articles 5 – 8) interact with general rules applicable to obligations and contracts. Other rules on third-party effectiveness, registration and priority (MLF Articles 9 - 19) could interact with general rules on property and rights *in rem.* Regardless of exactly how the substantive of content of the MLF needs to be implemented within a State's legal tradition, it is important to emphasise that the MLF has been carefully designed to provide a legal framework that facilitates factoring and can be effectively implemented in all States, regardless of their legal tradition.[32]

61. <u>Terminology:</u> Regardless of legal tradition, enacting States will likely make decisions about terminology within the context of their systems. In order for the rules of the MLF to be incorporated upon existing legal institutions, the enacting State may need to rely on existing and well understood legal concepts, rather than transplanting unfamiliar legal terms. When adapting the MLF's terminology to make it consistent with existing legal principles and concepts, States should exercise caution in ensuring that the use of existing legal principles and concepts do not complicate existing legal principles, or create inconsistency between the MLF and existing laws. For instance, rather than importing the term "receivable" the enacting State may prefer to rely on the existing concept of a "credit", "monetary claim", "payment right", a "contractual right to payment of a monetary sum", or a "right to be paid a monetary sum arising from a contract". Terminological changes do not create significant problems, as long as the term used by the State is a functional equivalent of the term used in the MLF (for example, using the term "right to payment" does not create a problem, at long as its meaning is consistent with the meaning of "receivable" under Article 2(g) of the MLF).

Coordinating the MLF with the existing law of the enacting State relating to transfers of rights.[33]

62. Before the implementation of the MLF, a State is likely to have a body of law dealing with transfers of contractual and other rights, including, but not limited to, receivables. This section sets

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[32] *Secretariat: At WG2 it was decided to redraft this subsection to focus on the point that the MLF can be implemented in States with different legal traditions without providing generalisations of issues that might arise in one particular legal tradition. It was also suggested to remove the sentences regarding where to put the MLF rules (enactment issues), as this matter is dealt with later.

[33] *LG: The is using 'coordinating' in the sense we agreed ie "there may or may not be the need to adapt either the rules in the MLF or the general law. We should use "coordinate" where we are not in a position to give the enacting State guidance on what might need to be changed, and whether the MLF rules should give way to the enacting State's other law, or vice versa." You will see that I suggest that the enacting State consider whether to amend the MLF or the existing law, or neither. Since the decision will depend on the content of the existing law, we can't say more than that.

out in general terms what a State has to consider in relation to this body of law when implementing the MLF. It discusses: (i) the situation where transfers fall within the MLF, (ii) the situation where transfers fall outside the MLF; and (iii) the interaction between the MLF and general law in relation to issues on which the MLF is silent.

63. Transfers within the MLF*:* Transfers of 'receivables' (that is, 'receivables' as defined in the MLF, see Art 2(g) and the commentary thereto) will, under the newly enacted MLF, fall within the MLF. When implementing the MLF, a State will have to consider what existing law relating to transfers of receivables (as defined in Art 2(g) needs to be repealed or amended.[34]

64. Transfers outside the MLF*:* The MLF does not apply to transfers of receivables, contractual rights and other transferable rights which do not fall within the definition of 'receivables' in Art 2(g). Prima facie, the other, non-MLF, law of an implementing State will continue to apply to these types of transfers. These transfers could be for a financing purpose or not for a financing purpose (eg sale of a business). In some States the former category would be covered by secured transactions law.

65. Many States have a general law of 'assignment' (or some other term) which covers transfers of receivables generally and, sometimes, transfers of other contractual rights eg rights to non-monetary performance and other non-contractual rights eg intellectual property rights. This law would continue to apply to transfers that are outside the MLF. The general law of 'assignment' may include some provisions which are very similar to those in the MLF, for example, in relation to debtor discharge. This is particularly the case in relation to MLF chapter VI (rights and obligations of the parties). In this case, the implementing State has to consider two things.

a. First, where the rules are similar but not entirely the same, the State has to consider whether the MLF rule (and language) should also apply to non-MLF transfers. This conclusion would avoid any discrepancy, and could also improve the other, non-MLF, law. If this solution is adopted, the language of the relevant provisions should match.
b. Second, where the existing rule is very similar to the MLF, the State has to consider whether the implementation of the MLF should use the language of the existing provision instead of the language of the MLF. This might be advisable in order to avoid discrepancies between transfers of receivables (as defined by the MLF in Art 2(g)) and transfers of other receivables, contractual rights or non-contractual rights.

Interaction[35] between the MLF and other, general, law of the enacting State

66. This section gives some brief examples[36] of general law of the enacting State which is likely to interact with the MLF. More detailed explanation of the relevant MLF articles and how they could interact with a State's general law is contained in Part IV of this Guide.

67. Contract law. The general applicable law of contract would apply to agreements to transfer receivables to the extent that the MLF does not provide a rule. For example, contact law would apply to the validity of such agreements, including issues as to formation of a transfer agreement not covered by Art 5(2) or to the formation of an agreement not to raise defences or set-off not covered by Art 28(1). It would also apply, for example, to the interpretation of the terms and conditions of the agreement referred to in Art 20(1) and what is required to modify the underlying contract mentioned in Art 29(1). The general applicable law of contract would also govern the contract giving

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[34] *LG: We also have an agreed use of the word 'amend': ""Amend" can be used instead of "adapt" where we are specifically suggesting that the enacting State will be likely to need to change a piece of legislation to give way to the MLF."

[35] *LG: I think 'interaction' is the correct word here given our agreement that it should be used in the situation where "there is likely to be a relationship between the MLF and the enacting State's "other" law. The enacting State will need to review their own general law to determine the degree of "interaction".

[36] *LG: At WG2 MDE suggested taking this out.

rise to the receivable, except where the MLF provides a rule, such as in Art 8(1) which renders a term in that contract ineffective if it provides that transfer of the receivable arising from that contract is prohibited or limited.

68. Law of obligations. More generally, the applicable law of obligations, including contract law, tort law and the law of restitution would apply if relevant. For example, it would govern if a contract or other transaction relating to a transfer of a receivable were affected by mistake, misrepresentation, duress or fraud. Thus, the consequences of a representation referred to in Art 21 not being true would be governed by the applicable law of obligations.[37]

69. Rights to payment governed by specific other law.[38] The transfer of certain rights to payment, such as those under a negotiable instrument, a letter of credit or an independent guarantee, are governed by very specific and detailed rules in many jurisdictions. These rules of applicable law continue to apply to those rights to payment, since they do not fall within the definition of 'receivable' in Art 2(g). However, Art 7 makes provision for the situation where payment of a receivable is supported by a personal right, which could include a right to payment under, for example, a letter of credit.

70. Law of guarantees. The term 'debtor' in the MLF could in some circumstances include a guarantor of the receivable, depending on the applicable law (see paragraph 139 (WG2(2)) below discussing the definition of 'debtor' in Art 2(b)). However, a State's law on guarantees as to the protection of the guarantor, when a guarantor's obligation to pay arose and the extent and nature of that obligation would continue to apply. Art 7(2) would override any anti-assignment clauses concerning guarantees, which is likely to be a change to the existing law.

71. Set-off and defences. The concepts of 'set-off' and 'defences' are referred to in Art 27, which sets out the situations in which a debtor can raise defences and rights of set-off against a transferee. The general law would apply to define what amounted to a valid set-off or a valid defence. This is an example of where the MLF could, in some circumstances, be adapted by an enacting State to coordinate with existing law. For example, in some States there may be no concept of a defence that is distinct from set-off in the context of Art 27. In that situation, Art 27 could be amended when the MLF was implemented to refer only to set-off.

72. Agency law. The law on agency in an enacting State would continue to apply on enactment of the MLF. Thus, for example, any of the agreements mentioned in the MLF could be made by an agent acting on behalf of a party to that agreement. Another example is that it would be up to the agency law of a State whether a transferee to whom a receivable has been transferred (Art 2(l)) included someone acting on behalf of a transferee. Also, Clause 7 of the Registry Rules provides that the requisite identification of a transferee in a notice can be satisfied by the identification of a representative of that transferee. This provision would override any contrary provision of the domestic law.[39]

73. Electronic commerce law. A State's law on electronic commerce would normally provide that 'writing' would include an electronic document and that a signature could be electronic. If a State's

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[37] *LG: have drafted it like this as some jurisdictions would treat this as a matter of contract law and some as a matter of tort law (and maybe some both).

[38] *LG: I put this in here, if we wanted to include it, as it relates to a very specific part of the law of obligations. This is the paragraph that previously was headed 'freestanding payment obligations' (which was really a reminder to me more than anything else). It is really saying that the law on neg instruments, letters of credit etc will continue to apply. If we want to keep it in I think it should go here with the rest of the law of obligations, though it could also go later, I suppose, just before 'property law'.

[39] *LG: These are examples that were suggested by the group considering this section. On reading them, they do seem quit niche, but I think they were considered examples of where there was very specific interaction between agency law the MLF.

law does not do this, the State should consider passing such a law, so that the requirements of writing and signing in the MLF (for example, in Art 5(2)(a)) can be achieved electronically.

74. Property law. The MLF deals with rights that are effective against third parties. In this regard, it will be seen by many States as forming part of its property law, although a number of its provisions deal solely with rights between contractual parties. Depending on the content of a State's property law, there may be interaction between the operation of the MLF and the operation of that State's property law. Some provisions of the MLF may have the effect of [amending][adapting] general principles of a State's property law (such as the basic priority principle of first in time) in the specific situations where the MLF priority rules apply. However, except for these specific situations, a State's general property law will continue to apply after the MLF has been implemented.

75. Insolvency Law. Generally speaking, the State's insolvency law will govern if any party involved in a transfer of a receivable under the MLF becomes insolvent and enters into insolvency proceedings. The MLF provides that a transfer of a receivable (as defined in Art 2(g)) that is made effective against third parties remains so effective and retains its priority if the transferor enters into insolvency proceedings (Art 15). However, this is subject to priority given to specified claims under a State's insolvency law (such as preferential creditors) and a State is given the option of providing an amount for each category of claim (Art 16).

76. Procedural law. When a party wishes to enforce a right it has under the MLF, it may need to go to court or otherwise use the State's procedural law. While the MLF does not include any provisions dealing with procedural law, an enacting State could consider the UNIDROIT Best Practices for Effective Enforcement, which gives guidance in this regard.

77. Consumer protection law. The MLF does not affect a State's consumer protection law (Art 1(2)), which therefore continues to apply once a State has enacted the MLF.

78. Financial Regulatory Law.[40] The operation of the MLF in an enacting State is very likely to interact with that State's body of rules governing financial services, activities, and entities. This interaction between the MLF and regulatory law is dealt with in III(4).

79. Financial law.[41] Some States have a specific 'financial law' which applies to financial transactions. If so, it may be necessary for a State implementing the MLF to amend its language, and maybe even the content, of the MLF to fit in with that State's financial law, or to amend the financial law to be consistent with the MLF. The financial law may, for instance, define the content of "financing agreements" that would include a transfer agreement as defined in Art 2(k) of the MLF. Typically, the requirements for an effective financing agreement would go beyond the minimal requirements set out in Article 5 of the MLF.

Coordinating the MLF and the existing secured transactions legal framework

80. States implementing the MLF will need to ensure that the MLF and the existing secured transactions framework are properly coordinated. In particular, the benefits of the MLF for a State will depend on how well the existing legal framework facilitates factoring:[42]

a. If a State does not have a law that enables the development of a factoring market, the MLF provides a model for a complete law. This could provide a stepping stone to the future implementation of a full secured transactions law based on the MLST. As discussed

[40] *GC: Consider using the term "Financial Regulation" throughout.

[41] *LG: This reflects a point made by MD at WG2 from his experience.

[42] *Secretariat: *Secretariat: At WG2 it was decided to retain the "waterfall" paragraph at the beginning of this section, with amendments to clarify that the MLF needed to be coordinated with existing law, and should not defer to existing secured transactions law, especially if that law was not consistent with the MLST.

at the beginning of Part II of this Guide, in these circumstances States are encouraged to implement the entirety of the content of the MLF, or at least implement the MLF's core concepts.[43]

b. If a State has implemented a secured transactions law that is fully consistent with the core concepts of the MLF in relation to receivables, it is not suggested that a separate factoring law based on the MLF be enacted. As discussed in Part I(5) of this Guide, States that have already established a registry for notices of security rights should not establish a separate registry for notices relating to the transfer of receivables. Where a State's secured transactions law is already consistent with the MLST, it may have omitted some aspects specific to factoring which it could include from the MLF.

c. If a State has a fully functioning law on factoring, it could still take inspiration from the MLF to update its existing law to make it consistent with international best practice standards.

81. There are a number of situations where coordination between the MLF and the existing secured transactions law may be needed, in particular in relation to priority against competing transfers (Article 13), rights in proceeds (Articles 6, 13 and 14), and the applicable law as to when a judgment creditor has rights in the collateral (Article 17). These matters are dealt with in detail in the article-by-article commentary in Part IV of this Guide.[44]

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[43] See [Part II paragraph 54 WG3].

[44] *Secretariat: At WG2 it was decided to delete paragraphs 76 – 83 (WG2 draft) on the basis that they provided too much detail on complex matters (proceeds) for this point in the Guide, and that these matters should instead be explained in the article-by-article commentary in Part IV.

SECTION 2 – METHODS OF IMPLEMENTATION

Legislative implementation of the MLF

82. There are various methods through with the MLF can be implemented through legislation. As an initial matter, States will need to analyse the extent to which matters within the scope of the MLF are currently included in their existing law. If the content of some of the MLF's provisions are already in the law, a State will need to decide whether they are included in a new piece of legislation or whether new legislation just includes new law. The enacting State may decide to omit some provisions of the MLF because issues such as mutual rights and obligations of the parties under a transfer agreement (MLF Article 20) or a subordination agreement (MLF Article 18) may already be adequately covered by general contract or property law.

83. The preferable method of legislative implementation of the MLF will depend on the State's legal tradition, general law and existing secured transactions law. This section explains several methods of legislative implementation. Regardless of a State's approach to legislative implementation, it should be noted that it is important for the private law rules contained in the MLF to be cohesive with the State's regulatory framework for factoring (see Part III (2) of this Guide).[45][46]

84. A standalone law, which could include both the MLF's private law rules alongside key regulatory provisions. This has been the most common form of reform approach.

85. Amendment to existing legislation, such as a civil or commercial code. States with traditional concepts of codification will often have addressed many matters covered by the MLF in their existing commercial or civil codes. States with codified laws will need to consider whether to codify the MLF as a standalone piece of legislation or, rather, to integrate its provisions into the existing structure. In some circumstances, it might be preferable for States not to amend their civil code to implement the MLF, if its possible to instead implement it as a standalone piece of legislation.[47] The code may contain a chapter on factoring contracts that primarily governs contractual relationships. It may cover only outright transfers, which are effective against third parties without any form of registration. This chapter may need to be revised to provide a foundation for a standalone factoring law that comprehensively deals with transfers of receivables and resulting relationships. A code reform would also affect other sections and chapters, such as on assignments and pledges of intangible rights. States with traditions that include significant areas in which law is developed in the context of cases as well as areas that have been the subject of modern codification will need to consider how to integrate language and concepts of the MLF, taking into account both existing statute and case law.

86. More integrated amendments to existing legislation. The legal framework may govern factoring through a combination of a code and specific law(s).

87. Whether to amend or repeal existing law: Where the content of the MLF interacts with a State's existing general law (see [Part II Section 2], above). The State will need to decide whether to repeal or adapt the existing law to accommodate the MLF. For example, in relation to transfers of 'receivables' ('receivables' as defined in the MLF, as opposed to transfers of receivables of types that

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[45] *Secretariat: This was a point made by GC at WG2. Rather than dealing with the regulatory issue under the different legislative implementation approaches, it is suggested it might be better to address it right at the outset in paragraph 88.

[46] Often, the most effective way to implement a legal reform to facilitate factoring is through a partnership of central banks and regulatory authorities and other relevant government ministries, such as the ministries of justice, economy and finance.

[47] *Secretariat: At WG2 it was suggested that this paragraph should not make generalisations about "civil law" and "common law", but should keep the implementation guidance. AG also suggested that it might be worth more explicitly making the point that tampering with the civil code might cause delays and concerns, which we have tried to do here in a gentle way.

do not fall within the MLF), the implementing State will need to consider what existing law relating to transfers of MLF receivables needs to be repealed or amended.

SECTION 3 – COMMON IMPLEMENTATION CHALLENGES

Examples of challenges in implementation

88. Several ongoing factoring law reforms contemplate approaches that substantially deviate from those of the MLF. Given the broad range of contexts and the evolving nature of these deviations, this Section highlights the risks but does not attempt to provide solutions. States are encouraged to implement the MLF as explained in Section [XXX] to create a coherent and predictable factoring regime.

89. Several law reforms, including enacted laws define 'factoring'. While the Working Group attempted to craft a definition, an adequate solution could not be found. Many factoring laws and reforms define 'factoring' along the lines of Article 1(2) of the UNIDROIT Factoring Convention that specifies the elements of a factoring contract. A definition of that nature effectively narrows the scope of the law with the effect that many types of transactions and factors would not be covered by the legislation, undermining the comprehensiveness of the regime, transparency as many types of transfers would not require registration, and priority. States may wish to consider including a definition of 'factoring activity' to provide a bridge between the private law and regulatory framework (see paras. [XXX]).

90. Several law reforms, including enacted laws confine the scope to outright transfers, as that is how factoring has been 'traditionally' defined. Excluding security transfers of receivables, as defined in Article 2 of the MLF has the effect of undermining the comprehensiveness of the regime, transparency as many types of transfers would not require registration, and priority. A less ideal solution than implementing the core principles of the MLF would be to provide for a priority rule as against security transfers that may, for instance, require registration in the general secured transactions registry as a condition of their third-party effectiveness.

91. Several law reforms, including enacted laws attempt to confine the scope to short-term receivables, defined as those where the maturity does not exceed a statutorily fixed period of time. This approach raises several issues, including the legal regime that would govern receivables exceeding the statutory maximum, refinancing 'short-term' receivables extending their maturity beyond the statutory maximum, etc. While this approach might have reflected the nature of 'traditional trade finance' receivables arising from the sale of goods and provision of services, modern factoring arrangements extend to other types of receivables, defined in the MLF, for which practices may differ.

92. Several law reforms, including enacted laws attempt to exclude transfers of overdue receivables. This is because a factoring framework has been used primarily to collect overdue debts, so factoring has built a bad reputation. The MLF applies to the collection of receivables, whether current or overdue. It provides a balanced approach that protects the debtor against overzealous collection efforts. In fact, the MLF implementation would address the policy concerns with respect to actions of 'debt collectors'.

PART III

COORDINATION OF THE MODEL LAW ON FACTORING WITH SPECIFIC MATTERS

SECTION 1 - THE MODEL LAW ON FACTORING AND THE DIGITAL ECONOMY

93. This section deals with the interaction between the MLF and the digital economy. Since the technology and resulting commercial practice changes so rapidly and frequently in this area, this section consists of a brief overview. A detailed discussion of the specific issues concerning the definition of money, currency and monetary sum, the effect of transactions on digital platforms and exchanges, and the use of technologies such as artificial intelligence is contained in the Digital Economy Supplement, which is annexed to the electronic version of this Guide, and available on the UNIDROIT website. The Digital Economy Supplement is designed to be updated periodically, in order to address new technological developments. States interested in understanding the impact of emerging technologies and the digital economy on the MLF and seeking further guidance on the matters noted in this section are encouraged to consult the Digital Economy Supplement.

Digital assets and Private Law

94. A receivable that is an pure intangible asset may also be incorporated in a digital asset or invoice that is transferred to a financier. Depending on how the domestic law treats such linked digital assets (see Principle 4 of the UNIDROIT Principles on Digital Assets and Private Law) or invoice, a transfer of the digital asset or invoice may also convey to the transferee a proprietary right in the receivable itself. This could generate conflicts between on the one hand, the law governing digital assets linked to receivables or the law that governs digital invoices, and a factoring law, on the other hand.

Virtual currencies

95. As discussed in [XXX], where the MLF refers to 'money' in Art 2(f) (definition of 'proceeds'), other law of the implementing State will determine whether this definition includes virtual currency. The other law will also determine the meaning of 'currency of the payment' in Article 24(2)(a). Similarly, it will be up to the implementing State to decide whether to include obligations denominated in digital currency within the phrase 'a contractual right to payment of a monetary sum' in the definition of 'receivable' in Art 2(g). The MLF does not take a position on the meaning of these terms and enables States to confine these terms to what is traditionally understood as 'legal tender' or expand them to include virtual currencies.

Platforms and Exchanges

96. The private sector and States have established many electronic platforms and exchanges that facilitate transfers of receivables. They vary in the types of transactions they enable, the types of factoring they support,[48] the way they operate, the markets which they serve, and the legal effect of transactions. The MLF facilitates transactions[49] on such platforms and exchanges, but does not provide for their establishment or governance. Regardless of the terms and conditions binding on the participants, if the transfer is subject to a domestic law that has implemented the MLF, a notice in relation to a transfer made on a platform or exchange must be registered in the MLF registry to be effective against third parties.

[48] *MD: Several exchanges work for reverse factoring only.

[49] *MD: A platform may be used to collect a receivable only, rather than effectuate its transfer.

Domestic electronic commerce laws

97. It is intended that electronic writing and signatures are included in the MLF's references to writing (in (Arts 5(2)(a), 25(1), 28(1) and (3), 34(3)(b) and Clauses 2(1), (2) and (3) and 14(4) of the Registry Provisions) and signing (see (Arts 5(2)(a), 28(1) and (3)). These terms are not defined as it is assumed that a State would have already enacted an e-commerce law that would ensure functional equivalence between paper and electronic writing and signatures. A State should review its e-commerce law to ensure that it provides for such functional equivalence and, more widely, that it is kept up to date with relevant new technologies. This aspect does not raise any novel challenges and thus it is not addressed in the Digital Supplement.

SECTION 2 - THE MODEL LAW ON FACTORING AND FINANCIAL REGULATION [MATTERS][50]

98. This section focuses on the alignment between the MLF and financial regulation, comprising the body of rules governing financial markets, services, activities, and entities. These rules are part of different regimes intended to promote and maintain the integrity, fairness, efficiency, and stability of financial systems. Their implementation, application, and enforcement largely relies on administrative authorities entrusted with regulatory and supervisory powers, often referred to as (financial) 'regulators' or 'supervisors'.[51] The importance of ensuring coordination between private law rules to facilitate access to credit has been widely recognised. UNCITRAL, for instance, provided guidance on this matter in its Practice Guide to the Model Law on Secured Transactions.[52] Other organizations, such as the IFC and the EBRD, have highlighted the need to address coordination issues in the context of reforms concerning both secured transactions law in general[53] and in receivable finance in particular.[54] Furthermore, regulators and supervisors have been playing an increasingly active role in such reforms. In particular, reforms implementing the MLF are often driven and executed by authorities tasked to regulate and supervise credit activities within or outside the banking sectors.[55]

99. Financial regulation is outside the scope of the MLF, which provides a complete and self-standing private law framework. However, regulatory rules and structure inevitably intersect with factoring products and, thus, with the implementation of the MLF. This is due to different reasons. Factoring encompasses a range of financial products[56] and services normally offered by regulated entities, including deposit-taking institutions (typically banks), and non-deposit-taking institutions (such as factoring companies). As a result, an intersection between different branches of the law arises, as financial institutions applying the MLF must also comply with: (i)[57] authorisation and licensing regimes to undertake factoring activities, (ii) prudential requirements, such as capital and loan-loss provisioning standards, and (iii) conduct of business rules, governing governance, customers protection, and anti-money laundering and counter-terrorism financing (AML/CTF).

100. At the international level, there are no harmonised standards specifically concerned with the regulation of factoring. As a result, the regulatory treatment of such products varies considerably across jurisdictions and entities. In some cases, domestic laws enumerate factoring as one of the regulated activities that regulated financial institutions may be authorised to offer. In these circumstances, the factoring arrangements covered by the MLF are subjected to the regulatory regimes applicable to the regulated entities offering them. For instance, factoring may fall within the definition of credit activities requiring banking or other types of licenses. In other cases, specific licensing requirements might not be established. Yet, some rules for AML/CTF purposes should normally apply.[58]

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50 *GC: The word "matters" might not be needed if we refer to Financial Regulation.

51 *GC: I thought this could add clarity as administrative authorities are commonly and interchangeably defined as "regulators" or "supervisors"… While we do not need to clarify the distinction, this addition is just to clarify that we are dealing with all authorities in this space.

52 *GC to **Secretariat:** Should we add a reference to the UNCITRAL Practice Guide relevant Chapter/Section (Ch 3) in fn or mention it in the text suffice?

53 IFC Primer on Prudential Regulation (2020).

54 EBRD New Finance Support (2023).

55 *GC: The preceding four sentences were adjusted to reflect our discussion and MD's suggestions on giving more relevance to the role of regulators. I have also flagged the general relevance of the matter, with reference to the UNCITRAL Practice Guide and the IFC and EBRD works in this area.

56 *GC: we can refer to the products mentioned earlier (such as reverse factoring, etc)

57 *GC: I've changed the order in this list to reflect the order followed in this section. I have also added some references to specific rules to sound less abstract.

58 *GC: I have separated this paragraph here, and simplified the next paragraph. These two paragraphs cover two distinct points.

101. Moreover, financial institutions providing factoring may be required to comply with various customer protection requirements also when serving small businesses. In several jurisdictions, requirements may also include disclosure obligations, fair treatment principles, and standards governing collection practices. They may also encompass limitations on fees and the imposition of caps on interest rates, particularly when factoring entails a security transfer, which may be regarded as a lending activity subject to relevant limitations.[59]

102. The supervisory framework applicable to factoring activities and companies varies depending on how powers and functions to govern financial markets are allocated in the implementing State. Factoring may, thus, fall within the purview of either a single supervisory agency or multiple supervisors. In the latter case, it may fall within the remit of the authority tasked to oversee the banking sector (which may be the central bank), the one tasked to supervise the non-banking activities and entities, or a combination of both. Hence, implementing States should consider how factoring fits within the existing regulatory and supervisory framework to ensure coordination with the MLF.

103. The effective implementation of the MLF requires careful coordination between private law and regulatory rules. In this regard, an implementing State may wish to consider the adoption of the MLF as a stepping stone to rationalise existing regulatory frameworks and address outstanding gaps that limit the development of a sound and inclusive factoring market. Strategies and approaches to promote coordination between these two areas of the law have been outlined by the International Finance Corporation (IFC);[60] in particular, the IFC Knowledge Guide on Factoring Regulation and Supervision (2024) provides detailed guidance on how to establish a coherent regulatory framework that dovetails with and complements the rules enshrined in the MLF. Based on such international best practices, the remainder of this section offers an overview of the main regulatory aspects that implementing States must consider. States are encouraged to consult the IFC Knowledge Guide on Factoring Regulation and Supervision for detailed guidance on regulatory matters.

Regulatory Definitions

104. The MLF does not define factoring as such; its rules govern the transfer of receivables, which are broadly defined to include outright and security transfers of receivables. Regulation is not directly concerned with these transactions but rather with the rules applicable to financial institutions extending funds upon the transfer of receivables. Hence, while the MLF applies to such transfers regardless of the parties involved, financial regulation only applies to those transferees undertaking a regulated activity. Factoring is typically included in the services that banks offer. It can also be enumerated among the regulated activities that (regulated) non-banking financial institutions are permitted to undertake. In these instances, a reference to factoring or receivable finance is typically contained in extant legislation or administrative instruments, establishing specific licensing, prudential, and conduct of business requirements for various types of financial institutions.[61]

105. However, the understanding of factoring for regulatory purposes may differ from the MLF. Hence, if factoring is enumerated as one of the activities regulated financial institutions can undertake, implementing States must ensure coherence with the notions of transfer and receivables advanced in the MLF. Absent this clarification, whether a transferee should comply with specific regulatory

[59] *GC: This has been added to address MH's and Ivor's comment during WG2 and subsequent decisions taken by the WG.

[60] *GC: Note: we might have used the IFC acronym earlier; not sure if the house-style allows us to just use "IFC".

[61] *GC: The preceding two sentences have been adjusted to address the World Bank's comment about the need to flag the difference between banks and NBFIs.

requirements may be unclear. To avoid such ambiguities, two intertwined aspects must be addressed.[62]

106. First, the regulatory definition and understanding of factoring should include the outright and the security transfer of receivables arising from different types of contracts in alignment with the MLF. In many jurisdictions, regulatory regimes rely on outdated notions of factoring that are unclear or limited to the outright transfer of receivables generated by the supply or lease of goods or services. In these instances, the application of licensing requirements to various factoring transactions becomes uncertain or excessively restrictive, and some financial institutions are precluded from entering the market. This problem is particularly salient for non-banking financial institutions that may be authorized only to undertake factoring activities deploying outright transfers, as security transfers require a different license type. But it may also affect banks, as the scope of their licenses may be questioned in jurisdictions where outright transfers of receivables fall under the purview of non-banking authorities while security transfers are lending activity under the remit of banking authority.[63] These ambiguities and limitations may distort market incentives, creating an asymmetric regime for different types of transactions, ultimately curtailing the economic benefits that implementing States seek to achieve with the MLF.[64] Regulatory requirements should apply uniformly to products involving either the outright or the security transfer of receivables. Moreover, the types of contracts generating receivables that can be transferred should reflect those enumerated in the MLF—including, in particular, the license of intellectual property and the provision of data.

107. Second, implementing States must clearly define the regulatory perimeter by indicating under what circumstances offering factoring services falls within the regulatory framework. To this end, implementing States may introduce a definition of "factoring activity" as the focus of regulation. A factoring activity is a financial service offered to the public by a business organisation and consists of providing funds against the outright or the security transfer of a receivable as defined in Article 2(g) of the MLF. This definition aligns regulatory requirements with the MLF but excludes from regulatory requirements situations where transfers of receivables are not offered as a financial service. For example, the transfer of an invoice made by an individual in lieu of payment, although governed by the private law rules, does not fall within the regulatory purview as it does not qualify as a regulated activity. Based on this definition, the regulatory requirements for undertaking factoring activities can be established.

Authorisation and Licensing

108. Different modes can be established to authorise financial institutions that undertake factoring activities. In general terms, it should be clear whether a special authorisation is needed to undertake factoring activities and, if so, whether such authorisation requires a new license or other forms of approval granted by the competent authority. To this end, a distinction should be made between banks, comprising credit institutions authorised to take deposits, and non-banking financial institutions, including specialised lenders not taking deposits.

109. Banks should be permitted to undertake factoring activities without applying for an additional license. Especially in implementing States that adhere to the international regulatory standards elaborated by the Basel Committee on Banking Supervision, banking regulation is usually robust and sufficiently developed to encompass a variety of financing arrangements. In addition, banking

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[62] *GC: The point of this paragraph has been separated from the preceding and simplified to highlight the main message for implementing States. Please note that here, the problem is whether, for regulatory purposes, a notion of factoring is already used (for banks and/or other NBFIs). If the term "factoring" is already used for regulatory purposes, it most likely does not match the MLF.

[63] *GC: This addition reflects the World Bank's comment and decision to clarify the impact on banks and non-banks. It is not an exhaustive analysis, but reflects some of the key issues emerged in different reforms.

[64] *GC: This sentence has been amended based on comments from MH, the WB and EBRD at WG2 asking to avoid wording like "circumvention" or "regulatory arbitrage".

activities already entail a variety of transactions, including the assignment of rights to payment for financing purposes. While the implementation of the MLF facilitates these financing mechanisms, the establishment of new regulatory regimes or coordination with existing regulatory regimes should not limit the possibility for banks to offer factoring services based on outright and security transfer of receivables arising from various underlying contracts enumerated in the MLF.

110. For existing non-banking financial institutions, implementing States can decide to extend existing licensing regimes to cover factoring activities. For instance, regulated micro-finance institutions may, within the limits set for their activities, engage in different transactions entailing the assignment of receivables or their use as collateral. Although these entities may not engage in complex or large supply chain financing, in most developing and emerging economies, they are the primary credit provider to MSMEs, and the enactment of the MLF coordinated with regulatory regimes may stimulate the diffusion of factoring to promote financial inclusion.

111. In addition to existing licensing regimes, implementing States are encouraged to establish a "factoring license" for non-banking financial institutions offering factoring products, namely "factoring companies". Following the approach advanced in international best practices and set out in this section, factoring companies can be defined as specialised, non-deposit-taking financial institutions authorised to undertake factoring activities under a license granted by the competent authority. This licensing regime is the centrepiece of a regulatory and supervisory framework for factoring companies that implementing States can establish to promote coordination with the MLF.

Regulation and Supervision of Factoring Companies

112. Factoring companies are non-deposit-taking institutions. They are typically financed by banks and other financial institutions willing to enter the market indirectly rather than offering factoring products to retail clients. Crucially, they cater to the financing needs of a market segment not served by smaller entities, such as micro-finance institutions. In this context, a licensing regime with proportionate regulatory requirements and ongoing supervision for factoring providers supports the emergence of a diversified, liquid, and sound market.[65] In fact, banks and other investors face significant risks and regulatory limitations when they invest in non-licensed and supervised entities offering financing products to the public. Hence, a coherent regulatory framework premised on a streamlined licensing regime for factoring companies increases confidence and unlocks new liquidity.

113. A proportionate regulatory framework for factoring companies promotes the emergence of a sound and diversified market supporting the implementation of the MLF. To this end, it typically includes four core areas: (i) a supervisory framework, (ii) licensing requirements, (iii) a simplified set of prudential rules, and (iv) conduct of business and AML/CTF regulations.

114. Supervisory Framework: In implementing a regulatory framework for factoring, it is key to allocate supervisory and licensing powers over factoring companies to a designated authority. In some instances, determining the competent authority for factoring companies is a straightforward exercise, as only one authority exists (integrated model) or the competencies of multiple authorities are clearly defined. In any respect, where multiple authorities coexist, regulatory, supervisory, and licensing powers over factoring companies should be clearly attributed.

115. Licensing Requirements: Factoring companies must be authorised by the competent authority to undertake factoring activities by applying for a factoring license. Licensing requirements can be adjusted depending on the jurisdictions and usually cover the following aspects: (i) the definition of factoring activities in alignment with the MLF; (ii) the legal status of the factoring company, normally incorporated in accordance with applicable company law; (iii) the ownership structure, whereby shareholders and beneficial owners must be disclosed; (iv) the corporate

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65 *GC: This sentence has been changes to address NC's comment at WG2.

governance arrangements detailing the responsibilities and functions of different organs within the factoring company; (v) the fitness and propriety standards for the board of directors and senior managers; and (vi) a minimum level of paid-up capital.

116. Prudential Rules: Factoring companies are not authorised to take deposits. Hence, prudential regulation for factoring companies is more straightforward than the one applied to banks and typically consists of a fixed amount of equity, which can be raised periodically or adjusted depending on business volume and turnover, paired with loan-loss provisioning allowances coordinated with international accounting standards. While implementing States may consider extending existing prudential rules for non-deposit-taking lenders to factoring companies, the prudential treatment of different factoring arrangements requires specific adjustments in alignment with the MLF. In particular, different rules should apply to factoring products that do not entail a secured loan because they are based on outright transfers of receivables.

117. Conduct of Business and Customer Protections Rules: Broadly, these rules pertain to how firms carry out their business and how they treat their customers while safeguarding market integrity. The conduct of business rules applicable to factoring companies are primarily aligned with those adopted for other financial entities and are consistent with the licensing requirements. For example, the board of directors' and senior managers' fitness and propriety are conditions for obtaining and retaining the factoring license. Implementing States may also adopt mechanisms to protect customers without imposing excessive burdens on factoring providers catering to MSMEs. Such rules could include a requirement to disclose, in clear and comprehensible terms, fee structures, discount rates, and other material features of a factoring arrangement. In addition, fair collection requirements, ensuring that the collection of receivables is carried out transparently, can be established along with streamlined complaint-handling procedures that may be resolved through summary administrative processes, settled by financial ombudsman or the competent supervisor.[66]

118. AML/CTF Rules: AML/CTF rules are essential to support the development of a factoring market. Implementing States should adhere to international recommendations elaborated by the Financial Action Task Force.[67] In implementing these standards, particular attention may be given best practices dealing with specific types of transactions, such as those elaborated for "trade-based money laundering". To this end, a risk-based approach paired with adequate technological solutions can be critical in ensuring compliance while limiting costs. Technological systems, for instance, have been deployed to identify suspicious activity related to the transfer and trading of receivables; upon identification, they are reported to relevant authorities for further investigation. These systems, connected to centralised platforms, detect specific risk indicators, examining, amongst others, the type of transactions, the underlying documentation, the customer profile, and the financing methods.

Legislative Approaches

119. The implementation of the MLF requires coordination with relevant regulatory regimes. To this end, the establishment of a cohesive set of private law and regulatory rules is premised on a notion of factoring activities that is aligned with the definitions of transfers and receivables contained in the MLF. Upon this notion, implementing States can establish a governance framework for factoring activities, which allocates regulatory, licensing, and supervisory powers over factoring activities to existing authority. While banks should be authorised to undertake factoring activities under existing licensing regimes, implementing States will benefit from establishing a new licensing regime for non-

[66] The preceding two sentences have been added to reflect the comments advanced by the World Bank and MH at WG2 and reflect the WG decision.

[67] Financial Action Task Force, International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation (FATF, Paris).

deposit-taking financial institutions (factoring companies) accompanied by a simplified set of prudential and conduct of business rules.

120. To ensure coordination between private law and regulatory elements, implementing States have two main options. The first option is to enact a unified legislative act containing the private law rules of the MLF, together with key regulatory provisions, as detailed in the IFC Knowledge Guide on Factoring Regulation and Supervision (2024). Typically, key regulatory elements contained in a factoring law are limited to the identification of the competent authority, the designation of factoring as a regulated activity, the coordination with existing licensing requirements, and the establishment of a new licensing regime for factoring companies; additional delegated and administrative acts define more precise regulatory requirements. A second option is to implement the private law rules of the MLF and regulatory standards in separate acts. The choice is influenced by the legislative style and constitutional framework of each implementing State. Nonetheless, enacting a unified legislative act is usually the most effective approach to ensure the cohesive implementation of the MLF.

PART IV

ARTICLE-BY-ARTICLE GUIDE

121. Part IV provides an article-by-article commentary on the 54 Articles and 25 Registry Clauses in the MLF. The purpose of this article-by-article commentary is to (i) provide detailed guidance on the operation of each article, (ii) explain why it is necessary, (iii) explain how it might interact with other MLF articles as well as the State's broader law, (iv) connect specific articles to the MLF's policy objective and core concepts, and (v) illustrate the operation of articles through the use of practical examples.

GENERAL INSTRUCTIONS ON READING THE MLF

122. In reading the MLF, it is advised that the following instructions are considered:

123. The MLF should be read as a complete law. The MLF provides a comprehensive instrument for States seeking to modernise and optimise their legal framework governing factoring. The text has been drafted to allow direct incorporation into the enacting legislation (aside from bracketed text, as explained below). While States will need to tailor the implementation of the MLF to suit their legal culture and existing legal framework (and may not enact the law verbatim), States are encouraged to recall the main implementation recommendation that the MLF should be implemented in its entirety (see Part II).

124. Bracketed text requires States to make certain decisions. The MLF contains 49 sets of square brackets (27 sets in the main articles and 22 sets in the registry clauses). The purpose of the square brackets in the text is to signal to enacting States that they cannot implement the relevant part of the text verbatim, and will need to make a decision in relation to the implementation of the relevant section. Generally, bracketed text will require States to take one of the following actions:

i. States need to specify something. Bracketed text is often used where the enacting State is required to insert additional language that specifies something within their domestic context. For example, the bracketed text in Article 2(e) requires States to specify a definition of "judgment creditor" which is consistent with their broader law. Similarly, Article 2(h) requires States to specific the relevant domestic authority responsible for establishing the registration system under the law. These types of bracketed text are usually found within articles or clauses (rather than on the outside of entire articles) and should be considered as mandatory for States to properly implement the relevant articles.

ii. States need to decide whether to include a certain rule: Bracketed text is sometimes used around an entire Article where the enacting State is required to consider whether to include or exclude the relevant Article from their implementing legislation. For example, the bracketed text around the entirety of Article 16 (transfers competing with claims arising by operation of other law) requires States to consider whether there are other claims under their general law that should have priority over a transfer that is effective against third parties under the MLF. If States have such claims, they should include Article 16 and list such claims. However, if States do not have such claims, States should not implement Article 16 at all. Another example is Article 52 (transitional rules for determining the third-party effectiveness of a prior transfer), which has separate square brackets around the entirety of paragraph 5 and the entirety of paragraph 6. Here, States need to decide whether to include paragraph 5, paragraph 6, or both (depending on how transfers are made effective against third parties in the enacting State under the prior law).

125. In certain circumstances, interrelated sets of square brackets might require States to both (i) decide whether to include a certain rule, and (ii) specify something. For example, as previously noted above, the bracketed text around the outside of the entirety of Article 16 requires States to consider whether there are other claims under their general law that should have priority over a transfer that is effective against third parties under the MLF. If a State does decide to include Article 16, the additional bracketed text inside Article 16 requires States to specify both (i) the types of claims that will have priority over transfers effective under the MLF, and (ii) the amount for each type of claim. The article-by-article commentary in this part provides further guidance on the decisions that States will need to make in relation to each set of bracketed text.

126. The MLF needs to be read in the context of its defined terms: Article 2 sets out 13 defined terms that are essential for the successful operation of the MLF. States should be careful in reading the MLF to consider these terms with reference to their definitions in Article 2, and not their own domestic law conceptions of these terms. This is particularly important of the definitions for "receivable" in Article 2(g), "transfer" in Article 2(j), "security transfer" in Article 2(i) and "proceeds in Article 2(f).

CHAPTER I – SCOPE AND GENERAL PROVISIONS

127. This introductory chapter does a number of things. First, it defines the scope of application of the MLF, then it includes a large number of definitions of words and concepts used in the MLF, and finally there are some provisions of general application throughout the MLF. The scope of application of the MLF is delineated through the definitions of 'receivable' and 'transfer'. A receivable, under the MLF, is broadly speaking, a trade receivable (see paragraphs 150 – 161 (WG2(2)). Receivables arising out of other types of contracts, such as loan agreements, are not included. 'Transfer' encompasses both outright transfers and security transfers (see paragraphs 164 – 168 (WG2(2)).[68] An outright transfer is where all rights in a receivable are transferred from the transferor to the transferee. A security transfer includes any type of right created for the purposes of security; a functional approach is adopted. What is meant by 'security transfer' is discussed in detail under [paragraph 168 (WG2(2)) Art 2(i)].

128. Security transfers are included in the definition of 'transfer' (and therefore within the scope of the MLF) for several reasons which are discussed in the next three paragraphs . [For these reasons, the inclusion of security transfers was supported by a wide variety of stakeholders.][69]

129. First, it is very important that the same priority rules should apply to all consensual rights in a receivable, as otherwise priority issues could be covered by different rules leading to uncertainty and circularity problems. By including security transfers within the MLF, the priority rule in article 13 (first to file a notice) applies to both outright and security transfers. Thus, a person (TE) considering whether take a transfer of a receivable (R), can check the MLF registry and see whether there are any prior registrations that cover that receivable. If the transferor had previously transferred R by way of security but security transfers were not included in the MLF, a notice relating to that prior security transfer would not be registered in the MLF registry and it would be difficult or perhaps impossible for TE to find out about the prior security transfer. Moreover, if security transfers are included in the MLF, if TE finds no notices on the registry in relation to R and TE registers a notice in relation to the transfer to it, TE can be sure that it will have priority over all other transfers (outright

[68] *LG: As instructed at WG2 I have included what used to be paragraph 162 - 166 here. However, I do have some misgivings that the level of detail is quite high for an introduction. I wonder whether we should just include what is now in 123 and keep the rest in the commentary to 2(j).

[69] *LG: Whether we refer to stakeholders was debated at WG2. I have put it in square brackets. I can see argument both for and against keeping it.

or security) in relation to which notices are registered subsequently. However, if security transfers were not included in the MLF, TE's registration in the MLF registry would not ensure its priority over any other security transfers, since this priority contest would be governed by other law. For these reasons, implementing the MLF by only addressing outright transfers would be likely to cause difficulties in relation to priorities.

130. A second reason is that including security transfers in the MLF obviates the need to determine whether a transfer is an outright transfer or a security transfer for the purpose of determining whether the MLF applies to that transfer. [This type of characterisation has caused problems in some States, as sometimes the line can be difficult to draw, especially in relation to non-recourse financing, (see paragraph XX)].[70] However, the rules under the MLF in relation to collection of the receivable and enforcement (chapter VII) differ depending on whether the transfer is an outright transfer or a security transfer (see ch VII sections 1 and 2). Therefore the need to characterise may still arise in some circumstances under the MLF, and might also be necessary for other purposes under general domestic law, such as insolvency law, or regulatory law.

131. A third reason for including both outright and security transfers in the MLF is to ensure that the same conflict of law rules apply to both types of transfers. The relevant conflict of laws rules under the MLF are in Chapter VIII.

132. It is for these three reasons that the MLF applies to both outright transfers and transfers by way of security, and that this aspect of the MLF is considered one of the instrument's seven core concepts. It is important to remember that the definitions in Article 2 are only for the purpose of the MLF. The commentary explains the definitions, using generic practical examples where appropriate. This practice of using examples continues throughout Part 4 of the Guide to Enactment. There is a consistent set of acronyms used in these examples. TR is used for the transferor of the receivable, and TE for the transferee (TE1, TE2 etc if there is more than one transferee). The person who owes the receivable (the debtor) is D.

Article 1 — Scope of application

1. This Law applies to transfers of receivables.

2. Nothing in this Law affects the rights and obligations of a person under any other law governing the protection of parties to transactions made for personal, family or household purposes.

3. Nothing in this Law overrides a provision of any other law that limits the transfer of specific types of receivable.

Comment:

133. The scope of the MLF is defined through the definitions of 'transfer' and 'receivable' in Art 2, together with the provision in Art 1(1) that it applies to transfers of receivables. These definitions will be discussed in the next section. Generally speaking, the scope of the MLF as implemented in a particular State could be different from the scope of regulation addressing 'factoring'. If this is the case, an enacting State should amend the regulatory scope to ensure that it is the same as that of the MLF. [For example, if, under a regulatory law on factoring the definition of 'receivable' did not

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[70] *LG: I don't think I got a clear steer at WG2 whether to keep in this sentence or not.

include a contractual right to payment of a monetary sum arising from the provision or processing of data (Art 2(g)(iii), that regulatory law should be amended to include such a contractual right.][71]

134. There are some specific savings for national law in Art 1(2) and 1(3).

135. In relation to both these paragraphs it should be noted that the MLF applies to consumers, primarily as debtors but also (much less often) as transferors and as transferees. Art 1(2) makes it clear that the MLF does not affect the operation of any consumer protection law in an enacting State, which could have the effect of protecting consumers as debtors, but also as transferors or transferees.[72]

136. Art 1(3) makes it clear that the MLF is not intended to override policy-based statutory provisions limiting what receivables are transferable. An enacting State is advised to make this clear in the implementing legislation, especially if these statutory provisions are in another piece of legislation.

137. Examples of such provisions include limitations on the transfer of receivables arising out of some contracts with the Government. A supplier's contract with the Government giving rise to a receivable could be for the supply of goods, services or data, and the receivable would then fall within the definition in Art 2(g). A restriction on the transfer of such a receivable is typically imposed for reasons of national security.

Article 2(a) — Competing Claimant

(a) "Competing claimant" means a person with rights in a receivable that may be in competition with the rights of a transferee of the receivable.

Comment:

138. The definition of 'competing claimant' is important in relation to certain provisions about priority. The definition must be understood in relation to a receivable which has been transferred by a transferor TR to a transferee TE. TE therefore has rights in the receivable. A competing claimant is a person C who also has rights in the receivable, even though there may not actually be any competition on the facts. C may not be a transferee, its rights may arise in a way other than from a transfer. For example, C could be a judgment creditor with rights in the receivable (see Art 17). If there are competing claimants, the priority between them is determined by Art 13 or 17.

139. The following are some examples of when TE and C are, or are not, competing claimants.

a. The transfers by TR to TE and to C are both outright transfers. After the transfer to TE, TR has no further rights in the receivable. If, by the time of the transfer to C, TE has made the transfer to it effective against third parties by registering a notice relating to it under Art 9, C acquires no rights in the receivable, and is not a competing claimant. However, if, by the time of the transfer to C, TE has not registered a notice, and the transfer to TE is not effective against third parties (see paragraph 215 (WG2(2)). In this situation, TR has a 'power to transfer' the receivable (see Art 5(1) and paragraph 187 (WG2(2))) and so C will acquire rights in the receivable and will be a competing claimant.

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[71] *LG: This example is that given by MD at WG2. I am not sure whether we want to include a detailed explanation like this in an early paragraph, but I put it in for discussion.

[72] *LG: This redraft is meant to 'change the emphasis'. I have taken out the reference to peer-to-peer platforms but this could go into the annex and the regulation part.

b. The transfers by TR to TE and C are security transfers. After the transfer to TE, TR still has rights in the receivable, and so C will acquire rights in the receivable and will be a competing claimant.

c The transfer by TR to TE is an outright transfer and C is a judgment creditor. After the transfer to TE, TR has no further rights in the receivable. If, by the time C takes the steps to acquire rights in the receivable that are stipulated in Art 17, TE has made the transfer to it effective against third parties by registering a notice relating to it under Art 9, C acquires no rights in the receivable, and is not a competing claimant. However, if, by the time C takes those steps, TE has not registered a notice, C will acquire rights in the receivable (as TR has a 'power to transfer') and will be a competing claimant.[73]

Article 2(b) — Debtor

(b) "Debtor" means a person who owes payment of a receivable.

Comment:

140. A debtor is someone who owes a receivable or who, in respect of a future receivable, will become a debtor in the future when the receivable arises. This is the case even though, on a literal reading, a person who will become a debtor in the future does not fall within the wording, since that person does not presently 'owe' the receivable. If a State has a literal approach to interpretation, and the interpretation of the wording in the MLF to include a person who will become a debtor in the future is likely to cause difficulties, extra wording could be included in the definition in Art 2(b). For example, it could read 'a person who owes payment of a receivable, or, in the case of a future receivable, the person who will owe payment of that receivable when it arises'.[74]

141. It is important that the term 'debtor' includes a person who will become a debtor in the future as future receivables can be the subject of a transfer agreement (see Art 5(5)), and certain steps can be taken with regard to such a debtor before the receivable has arisen. For example, a debtor of a future receivable can be sent an effective notification or a payment instruction in relation to that future receivable if the debtor can be identified (Art 25(3)). Such notification could be significant, for example, in determining whether a set-off can be raised by the debtor against the transferee under art 27.

142. The definition of 'debtor' could also include a person who has guaranteed a transferred receivable, depending on the wording of the guarantee and the applicable law. In some jurisdictions, a guarantor may fall within the definition of 'debtor' once the guarantor's obligation to pay the guaranteed debt has arisen. If a guarantor is, or becomes, a debtor, the MLF will apply to it; the most significant sections in this regard are chapter VI part 2 (dealing with the rights and obligations of the debtor) and chapter VII dealing with collection and enforcement. However, generally, the applicable law relating to guarantees will apply (see Part II(1) paragraphs [XXX]). Since the provisions of the MLF can be derogated from or varied by agreement (with some exceptions, see Art 3(1)) parties to a guarantee agreement could do this in relation to the guarantor except to the extent that this agreement affects third parties (see Art 3(2))

[73] *LG: I tried to shorten this a bit, but actually by shortening it any more it actually becomes both longer and less informative (eg it takes just as long to say 'C has not made the transfer effective under Art 9' as 'C has not registered a notice'. The points cannot be made merely by referring to other articles.

[74] *LG: This paragraph does not say when a receivable arises or that the question of when it arises depends on applicable law. We should say that latter point somewhere but not here.

Article 2(c) — Default

(c) "Default" means the failure of a person who owes an obligation secured by a security transfer to pay or otherwise perform that obligation and any other event that constitutes default under the terms of an agreement between the transferor and the transferee.

Comment:

143. This definition of 'default' is only relevant when a receivable is subject to a security transfer. The term is limited to (a) default in respect of the secured obligation and (b) any other event constituting default under the security transfer agreement. The term 'default' is not used in the MLF for failure to pay a receivable.

Article 2(d) — Future receivable

(d) "Future receivable" means a receivable that arises or is acquired by the transferor after the time a transfer agreement is entered into, whether or not the contract giving rise to the receivable has been entered into at that time.

Comment:

144. There are two senses in which the term 'future receivable' is used. Each sense refers to a different situation.

145. The first sense refers to a situation in which the receivable has not yet arisen at the time of the transfer agreement. For example, a manufacturing business TR could enter into a transfer agreement with TE on day 10 in relation to all its present and future receivables (see Art 5(5), which provides that a transfer agreement can provide for the transfer of future receivables). In that context, a receivable relating to a supply contract X that had not been entered into on day 10 would be a future receivable.

146. A future receivable in this sense which is included in a transfer agreement is transferred at the time it arises, as long as the transferor has rights in it or the power to transfer it (Art 5(5)). Thus, if the receivable under supply contract X arises on day 20, that will be time at which it is transferred. Article 5(5) provides that the transfer takes place when the transferor acquires rights in the receivable or the power to transfer it, but before the receivable arises the transferor cannot have rights in it or the power to transfer it. The time at which a receivable arises is a matter for the applicable law.[75] [In many jurisdictions a receivable will arise at the time when the contract giving rise to it is entered into by the parties.][76]

147. A notice relating to the transfer of future receivables can be registered at any time (Annexe, clause 4). Thus, in the example in paragraph 142 (WG2(2)) above, TE could register a notice in relation to the transfers set out in the transfer agreement on day 1 (before the transfer agreement) or day 12 (after the transfer agreement but before the transfer) or in day 24 (after the transfer). The time of registration will be the relevant moment for the priority rule in art 13. If the notice is

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[75] *LG: I think this is quite a good place to put this sentence (which has to go somewhere) and so I suggest that it comes out of square brackets.

[76] *LG: I'm not sure we finally decided whether we wanted to include this statement, but if we do I think it should go here, ie the first time that future receivables are mentioned.

registered on day 1, then TE will have priority over any transfer a notice in respect to which is registered after day 1. Further, as mentioned above, a notification of a transfer of a future receivable (or a payment instruction) can be sent to a debtor provided that the information that must be contained in a notification (identification of the receivable) is ascertainable and the debtor can be identified (Art 25(3)). Thus, in the example in paragraph 142 (WG2(2)), a debtor (D) could be notified, at any time after day 1, of the transfer to TE of all the present and future receivables D owes to TR. After such notification, for example, any right of set-off that did not fall within art 27(1) could not be raised by D against TE (art 27(2)).

148. The second sense in which 'future receivable' is used is where a receivable included in a transfer agreement has arisen but has not yet been acquired by the transferor. For example, a transfer agreement entered into on day 10 between an export factor and an import factor covers present and future receivables. A receivable that, on day 10, was owed to a client of the export factor (and which was therefore not a future receivable in the first sense) but which had not yet been transferred to the export factor, would be a future receivable in the context of the transfer agreement between the export and the import factor. A future receivable in this sense is transferred when the transferor acquires rights in it or the power to transfer it (Art 5(5)). Thus, if the receivable in the example was transferred to the export factor on day 20, it then ceases to be a future receivable in the context of the transfer agreement between the export factor and the import factor, and will be transferred to the import factor on day 20. However, as set out above, the import factor can register a notice relating to the transfer and can give notification to the debtor before day 20 and the date of this registration will determine its priority against competing claimants.

Article 2(e) — Judgment creditor

(e) "Judgment creditor" means [the enacting State to specify the definition].

Comment:

149. The term 'judgment creditor' refers to a person C who has obtained an enforceable [court] order,[77] against another person TR ordering TR to pay C a sum of money. If TR does not pay, a State typically will enable C to obtain rights in TR's assets, including any receivables that are owed to TR. The precise definition of a judgment creditor will vary from State to State, as will the steps that must be taken for C to obtain rights in receivables owed to TR. Therefore, the MLF leaves it up to the enacting State to decide on its own definition of 'judgment creditor' in order to fit in with its existing law. It is important, however, that the definition is consistent with Art 17, and with the specification made by the enacting State in Art 17 as to the steps that need to be taken for the judgment creditor to acquire rights in the receivable.

Article 2(f) — Proceeds

(f) "Proceeds" of a receivable means any:

(i) money;

(ii) negotiable instrument; or

(iii) right to payment of funds credited to an account with an authorised deposit-taking institution,

[77] *LG: I've changed this to reflect the discussion at WG2 but I am not sure if it is now too wide (if "court" is taken out). It will need to be checked against the effective enforcement instrument.

that is received in respect of the receivable, whether in full or partial payment of the receivable. It includes proceeds of proceeds.

Comment:

150. 'Proceeds' are important in the MLF as the right of a transferee of a receivable extends to its proceeds under art 6, as does its third party effectiveness (art 10) and its priority position (art 14). These articles are discussed in detail later in this Guide. 'Proceeds' are 'cash proceeds' received in respect of a receivable, and includes any interest paid in respect of the receivable as this is part of the receivable itself. Payment under a negotiable instrument would not constitute proceeds, since this is not payment received in respect of a receivable (as defined in art 2(g)); but could be proceeds of proceeds (see paragraph 145 (WG2(2)).

151. Under the MLF definition in art 2(f) 'proceeds' are limited to cash proceeds. Non-cash proceeds are not included since including them might result in the MLF registry becoming a collateral registry and also could encroach on an enacting State's law governing other types of assets (for discussion of the law governing priority disputes in relation to proceeds see paragraphs 240 – 243 (WG2(2)). Another reason for the limitation is that, in the context of factoring, the proceeds of receivables are usually money, negotiable instruments or bank accounts. 'Proceeds' also does not include returned goods, but if a transferee wants rights in respect of returned goods or other non-cash proceeds, it can provide for these in the transfer agreement. However, the MLF provisions on proceeds will not apply to those types of proceeds.

152. There are three types of 'cash proceeds' in the definition. Each will be considered separately in the paragraphs below.

(i) Money

153. 'Money' is not defined in the MLF as the meaning of 'money' differs in different domestic laws, and also the meaning can change over time. It is up to an enacting State to decide whether, and how, to define 'money' and how to make its meaning consistent with the rest of its domestic law. It would be up to a State to decide what counted as 'money', whether it included 'digital currency', and if so which type(s), taking into account its own law on money and what counts as legal tender in that State.[78] As will be seen below, 'money' does not include funds in an account with a bank or other deposit-taking institution since these are covered in (iii).

(ii) Negotiable instrument

154. Negotiable instruments are included in the definition of proceeds as they are a common form of 'cash proceeds' of a receivable in a factoring context. However, as discussed in paragraph 151 (WG2(2)), negotiable instruments are not included in the definition of 'receivable' in art 2(g) and therefore the transfer of negotiable instruments is outside the scope of the MLF.

(iii) Right to payment of funds credited to an account with an authorised deposit-taking institution

155. Art 2(f)(iii) refers, broadly speaking, to a bank deposit. However, deposits are also taken by institutions that are not banks. The term 'an authorised deposit-taking institution' is used to include, but not be limited to, banks. An enacting State should consider inserting the terminology that best reflected its domestic law.

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[78] *LG: We need to make sure that this sentence is consistent with what is in the digital annexe.

(iv) Proceeds of proceeds

156. The definition of 'proceeds' also includes 'proceeds of proceeds', which are anything falling within (i), (ii) or (iii) that is received in respect of proceeds. For example, the proceeds of a receivable could be paid in money (banknotes). The money is then paid into a bank account. The funds in the bank account are proceeds of proceeds. Or the proceeds of a receivable could be a negotiable instrument. The negotiable instrument is then paid in money (banknotes). The money would be proceeds of proceeds.[79]

157. It is possible, however, that something other than money, a negotiable instrument or funds in a bank account was received in respect of proceeds. For example, suppose funds in a bank account are received in respect of a receivable (R1), and those funds are used to purchase another receivable (R2). Since R2 is not within the definition of 'proceeds' it cannot be proceeds of proceeds, and the applicable law (including the terms of the transfer agreement) governs whether the transferee of R1 has rights in R2.

Article 2(g) — Receivable

(g) "Receivable" means a contractual right to payment of a monetary sum arising from one or more of the following:

(i) the supply or lease of goods or services;

(ii) the assignment or licence of intellectual property;

(iii) the provision or processing of data; or

(iv) the payment obligation for a credit card transaction.

If a receivable is refinanced or consolidated with other receivables, the resulting right to payment is also a receivable.

Comment:

158. The definition of 'receivable' is critical to the delineation of the scope of the MLF, since the MLF only applies to transfers of 'receivables'. In fact, the MLF's clarity in what constitutes a 'receivable' is one of the instrument's seven core concepts. The consequent need for clarity is why the definition of 'receivable' lists what is included as a 'receivable' rather than consisting of a general definition with exceptions. [As mentioned in the overview] the definition of 'receivable' is, very broadly speaking, limited to 'trade receivables', that is, receivables arising from the underlying contract between the creditor (the transferor TR) and the debtor (D).

159. A receivable is defined as a contractual right to payment. The definition therefore does not include rights to payment based on tort claims or tax debts or any other non-contractual receivables. The contract referred to in the phrase 'contractual right to payment' is the underlying contract, that is, the contract for the relevant performance set out in Art (g)(i) to (iv). For example, the contract referred to could be a contract for the supply of goods, or a contract for the provision of data. A 'contractual right to payment' does not refer to a negotiable instrument or a letter of credit. This is because rights to payment in such instruments are independent from the underlying contract. Thus, rights to payment under negotiable instruments and letter of credit, are not included in the MLF, and existing domestic law will continue to apply.

[79] *LG: I put this in as it is an illustration of the point made in paragraph 141.

160. The right to payment in the definition is of a 'monetary sum', that is the right is a right to payment denominated in money. As discussed in para 144 (WG2(2)) above, a State may want to define 'money' in accordance with domestic law. However, in relation to art 2(g) it is the denomination that is important; a payment denominated in 'money' can be made in ways other than a transfer of money, such as by a transfer of funds from one account to another.

161. The sub-paragraphs (i) to (iv) set out the subject matter of the underlying contracts, the receivables arising from which are included within the definition of 'receivable'. These sub-paragraphs are not mutually exclusive: it is possible that a contract could fall into more than one category. This does not matter; as long as the contract falls into one or more categories, the MLF applies to transfers of receivables arising from such a contract. This approach is particularly important because of the increasing use of 'bundled' contracts that include different categories in one contract. For example, a contract could include the supply of goods (eg computing equipment), a license of intellectual property and the provision of data. This approach also has the result that the categories do not need to be treated as precise (and discrete) definitions. For example, it can sometimes be difficult to determine whether a contract is for services or for the provision or processing of data. However, under this approach the distinction does not need to be made.

162. The counter-party to the underlying contract can be anyone, whether a private person or entity or a public authority. The definition of 'receivable' therefore includes debts owed by public authorities, but, as discussed in paragraph 128 (WG2(2), there may be statutory restrictions on the transfer of receivables arising from certain contracts with public authorities. Such restrictions would fall within Art 1(3).

163. The following paragraphs discuss the various categories in sub-paragraphs (i) to (iv).

(i) The supply or lease of goods or services

164. In relation to goods, 'supply' includes sales and also any other type of supply possible under domestic law, such as under a license or a type of rental agreement that would not fall within the term 'lease' under national law. 'Services' is a wide term, but it does not include financial arrangements such as loans and derivative contracts that are, colloquially and sometimes under regulatory law, referred to as 'financial services.' Transfers of receivables arising from such arrangements (while common in some markets) are not covered by the MLF, and therefore are governed by applicable law. This is in order not to encroach on financial markets law. Netting agreements, foreign exchange transactions and inter-bank payments are also not included in the MLF. However, receivables arising from the provision of services by financial advisers are included.

165. The definition of receivables does not include receivables arising from contracts for the sale or lease of real estate. This is because of the difficulties of coordinating such an inclusion with the domestic law of real estate and also because such receivables are rarely factored. However, receivables from contracts for services, such as construction contracts, are included.

(ii) The assignment or license of intellectual property

166. Here, 'intellectual property' has a wide meaning and includes copyright, trademarks, geographical indications , industrial designs, patents, topographies of integrated circuits and trade secrets. What counts as 'intellectual property' in the enacting State will be a matter of the applicable law. As appears from the text of art 2(g), receivables arising from an assignment of intellectual property and from a license in relation to intellectual property are included in the definition.

(iii) The provision or processing of data

167. Data is not defined in the MLF, [but is generally speaking described as [ ][80]. The term 'provision' of data is intended to be wider than just including supply of data. However, the phrase 'provision or processing of data' is not intended to include contracts for the supply of digital assets, that is, electronic records that are capable of factual control (See Part IV Annexe A paragraph [XXX].

(iv) Payment obligation for a credit card transaction

168. The definition includes both (a) receivables owed by credit card users to the credit card issuer and (b) receivables owed by the credit card issuer to the merchant. The latter type of receivables are short-term and very rarely factored. The former are typically only settled after a month or more, and so are often the subject of factoring.

(v) Refinancing and consolidation of receivables

169. The definition of 'receivable' also includes a right to payment resulting from the refinancing of a receivable or its consolidation with other receivables. 'Refinancing of a receivable' refers to a situation where a debtor D owes a receivable to a creditor TR. D and TR might agree to replace that receivable (R1) with another receivable (R2), on different terms. The inclusion of the right to payment of a receivable resulting from refinancing in the definition of 'receivable' removes any doubt whether R2 (as a new receivable replacing RI, the previous receivable) falls within the definition of 'receivable'. R2 clearly does fall within that definition. 'Consolidation with other receivables' refers to the situation where D owes several receivables to TR, and they agree that these receivables are replaced by one receivable (R2). Again, R2 falls within the definition of receivable.

Article 2(h) — Registry

(h) "Registry" means the registration system for this Law established by [the enacting State to specify the relevant authority].

Comment:

170. When implementing the MLF, the enacting State needs to establish a registration system, in which notices can be registered and which can be searched, in accordance with the rules set out in Annexe A. This registry will need to be established by an authority within a State, and it is for the enacting State to specify the relevant authority in the definition of 'registry'.

Article 2(i) — security transfer

(i) "Security transfer" means:

[(i) enacting State to list any transactions already regarded by domestic law as security transfers; and]

(ii) any [other] transfer of a receivable by agreement, or creation of a right in a receivable by agreement, to secure payment or other performance of an obligation, regardless of the way in

[80] *LG: After WG2 NC was going to provide some wording from the ELI principles to add here, But we could just say that data is not defined.

which the parties have described the transaction, the status of the transferor or the transferee or the nature of the secured obligation.

Comment:

171. The definition of 'transfer' (which is discussed in paragraphs 163 – 171 (WG2(2)) includes a 'security transfer'. The term 'security transfer' is intended to include anything which under a State's law is any of the following: a security assignment, any other type of security right created by the grantor and any other transactions that have the function of security. Art 2(i)(ii) reflects this functional approach, that is, that a security transfer is any transaction which has the function of security regardless of how the parties describe it. Art 2(i)(ii) is the primary way of defining 'security transfer' under the MLF. However, a State might prefer to add to this functional definition, by listing, in a separate paragraph (Art 2 (i)(i)), transactions which are regarded as security assignments or as creating security rights under its law[81] [(such as a charge or a pledge)]. Art (i)(i) is therefore in square brackets and optional.

Article 2(j) — transfer

(j) "Transfer" of a receivable means:

(i) an outright transfer of the receivable by agreement; and

(ii) a security transfer of the receivable.

Where the context requires, "transfer" also means the rights of a transferee arising from a transfer.

Comment:

172. The term 'transfer' includes both an outright transfer and a security transfer. The reasons security transfers were included in this definition, and therefore within the scope of application of the MLF, are discussed in paragraphs 123 to 128 (WG2(2)) above.

173. The word 'transfer' was chosen for use in the MLF rather than another word, such as 'assignment'. In some States the two words will mean the same but in others 'transfer' is wider and, for example, includes novation (the creation of a new contract). While, if implementing States use the more neutral word 'transfer' in the law implementing the MLF there will be the benefit of consistency between States, it is ultimately up to an enacting State to choose the most appropriate word to fit with its domestic law, bearing in mind that the word 'transfer' could also be used for transfers that do not fall within the scope of the MLF.

174. While the focus of the MLF is on outright transfers made for financing purposes, the MLF includes outright transfers made for other purposes, for example, a transfer of receivables on the sale of a business or a transfer of receivables for collection. This is so that the same priority rule applies to all types of outright transfers, and brings the same benefits as those discussed in paragraph 125(WG2(2)) above. Inclusion of these non-financing transfers also means that the MLF provides a legal framework facilitating these types of transfers.

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81 *LG: I think it is important to make it clear that security rights as well as security assignments can be listed under (i), despite the word in the MLF. Is the wording clear enough without examples? Or would it be useful to give examples as in square brackets (charge is a common law example and pledge ie a non-possessory pledge is a civil law one).

175. A transfer (outright or security) includes the transfer of part of or an undivided interest in a receivable (Art 5(4)(a)). The details in this regard are discussed in paragraph [Part IV(II) paras XXX Article 5] below.

176. The definition of 'transfer' expressly includes the rights of a transferee arising from a transfer because, in the rules in the MLF relating to priority (Arts 13 to 19), this reading is necessary to make sense of the provisions. In those rules, 'transfer' refers to the rights of a transferee, since it is those rights that are in competition with the rights of another (competing) transferee. Thus, for example, if TR made a security transfer of a receivable to TE1 and then made an outright transfer of the same receivable to TE2, TE1's rights in the receivable arising from the security transfer are in competition to those of TE2 arising from the outright transfer.[82]

Article 2(k) — Transfer agreement

> **(k) "Transfer agreement" means an agreement providing for the transfer of a receivable.**

Comment:

177. A transfer agreement is an agreement between a transferor and a transferee for the transfer of a receivable. It is also possible that there could be multiple parties on either side of the agreement. For example, there could be multiple transferors in a single agreement, where the transferors are all part of the same corporate group.[83] A transfer agreement could be contained in one single instrument or document, or more than one instrument or document. Examples of the latter are included in section I(2) above.[84]

178. A debtor will not usually be party to a transfer agreement. However, in some types of factoring (for example, reverse factoring) a debtor may be party to a separate, but related, agreement with a transferee. This will not be a transfer agreement as defined in Art 2(k). Moreover, in some circumstances there may be an agreement between transferees setting out their respective priority. This is also not a transfer agreement.

179. A transfer agreement has the effect of transferring a receivable falling within its scope in the circumstances set out in Art 5. Subject to the requirements set out in Art 5, the question of whether a transfer agreement is an enforceable contract and its interpretation is governed by the applicable domestic law of contract ([see <Part II(1). The scope and content of a transfer agreement will depend on its context and what the parties agree. For example, in some circumstances it could be an agreement for the transfer of a single, present, receivable, while, in other circumstances, it could be an agreement for the transfer of many receivables, described generically, both present and future (see I(2) and annexe).

180. The default set of rights and obligations between the transferor and the transferee set out in Chapter VI Section 1 of the MLF are, unless varied by the parties, included in a transfer agreement

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[82] *LG: I was asked to give examples of where this extended meaning of 'transfer' is important. The only ones I could think of were the priority rules so I have redrafted just to refer to those. If anyone can think of other rules (I haven't really thought about transition or conflict of law rules, NC) them I could add those in.

[83] *LG: This example could refer to a more detailed example in section I(2) above (description of factoring).

[84] *LG: The WG suggested that there could be a description in section I(2) of the structure (quite usual in North America and UK) consisting of a master agreement and then separate documents identifying receivables to be transferred, and this paragraph could refer to that description.

and can be varied by the transfer agreement. The transfer agreement may also set out other rights and obligations between the parties that are not included in the MLF.

Article 2(l) — Transferee

(l) "Transferee" means a person to whom or in whose favour a receivable is transferred.

Comment:

181. The transferee is the recipient of the receivable under the transfer agreement. The words 'in whose favour' are included to cover security transfers since the definition of 'security transfer' includes transactions which are not [transfers][assignments][85] under domestic law, but which consist of the creation of a security right (see paragraph 167 (WG2(2)).

Article 2(m) — Transferor

(m) "Transferor" means a person who transfers a receivable.

Comment:

182. The transferor of a receivable is the person who transfers it. A person is a 'transferor' under the MLF if it enters into a transfer agreement in relation to a future receivable, even though the receivable is not actually transferred until it arises and until the transferor has rights in or the power to transfer it (Art 5(5)).

Article 3 — Party autonomy

1. With the exception of Articles 4, 5, 7(2), 8, 32(3), 36(1) and 37 to 46, the provisions of this Law may be derogated from or varied by agreement.

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.

Comment:

183. Parties can vary or derogate most of the provisions of the MLF by agreement, meaning that those provisions are default rules. There are, however, two very significant exceptions to this. First, the provisions which cannot be varied or derogated from are listed in Art 3(1). Second, an agreement to vary or derogate cannot affect the rights or obligations of any third party. These two exceptions are discussed below.

184. An example of derogation from a 'default rule' in the MLF is where the transferor and the transferee agree that the transferor does not make one or more of the representations set out in Art 21(1). One example of variation from the MLF 'default rules' is where the parties agree that the transferor represents that the debtor has, and will have, the ability to pay: this varies the representation otherwise made by the transferor in Art 21(2). Another example of variation of a

85 *LG: I'm not sure which word is best here.

'default rule' in the MLF is where the transferor and transferee agree that the transferee will not send a notification or payment instruction to the debtor until one of a list of specified events has occurred, which varies Art 22(1).[86] However, under Art 22(2) a notification or payment instruction sent in breach of such an agreement will not be ineffective against the debtor for the purposes of Art 26, which sets out the circumstances in which payment will discharge a debtor. This is an example of the limits on variation or derogation discussed below in paragraph 182 (WG2(2)).

185. Art 3(1) lists certain mandatory rules in the MLF which are there for the general protection of all parties and the smooth functioning of the legal regime and which cannot be modified by the parties. Thus, for example, the general standards of conduct in Art 4 cannot be varied or derogated from, nor can the formal and other requirements for the transfer of a receivable in Art 5. The override of contractual limitations on transfer in Art 8, which is critical for access to finance, cannot be varied or excluded and nor can the conflict of laws rules in chapter VIII. Of course, in addition, the parties cannot derogate from a State's transitional rules, set out in chapter IX nor the registry provisions in Annexe A. Moreover, the rules protecting a debtor on enforcement set out in chapter VII part 2 cannot be waived or varied by one or both parties before default (Art 32(3)).

186. Art 3(2) provides that any derogation from or variation of the legal provisions by party agreement cannot affect the rights and obligations of any third parties. Art 7(2) (which is listed in Art 3(1) is an example of this rule in a particular context and cannot itself be waived or derogated from by agreement. However, art 3(2) also applies to many of the MLF rules in a more general context. For example, parties cannot agree that a transfer is effective against third parties by a method other than by registering a notice in the MLF registry (art 9) since this agreement would potentially affect all persons other than the parties to the agreement.

Article 4 — General standards of conduct

A person must exercise its rights and perform its obligations under this Law in good faith and in a commercially reasonable manner.

Comment:

187. Art 4 applies to the exercise of rights and performance of obligations throughout the MLF, although it has particular resonance in relation to Chapter VII (on collection and enforcement). It refers to both good faith and commercial reasonableness. The precise contours of the concept of good faith varies between jurisdictions. The MLF does not define good faith, which is determined under the applicable law, while commercial reasonableness will vary according to the relevant markets.[87]

188. The effect of Art 4 is that things that may or must be done by a party under the MLF may or must be done in a commercially reasonable manner. A specific example is that when an outright transferee is enforcing its right to collect the receivable under Art 31(1), it must do so in a commercially reasonable manner, and must not make undue threats or seek to intimidate the debtor. Another example is that where a security transferee sells a receivable under Art 34 it would have to do so in a commercially reasonable manner, such as by selling it on a recognised market, or, if sold privately, by obtaining an objectively reasonable price.

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86 *LG: I would like to keep this example in as well as the representation example, as it is an example of an actual rule being varied rather than just a deemed representation.

87 *LG: his as suggested by BW at WG2: I hope that this captures the idea (paragraph 693 of the recording)

CHAPTER II – TRANSFER OF A RECEIVABLE

189. This chapter deals with the transfer of a receivable, which takes effect by a transfer agreement if certain conditions are satisfied, in which case the receivable is transferred as between the transferor and the transferee. In order for the transfer to be effective against third parties, the additional step of registration of a notice (Art 9) has to be taken. This chapter also sets out the additional rights a transferee of a receivable has in the proceeds of that receivable and in any rights securing or supporting the receivable. Importantly, from the aspect of access to finance, it includes an override of contractual limitations on transfer.

Article 5 — Requirements for the transfer of a receivable

1. A receivable may be transferred by a transfer agreement if the transferor has rights in the receivable or the power to transfer it.

2. A transfer agreement is effective to transfer a receivable only if it:

(a) is in writing and signed by the transferor;

(b) identifies the transferor and the transferee; and

(c) describes the receivable in a manner that reasonably allows its identification.

3. A description of receivables in a transfer agreement is sufficient if it indicates that the receivables consist of all of the transferor's receivables, or all of the transferor's receivables within a generic category.

4. A transferor may transfer:

(a) a part of or an undivided interest in a receivable;

(b) a generic category of receivables; and

(c) all of its receivables.

5. A transfer agreement may provide for the transfer of a future receivable, but the transfer is effective only when the transferor acquires rights in the receivable or the power to transfer it.

Comment:

190. Art 5(1) makes it clear that an agreement between the transferor and the transferee is necessary to transfer a receivable. It is, however, not sufficient, as for a receivable to be transferred the transferor has to have either rights in the receivable or the power to transfer it. These two situations will be discussed separately in the following two paragraphs.

191. The first situation is where the transferor has rights in the receivable. As a matter of logic, and under what is usually the basic rule in most jurisdictions, a transferor will only be able to transfer rights in the receivable which it actually has (see below for where a transferor has the power to do more than this). Although, in theory, a transferor's rights in the receivable can be of any kind and extent, the most usual situation in the factoring context is where the transferor owns the receivable, that is, it is owed the receivable under a underlying contract (see definition of 'receivable') or is the transferee of the receivable under an outright transfer. In order for the transferor to have rights in a receivable, the receivable has to have arisen, that is, it must not be a future receivable in the sense of the first situation described in the definition of 'future receivable' (see paragraph 141 (WG2(2)) above).

192. The second situation is where the transferor has the power to transfer the receivable. This refers to the situation where a transferor does not have rights (or sufficient rights) in the receivable enabling it to effect a transfer as described in the previous paragraph, but, under an exception contained in the MLF to the basic rule described in the previous paragraph, it can nevertheless transfer the receivable so that the transferee obtains rights in the receivable, either at that moment or at a later date. One exception contained in the MLF to the basic rule described in the previous paragraph, arises by necessary implication from Art 13. This exception occurs where, under the priority rule in Art 13, a transfer by a transferor without rights in the receivable has priority over a transfer by a transferor with rights in the receivable. For example, if TR (the owner of a receivable) transferred the receivable outright to TE1 on Day 1 but TE1 did not register a notice in relation to the transfer until Day 20, and, in the meantime, TR transferred the receivable outright to TE2 on Day 5 and TE2 registered a notice on Day 10, TE2 would have priority over TE1, and therefore acquired rights in the receivable. Despite the fact that, at the time of the transfer to TE2, TR did not have any rights in the receivable, TR did, at that time, have the power to transfer it.

193. Another exception to the basic rule arises even if TE1 registers a notice before TE2 does so. This is through the operation of the registration provisions in the Annexe, which enable TE2 to obtain rights in the receivable if TE1's rights cease to be effective against third parties through failure to extend the period of effectiveness of the registration of its notice under Clause 12(2). Clause 12(1) states that a registration of a notice is effective for the time indicated in the designated field of the notice. Thus, on the expiry of that period of effectiveness, if not extended under Clause 12(2), the transfer to TE1 would become ineffective against third parties, and TE2's transfer (if registered) would be effective against third parties, including TE1. Thus, at that moment, TE2 acquires rights in the receivable, even though it had none before.[88]

194. [Another example of an exception to the basic rule that arises under the law of many jurisdictions is that of 'apparent authority'. This exception arises where a person (TR) represents to a transferee (TE) that they have authority from the owner of a receivable to make a transfer but they do not in fact that such authority; in this situation a transfer made by the TR to TE is an effective transfer. If this is the case under the applicable law, TR has the 'power to transfer'.[89]]

195. If, at the time of the transfer agreement, a transferor has rights in a receivable or the power to transfer it, the transfer takes place when the agreement is entered into, in the absence of any contrary intention. Where the transferor does not have rights in a receivable or the power to transfer it (including where the receivable has not yet arisen) the transfer takes place when it obtains these rights or the power. For further discussion see paragraph 198 (WG2(2) below.

196. Articles 5(2) and 5(3) set out the requirements for an effective transfer agreement, while article 5(4) sets out, for the purposes of clarification, some examples of what can be transferred under a transfer agreement.

197. Art 5(2)(a) includes minimal formal requirements, namely that the agreement should be in writing and signed by the transferee. This has the effect that a State's legal requirements are, typically, simplified on enactment of the MLF. This simplification of the legal requirements for the transfer or grant of security in receivables is one of the MLF's seven core concepts and is important to facilitate transactional efficiency (one of the MLF's policy objective). These simple requirements align with usual commercial practice in factoring transactions. A State's electronic commerce law will

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[88] *LG: These exceptions take the 'easy' case of outright transfers, which transfer all the rights in the receivable to the transferee. The position in relation to security transfers is more complicated (the transferor arguably retains some rights but can transfer more rights than it has). However, given that the chief focus is on factoring and outright transfers I suggest we don't give a long explanation of power to transfer in relation to security transfers. The point in para 189 is BW's point which is, I think, a good one.

[89] *LG: This is a placeholder mentioning apparent authority as requested by the WG. I would like to keep this in if possible as it is an example of a power to transfer that arises outside the MLF.

determine precisely what electronic documents count as 'writing' and what counts as an electronic 'signature' (see Part III(1) paragraph [XXX]. It is also simple to comply with the requirement in Art 5(2)(b) that the transferor and the transferee must be identified in the agreement.

198. The requirement in Art 5(2)(c) that the transferred receivables must be described so that they can reasonably be identified is important as it enables the subject matter of the transfer to be identified. This is important for certainty and also would provide proof of the transfer to a debtor (for example, in the context of proof provided under Art 26(7)) or anyone else that needs to know. One way of complying with Art 5(2)(c) is for an agreement to cover only one receivable, which is described in that agreement. Another way, where the agreement covers multiple receivables, is to describe each receivable individually. However, this is not the only manner of description that satisfies Art 5(2)(c). Instead, Art 5(3) makes it clear that the transferred receivables do not need to be individually identified, and gives two examples where receivables would be sufficiently identified : where the agreement says that it covers 'all of the transferor's receivables' and where it says that it covers all of the transferor's receivables within a generic category. An example of the latter would be 'all of my receivables arising from the sale of motor vehicles'. However, other similar descriptions would also be sufficient as they describe receivables in a way that reasonably allows them to be identified, and thus satisfies the requirement in Art 5(2)(c). Thus, for example, a transfer agreement that refers to 'all receivables that are purchased by [the transferee]' would be sufficient. It is important that an enacting State does not introduce descriptive requirements other than that set out in Art 5(2)(c) (with the clarification included in Art 5(3)) such as requiring the name of the debtor to be part of the description.

199. As mentioned above, Art 5(4) sets out some examples of what can be transferred under a transfer agreement. These examples are for clarification, and Art 5(4) is not an exhaustive list of what can be transferred. Art 5(3) describes how the categories of receivables included in Art 5(4)(b) and (c) can be identified in a transfer agreement in order to comply with the requirement in Art 5(2)(c).

200. Art 5(4)(b) and (c) clarify that a generic category of, or all of, the transferor's receivables can be transferred under a transfer agreement. On the basis that these greater categories include lesser categories, arts 5(4)(b) and (c) also permit the transfer of all of a transferor's receivables within a generic category other than a specific type of receivable, or all its receivables other than a specific category. In these situations, care would need to be taken by the parties to reasonably identify the transferred receivables in order to comply with the requirement of art 5(2)(c).

201. Art 5(4)(a) permits the transfer of a part of a receivable, or an undivided interest in a receivable. An example of 'part of' a receivable is where an invoice enumerated various sums for particular services but the resulting receivable related to all the enumerated services, the transferor could transfer the parts of the receivable relating to some of the enumerated services and not others. The transfer of an undivided interest in a receivable could be, for example, the transfer of half of a receivable, or the transfer of $500 out of a $1200 receivable.

202. Art 5(5) expressly states that, although a future receivable can be included within a transfer agreement, the transfer of that receivable does not take place until[90] the transferor has rights in the receivable or the power to transfer it (as discussed in paragraph 191 (WG2(2) above). While Art 5(5) expressly relates to a receivable that is a 'future receivable' in the second sense discussed in paragraph 144 (WG2(2)) above (because the transferor does not have rights in it or the power to transfer it), it is implicit in Art 5(5) that where a receivable is a 'future receivable' in the first sense discussed above (because the receivable has not yet arisen) the transfer of the receivable does not take place until the receivable arises. This is because it is only at that time that the transferor will

[90] *LG: Is this correct? Is this the effect of 'is not effective' in 5(5)?

acquire rights in the receivable or the power to transfer it. The time at which a receivable arises is a matter of applicable law.[91]

Article 6 — Proceeds

The right of the transferee of a receivable extends to its identifiable proceeds.

Comment:

203. Art 6 extends the right of a transferee in a receivable to its proceeds. 'Proceeds' are limited to 'proceeds' as defined in art 2(f), that is, cash proceeds.

204. For the transferee's right to extend to the proceeds, the proceeds must be identifiable. This requirement is particularly important where the proceeds consist of funds in a bank account which also contains other funds, although it could also apply to other types of cash proceeds. The applicable law relating to how rights are determined in commingled assets would normally govern whether the proceeds are identifiable.

Article 7 — Personal or property rights securing or supporting payment of a receivable

1. 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 the transferee would have the benefit of that right 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.

2. A transferee has the benefit of a right under paragraph 1 notwithstanding any agreement between the transferor and the debtor or other person granting the right that secures or supports payment of the receivable that limits in any way the transferor's right to transfer the receivable or the ability of the transferee to have the benefit of that right.

Comment:

205. Art 7(1) applies where a receivable is supported or secured by a personal right (such as a guarantee or a right under a credit insurance agreement) or a property right (such as a security right). Broadly, it is intended that the transferee of the receivable (TE) obtains the benefit of that right.

[91] *LG: There was previously a paragraph here (as below). The WG said to move this but the substance is already in paragraph 218 below.

[For example, a manufacturing business TR that supplies a particular retailer D enters into a transfer agreement with TE1 on day 1 in relation to all its present and future receivables that are owed by D. A receivable (XR) relating to a supply contract X that had not been entered into on day 1 is a future receivable in the first sense. TE1 registers a notice in relation to the transfers in that transfer agreement on day 2. TR enters into a transfer agreement with TE2 including XR on day 5 and TE2 registers a notice in relation to the transfers in that transfer agreement on day 8. XR arises on day 20. The transfer is therefore effective against third parties from day 20 and, under the priority rule in art 13, the transfer of XR to TE1 has priority over that to TE2.]

206. However, Art 7(1) covers two situations: which of these applies in any specific case will depend on the applicable law. The first is where, under the applicable law, the benefit of the personal or property right can transfer to TE without a new act of transfer. This could be the case, for example, where the personal right was a right under a guarantee In that case, TE obtains the benefit under Art 7(1). The second is where the applicable law requires a new act of transfer for TE to obtain the benefit of the personal or property right, for example, this could be the case where the supporting right is a letter of credit.[92] In that case, the transferor is obliged to transfer that benefit to TE. It is likely that in many cases the transfer agreement would include an express obligation to that effect, and/or such an obligation would exist under existing domestic law in an enacting State (in which case coordination with the MLF would be required). Art 7(1), however, provides legal certainty in this regard.

207. Art 7(2) deals with two situations. The first is where there is an agreement between the transferor and the debtor limiting the transferor's right to transfer the receivable. Notwithstanding such a limitation, under Article 8 the transfer of the receivable is effective and Art 7(2) therefore provides that the transferee obtains the benefit of any personal or property right securing or supporting the receivable.

208. The second situation is where the receivable is secured or supported by a personal or property right, and there is an agreement between the transferor and the debtor, or between the transferor and the person who granted that right, limiting the ability of the transferee to have the benefit of the personal or property right. Notwithstanding this agreement, the transferee does obtain the benefit of the personal or property right under Art 7(1) and (2).

Article 8 — Contractual limitations on the transfer of a receivable

1. A transfer of a receivable is effective notwithstanding any agreement between the debtor and a transferor limiting in any way a transferor's right to transfer the receivable.

2. Neither a transferor nor a transferee is liable for breach of an agreement referred to in paragraph 1, and the debtor may not avoid the contract giving rise to the receivable on the sole ground of the breach. A person that is not a party to an 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.

Comment:

209. Underlying Contracts (that is, the types of contract from which 'receivables' as defined in the MLF result) not infrequently include a contractual term prohibiting transfer of any resulting receivable or limiting transfer to specific situations, such as where the debtor consents to the transfer. Art 8(1) provides that notwithstanding such a term, a transfer of a receivable arising from such a contract is effective. The term prohibiting or limiting transfer is therefore rendered ineffective. The reason for including such a provision in the MLF is that it greatly facilitates factoring. First, it increases the number and amount of transferable receivables that can be factored, and therefore increases the availability of credit using factoring transactions. Second, it removes any uncertainty about the legal effect of prohibitions or limits on transfer, thus potentially reducing the transaction costs of factoring. Third, it obviates the need for a potential financier to look at all the underlying contracts giving rise

[92] *LG: I think this reflects the discussion at WG2, but I would be grateful if people could check that it is correct. A letter of credit is a personal and not a property right. Does it require a new act of transfer? MDE says not always, hence 'this could be the case'

to the receivables offered for factoring to discover if any contracts include a prohibition or a limit on transfer, which could have an adverse effect on the costs of factoring generally. Fourth, it obviates any need for a financier to negotiate with the contractual counterparty for a waiver of any prohibition or limit included in the underlying contract.

210. An example of the operation of Art 8(1) is as follows. If a contract (X) between TR (a seller) and D (a buyer) for the supply of 1 tonne of potatoes contained a term (Y) prohibiting the transfer of the receivable arising from that contract, TR could still transfer the receivable to TE1 under the MLF. As discussed above in the previous paragraph, the rule in Art 8 is likely to greatly increase access to credit. Because of its importance, Art 8 cannot be derogated from or varied by the parties (Art 3(1)).

211. Art 8(1) is limited to agreements between the debtor and a transferor. Thus, in the example in the previous paragraph, if the TR had agreed with another person (for example, a bank lender) that TR would not transfer any of its receivables, that agreement would not fall within Art 8(1). Instead, other law would determine the effect of that agreement on the transfer to TE. However, this limited scope in Art 8(1) includes any agreement with 'a' transferor, and is not limited to an agreement with the initial transferor (that is, to the party to the underlying contract X). Thus, if D made an agreement with TE limiting the transfer of the receivable, any transfer by TE1 to TE2 would nevertheless be effective. Art 8(1) is drafted in this way to broaden its effect, given its beneficial impact on access to credit.

212. Art 8(2) has the effect that the term in the contract between the debtor and a transferor is entirely ineffective, and that, broadly, no action in respect of its breach can be taken against anyone. The benefit of Art 8(2) specifically covers 'a transferor' (that is, TR but also a subsequent transferor other than TR, for example, TE1 when it transfers to TE2) and 'a transferee' (TE1 and also TE2). Thus, in the example above, D cannot sue TR (who is a 'party to the agreement') for damages from breach of term Y and cannot avoid the agreement on the grounds that the transfer was made in breach of term Y. Nor is TE1 liable in relation to the breach of term Y, for example, under a tort liability for inducing breach of the term.

213. Art 8(2) also benefits 'any other person who is not a party to the agreement', in the sense that such persons are not liable for a transferor's breach on the sole ground of knowledge of the agreement. This protection covers any person who knew about the agreement (term Y) and was in some way involved in the transfer from TR to TE1 (for example, by inducing TR to transfer the receivable to TE1).

214. The text of the MLF involves the deliberate choice for Art 8(2) to render a limiting term entirely ineffective rather than permitting a debtor to sue the transferor or the transferee for breach of the term (but not avoid the underlying contract) as is found in some other national laws and the MLST Art 13(2).

215. There are a number of reasons for this choice. First, rendering the limiting term entirely ineffective further facilitates the aim of increasing access to credit by factoring. Second, preservation of the right to sue the transferor for breach of the limiting term could cause legal uncertainty [which could have a chilling effect on factoring]. Third, given the provisions in Chapter VI Part 2 of the MLF for the protection of the debtor, the debtor is very unlikely to suffer any pecuniary loss as a result of the breach of the limiting term, since most of its rights and obligations remain the same despite a transfer of the receivable (Art 24(1). Even where the debtor's obligations are changed by the transfer (for example, after notification of the transfer and a payment instruction to pay the transferee) changes which could result in the debtor incurring costs cannot be made without the debtor's consent. Thus, under Art 24(2), the currency of payment cannot be changed without the consent of the debtor, nor can the debtor be obliged to pay in a State other than where that debtor is located without its

consent. [For these reasons, the complete override of anti-assignment clauses is one of the MLF's seven core concepts.][93]

216. Art 8 only applies to contractual prohibitions or limits on transfer of receivables. Statutory prohibitions or limits on transfer are dealt with in Art 1(3), see paragraph 133 (WG2(2) above.

[93] *Secretariat: whether to include this additional sentence will depend on whether the WG confirms this as one of the core concepts in Part I(3).

CHAPTER III – EFFECTIVENESS AGAINST THIRD PARTIES OF A TRANSFER OF A RECEIVABLE

217. This section deals with the effectiveness of a transfer of a receivable against third parties. If the conditions set out in Art 5 are satisfied, the receivable is transferred as between the transferor and the transferee, but in order for the transfer to be effective against third parties, the additional step of registration (Art 9) has to be taken. The order of registration under Art 9 determines the order of priority between competing transfers (Art 13) whether transfers are made before or after registration.

Article 9 — Registration

A transfer of a receivable is effective against third parties only if a notice with respect to the transfer is registered in the Registry.

Comment:

218. Art 9 provides that the only way of making a transfer of a receivable effective against third parties is to register a notice with respect to it. Other methods of third party effectiveness that may exist in a enacting State, such as the giving of notice to a debtor, do not apply under the MLF and any law providing for such methods must therefore be repealed. For transitional provisions, see Arts 51 and 52.

219. The rules as to registration are set out in Annexe A. Clause 4 of Annexe A makes it clear that a notice can be registered before the transfer agreement is entered into or before the transfer is made, It also makes it clear that a registered notice can cover the transfer of future receivables.

220. A transfer will only be effective against third parties if the transfer agreement relating to it complies with the requirements in Art 5(2), so that the transfer agreement is effective to transfer receivables included in it. Moreover, the transfer of a receivable must have taken place for it to be effective against third parties. See [paragraphs 191 and 198 (WG2(2): 5(1) and 5(5)] for discussion of when the transfer of a receivable takes place.

221. The following example relates to a present receivable. Take, for example, a receivable arising out of an underlying contract between TR and D. TR and TE enter into a transfer agreement including that receivable on Day 10, and (on the assumption that by then TR has rights in the receivable) the transfer of the receivable occurs on Day 10. If a notice relating to this transfer had been registered on Day 1, the transfer would only become effective against third parties on Day 10. If, however, a notice relating to a transfer is not registered until Day 20, the transfer is only effective against third parties from Day 20.

222. This example relates to a future receivable. Consider the situation where on Day 10 TR did not have rights in, or the power to transfer, a receivable referred to in the transfer agreement entered into between TR and TE on Day 10. Here, even though a notice relating to this transfer was registered on Day 1, the transfer would not be effective against third parties until TR obtained rights in that receivable, for example on Day 15. If, however, the notice relating to that transfer is not registered until Day 20, the transfer is only effective against third parties from Day 20. For further discussion of the transfer of future receivables see [paragraphs 141 – 144 and 192 and 198 (WG2(2)].

223. The third parties against whom a transfer becomes effective include any insolvency representative of the transferor if insolvency proceedings are commenced against the transferor (Art 15).

224. The purpose of registration is to give public notice of a transfer (or the possibility that a transfer has taken or will take place) [see Part IV(Annexe A) paragraph XXX]. The information required in a registered notice is quite limited, and receivables can be described generically (Clause 7 Annexe A). For these reasons, registration of a notice relating to a transfer is not notification to the debtor of that transfer (art 25), and for the rules in arts 25 – 29 to apply, a notification has to be sent to the debtor in accordance with those rules.

225. Moreover, a transfer has effect against a debtor by notification of the debtor, in the sense that the debtor is discharged only by paying the transferee or someone whom the transferee instructs the debtor to pay, (Art 26). It is possible for a transfer to have effect against a debtor in this way without a notice in respect of that transfer having been registered (in which case it would not be effective against 'third parties'). In this sense, then, the term 'third parties' in Art 9 does not include the debtor.

226. Conversely, it is possible for a transfer to be effective against third parties if a notice in respect of it has been registered even if the debtor has not been notified of the transfer. A transferee under a non-notification factoring agreement, therefore, can register a notice in respect of receivables without identifying the debtors, since identification of debtors is not required by clause 10 of Annexe A which deals with the description of the receivables in a registered notice. [Moreover, an enacting State may choose (under clause 8 of Annexe A) for the identifier of the transferor in a registered notice to be by an identification number rather than the name of the transferor.][94]

Article 10 — Proceeds

If a transfer of a receivable is effective against third parties, the transferee's right to any proceeds of that receivable under Article 6 is also effective against third parties.

Comment:

227. Art 10 operates in tandem with art 6, which provides that a transferee of a receivable obtains rights in the proceeds of that receivable. 'Proceeds' as defined in art 2(f) are cash proceeds. Under Art 10, the third party effectiveness of the transfer also applies to the proceeds of the transferred receivable. There is no need to register a notice in relation to proceeds and any attempt to cover proceeds in a notice will have no effect, since the transferee's right in relation to the proceeds is already effective against third parties due to the wording of Article 10. that .

[94] *LG: I have left this in but in square brackets but it is likely to come out depending on what is said in the commentary to clause 8 of Annexe A.

Article 11 — Continuity in third-party effectiveness upon the relocation of the transferor to this State

1. If a transfer is effective against third parties under the law of another State and the transferor relocates to this State, the transfer remains effective against third parties under this Law if it is made effective against third parties in accordance with this Law before the earlier of:

(a) the time when third-party effectiveness would have lapsed under the law of the other State; and

(b) the expiry of [the enacting State to specify a short period of time] after the transferor relocates to this State.

2. If a transfer continues to be effective against third parties under paragraph 1, the time of third-party effectiveness under this Law is the time when it was achieved under the law of the other State.

3. Subject to paragraph 4, the time of third-party effectiveness under this Law of a transfer that continues to be effective against third parties under paragraph 1 is the time to be used for the purposes of applying the priority rules of this Law that refer to the time of registration of a notice relating to a transfer.

4. If a transfer that continues to be effective against third parties under paragraph 1 was made effective against third parties under the law of the other State by the registration of a notice, the time of registration under that law is the time to be used for the purpose of applying the priority rules of this Law that refer to the time of registration of a notice relating to a transfer.

Comment:

228. Art 11 provides detailed rules for inclusion by an enacting State B for the situation where a transferor locates from State A to State B. Under Art 37, the law applicable to the third party effectiveness of a transfer of a receivable is the law of State in which the transferor is located, so if transferor TR moves from State A to State B, the applicable law after that move is the law of State B, that is, the MLF. Art 11 provides a type of transition rule which seeks to preserve a balance between protecting settled expectations of already accrued rights while enabling the benefits of the law in State B to apply as soon as possible. In that way, it has a much in common with the transition rule in Art 52.

229. Art 11 relates to a transfer (in this example, from TR to TE1) that was made effective against third parties under the law of State A (in this example, on Day 1) before TR relocated to State B (in this example, on Day 30). That transfer remains effective against third parties if a notice in respect of it is registered in the State B's MLF registry before the earlier of two dates, which are described in the next paragraph.

230. The first date is that on which third-party effectiveness would have lapsed under the law of State A (let us assume Day 60). The second date is the end of a period of time after the relocation of the transferor (the 'grace period'). The enacting State (State B) must specify that period when implementing Art 11 of the MLF (let us assume that State B has specified 15 days, so the relevant date is Day 45). The transfer therefore remains effective against third parties if it is made effective against third parties under the MLF (that is, that a notice is registered in State B's MLF registry) before Day 45. Let us assume it does so on Day 40.

231. The purpose of Art 11(1) is therefore to protect TE1's settled expectations of third-party effectiveness under the law of State A as long as TE1 takes steps to protect itself under the law of State B (the MLF) within an ascertainable, and reasonably short, period of time. The period of time has to be reasonably short since until TE1 registers in State B's MLF registry, other people in State B who search the MLF registry using TR's identifier will not find out about the transfer to TE1. The shortness of the time period provides a balance between the settled expectations of TE1 and the benefits of State B's law as mentioned above.[95]

232. Art 11(2) concerns the time from which third party effectiveness dates if the transfer remains effective against third parties by the operation of Art 11(1). That time is the time when third-party effectiveness was achieved in State A (in the above example this is Day 1).

233. Art 11(3) and (4) concern the application of the priority rule in Art 13 to the situation where a transferor relocates. Under Art 13 priority between two transfers depends on the order in which a notice in relation to each transfer is registered in the MLF Registry. Thus, a comparison has to take place between the date on which such a notice was registered in the MLF Registry with respect to each transfer. In the example, assume that TR transfers the receivable to TE2 on Day 32 and TE2 registers a notice in respect of that transfer on Day 35. Applying the comparison in Art 13 to the example, TE2 would have priority, since its notice was registered on Day 35 while TE1's notice was registered on Day 40.

234. However, this conclusion is inappropriate here, since TE1 has registered within the grace period, and therefore its transfer is continuously effective against third parties from the time it became so under the law of State A (Day 1). Art 11(3) therefore has the effect that, for the pre-relocation transfer, the relevant date for priority under Art 13 is the time the transfer became effective against third parties under the law of the other State (State A in the example). Thus, in the example, the relevant date for TE1's transfer for the comparison under Art 13 would be Day 1, so that TE1 would have priority over TE2 because Day 1 is before Day 35.

235. Art 11(3) is subject to 11(4), however. Under Art 11(4), if a transfer is made effective against third parties by registering a notice under the law of the other State, the date of registering that notice would be the date for the comparison under Art 13. Thus, in the example, if State A had a system whereby transfers could be made effective against third parties by the registration of a notice, and TE1 had made the transfer effective against third parties by registering such a notice on Day 1, TE1 would have priority over TE2 as above.[96] For the purposes of Art 11(4), the transfer was made effective against third parties under the law of the other State (State A) by registration even if, as is the case under the MLF, in a transaction in which a notice is registered before the transfer is made, the transfer is not effective against third parties until it is made.

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[95] *LG: Should we make any suggestion as to what is a reasonable amount of time for a State to specify?

[96] *LG: I have stolen a sentence from NC's commentary to Art 52(6) to add to the end of here. I am still not entirely happy about it, in the sense that (technically) it should say 'the transfer is deemed to have been made effective against TPs by registration etc etc" but that is probably far too nit-picky, and solved by the 'For the purposes of Art 11(4)".

CHAPTER IV – THE REGISTRY SYSTEM

Article 12 — The Registry

The rules relating to registrations and searches in the Registry are set out in Annexe A.

Comment:

236. The establishment of a registry for the registration of a public notice in order to achieve third party effectiveness and priority of a transfer is one of the MLF's seven core concepts. The MLF contains a comprehensive set of rules for the establishment and operation of a registry in Annexe A. These are in a separate annexe to give a enacting State the choice as to whether to incorporate them into the legislation enacting the Model Law, or whether to enact them separately, perhaps by incorporating them into legislation relating to an existing registry system.[97] However, the rules in Annexe A are intended to come into effect simultaneously with the coming into effect of the MLF, as the MLF cannot operate without a functioning registry and the necessary rules to govern it.

[97] *LG: This may need adjustment depending on what is put in the introduction to the commentary on the registry provisions.

CHAPTER V – PRIORITY OF A TRANSFER

237. This chapter deals with priority issues in relation to transfers. The word 'transfer' is used throughout the chapter, but in this chapter 'transfer' usually means 'rights of a transferee arising from a transfer' since it is the rights that are competing rather than the process of transfer (see paragraph [170] (WG2(2) definition of 'transfer' art 2(j))

Article 13 — Competing transfers

1. Priority between competing transfers is determined by the order of registration of the notices relating to those transfers.

2. Paragraph 1 applies whether the transferred receivable arises or is acquired by the transferor before or after the time of registration of the notices relating to those transfers.

3. Subject to Article 17, the priority of a security transfer extends to all obligations secured by the transfer, including obligations incurred after the transfer became effective against third parties.

Comment:

238. There is only one priority rule applicable to competing transfers of receivables under the MLF: the 'first to register' rule established in Art 13. This is an essential element of the MLF; the registration of a public notice in order to achieve third party effectiveness and priority of a transfer is one of the instrument's seven core concepts. Any other priority rules in relation to competing transfers that previously existed in the law of an enacting State will need to be repealed. For transitional provisions, see Arts 52 and 53.

239. The effect of the rule in Art 13 is that, when there are competing transfers, the one in respect of which a notice is first registered in the MLF Registry, has priority over the one in respect of which a notice is registered second. The second to be registered, in turn, has priority over the third and so on.

240. Since a notice can be registered in respect of a transfer before that transfer actually takes place (clause 4 Annexe A), the rule in Art 13 can operate as an exception to the basic rule referred to in paragraph 186 (WG2(2)) (art 5(1) commentary). This exception arises where the order of registration is different to the order of the transfers. For example, assume that TR makes an outright transfer of a receivable to TE1 on Day 1 but TE1 does not register a notice in relation to the transfer until Day 20. In the meantime, TR makes an outright transfer of the receivable to TE2 on Day 5 and TE2 registers a notice on Day 10. Here, TE2 has priority over TE1 because TE2's transfer is the first in respect of which a notice was registered. However, when TR makes the transfer to TE2, TR has no rights in the receivable (and so has nothing to transfer to TE2). The effect of the priority rule in Art 13 is that TE2 receives more rights than TR had to give. This means that, at the time of the transfer to TE2, TR has the power to transfer the receivable (see Art 5(1)).

241. Further, Art 13(2) makes it clear that it is possible for a registered notice to cover transfers of future receivables (Art 13(2)). Art 13(2) expressly covers future receivables in both senses discussed in [paras 134 – 138 (WG2(2)) commentary to Art 2(d)]. When a receivable included in an otherwise effective transfer agreement is a future receivable because it has not yet arisen (the first sense), its transfer takes place when it arises. However, the priority of transfers will depend on the date of the registration of relevant notices rather than the date the actual transfer of the future receivable takes place. For example, TR enters into a transfer agreement on Day 1 with TE1 in respect

of a receivable that had not yet arisen. TE1 does not register a notice in relation to the transfer until Day 20. In the meantime, TR enters into a transfer agreement on Day 5 with TE2 in respect of the same future receivable and TE2 registers a notice on Day 10. The future receivable actually arises on Day 30, at which time both transfers take place. Here, TE2 would have priority over TE1 because TE2's transfer was the first in respect of which a notice was registered.

242. When a receivable included in an otherwise effective transfer agreement is a future receivable because it has not yet been acquired by the transferor (the second sense), its transfer takes place when the transferor acquires it (Art 5(5)). However, the priority of transfers will depend on the date of the registration of relevant notices rather than the date the actual transfer of the future receivable takes place. For example, TR enters into a transfer agreement on Day 1 with TE1 in respect of a receivable that TR has not yet acquired, but TE1 does not register a notice in relation to the transfer until Day 20. In the meantime, TR enters into a transfer agreement on Day 5 with TE2 in respect of the same future receivable and TE2 registers a notice on Day 10. TR acquires the future receivable on Day 30, at which time both transfers take place. Here, TE2 would have priority over TE1 because TE's transfer was the first in respect of which a notice was registered.[98]

243. The priority rule in Art 13 applies to all transfers, whether they are outright transfers or security transfers. Where the competing transfers are both security transfers, the priority rules determines the order in which each transferee recovers, on enforcement, from the proceeds of the enforcement (for the distribution of proceeds of enforcement, see Art 35). How much each transferee recovers will depend on the amount of the proceeds of the enforcement and the amount of the obligations secured. Art 13(3) makes it clear that the priority of a security transfer (as regards an outright transfer or as regards another security transfer) applies in relation to all secured obligations whenever they arise, even if they arise after the notice relating to the transfer is registered. In relation to the priority between a security transfer and the right of a judgment creditor, however, the rule is different, see paragraph [para 254 (WG2(2)) Art 17(2)].

244. Art 13 only applies to competing 'transfers', that is, transfers as defined in the MLF. Thus, it applies where there are two competing outright transfers (see para 129(a) and para 235 (WG 2(2)), or two competing security transfers (see para 129(b) and para 238 (WG2(2)) or where an outright transfer competes with a security transfer. However, a person could have rights in a receivable through a means other than transfer. One example is a judgment creditor (the priority rule is included in Art 17). Another example is where a receivable constitutes 'proceeds' of another asset, such as goods, under an applicable secured transactions law under which a security right in that other asset automatically extends to its proceeds. An enacting State whose secured transactions law has this effect will need to coordinate that law with the MLF.

Article 14 — Proceeds

The priority of a transfer extends to any proceeds to which the transferee has rights under Article 6.

Comment:[99]

245. Art 14 provides that the priority of a transfer extends to the proceeds of the transferred receivable. It is thus consistent with art 6, which extends the right of a transferee of a receivable to

[98] *LG: This is pretty much the same as the previous example except that it relates to a future receivable in the second sense. It seems to me that this point is difficult enough to warrant a slightly repetitive commentary, and the clarity could be lost if I try to combine the two senses of future receivables.

[99] *LG: I did not need to tweak the comment too much to include all the points made in the para from Art 6 commentary which the WG said to move here, as most of the points were already made in para 239 -242.

its proceeds, and art 10, which extends the third party effectiveness of a receivable to its proceeds. The extension of the priority of a transfer to its proceeds means that where there would have been competing transfers of a receivable, had the receivable not been paid, the priority of the competing claims to the proceeds of that receivable depends on the order of registration of notices in respect of the transfers of the receivable, in the same way as the order of registration of notices governs the priority of the transfers. A competition between two transferees of the receivable, however, is the only situation, however, where Art 13 will apply to a priority contest in relation to proceeds of a receivable.

246. Thus, the right of TE, a transferee, who has a right in proceeds because a receivable has been transferred to it (Art 6) and who has registered a notice in respect of the transfer (Art 9) may be in competition with the rights of other people in those proceeds which arise by other means. In that situation, the rights of those people will not have been made effective against third parties by registration in the MLF registry, but by some other means such as registration in another registry or control. Therefore, priority will not be determined by the rule in Art 13.

247. An example of the situation mentioned in the previous paragraph is where the right of TE in funds in TR's bank account (as proceeds of a receivable transferred by TR to TE) is in competition with a secured creditor C who has a security right in the funds in TR's bank account. C has registered its security right in the State's collateral registry. Other law will apply to the priority between TE's right and C's right. Under some secured transaction laws, the right of a person who has control of a bank account will have priority over the right of a person who has made its right effective against third parties by other means. TE might then want to take control of the bank account by means of a control agreement as well as registering a notice in the MLF registry in respect of the transfer to it.[100]

248. Although 'proceeds' are not specifically mentioned in Art 15, the right of a transferee in proceeds remains effective against third parties and keeps its previous priority if the transferor enters insolvency proceedings. This follows from Art 14, and the reasoning in Art 15 applies mutatis mutandis to proceeds.

Article 15 — Impact of the transferor's insolvency on the priority of a transfer

A transfer that is effective against third parties at the time of the commencement of insolvency proceedings in respect of the transferor remains effective against third parties and retains the priority it had before the commencement of the insolvency proceedings, unless another claim has priority pursuant to the applicable insolvency law.

Comment:

249. Art 15 confirms that the pre-insolvency third party effectiveness and priority of a transfer is retained after insolvency proceedings have commenced in relation to the transferor. This is a critically important provision, as it is the protection of the transferee in the transferor's insolvency that makes factoring attractive to financiers. Outside insolvency a financier could rely on its personal rights against its client, but within insolvency rights with third party effect are crucial.

250. [The term 'insolvency proceedings' is not defined in the MLF, and will need to be coordinated with the insolvency law of an enacting State. However, it is advisable for an enacting State to give it a broad meaning so that all proceedings that might otherwise affect the rights of a transferee of

[100] *LG: BW suggests taking this sentence out. I can see that it is not strictly necessary, but I thought that here (and in other places) it might be useful to give examples of the interaction between the MLF and another law, as this illustrates the way it can fit into national law.

receivables are included.][The term 'insolvency proceedings' is not defined in the MLF, and so it is up to applicable law whether and how insolvency law would apply to a transfer that is effective against third parties. What Art 15 does to is to ensure that the application of insolvency law cannot affect the effectiveness against third parties or the priority of that transfer.][101]

251. There is one exception to the retention of priority under Art 15, which is where another claim has priority under the applicable insolvency law. What law is the applicable insolvency law will depend on relevant conflict of laws rules and may not be the law of the enacting State.

[Article 16 — Transfers competing with claims arising by operation of other law

The following claims arising by operation of other law have priority over a transfer that is effective against third parties but only up to [the enacting State to specify the amount for each category of claim]:

(a) […];

(b) […].]

Comment:

252. Art 16 enables a State to enumerate any claims which, as a matter of policy, it decides should have priority over a transfer, and to specify a limit for each category of claim. Such priority would normally only apply to security transfers. The priority could be (a) both within and outside the insolvency of the transferor, or (b) only within insolvency. In many States the existing enumeration of such claims will be in statutory provisions dealing with insolvency law, or other types of law, and the priority of these claims in those instruments is likely to extend to rights other than those of a transferee, such as security rights in types of assets other than receivables. In this situation, article 16 could achieve its purpose by making reference to the other statutory provisions, with qualifications that are specific to transfers of receivables, if desired.

253. In relation to factoring, enacting States are encouraged either to leave out this article altogether (hence the fact that it is in square brackets) or to limit the number and extent of listed claims severely, in order not to have a detrimental effect on access to finance.

Article 17 — Transfers competing with rights of judgment creditors

1. The right of a judgment creditor has priority over a transfer if, before the transfer is made effective against third parties, the judgment creditor has [the enacting State to specify the steps to be taken for a judgment creditor to acquire rights in the receivable or the enacting State to specify the relevant provisions of other law which contain the steps].

2. In the case of a security transfer, if the transfer is made effective against third parties before or at the same time the judgment creditor acquires its right in a receivable by taking the steps referred to in paragraph 1, the transfer has priority but that priority is limited to the greater of the credit extended by the transferee:

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101 *LG: The first two sentences are those I originally included (partly because I thought Ignacio would want them) but MD suggested drafting on the lines of the second two sentences. So I have kept both in square brackets. I suggest Ignacio is consulted and if he is happy with the second set then that can stand.

(a) before the transferee received a notice from the judgment creditor that the judgment creditor has taken the steps referred to in paragraph 1 [or within [the enacting State to specify a short period of time] thereafter]; or

(b) pursuant to an irrevocable commitment of the transferee to extend credit in a fixed amount or an amount to be fixed pursuant to a specified formula, if the commitment was made before the transferee received a notice from the judgment creditor that the judgment creditor had taken the steps referred to in paragraph 1.

Comment:[102]

254. Art 17 deals with a category of persons whose could have a claim competing with that of a transferee but who themselves are not transferees. As discussed in paragraph 139 (WG@2(2)(commentary to art 2(e)) a judgment creditor is a person C who has a court order [for the payment of money] against another person TR and who, under the applicable law, can take steps to obtain a right in an asset of TR. Such a right enables the judgment creditor (often, via an officer of the State) to obtain the value in that asset and use it in satisfaction of the court order. Different States use different terms for such a person, and precise definitions may vary from State to State, and so an enacting State is given the opportunity of defining the term 'judgment creditor' in the MLF according to its own terminology and to be consistent with its own law (Art 2(e).

255. Art 17 applies where the enacting State permits a judgment creditor to obtain a right in a receivable, for example, a judgment creditor is able to take certain steps which have the effect that the debtor who owes the receivable is obliged to pay the judgment creditor, such as obtaining a garnishment order relating to the receivable. An enacting State must specify in Art 17(1) the steps that must be taken for the judgment creditor to obtain a right in the receivable. For example, the relevant step could be the service of a garnishment order on a debtor[103]. If those steps are already set out in another piece of legislation, the enacting State can instead include in Art 17(1) a reference to the relevant other statutory provisions.

256. The priority rule in Art 17(1) is that the right of the judgment creditor has priority over the right of the transferee if the judgment creditor took the steps specified before the transfer became effective against third parties. Normally this will mean that, to obtain priority, the judgment creditor will have to take the specified steps before a notice relating to the transfer is registered, as registration is the only method of obtaining third party effectiveness under the MLF.

257. However, it is possible under the MLF to register a notice relating to a transfer before the transfer takes place (see paragraph 215). For example, on Day 1 a potential transferee TE registers a notice in relation to a transfer of a receivable arising from a underlying contract between TR and D. On Day 3, a judgment creditor C takes the necessary steps under Article 17 to acquire rights in the receivable. On day 5, TE and TR enter into a transfer agreement. The transfer of the receivable from TR to TE takes place on Day 5, so Day 5 is the time of third party effectiveness of that transfer. Thus, the right of C has priority over that of TE.

258. In relation to future receivables (in both senses) it is very unlikely that a judgment creditor can take the necessary steps in relation to a receivable before it arises, or before the person against whom the judgment creditor has a judgment has rights in the receivable. Therefore, although in theory a transfer of a future receivable included within transfer agreement takes place when the

[102] *LG: NC suggested at WG2 that the commentary (especially, I think, the first two paragraphs) should be aligned with the best Practices on Effective Enforcement project instrument.

[103] *LG: This example comes from the GtE of the MLST.

receivable ceases to be a future receivable, and therefore it is at that moment that the transfer becomes effective against third parties, that point is likely to be before the time when the judgment creditor has taken the necessary steps, and so the transferee is likely to have priority in most situations.

259. The rule in Art 17(2) only applies to security transfers, that is, a right securing a payment obligation owed by the transferor (TR). Under this rule, if the right of a security transferee (TE) has priority over the right of a judgment creditor (C) under art 17(1), the priority of the security transfer is limited to a certain amount of credit extended to the TR by the TE. The reason for this limit is that, once TE knows of the rights of judgment creditor, it can protect itself by not advancing any further credit to TR, unless it is already committed to do so. The limit is, therefore, the greater amount of credit extended by the TE to TR (a) before it is notified by C that C has taken the necessary steps to obtain rights in the receivable, or (b) pursuant to an irrevocable commitment made before TE receives such a notification. The enacting State can extend the relevant point in time beyond the time of notification by specifying, in the enacting legislation, a short period of time. This will give TE a grace period within which to adjust to the information that C has rights in the receivable, but it is suggested that the period should be short e.g. 15 days.

Article 18 — Subordination

1. A person may at any time modify or subordinate the priority of its rights under this Law in favour of any existing or future competing claimant. The beneficiary need not be a party to the modification or subordination.

2. A modification or subordination under paragraph 1 does not affect the rights of competing claimants other than the person modifying or subordinating its priority and the beneficiary of the modification or subordination.

Comment:

260. Art 18(1) permits a person to modify or subordinate its priority in relation to any competing claimant. Thus, for example, a transferee (TE1) can agree to rank lower than another transferee (TE2) (subordination) or a judgment creditor (C) can agree to rank pari passu with a transferee (TE1) (modification). Art 18 therefore confirms the position that would, largely, apply under Art 3 (derogation or variation of the MLF rules by agreement) in any event, but it also goes further in that a person's priority position can be improved by agreement without that person's consent (see discussion of Art 3(2)). Thus, under Art 18(1), there is no need for the beneficiary of the subordination or modification (in the example, TE2 or C) to be a party to the subordination or modification. Thus there can be a unilateral subordination or modification. However, a subordination or modification cannot affect a non-party competing claimant except the person benefitted (Art 18(2)).

261. In practice, in the context of factoring, a release is often used instead of a subordination. Hence, a factor may obtain a release from a secured creditor from the latter's rights in relation to certain receivables to be transferred to the factor.

Article 19 — Irrelevance of knowledge of another transfer

The priority of a transfer is not affected by any knowledge that the transferee has of another transfer.

Comment:

262. Art 19 makes it clear that, unlike priority rules in some domestic laws, the priority rules in relation to transfer of receivables under the MLF are not affected by the fact that a transferee knows of another transfer. This rule makes the priority position more certain and avoids difficult questions of proof of knowledge.

CHAPTER VI – RIGHTS AND OBLIGATIONS OF THE TRANSFEROR, TRANSFEREE AND DEBTOR

263. This chapter is divided into two sections. The first section relates to the rights and obligations between the transferor and the transferee. This relationship is largely governed by the agreement between them which will be governed by the applicable contract law. Thus, for example, that law will determine what is incorporated in the agreement and how it is interpreted. The parties can agree whatever rights and obligations between them that they want, but the MLF provides for certain rights and obligations which will form part of that agreement even without any express provision unless varied by the parties. The second section provides various rules governing the protection of the debtor when a transfer takes place. These rules reflect the balancing of interests between that of the debtor (who is concerned that its position vis a vis the receivable does not change) and the transferee (who wishes to have an unrestricted right to the receivable and its proceeds). The balance between these interests is carefully constructed so that, while consent of the debtor to a transfer is not required for an effective transfer, the debtor's position is protected so that it only changes once the debtor has been given relevant information about the transfer and who it needs to pay to obtain a discharge of the receivable, and even then, the debtor's position only changes in limited respects.

264. There are two terms used in this chapter which are worth explaining at the outset. The first is 'notification of a transfer'. This is a document (paper or electronic) which is sent to a debtor to notify it of a transfer. As mentioned in paragraph 220 (WG2(2) above (commentary to Art 9), it is possible to have a transfer that is made effective against third parties by registration of a notice in relation to which no notification has been sent to the debtor. Non-notification factoring is a well-known business practice.[104] However, in other types of factoring the debtor will be notified, and certain important consequences flow from the receipt by a debtor of the notification of a transfer, which are set out in this chapter.

265. The second term is 'payment instruction'. This is a document which is sent to the debtor to instruct it whom to pay, and sometimes where to pay. It changes these matters from the terms set out in the underlying contract in relation to payment (see paragraph 280-281 (WG2(2)) commentary to Art 24 below). It is not a notification of transfer, and the person the debtor is instructed to pay need not be the transferor or the transferee. It can be sent together with a notification of transfer or separately. Most notifications of transfer will usually include a payment instruction, as it is important that the debtor knows how it can pay and obtain a good discharge.

266. The rules in this chapter, including those on the legal effect of notifications of transfer and payment instructions, apply irrespective of whether or not a notice in respect of the transfer has been registered in the registry.

267. In the context of this chapter it is important to remember that there are two ways in which a receivable can be the object of multiple transfers. The first is where a transferor TR transfers a receivable more than once to different transferees ('transfers by the same transferor'). Here, TR transfers the receivable to TE1 and then transfers the same receivable to TE2. In this situation, the transfers to TE1 and TE2 are usually competing transfers, and the relevant priority rule is that set out in Art 13. It is also possible in this situation that there is no competition between transfers to TE1 and TE2, such as where they are both security transfers or each are transfers of a part of the same debt.[105] The second is where there is a chain of transfers from transferee to transfer. Here, TR transfers a receivable to TE1 and TE1 transfers the same receivable to TE2 (ref to discussion of

[104] Cross-reference to business practice section.

[105] *LG: This reflects what MD at WG2. I hope I have it right. The important distinction is between the TR to TE1 and TR to TE2 situation (on the one hand) and the TR to TE1 to TE2 (on the other hand) as different parts of Art 26 apply to each one.

import/export factoring in paragraph xxx). In this situation the transfers are not competing since only one transferee is entitled to the receivable at any one time.

SECTION 1. TRANSFEROR AND TRANSFEREE

Article 20 — Rights and obligations of the transferor and the transferee

1. The mutual rights and obligations of a transferor and transferee arising from their transfer agreement are determined by the terms and conditions set out in that agreement, including any rules or general conditions referred to therein.

2. The transferor and the transferee are bound by any usage to which they have agreed and, unless otherwise agreed, by any practices they have established between themselves.

Comment:

268. Art 20 makes it clear that, as a general matter, the content of the transfer agreement governs the rights and obligations between them.[106] The relationship between the transferor and the transferee is also governed by any usage, for example, a specific trade usage that [ ], to which the parties have agreed. They are also bound by any practices they have established between themselves, such as [ ] unless they agree otherwise. (Art 20(2))[107]

Article 21 — Representations of the transferor

1. The transferor of a receivable represents, at the time of entry into the transfer agreement, that:

(a) the transferor has, or in the case of a future receivable will have, the right to transfer the receivable;

(b) the transferor has not previously transferred the receivable to another transferee; and

(c) the debtor does not and will not have any defences or rights of set-off.

2. The transferor does not represent that the debtor has, or will have, the ability to pay.

Comment:

269. Art 21 sets out various representations that the transferor, as a matter of law, is treated as having made to the transferee, unless the agreement provides otherwise. These representations are often set out expressly in the transfer agreement and are very important commercially in relation to

[106] *LG: I have taken out a sentence (The applicable contract law will determine what is included within the agreement (for example, what rules and general conditions, referred to in Art 20(1), are actually incorporated within that agreement) and put a general statement in the introduction, as requested, but I still think it is more relevant to point out in the commentary to Art 20 that the incorporation of general rules and conditions referred to in the agreement is a matter of contract law and that there isn't some special MLF rule that a general condition referred to in the agreement governs the relationship between the parties even if it would not have been incorporated into the contract under the applicable contract law.

[107] *LG: It would be useful to have suggestions from the WG as to examples here

the allocation of risk between a transferor and a transferee, and for this type of financing to work. Article 21 is not an exhaustive list, and a transferor can, and often will, make other representations to a transferee. The effect of these, and any other, representations not being true or accurate will depend on the applicable law, taking into account the agreement between the parties (see paragraph xxx for a discussion of how the applicable law is determined (Art 36(1)).[108] It will usually be the case is that if any of the represented facts are not true or accurate, the transferee will have a right against the transferor to terminate the agreement and/or to sue for damages and/or other contractually agreed consequences will follow.

270. Under Art 21, the representations are made at the time of the entry into the transfer agreement, but those contained in Art 21(a) and (c) do not just relate to existing facts but relate to the future. While, in the absence of specific agreement between the parties, the effect of a representation as to the future will depend on the applicable law, representations as to the future should be viewed as continuing representations.

271. The representations set out in Art 21 are discussed individually below.

Art 21(1)(a)

272. Even if the transferor does not have the right to transfer the receivable, it will sometimes have the power to effect a valid transfer, (see paragraph 187 (WG2(2))(commentary to Art 5(1) and Art 13)). If the receivable is a future receivable in the first sense (see paragraph 135 (WG2(2)), the representation is that the transferor will have the right to transfer it when it arises. If it is a future receivable in the second sense, the representation is that the transferor will have the right to transfer it in the future. In either case, these are continuing representations, so that if the transferor does not obtain the right to transfer the receivable, the consequences mentioned in paragraph 263 (WG2(2)) above will follow.

Art 21(1)(b)

273. This representation (made by transferor TR to transferee TE2) will be untrue where TR has already transferred the receivable to TE1. In this situation, the consequences mentioned in paragraph xxx will apply. However, the parties could, by agreement, widen or narrow the scope of this representation. For example, the agreement with TE2 could provide that TR represents that there are no competing rights in the receivable. If a judgment creditor had rights arising before the transfer to TE2, the representation would be untrue and the consequences mentioned above would apply. If, however, the transfer to TE2 is a security transfer, TR might disclose to TE2 a previous security transfer to TE1. The representation in Art 21(1)(b) would then be narrowed by agreement to cover only transfers other than the transfer to TE1, since TE2 already knows about that transfer.[109]

Art 21(1)(c)

274. If the debtor does have defences or set-offs they can bind a transferee under certain circumstances, which are set out in Art 27, unless the debtor has made an agreement not to raise

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[108] *LG: I think it is important to keep this in here: the law of remedies for misrepresentation varies between jurisdictions and this needs to be pointed out. See also the comment to Art 21(1)(b) commentary below. The part in brackets (the reference to art 36) can be take out if desired.

[109] *LG: I tried to reflect what MD and NC said at WG2 about party autonomy meaning that the parties could widen or narrow the representation in 21(1)(b). We also had a discussion about whether the text meant a representation or a contractual promise (eg a warranty). Since it says 'representation' I assume that is what is meant, but what is meant by 'representation' in any applicable law could vary. In some jurisdictions (perhaps) a representation entails a promise that it is true, for example. I think it would get far too complicated to go into this, or to mention what we discussed in the WG which is that the parties could agree that one or more of the representations in Art 21 were actually promises of truth. I think it is best today that the parties can extend or narrow the reps, and that applicable law determined the effect of a rep not being true.

them under Art 28. A transferee would therefore be concerned about this point. This representation relates to the future, and would therefore be a continuing representation. This is particularly important since some defences or rights of setoff (those arising out of the underlying contract or any other contract that was part of the same transaction) can bind the transferee even after it has given a notification of the transfer to the debtor (Art 27(1)).

Art 27(2)

275. While the 'default' position under the MLF is that the transferor does not make any representation about the debtor's ability to pay, in 'recourse' factoring the risk of non-payment by the debtor is borne by the transferor. The precise legal means by which this risk is put on the transferor will depend on the wording of the agreement between the transferor and the transferee, and may depend on the applicable law.

Article 22 — Right to notify the debtor

1. The transferor, the transferee or both may send the debtor a notification of a transfer and a payment instruction, but after a notification of the transfer has been received by the debtor only the transferee may send a payment instruction.

2. A notification of a transfer or a payment instruction sent in breach of an agreement between the transferor and the transferee is not ineffective for the purposes of Article 26, but nothing in this Article affects any obligation or liability of the party in breach for any damages arising as a result of the breach.

Comment:

276. Under Art 22(1), either the transferor or the transferee (or both) are permitted to send a notification of a transfer (see paragraph 258 (WG2(2)) above) to the debtor at any time. The requirements for an effective notification are set out in Art 25.

277. A transferor is permitted to send a payment instruction (see paragraph 259 (WG2(2)) above) to the debtor, but only before the debtor receives a notification. For example, a transferor might want to send a payment instruction even though no notification had been sent in order to change the requirements of payment from that in the underlying contract. After the debtor has received a notice of transfer, a transferor is not permitted to send a payment instruction, and if it did so, the debtor is entitled to ignore it. This rules is to prevent 'double-financing', that is, where the transferor undermines the transferee's right to payment by instructing the debtor to pay elsewhere.

278. In contrast, a transferee can send a payment instruction to the debtor at any time. In practice, a notification is likely also to include a payment instruction. However, if, after debtor has been notified, the transferee wants payment to be made to a different person, account or place from that set out in the payment instruction sent as part of the notification, the transferee will need to send another payment instruction to the debtor. The requirements for an effective payment instruction are set out in Art 25.[110]

279. Sometimes, particularly in non-notification financing, there will be a term in the transfer agreement prohibiting either party notifying the debtor of the transfer, except in the very specific

[110] *LG: MD wanted this out a WG2 as he said it was the same as in 270. But it isn't: 270 relates to a notification and 272 relates to a payment instruction. So I have left it in.

circumstances set out in that agreement. Under Art 22(2) a notification in breach of such an agreement, however, does not stop a notification being effective for the purposes of Art 26, that is, in relation to debtor discharge[111]. The liability of the party in breach, if any, however, is retained under Art 22(2).

Article 23 — Right to payment

As between the transferor and the transferee, whether or not a notification of a transfer has been sent to the debtor:

(a) if payment with respect to the receivable is made to the transferee, the transferee is entitled to retain the payment;

(b) if payment with respect to the receivable is made to the transferor, the transferee is entitled to be paid that amount by the transferor; and

(c) if payment with respect to the receivable is made to another person over whom the transferee has priority, the transferee is entitled to be paid that amount by the other person.

Comment:

280. Art 23 deals with who, as between the transferor and transferee, has a right to the amount paid by the debtor in purported discharge of the receivable, irrespective of to whom that sum is paid. The rules in art 23 apply whether or not notification of a transfer has been sent to a debtor. However, the rules in art 23 are subject to contrary agreement of the parties. For example, if a transfer is a security transfer, the parties are likely to agree who is entitled to payment in what circumstances. In that situation, the parties' agreement governs if it is inconsistent with the rules in Art 23.

Art 23(a)

281. The transferee is always entitled to retain any payment made to it, even if the debtor has not (officially) been notified of the transfer. Clearly, the debtor must know of the transferee's existence and of the transfer in order to know to pay that transferee.

Art 23(b)

282. If the debtor pays the transferor, the transferee is entitled to be paid, by the transferor, the sum received by the transferor in respect of that receivable. This reflects the position that is intended to apply in non-notification financing (that the debtor pays the transferor who then remits that payment to the transferee) but it also covers the position where, after notification, the debtor pays the 'wrong' person (that is, the transferor). In this situation, as between the transferor and the transferee, the transferee is entitled to be paid the relevant sum by the transferor, but the debtor is not discharged under Art 26 and so the transferee is also entitled to be paid by the debtor. Whether the debtor has any claim against the transferor in this situation is a matter for other law. If, however, the debtor is discharged under the rules in Art 26 by making the payment, it cannot be obliged to pay another person. Thus, when the debtor pays the transferor because it has not been notified of

[111] *LG: Does this mean that it can be ineffective in relation to defences, set-offs and modifications? Should we say this? This matter was deferred to WG3 for discussion. It may be that this point is too technical for the GtE.

the transfer, the debtor does not have to pay the transferee: it is the transferor who must remit the payment it has received to the transferor.

Art 23(c).

283. If the debtor pays someone else (for example, another transferee, or a judgment creditor) over whom the transferee has priority on the application of the rules in Chapter V, the transferee is entitled to be paid the amount by that other person. If the debtor is discharged under the rules in Art 26 by making the payment, it cannot be obliged to pay another person. Thus, when the debtor (D) pays a transferee TE2 because TE2 notified the debtor, but transferee TE1 has priority over TE2 because a notice in relation to TE1's transfer was registered before a notice in relation to TE2's transfer, D does not have to pay TE1. Instead, TE2 has to remit the payment to TE1. Examples of this situation are where [a junior factor collects payment for a senior factor, see paragraph xxx or][112] where a junior secured creditor (that is, a secured creditor who does not have the highest priority of all secured creditors) collects on a receivable, when the distribution of the collection must be distributed according to Art 35.

SECTION 2. DEBTOR

Article 24 — Principle of debtor protection

1. Except as otherwise provided in this Law, a transfer does not, without the consent of the debtor, affect the rights and obligations of the debtor, including the payment terms contained in the contract giving rise to the receivable.

2. A payment instruction may change the person, address or account to which the debtor is required to make payment, but may not change without the consent of the debtor:

(a) the currency of payment specified in the contract giving rise to the receivable; or

(b) the State specified in the contract giving rise to the receivable in which payment is to be made to a State other than the State in which the debtor is located.

Comment:

284. Art 24 states the basic principle that a transfer of a receivable should not affect the rights and obligations of the debtor without its consent, except to the limited extent set out in the MLF. This gives effect to the balance referred to earlier (paragraph 257 (WG2(2))) between the interests of the debtor and those of the transferee. The rights and obligations that are not affected without the debtor's consent include the terms of payment in the underlying contract. As mentioned above, a payment instruction is sent to a debtor to instruct it to pay someone (or somewhere) other than the person or place specified in the underlying contract. A notification is likely to include a payment instruction, so that the debtor knows how to obtain a discharge the receivable by paying the transferee, but a payment instruction can also be given subsequently.[113]

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[112] *LG: This was mentioned in one of the WGs, but is only worth including if junior and senior factors are mentioned in the discussion of business financing practices earlier in the GtE. Whether this is kept in depends on the text on business practices.

[113] *LG: This is also said in the introduction but given the discussion the WG had in relation to Art 8 on this point I thought I would put it in both places for the moment.

285. As mentioned in paragraph 257(WG2(2) above, the debtor is further protected by limitations on what can be changed by payment instruction without the consent of the debtor. These limitations are set out in Art 24(2); the currency of payment cannot be changed nor can the State in which payment is to be made be changed to a State other than that of the location of the debtor. Thus, the debtor is protected from changes which deviate from the underlying contract terms which could result in it incurring significant costs (see paragraph 212 (WG2(2)) Art 8)

Article 25 — Notification of a transfer or payment instruction

1. A notification of a transfer and a payment instruction must be in writing.

2. A notification of a transfer or a payment instruction is effective when received by the debtor if it reasonably identifies the receivable and the transferee, and is in a language that is reasonably expected to inform the debtor about its contents. It is sufficient if the notification of the transfer or the payment instruction is in the language of the contract giving rise to the receivable.

3. A notification of a transfer or a payment instruction may relate to receivables arising after notification.

4. In the case of a series of transfers of a receivable from a transferee to a subsequent transferee, a notification of one transfer constitutes a notification of all previous transfers.

Comment:

Article 25(1)

286. 280 There are minimal formal requirements for a notification and a payment instruction. Art 25(1) merely provides that each must be in writing. *Article 25(2)*

287. Art 25(2) specifies information that must be included in a notification or a payment instruction, namely, reasonable identification of the receivable and of the transferee. The receivable needs to be identified so that the debtor knows which receivable is being referred to. If only part of a receivable was being transferred, notification of transfer would need to indicate which part was being transferred. Although Art 25(2) (as with the rest of the MLF) refers to a single receivable, a notification of a transfer or a payment instruction can refer to one receivable, a generic category of receivables or all receivables owed by the debtor to one [or more than one] creditor. While the notification or payment instruction needs to be in a language that reasonably informs the debtor about its contents, this requirement is satisfied by the use of the language of the underlying contract, on the basis that this will not disadvantage the debtor, who is already a party to the underlying contract.

288. The transferee needs to be identified as, in the case of a notification, the debtor will be discharged only if it pays the transferee (in the absence of a subsequent payment instruction) (Art 26(2)). There is, however, no requirement that the transferor be identified. There are several reasons for this. First, it is not always industry practice. Second, in a chain of transfers (see paragraph 261 (WG2(2)) it could confuse the debtor if intermediate transferors were identified. Third, if the debtor needed that information, it could ask for it under Art 26(7).

Article 25(3)

289. Art 25(3) specifically provides that a notification of a transfer or a payment instruction can relate to receivables arising after notification. This means that either document can relate to future receivables in the first sense discussed in paragraph 135 (WG2(2)) (commentary to Art 2(d))). In the example given in that paragraph[114], TE could send a notification of a transfer to D relating to all the present and future receivables owed by D to TR. The provisions of Art 26 relating to discharge, however, would not apply to any particular receivable until it arose. It is common practice in factoring for notifications to include present and future receivables.

290. Although there is no specific mention of future receivables in the second sense (receivables which have arisen but which have not yet been acquired by the transferor, see paragraph 138(WG2(2)), they can also be the subject of a notification of transfer or a payment instruction. A future receivable of this type is transferred when the transferor acquires rights in it or the power to transfer it. However, because such a receivable has already arisen, if it is included in a notification of transfer (or a payment instruction) and becomes payable, the provisions of Art 26 relating to discharge would apply. Therefore, the debtor would be discharged by payment to the notified transferee or as otherwise instructed (Art 26(2)). If another person had a better claim to the receivable than the transferee, that person would be entitled to be paid the amount of the payment under Art 23(c).

Article 25(4)

291. Art 25(4) relates to a chain of transfers as described above in paragraph 216 (WG2(2)), an example of which is where there is transfer of a receivable owed by D from TR (the original creditor) to TE1 and then from TE1 to TE2. Art 25(4) makes it clear that a notification of a transfer lower in the chain (that is, further away from TR) is also a notification of all previous transfers. In this context, 'previous transfers' means all transfers of that receivable further up the chain, that is, nearer TR. Thus, a notification to D by TE2 of the transfer from TE1 to TE2 would also be a notification of the transfer from TR to TE1. Since D would get only get a discharge under art 26(2) by paying TE2, D is not interested, and does not need to know about, the transfer from TR to TE1; a notification of the transfer from TR to TE1 could even confuse the debtor. Art 25(4) is therefore included to disincentivise intermediate transferees from notifying the debtor. It is also common practice in international factoring, where chains of transfers are common, for notification only to be given by the transferee at the 'bottom' of the chain as this is the transferee to whom the debtor must make payment.[115]

Article 26 — Debtor's discharge by payment

1. Until the debtor receives a notification of a transfer, the debtor is discharged by paying in accordance with the contract giving rise to the receivable.

2. After the debtor receives a notification of a transfer pursuant to Article 25, subject to paragraphs 3 to 8 of this Article, the debtor is discharged only by paying the transferee or as otherwise instructed in the notification, subject to any payment instruction subsequently received by the debtor from the transferee.

3. If the debtor receives more than one payment instruction relating to a single transfer of the same receivable by the same transferor, the

[114] *LG: Is it OK to cross-refer to examples like this?

[115] *LG: Can we please check with FCI that this is correct as a matter of practice?

debtor is discharged by paying in accordance with the last payment instruction received from the transferee before payment.

4. If the debtor receives notifications of more than one transfer of the same receivable by the same transferor, the debtor is discharged by paying in accordance with the first notification received.

5. If the debtor receives a notification of a transfer by a transferee, the debtor is discharged by paying in accordance with that notification. In the case of a series of transfers from a transferee to a subsequent transferee, the debtor is discharged by paying in accordance with the notification of the last of those transfers.

6. If the debtor receives a notification of the transfer of a part of or an undivided interest in a receivable, the debtor is discharged by paying in accordance with the notification or in accordance with this Article as if the debtor had not received the notification. If the debtor pays in accordance with the notification, the debtor is discharged only to the extent of the part or undivided interest paid.

7. If the debtor receives a notification of a transfer from the transferee, the debtor is entitled to request the transferee to provide within a reasonable period of time adequate proof that the transfer from the initial transferor to the initial transferee and any intermediate transfer has been made. Until the transferee does so, the debtor is discharged by paying in accordance with this Article as if the notification had not been received. Adequate proof of a transfer includes but is not limited to any writing emanating from the transferor that indicates that the transfer has been made.

8. This Article does not affect any other ground on which payment by the debtor to the person entitled to payment, to a competent judicial or other authority, or to a public deposit fund, discharges the debtor.

Comment:

292. Art 26 is an important provision that determines when a debtor is discharged by payment. The governing principle underlying this article is that it should be clear to a debtor, both as a matter of law and fact, whom it should pay (and where it should pay) to obtain a discharge. Where the relevant facts are not clear to a debtor, it has the possibility to request further information.

293. Once a debtor has paid and been discharged by payment, the question of whether the person to whom payment has been made is entitled to that payment is governed by the priority rules in Chapter V. Whether the person entitled to payment under the priority rule can claim the remitted sum from the person to whom payment is made may depend on art 23 in some circumstances, and in other circumstances will depend on the applicable law. For example, Art 23 only deals with entitlement of a 'transferee', and not, for example, with the entitlement of a judgment creditor. If the debtor makes payment in a way that does not discharge it under Art 26, it may have to make another payment to obtain a discharge from the receivable. Whether the debtor can obtain the first payment back from the payee is a matter for the applicable law and not covered in the MLF.

Article 26(1)

294. Art 26(1) deals with the situation before the debtor has received a notification of transfer. In this situation, the debtor (D) is discharged by paying according to the underlying contract. If, however, the creditor under that contract (the transferor TR) has sent a payment instruction to D

(see art 22(1)) changing the person, account or location to which payment is to be made then D will obtain a good discharge only by paying in accordance with that payment instruction, although the currency of the payment cannot be changed without D's consent, nor can the State where payment is to be made to changed to a State other than that in which the debtor is located (Art 24(2)). In a situation where non-notification factoring is used, TR often sends a payment instruction stating that payment is to be made to a different bank account from that specified in the underlying contract; this is because the second bank account is one over which the non-notification factor (TE) has some control.[116]

Article 26(2)

295. Art 26(2) deals with the situation once a debtor has received one notification of transfer. (The situation where a debtor receives more than one notification of transfer is dealt with in Arts 26(4) and (5)). Normally, a debtor would receive only one notification of transfer where the receivable has only been transferred once, although in that situation it is possible that a second transfer has occurred but has not been notified to the debtor. A debtor who has received one notification is discharged under art 26(2) only by paying the transferee identified in that notification and not by paying anyone else unless:

a. A payment instruction received together with the notification (see paragraph 278 (WG2(2)) Art 24) instructs the debtor to pay someone other than the transferee, in which case the debtor is discharged by paying that other person, or
b. The debtor receives a payment instruction after it has received the notification of transfer. That payment instruction can only be sent by the transferee (Art 22(1)) and not by the transferor.

296. Example: D owes TR a receivable. TR transfers the receivable to TE. On Day 1 TE sends a notification to D, including a payment instruction, instructing D to pay the receivable to TE into account 12345. D is discharged only by paying the receivable to TE into account 12345. However, if the payment instruction instructs D to pay the sum to X into account 12345, D is discharged only by paying the sum to X into account 12345. If there is no payment instruction with the notification, but, on Day 5, TE sends a payment instruction instructing D to pay X into account 98765, D is only discharged by paying X into account 98765.

Article 26(3)

297. Art 26(3) deals with the situation where a debtor receives more than one payment instruction from the same transferee in relation to a single transfer of the same receivable. For example, D owes TR a receivable, and TR transfers the receivable to TE. On Day 1 TE sends a notification to D, including a payment instruction, instructing D to pay the receivable to TE into account 12345. On Day 5, TE sends a payment instruction instructing D to pay X into account 98765. Under article 26(3), D is only discharged by paying X into account 98765, as this is the last payment instruction received from the transferee before payment.

Article 26(4)

298. Art 26(4) and Art 26(5) deal with the 2 situations discussed in [paragraph 261 (WG2(2) in the Introduction]. Art 26(4) deals with where there are multiple transfers by the same transferor. Art 26(5) deals with the situation where there is a chain of transfers. It is often difficult for a debtor to know whether a situation falls within Art 26(4) (multiple transfers by the same transferor) or within Art 26(5) (a chain of transfers). A debtor who is uncertain can request information from a

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116 *LG: This reflects the discussion in WG1 of GtE.

notifying transferee under Art 26(7) or, if that course of action does not clarify the situation, the debtor may be able to make payment to a court or a public deposit fund, depending on the applicable law.

299. Art 26(4) provides that where a debtor receives more than one notification of transfers in a situation where there are two or more transfers by the same transferor, the debtor is discharged by paying in accordance with the first notification. For example, D owes TR a receivable. TR transfers the receivable to TE1, who notifies D of the transfer. TR then transfers the receivable to TE2, who also notifies D of its transfer. D is discharged by paying TE1 (the first notification). This is irrespective of the priority position between TE1 and TE2 under Art 13. D will know that the transfers are by the same transferor (TR) if the notifications both name TR as the transferor. However, it is not mandatory for a notification to identify the transferor (Art 25(2)). If the transferor is not named in one or both notifications, D will not know whether the situation falls within Art 26(4) but can ask for information under Art 26(7) (discussed below).

300. The words 'by the same transferor' in Art 26(4) refer to the person who has made the multiple transfers (here, the transferor TR), not the person(s) who send the notifications (in most cases this is likely to be the transferees, although either the transferor or the transferee can send a notification in relation to a transfer).

Article 26(5)

301. Art 26(5) deals with where the debtor is notified of a transfer by a transferee, or more than one transfer by more than one transferee. In the first case (the single transfer) the debtor is discharged by paying in accordance with the notification: this is consistent with Art 26(2). The second case is that of a chain of transfers (see paragraph 261 (WG2(2)) above). Where there is a chain of transfers, and the debtor receives notification of more than one transfer in the chain, it is discharged by paying in accordance with the last notification. For example, TR is owed a receivable by D, which TR transfers to TE1. TE1 notifies D of the transfer. TE1 then transfer the receivable to TE2. TE2 notifies D of the transfer. D is discharged by paying TE2. TE2 is, in the language of the section, a 'subsequent transferee'.

302. In a chain of transfers, the transferee in transfer 1 (TE1) becomes the transferor in transfer 2. If, then, TE2's notification identifies TE1 as the transferor in the transfer to TE2, A will know that the transfers are part of a chain (since the notified transfer was not made by TR, and it was TR to whom D originally owed the receivable). D will therefore know to pay TE2, that is, according to the last notification. If, however, the position is unclear, A can make a request for information under Art 26(7) (discussed below in paragraph 297 (WG2(2))). As mentioned above, Art 25(4) is designed to disincentivise the sending of notices by intermediate transferees to avoid the situation to which Art 25(4) relates.

Article 26(6)

303. A difficult point arises where a debtor receives notification of a transfer of part of a debt or an undivided interest in the debt (see paragraph 261 (WG2(2)). Art 26(6) provides that the debtor is discharged either by paying in accordance with the notification (in which case they are discharged to the extent of the part paid) or in accordance with the rest of Art 26, ignoring Art 26(2). Thus, for example, if a debtor D is notified of a transfer to TE1 of half a receivable that D owes to TR, D can either pay half the receivable to TE1 or can pay the entire receivable to TR according to the contract under which the receivable arose (in which case, TR would have to pay TE1 half the amount paid under Art 23(b)). This provision is to protect a debtor from being involved in a dispute as to whether the receivable has been fully discharged.

Article 26(7)

304. If a notification does not comply with the requirements in Art 25, the debtor can ignore it as it is not an effective notification. However, even if the notification is effective, the debtor might want more information in order to decide who to pay, in which case it can make the request set out in Art 26(7) for 'adequate proof' that the initial transfer and any intermediate transfer has been made. Examples of where a debtor might want more information are set out in paragraphs 292 and 295 (WG2(2)) above. Written proof from either the transferor or the transferee will be sufficient to be 'adequate'. Until the debtor receives adequate proof it is discharged by paying according to Art 26, ignoring the notification triggering the request for information. The debtor cannot, and need not, request proof of the transferee's priority over other claimants, since it will be discharged only by paying in accordance with Art 26.

305. The information must be given within a reasonable time of the request. What is a reasonable time is not defined in the MLF, but it must be consistent with commercial reasonableness, given that persons must exercise rights and obligations under the MLF in a commercially reasonable manner (Art 4).[117] There is no requirement for the request for information to be made within a reasonable time, but the time for payment to be made is not extended by the request for information. The debtor is protected by making the request as soon as possible and paying in accordance with Art 26 ignoring the notification if the information is not forthcoming. If a debtor is really unsure of the position it can go to court to ask for a ruling who to pay.[118]

Article 26(8)

306. Art 26(8) recognises that there could be other means of discharge under applicable law, such as payment to a court or to a public deposit fund, or paying, by chance, the person entitled to payment where no notification of transfer complying with the requirements in Art 25 has taken place.

Article 27 — Defences and rights of set-off of the debtor

1. In a claim by the transferee against the debtor for payment of a receivable, the debtor may raise against the transferee all defences and rights of set-off arising from the contract giving rise to the receivable, or any other contract that was part of the same transaction, of which the debtor could avail itself as if the transfer had not been made and the claim were made by the transferor.

2. The debtor may raise against the transferee any other right of set-off, provided that it was available to the debtor at the time it received a notification of the transfer.

Comment:

307. Art 27 deals with when a transferee take free of any right of set-off or defence that could be successfully asserted against the transferor by the debtor. It reflects the balance, mentioned above in paragraph 257 (WG2(2)), between protection of the debtor and the interests of the transferee. Thus, as set out in Art 27, in some circumstances the transferee takes subject to defences and set-off while in other situations it does not. If the transferee does take subject to a right of set-off or a defence, this will reduce the amount it can collect on the receivable, and may affect its ability to collect on the receivable at all. If the amount the transferee receives from the debtor in relation to

[117] *LG: NC suggested that this was moved here from the commentary on Art 4.

[118] *LG: not clear to me that Art 26(8) addresses this situation: it seems to be addressing another situation.

the receivable is reduced or if it is unable to collect at all, the transferee may have a claim against the transferor in relation to the representation in Art 21(1)(c). It should be noted that the term 'defence' in Art 27 does not include the assertion of an anti-assignment clause, as such a clause will be ineffective under Art 8. It is important that consideration is given to coordinating[119] Art 27 with an enacting State's law on set-off and defences (see III(1)) so that the law relating to transfers not falling within the MLF is not different from the application of the MLF to transfers falling within its scope unless there are considered to be good reasons for that difference[120].

308. The debtor can raise a right of set-off or defence whenever it arises if the right arises from the underlying contract or any other contract part of the same transaction (Art 27(1)). For example, if TR agrees to supply goods to D, D can set off any monetary claim for breach of contract arising from a defect in those goods against the receivable resulting from the supply whenever that claim arises.

309. The debtor can also raise any other right of set-off, but only if it arose before the debtor was notified of the transfer of the receivable (Art 27(2)). For example, TR agrees to supply goods to D (contract 1) on Day 1. D agrees to provide a service to TR (contract 2) in an entirely separate transaction on Day 30. TR transfers the receivable arising from contract 1 to TE on Day 10, and TE sends D a notification of the transfer on the same day. D cannot set off against TE the receivable arising from contract 2, as that receivable arose after the notification to D of the transfer of the receivable arising under contract 1. The reason for this rule is that once D knows of the right of TE in the receivable (in the example, TE's right in the receivable from contract 1) it should not, as a matter of balance between the interests of TE and D, be permitted to rely on later set-offs that reduce or extinguish the value of that right.

310. A notification of a transfer can relate to future receivables (Art 25(3) see para 286 (WG2(2)). Therefore, the rule in Art 27(2) applies even where the notification received by the debtor relates to a receivable that has not yet arisen. Thus, in the example above, if the notification was on Day 10 but contract 1 was not entered into until Day 15, the result would be the same. This is a scenario that is likely to happen where the debtor and the transferor are in an ongoing trading relationship, and the transferor factors all its present and future receivables under the trading relationship.

Article 28 — Agreement not to raise defences or rights of set-off

1. A debtor may agree with the transferor, in a writing signed by the debtor, not to raise against the transferee the defences and rights of set-off that it could raise in accordance with Article 27.

2. Such an agreement does not preclude the debtor from raising defences:

(a) arising from fraudulent acts of the transferee; or

(b) based on the debtor's incapacity.

3. Such an agreement may be modified only by an agreement in writing signed by the debtor. The effectiveness of such a modification as against the transferee is determined by Article 29.

[119] *LG: This complies with the agreed upon use of 'coordinate' as the enacting State's law on set-off and defences may either be identical to Art 27 (in which case no action is required) or may differ (in which case action is required).

[120] *LG: I don't know if we can put it in this way. But presumably sometimes an enacting state may consider that transfers outside the MLF should be subject to different rules and sometimes they won't. So here we should flag up that a State may want to take action but doesn't necessarily have to if it decides not to do so.

Comment:

311. The ability of a debtor to raise rights of set-off or defences against the transferee under Art 27 can be waived by the debtor in agreement with transferor under Art 28. This provision in the MLF overrides any general domestic law on waiver, but is subject to the limits set out in Art 28(2) and also any other domestic specific mandatory law (discussed below). These types of agreements are very important in certain types of factoring such as reverse factoring, where the waiver agreement is typically included in the debtor's confirmation (xx to Part I(2)). Art 28(1) covers not only defences and rights of set-off that have arisen at the time of the agreement with the transferor, but any future defences or rights of set-off. [example?][121]

312. Art 28(1) provides that the agreement between the debtor and the transferor must be in writing and by the debtor. This signature is required to indicate the debtor's consent to a waiver that reduces the rights the debtor otherwise has. It is not necessary for the transferor to sign the agreement.

313. Art 28(2) lists two type of defences that are not affected by an agreement under Art 28(1). A State's consumer law could also prevent the waiver of other defences by consumers.

314. The agreement between the debtor and transferor mentioned in Art 28(1) can be modified, but only by an agreement in writing signed by the debtor (see para 305 (WG2(2)) for the reason for this requirement) (Art 28(3)). Whether this modification is effective against the transferee of a receivable depends on the application of Art 29(1) and (2).

Article 29 — Modification of the contract giving rise to a receivable

1. A modification of the contract giving rise to a receivable that is made between the transferor and the debtor before the debtor receives a notification of the transfer and that affects the transferee's rights is effective as against the transferee, and the transferee acquires corresponding rights.

2. A modification that is made between the transferor and the debtor after the debtor receives a notification of the transfer and that affects the transferee's rights is ineffective against the transferee unless:

(a) the transferee consents to it; or

(b) the receivable is not fully earned by performance and either the modification is provided for in the contract giving rise to the receivable or, in the context of that contract, a reasonable transferee would consent to the modification.

3. Paragraphs 1 and 2 do not affect any right of the transferee arising from breach of an agreement with the transferor.

Comment:

315. Art 29 is concerned with when a transferee's rights are affected by a modification of the underlying contract. For example, a modification could change the amount due under the receivable, or could change the date of performance and therefore the date of payment. If the underlying

[121] *LG: Any suggestions from the FCI?

contract is modified before the debtor receives a notification of transfer, the transferee is bound by the modification (Art 29(1)). This rule protects the debtor, who agrees to the modification without knowing about the transfer.

316. However, once the debtor has received a notification of transfer, any subsequent modification only affects the transferee's rights in the two situations set out in Art 29(2)(a) and (b). The first situation (art 29(2)(a) is where the transferee consents to the modification, which is common practice for factors if the modification is minor. The second situation relates to a modification which is agreed before the receivable is fully earned by performance, that is, before the obligations of the payee have been fully performed (for example, before the goods to which the receivable relates have been fully delivered). In this situation, the modification is effective against the transferee if it is provided for in the underlying contract, or if a reasonable transferee would agree to the modification. Reasonableness here will be commercial reasonableness, given that persons must exercise rights and obligations under the MLF in a commercially reasonable manner (Art 4).[122] As a notification can include future receivables, that is receivables that have not yet arisen, Art 29(2) can apply to future receivables..

317. Art 29(3) relates to a situation where a transferee is affected by a modification, but that modification is in breach of a term in the transfer agreement (or another agreement) between the transferee and the transferor whereby the transferor promised not to modify the underlying contract that gave rise to the receivable. In this situation, the modification still binds the transferee, but the transferee may have a claim against the transferor. Art 29(3) refers only to a right of the transferee and not the transferor, since it is very unlikely that a transferor would assert rights against the transferee arising from a modification of the contract.

Article 30 — Recovery of payments

Failure of a transferor to perform the contract giving rise to the receivable does not entitle the debtor to recover from the transferee a sum paid by the debtor to the transferor or the transferee.

Comment:

318. Art 30 refers to a situation where a receivable has been transferred, and the debtor has paid the receivable either to the transferor or the transferee, but the transferor does not perform the underlying contract in compliance with that contract. Art 30 provides that the debtor is not entitled to recover the sum paid from the transferee. If the payment is still in the hands of the transferor, the debtor may be entitled to recover it, under the applicable law of contract or other law. Moreover, if the payment is in the hands of the transferee, the debtor may have a claim against the transferor for breach of the underlying contract under the applicable contract law.

319. For example, TR agrees under a underlying contract to perform a service to D on Day 1 on thirty days credit. TR purports to perform the service on Day 1 and transfers the receivable arising from the underlying contract to TE on Day 5. TE notifies D of the transfer on Day 10 and D pays the receivable to TE on Day 15. On Day 20 D discovers that TR has not in fact performed the service. D cannot recover the sum paid in respect of the receivable from TE, but may have a claim against TR under the applicable law.

[122] *LG: NC suggested at WG2 that this was moved here from the commentary on Art 4.

CHAPTER VII – COLLECTION AND ENFORCEMENT

320. This chapter of the Model Law provides clear, simple, and efficient methods for the collection and enforcement of receivables, both in the case of receivables that are the subject of an outright transfer and those that are the subject of a security transfer. Indeed, the efficient enforcement rules in Chapter VII are considered to be one of the MLF's seven core concepts. This chapter should be read in conjunction with Chapter VI, which addresses the relative rights of the transferor and transferee of a receivable and also addresses the effect of the transfer on the debtor.

321. Regardless of whether a receivable is assigned under an outright transfer or a security transfer, the transferee has the benefit of any security interest (in movable or immovable property) or personal right, such as a guaranty, securing or supporting the payment of the receivable.[123]

322. Also, both in the case of outright transfers and security transfers, the transferee's right to collect or enforce payment of the receivable is subject to Articles 24 to 30, protecting the debtor's rights against adverse effects of the transfer. In many other respects, however, the rules applicable to outright transfers (Art. 31) are simpler than those governing security transfers (Arts. 32-35).

SECTION 1. OUTRIGHT TRANSFERS

Article 31 — Collection of payment under an outright transfer

1. The transferee under an outright transfer of a receivable is entitled to collect the receivable at or after the time payment becomes due.

2. The transferee exercising the right to collect under paragraph 1 is also entitled to enforce any personal or property right that secures or supports payment of the receivable.

3. The right of the transferee to collect under paragraph 1 is subject to Articles 24 to 30.

Comment:

323. A transferee under an outright transfer becomes the owner of the receivable. It is entitled to collect on it when it becomes due. After collecting from the debtor, the outright transferee is entitled to keep whatever it collects, regardless of the amount it paid for the receivable and does not need to account to the transferor for any amount collected in excess of the amount it paid for the receivable.

324. In addition to being able to collect payment on the receivable, the transferee has the benefit of any security interest (in movable or immovable property) or personal right, such as a guaranty, securing or supporting the payment of the receivable. Thus, if the debtor does not pay the receivable when it is due, the transferee can enforce the rights provided under such a security interest or guaranty. Whether the transferee must first seek to collect payment from the debtor in such a situation depends on the law governing the security interest or guaranty, as would be the

[123] *NC: Is this and the following paragraph necessary in an introduction of this sort? I think not. These substantive points are addressed in the context of particular articles.

case had there been no transfer and the transferor sought to exercise rights under the security interest or guaranty.[124]

325. The transferee under an outright transfer should be aware, however, that the right to collect is subject to Articles 24 to 30, protecting the rights of the debtor of the receivables. An outright transferee of a receivable is also bound to proceed in good faith and in a commercially reasonable manner (Art. 4).

326. Of course, the transferee under an outright transfer may transfer the receivable to a subsequent transferee rather than collecting the receivable itself.

327. While the focus of the MLF is on outright transfers made for financing purposes, it should be remembered that the MLF also covers outright transfers made for other purposes, such as an outright transfer of receivables on the sale of a business or an outright transfer of receivables for collection. Thus, Article 31 applies to those non-financing transfers as well.

SECTION 2. SECURITY TRANSFERS

Article 32 — Post-default rights

1. After default, the transferor and the transferee under a security transfer are entitled to exercise:

(a) any right under this Chapter; and

(b) any other right provided in the transfer agreement or any other law, except to the extent it is inconsistent with this Law.

2. The exercise of one post-default right does not prevent the exercise of another post-default right, except to the extent that the exercise of one right makes the exercise of another right impossible.

3. Before default, the transferor under a security transfer and any person who owes the obligation secured by the security transfer may not waive unilaterally or vary by agreement any of their rights under this Chapter.

Comment:

328. When a transfer of a receivable is a security transfer, the allocation of rights and responsibilities under the MLF is more complicated because, when a transfer is made only to secure an obligation of the transferor, the transferor retains an interest in the receivable and the transferee's interest exists to protect the transferee against the consequences of default by the transferor (or any other person who owes the obligation secured by a security transfer).

329. In light of the purposes of a security transfer as indicated above, this Article provides that the rights of the parties as described in the Chapter, as well as those provided for in the transfer

[124] *NC: This paragraph has been added. MD mentioned independent undertakings at WG2 (and, by inference, I guess, letters of credit). I'm reluctant to start talking about them because issuers don't think that rights to draw on such undertakings are freely transferable, so we'd have to talk a lot about the distinction between the right to draw and the right to the proceeds of the draw (and probably talk about the independence principle, too).

agreement, are triggered by default. (Note, however, that under Article 32, there are some circumstances in which a transferee may collect the receivable even before default.)

330. This Chapter, combined with the provisions of the transfer agreement referred to in paragraph 1(b) of this Article, provide the parties with a number of rights. Paragraph 2 makes it clear that all of those rights are available to parties except when the exercise of one right would negate the possibility of the exercise of another right.

331. Because many of the rights in this Chapter exist to protect transferors under security transfers, paragraph 3 assures that protection by providing that transferors, and any other person who owes performance of the secured obligation, may not waiver or vary their rights under this Chapter before default. Otherwise, transferees under security transfers could easily insist on such waivers or variations as a condition of extending credit, undermining the policies of the Chapter. The prohibition on such waivers or variations does not apply after default, however, because the transferee no longer has that sort of leverage inasmuch as credit has already been extended.

Article 33 — Collection of payment under a security transfer

1. After default, the transferee under a security transfer is entitled to collect the receivable at or after the time payment becomes due.

2. The transferee may exercise the right to collect under paragraph 1 before default if the transferor consents.

3. The transferee exercising the right to collect under paragraph 1 or 2 is also entitled to enforce any personal or property right that secures or supports payment of the receivable.

4. The right of the transferee to collect under paragraph 1 is subject to Articles 24 to 30.

332. Articles 33 and 34 provide the two primary methods for the transferee under a security transfer to be made whole after default of the transferor under the secured obligation – collection of the receivable and sale of the receivable.

333. Under this Article, the transferee under a security transfer may collect the receivable after default of the transferor or other obligor. Note, however, that the right of the transferee to collect the receivable does not accelerate the obligation of the debtor; rather, the transferee may collect the receivable only at or after the time at which payment is due. This is consistent with the principle of Article 24.

334. In addition, paragraph 2 provides that the transferee may also exercise its right to collect the receivable before default so long as this is agreed to by the transferor. This is a relatively common arrangement in many credit transactions, where payments made by debtors are directed to the transferee and credited to the transferor's obligation that is secured by the security transfer.

335. Paragraph 3 makes it clear that the transferor's entire package of rights against the debtor – not only the transferor's claim against the debtor for payment but also the benefit of personal and property rights securing or supporting the debtor's obligation – may be utilized by the transferee of a security transfer. "Personal rights" include guaranties and the like, while "property rights" refers to property that serves as collateral for the debtor's obligation.

336. Paragraph 4 makes it clear that the full range of principles provided in Articles 24-30 provide the debtor with protection against adverse impacts of a security transfer, just as the debtor receives that protection in the case of outright transfers.

Article 34 — Right of the transferee to sell a receivable

1. After default, the transferee under a security transfer is entitled to sell the receivable.

2. The transferee may select the method, manner, time, place and other aspects of the sale, including whether to sell receivables individually, in groups or all together.

3. The transferee must give notice of its intention to sell the receivable to:

(a) the transferor and any person who owes the obligation secured by the security transfer;

(b) any person with a right in the receivable that informs the transferee of that right in writing at least [the enacting State to specify a short period of time] before the notice is sent to the transferor; and

(c) any other transferee that registered a notice with respect to a transfer of the receivable at least [the enacting State to specify a short period of time] before the notice is sent to the transferor.

4. The notice must be given at least [the enacting State to specify a short period of time] before the sale takes place and must contain:

(a) a description of the receivable;

(b) a statement of the amount required at the time the notice is given to satisfy the obligation secured by the security transfer, including interest and the reasonable cost of enforcement;

(c) a statement that the transferor, any person who owes the obligation secured by the transfer or any other person with a right in the receivable is entitled to terminate the enforcement process by paying or otherwise performing the secured obligation in full, including the reasonable cost of enforcement, at any time before the earlier of the sale of the receivable or the entry by the transferee into an agreement for the sale of the receivable; and

(d) a statement of the date after which the receivable will be sold or, in the case of a public sale, the time, place and manner of the intended sale.

5. The notice must be in a language that is reasonably expected to inform the recipient about its contents. It is sufficient if a notice to the transferor is in the language of the transfer agreement.

6. The notice need not be given if the receivable is of a kind sold on a recognised market.

Comment:

337. In the case of a security transfer, after default of the transferor, the transferee may collect payment of the receivable as described in Article 33.

338. As an alternative to collecting the receivable, the transferee under a security transfer may sell the receivable. A transferee may choose to sell a receivable rather than collect payment of it for any one of a number of reasons. For example, the due date of the receivable may be far in the future, while the transferee would prefer to obtain value for it now rather than waiting for eventual payment. Also, the transferee might conclude that it has insufficient expertise to collect the receivable and that more value can be obtained for it by selling it to a party who can more easily and efficiently collect it.

339. Because the sale of a receivable that is the subject of a security transfer has an economic impact on the transferor (see Article 35 for the transferor's potential right to a surplus or liability for a deficiency), the transferee's right to sell the receivable is subject to the Article 4 duties of good faith and commercial reasonableness. Before default, neither the transferor, the debtor, or any other obligor bound to perform the secured obligation may unilaterally waive this standard of conduct or any of the rights conferred under this chapter. Pursuant to a policy aimed at maximizing flexibility and efficiency in the enforcement process, the transferee under a security transfer is given the choice to select the "method, manner, time, place and other aspects of the sale" (Art. 34 (2)).

340. The secured transferee´s right to sell a receivable, however, is subject to procedural safeguards. For example, the transferee must give advance written notice to the transferor and other interested parties listed in Article 34(3) of the transferee's intention to sell the receivable.

341. There is no need to give notice of the planned sale of the receivable if the receivable is of a kind sold on a "recognized market". In this context, a "recognized market" for receivables may point to an organized market in which large volumes of similar receivables are bought and sold, so that their prices are set by the market and not individually negotiated. Examples of such receivables include ... [examples to be supplied].

342. Of course, it is also the case that in an outright transfer of a receivable, the outright transferee, as owner of the receivable, may sell it. In that case, however, because the transferor retains no economic stake in the receivable, there is no need to provide notice to the transferor.

Article 35 — Distribution of the proceeds of collection or sale of a receivable and liability for any deficiency

1. If the transferee exercises the right provided in Article 33 or 34:

(a) [subject to Article 16,] the transferee must apply the proceeds of its collection or sale to the obligation secured by the transfer after deducting the reasonable cost of collection or sale;

(b) except as provided in paragraph 1(c), the transferee must pay any surplus to any subordinate competing claimant that, prior to any distribution of the surplus, notified the transferee of its claim, to the extent of the amount of that claim, and pay any balance remaining to the transferor; and

(c) whether or not there is any dispute as to the entitlement or priority of any competing claimant under this Law, the transferee may pay the surplus to a competent judicial or other authority or to a public deposit fund for distribution in accordance with this Article.

2. A person who owes the obligation secured by the security transfer remains liable for any amount owing after application of the net proceeds of collection or sale to the obligation secured by the transfer.

Comment:

343. In the case of a security transfer, paragraph 1 provides rules for the application and distribution of the proceeds upon collection or disposition of the receivables:

a. Proceeds of collection or sale must be applied first to the obligation secured by the receivable (after deducting reasonable costs of collection or sale) (Art. 35 (1) (a)).

b. If there is a surplus remaining after that application of proceeds, the transferee must pay the surplus to any lower-ranking claimant that notified the transferee of its claim and the amount. If a surplus remains after paying the amount of such claim of any subordinate claimant, the transferee must transfer that surplus to the transferor (Art. 35 (1) (b)).

c. If proceeds of sale or collection are insufficient to satisfy the obligation secured by the receivable, the transferor or any other person who owes the secured obligation remains liable for the deficiency (Art. 35 (2)).

344. As an alternative to paying any surplus pursuant to paragraph 1(b), the transferee may pay the surplus to a judicial or other authority or a "public deposit fund" the like for distribution in accordance with this chapter. This is particularly useful if there is a dispute as to which party is entitled to be paid any surplus, although the transferee may avail itself of this option whether or not there is any dispute as to who is entitled to be paid first (Art. 35 (1) (c)). Note the similarity of this provision to Article 26(8), which provides that a debtor may pay the amount owed on the receivable to a competent judicial or other authority or to a public deposit fund.

345. If the proceeds of collection or sale are insufficient to satisfy the secured obligation and the reasonable costs of the collection or sale, the person owing the obligation secured by the security transfer remains liable for the difference. As a result, it can be seen that the receivable that is the subject of the security transfer supplements the rights of the transferee to obtain satisfaction of the obligation but does not replace them.

CHAPTER VIII – CONFLICT OF LAWS

346. Factoring transactions can easily relate to more than one State (either because the debtor and transferor are in different states or because the transferor and transferee are in different states), raising the question of which State's law will govern issues that arise under those transactions. Indeed, because the subject of factoring transactions consists of intangible rights, cross-border transactions can take place easily and at low cost, increasing the possibility that multiple States will be implicated. When multiple States are involved, it is likely that the law in these States will not be identical in all respects. Even if all the relevant States have adopted legal rules based on the MLF, it is highly likely that their implementation of the MLF will differ in some respects. In addition, there will certainly be States that do not reform their legislation based on the MLF. As a result, a State that enacts legislation based on the MLF is well-advised to include clear rules to determine which State's law will apply to issues that arise in cross-border transactions.

347. While the need for conflict of laws rules is obvious when the laws of the relevant States differ in material respects, such rules will be needed even when the relevant States have both enacted legislation that tracks the MLF closely. This is because the MLF's rules governing third-party effectiveness and priority of the rights of transferees are based on registration in the governing State's registry. Thus, conflict of laws rules are needed not only for situations in which the laws of the relevant States differ materially but also because of the need to identify which State's registration regime is controlling.

348. Finally, conflict of laws rules play an additional important role in factoring transactions – establishing the extent to which the parties to the factoring transaction can agree on the State whose law will govern the transaction, whether or not those parties are in different states. For these reasons, the conflict of laws rules in this Chapter [based on the location of the debtor][125] are one of the MLF's seven core concepts.

349. The conflict of laws rules of the MLF are consistent with those in the Receivables Convention and those in the MLST. Thus, courts in States that adopt the MLF (as well as arbitral tribunals applying the conflict of laws rules of such a State) should reach the same decisions as to applicable law as would be the case applying the conflict of laws rules of States that adopt the broader reforms of the UNCITRAL Model Law on Secured Transactions.[126]

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[125] *Secretariat: Whether to include this additional bracketed language will depend on the WG's decision at WG3 regarding the core concepts in Part I(3).

[126] *NC: At WG2, MD suggested, and the WG agreed, that most references to consistency with the MLST should be deleted. Should we delete this paragraph?

Article 36 — Mutual rights and obligations of the transferor, transferee and debtor

1. The law applicable to the mutual rights and obligations of the transferor and the transferee arising from their transfer agreement is the law chosen by them and, in the absence of a choice of law, the law governing the transfer agreement.

2. The law applicable to:

(a) the mutual rights and obligations of the debtor and the transferee;

(b) the conditions under which the transfer may be invoked against the debtor, including whether a contractual limitation on the transferor's right to transfer the receivable may be asserted by the debtor; and

(c) whether the obligations of the debtor have been discharged,

is the law governing the rights and obligations between the debtor and the transferor.

Comment:

350. Article 36 addresses two related but distinct topics involving the law governing the rights of the transferee. First, paragraph 1 addresses the law applicable to the mutual rights and obligations of the transferor and the transferee arising from their transfer agreement. Second, paragraph 2 addresses three aspects of the relationship between the transferee and the debtor – the law governing the mutual obligations with respect to each other, the law governing whether the transferee has the right to seek payment from the debtor as an assignee, and the law governing discharge of the debtor's obligations.

351. Paragraph 1 addresses the law governing the rights between the transferor and transferee – two parties to a contract with each other. As a result, that paragraph provides a conflict of laws rule that reflects general principles governing the determination of the applicable law for contracts. The first clause of paragraph 1, deferring to the law chosen by the parties, draws from, and is consistent with, most modern treatments of party autonomy to select the law governing contractual relations. See, e.g., the HCCH Principles on Choice of Law in International Commercial Contracts. While most international factoring contracts will contain a choice-of-law clause, some do not. In that case, the law applicable to the rights and obligations between the parties is "the law governing the transfer agreement." This rule assures that whatever choice-of-law principles the forum State utilizes in determining the law applicable to commercial contracts, those principles will be applied to the mutual rights and obligation of the transferor and transferee arising from the transfer agreement. Approaches to the determination of applicable law in the absence of a choice-of-law agreement tend to vary from State to State with States typically taking into account a number of connecting factors.

352. Paragraph 2 addresses a different choice-of-law situation – the law governing rights and responsibilities running between two parties that do not have a direct contractual relation with each other. As a result, these issues cannot be resolved by application of general principles that determine the law governing contracts. Instead, paragraph 2 adopts a principle that is protective of the rights of the debtor – applying the same law that governed the relationship between the debtor and the transferor – to assure that the debtor is not disadvantaged by the transfer. Thus, paragraph 2(a) provides that the law governing the obligations of the debtor to the transferee, and the correlative rights of the transferee against the debtor, are governed by the same law that governs the rights and obligations between the debtor and the transferor. The same analysis applies to paragraph 2(c), under which the determination of whether the debtor has been discharged (e.g., by payment or as the legal result of a defence) is made by application of the same law that governs the rights and duties as between the debtor and the transferor. Thus, in both cases, the debtor suffers no loss of

legal rights as a result of the transfer. Paragraph 2(b) deals with a very specific issue – the law governing whether the obligations of the debtor, originally owed to the transferor, can be asserted by the transferee as a result of the transfer. These rules are drawn from, and are consistent with, Article 11(b) of the Hague Principles on Choice of Law in International Commercial Contracts (2015).

Article 37 — Effectiveness and priority of transfers

Except as provided in Article 38, the law applicable to the effectiveness and priority of a transfer of a receivable is the law of the State in which the transferor is located.

Comment:

353. Unlike Articles 35 - 36, which address issues that are largely contractual in nature, Article 37 deals with issues that are proprietary – whether the transferee has acquired a property interest in the receivable as a result of a transfer and the priority of the transferee's interest as against competing claimants. As a result, the choice-of law rules in this Article differ from those in Article 36(1). The reason is simple. The rules in Article 36(1) govern the bilateral relationship between two parties to a contract and their impact is on the parties to that contract. Proprietary issues, on the other hand, are rights against the world – not just parties to the contract – and need a single answer for the question of what law governs. After all, a system in which the relative priority of the rights of Transferee 1 against those of Transferee 2 is determined by a different State's law than that which determines the relative priority of Transferee 2 as against Transferee 1 would be incoherent and lead to inconsistent answers to what is essentially the same question.

354. Article 37 designates the State in which the transferor is located as the State under whose law these proprietary issues are measured. This makes sense inasmuch as the claims of subsequent claimants will have as their common source the transferor's original claim, and there is no physical connecting factor, such as the location of tangible goods or real estate, that could be utilized.

355. The importance of the rule in Article 37 cannot be overstated. Potential transferees will be deterred from entering into transfers of receivables if they cannot identify with certainty the State whose law governs the steps necessary to make the transfers effective against third parties and the priority of such transfers against potential competing claimants.

356. Article 37 should be read in conjunction with the articles that follow it. In particular, two Articles provide more detail as to the components of the rule in Article 37. Article 41 provides rules for determining the location of a transferor, and, in the case of a transferor that moves from State to State, Article 42 provides rules providing the time as of which the transferor's location is determined. In addition, Article 38 provides a limited exception to the rule of Article 37, applicable in certain cases in which the transferred receivable is secured by a right in immovable property; Article 39 sets out a choice-of-law rule to govern the enforcement of transfers.

Article 38 — Priority of transfers of receivables secured by a right in immovable property

Notwithstanding Article 37, in the case of a transfer of a receivable that is secured by a right in immovable property, the law applicable to the priority of the transfer of the receivable as against the right of a competing claimant that is registrable in the immovable property registry in which rights in the relevant immovable may be

registered is the law of the State under whose authority the immovable property registry is maintained.

Comment:

357. Article 38 provides a special choice-of-law rule for determining the priority of a transfer of a receivable in cases in which the transferred receivable is secured by a right in immovable property. In those cases, if the right of a competing claimant is registrable (but not necessarily registered) in the relevant immovable property registry of the State in which the immovable property is located, it is the State in which the immovable property is located and under whose law the immovable property registry is maintained that governs priority. This rule is provided as an exception to the general rule in Article 37. The rule is useful because, when a receivable is secured by a right in immovable property that is registrable in an immovable property registry, that registry is likely the first place a potential transferee will search to determine whether there are any competing claimants. This means, however, that, for such a potential transferee to be certain which State's law is applicable to the priority of a security right in a receivable, the potential transferee needs to determine whether the receivable is secured by immovable property. If the potential transferee is unaware of that fact, and the receivable arose in the circumstances described in this article, it runs the risk of making an inaccurate determination of which law governs. This, in turn, can lead to searching in the wrong State's registry and, as a result, failing to discover the claim of a competing claimant.

Article 39 — Enforcement of transfers

The law applicable to issues relating to the enforcement of a transfer of a receivable is the law applicable to the priority of the transfer.

Comment:

358. The term "enforcement of a transfer of a receivable" is drawn from the term "enforcement of a security interest" in the MLST. In the context of transfers of receivables, the term can cover two sets of rights of the transferee described in Chapter VII. First, in the case of a security transfer, the term can refer to the right of the transferee to sell the receivable after default by the transferor. See Article 34. Second, in both an outright transfer and a security transfer, the term can refer to the right of the transferee to collect the receivable. See Articles 31 and 33. In either case, the State whose law governs enforcement is the same State whose law govern priority of the transfer under Article 37 or 38. Thus, the creation, third-party effectiveness, priority and enforcement of a transfer of a receivable are governed by the law of the same State.

Article 40 — Proceeds

1. The law applicable to the effectiveness as between the transferor and the transferee of a transferee's right in proceeds is the law applicable to the effectiveness as between the transferor and the transferee of the transfer of the receivable from which the proceeds arose.

2. The law applicable to the third-party effectiveness and priority of a transferee's right in proceeds is the law applicable to the third-party effectiveness and priority of a right in an asset of the same kind as the proceeds.

Comment:

359. Like Articles 36 and 39 with respect to transfers and their enforcement, this article provides two rules governing different aspects of the law related to proceeds. Article 40(1) addresses the law applicable to right to proceeds of a transferred receivable as between the transferor and transferee, while Article 40(2) addresses the third-party effectiveness and priority of the transferee's right to proceeds.

360. Under Article 40(1), whether, as between the transferor and transferee, there has been an effective transfer of proceeds of a receivable is governed by the same law as that governs the effectiveness of the transfer of the original receivable between those parties. This enables the law governing effectiveness of the original transfer of the receivable and the law governing the effectiveness of a right in proceeds to be determined in tandem. This, in turn, avoids incongruities that might result from different bodies of law governing those two issues.

361. Article 40(2) proceeds under a different theory. Because the proceeds of a receivable are likely to be a different type of property than the original receivable (such as money, deposit accounts, etc.), Article 40(2) refers outward to "the law governing third-party effectiveness and priority of a right in an asset of the same kind as the proceeds." Note that this requires two steps to be taken by the forum court – characterization of type of asset represented by the proceeds and identification of its conflict of laws rules governing third-party effectiveness and priority of a right in that type of asset.

362. Note that Article 40 does not address situations in which a receivable that has been transferred is itself proceeds of property that is not a receivable (such as goods) and which is subject to a security interest. That matter is left to otherwise applicable conflict of laws principles.

Article 41 — Location of the transferor

For the purposes of this Chapter, the transferor is located:

(a) in the State in which it has its place of business;

(b) if the transferor has a place of business in more than one State, in the State in which the central administration of the transferor is exercised; and

(c) if the transferor does not have a place of business, in the State of the transferor's habitual residence.

Comment:

363. Determining the location of the transferor is critically important in factoring transactions under this law because it is the law of that location that is applicable to key issues under this law. The law of that location is the law that governs the effectiveness of a transfer of a receivable, the priority of that transfer as against the claims of competing claimants, and the enforcement of that transfer against the transferor. See Articles 37 and 39.

364. Article 41 contains two rules for determining the location of a transferor for purposes of this chapter – one for transferors that are engaged in business and have a place of business and another for transferors that are not engaged in business. In the case of transferors engaged in business, their location for purposes of this chapter is its place of business; if the transferor has more than one place of business, its location is in the State in which its central administration is exercised. Note that this fact-based test does not point to the transferor's statutory seat or place of incorporation if those are

not where the transferor's central administration is exercised. Transferors not engaged in business are located at their habitual residence. Note also that, while the location of a transferor under these rules will usually be obvious, there will be occasions in which factual judgments may be necessary. For example, in the case of a transferor that does business in many States, a factual determination is necessary to determine the State in which the transferor's central administration is exercised. Similarly, in the case of a transferor with no place of business but with multiple residences, a factual determination is necessary to determine which of those residences is the transferor's habitual residence.

Article 42 — Relevant time for determining location of the transferor

1. Except as provided in paragraph 2, references to the location of the transferor in this Chapter refer:

(a) for issues relating to the effectiveness of the transfer as between the transferor and the transferee, to the location of the transferor at the time of the putative creation of the transfer; and

(b) for third-party effectiveness and priority issues, to the location of the transferor at the time the issue arises.

2. If the right of a transferee in a receivable is made effective against the transferor and third parties and the rights of all competing claimants are established before a change in the location of the transferor, references in this Chapter to the location of the transferor are references, with respect to third-party effectiveness and priority issues, to the location prior to the change.

Comment:

365. The rules in Articles 37 and 39 determine the applicable law by reference to the State in which the transferor is located. But a transferor may be located in different States at different times. Transferors that have a place of business may change the State in which they have their place of business, or place of central administration, and transferors that do not have a place of business may change their habitual residence. Thus, conflict of laws rules, such as those in Articles 37 and 39 require a subsidiary rule that identifies the relevant time as of which the transferor's location is to be determined.

366. Article 42(1) provides such a subsidiary rule. This rule has two parts, with subparagraph (a) addressing effectiveness of the transfer as between the transferor and transferee and subparagraph (b) addressing third-party effectiveness and priority.. For issues related to the effectiveness of the transfer between the transferor and transferee, subparagraph (a) provides that the relevant time for determination of the transferor's location is the time of the putative creation of the transfer. Accordingly, parties to a transfer are well-advised to maintain records indicating the transferor's location at that time so that, if there is a later dispute about the effectiveness of the transfer, it will be clear which State's law governs that dispute. For issues of third-party effectiveness and priority, subparagraph (b) provides that the relevant time for determination of the transferor's location is the time that the issue arises. Thus, a change in the transferor's location after a transfer can result in a change in the law governing third-party effectiveness and priority, issues of key importance to the transferee. Accordingly, transferees might wish to monitor the location of the transferor even after the transfer in order to be aware of any changes.

Article 43 — Exclusion of *renvoi*

A reference in this Chapter to the law of a State as the law applicable to an issue refers to the law in force in that State other than its rules of private international law.

Comment:

367. Article 43 makes it clear that, when the conflict of laws rules of this chapter direct the forum to apply the law of another State, the direction is to apply the substantive law of that State (the "referral State") other than the referral State's conflict of laws rules. This rule, common in most conflict of laws contexts, rejects the doctrine of "renvoi," under which a forum court would examine not only the substantive law of the referral State but also that State's conflict of laws rules to see if the referral State, based on its conflict of laws rules, would apply the law of a different State. Because renvoi can lead to complexity or even circularity (if, for a particular issue, State A's conflict of laws rules direct a State A forum to apply the law of State B while the conflict of laws rules of State B refer the matter to the law of State A), Article 43, like most conflict of laws instruments, reject renvoi in the interest of simplicity and predictability.

Article 44 — Overriding mandatory rules and public policy

1. The provisions of this Chapter do not prevent a court from applying overriding mandatory provisions of the law of the forum that apply irrespective of the law applicable under the provisions of this Chapter.

2. The law of the forum determines when a court may or must apply or take into account overriding mandatory provisions of another law.

3. A court may exclude the application of a provision of the law applicable under the provisions of this Chapter only if and to the extent that the result of its application would be manifestly incompatible with fundamental notions of public policy of the forum.

4. The law of the forum determines when a court may or must apply or take into account the public policy of a State other than the State the law of which would be applicable under the provisions of this Chapter.

5. This Article does not prevent an arbitral tribunal from applying or taking into account public policy, or from applying or taking into account overriding mandatory provisions of a law other than the law applicable under the provisions of this Chapter, if the arbitral tribunal is required or entitled to do so.

6. This Article does not permit a court to displace the provisions of this Chapter dealing with the law applicable to the third-party effectiveness and priority of a transfer.

Comment:

368. Conflict of laws rules typically contain a narrow exception that allows a forum State to decline to give effect to the law of another State when the law of that State contravenes certain fundamental norms. This Article, adapted from the HCCH Principles on Choice of Law in International Commercial Contracts ("the HCCH Principles") and from Article 93 of the MLST, is a manifestation of that exception tailored to address the factoring context. It is similar to such exceptions in the conflict of laws doctrines of most States.

369. The exception provided by Article 44 has two aspects. First, under paragraph 1, a court may apply "overriding mandatory provisions" of the law of its State (provisions that reflect a policy of the State is so strong as to justify a conclusion that it must be applied, notwithstanding the otherwise-applicable choice of law rule that would require application of foreign law). The explanation in the paragraph 11.16 of the Commentary to the HCCH Principles is instructive in this regard. Second, under paragraph 3, a court may decline to apply the law of a different State if application of that law would be "manifestly incompatible with fundamental notions of public policy of the forum." Here, the focus is not on the necessity of applying a forum State rule but, rather, on avoiding an offensive law of the other State. The bar is quite high here. This paragraph does not authorize a forum to decline to apply the law of a foreign State merely because the foreign State has made a different policy decision. Rather the forum State's policy must be a fundamental one and the foreign State's law must be "manifestly incompatible" with that policy. (It should be noted that, although the sort of exceptions provided by Article 44 are found in the conflict of laws doctrines of most States, not all States draw a formal distinction between the aspects indicated in paragraphs 1 and 3 and simply refer to both of them under the rubric of "fundamental public policy" or the like.) Paragraphs 2 and 4 are present here to reflect the practice in some States to examine not only the overriding mandatory provisions and fundamental policies of the forum state but also those of another State, such as the State whose law would govern in the absence of a choice by the parties, such as provided in Article 36.

370. Paragraph 6 provides that the exception provided by paragraphs 1 and 2 does not apply to the choice-of-law rules that determine the law applicable to third-party effectiveness and priority. This approach is justified by the need to achieve certainty with respect to the law applicable to third-party effectiveness and priority.

371. Paragraph 5 reflects the fact that, in the sphere of international commercial arbitration, somewhat different choice-of-law practices are often available. For example, in some circumstances, an arbitral tribunal might be required to take into account public policy or overriding mandatory provisions or another law. This article requires the tribunal to "consider the legal framework within which its decision making processes are conducted, having regard (in particular) to the agreement of the parties, the designated or deemed seat of the arbitration, any institutional rules applicable to the arbitration, and the potentially controlling influence of State courts applying local arbitration legislation."

Article 45 — Effect of insolvency proceedings on the law applicable to a transfer

The commencement of insolvency proceedings in respect of the transferor does not displace the law applicable to a transfer under this Chapter.

Comment:

372. Under the rule in Article 45, and insolvency tribunal in a State that enacts the MLF should, as a general matter, apply the law designated in this chapter to matters concerning the transfer of receivables. That does not preclude such a tribunal from applying the law of the State under whose laws the insolvency proceedings have been commenced (lex fori concursus) to matters related to the insolvency proceedings, such as laws governing the avoidance of fraudulent or preferential transfers, the ranking of claims, and the distribution of proceeds.

Article 46 — Multi-unit States

If the law applicable to an issue is the law of a State that comprises one or more territorial units each of which has its own rules of law in respect of that issue:

(a) any reference in this Chapter to the law of a State means the law in force in the relevant territorial unit; and

(b) the internal conflict-of-laws rules of that State, or in the absence of such rules, of that territorial unit determine the territorial unit whose substantive law is to apply.

Comment:

373. Some States are composed of territorial units that have the power to determine their own rules with respect to some matters. For example, Canada has 10 provinces, each of which has the power to enact its own rules governing factoring transactions. The question then arises as to what is meant when the conflict of laws rules of the MLF direct a forum to apply the law of Canada. Article 46 resolves this question with a two-part rule. First, Article 46(a) treats the territorial units as States in their own right, so that, for example, when a conflict of laws rule directs a forum to apply the law of Canada, the rule should be applied so as to refer to the relevant province. So, for example, if the issue is the priority of the transfer of a receivable as against competing claimants, for which Article XX directs a forum to apply the law of the transferor's location, the reference in Article 46(a) for a transferor located in Ontario, Canada would be to the priority law of Ontario.

374. The second part of the rule of Article 46 is found in paragraph (b). Under paragraph (b), the forum is directed to follow the conflict of laws rules of the State or of the territorial unit referred to in paragraph (a) if those rules would direct a court to apply the law of a different territorial unit. [more elaboration to be inserted here].

CHAPTER IX – TRANSITION

375. Enactment of the MLF will result in the replacement of an enacting state's prior law that governs factoring transactions with a new body of law that may differ from the prior law in many respects. Whenever such a legal reform is embarked upon, it is important to have clear rules governing the process of transition from the previous legal regime to the new one. When, as here, the subject of the legal reform relates to transactions that may operate over a long period of time, many transactions may start when the prior law is in effect and continue under the new legal regime. In those cases, it is particularly important to have clear and sensible rules governing when prior law ceases to govern those transaction and they become governed by the rules of the new law.

376. The transition rules in this Chapter address three issues that must be resolved in order to have a successful transition from the prior legal regime to the regime embodied by the MLF. Those issues are:

a. Determining the date on which the new law enters into force;
b. Indicating which existing laws and doctrines are repealed or amended by the new factoring law; and
c. Delineating the circumstances in which former law continues to apply to some transactions and disputes that pre-date the entry into force of the new law.

Article 47 — Entry into force of this Law

This Law enters into force [on the date or according to the mechanism to be specified by the enacting State].

Comment:

377. Article 47 states the date on which the new factoring law enters into force. It leaves selection of that date to the legislator, rather than recommending a uniform effective date or period after enactment before the law becomes effective.

378. States are advised to resist the temptation to have the new law enter into force on the date of its enactment or only a short period of time thereafter. This is because:

a. It will take time to educate stakeholders about the enactment and effect of the new factoring law;
b. Parties that engage in factoring transactions will need time to adjust their transactional methods to the new rules; and
c. It will take time to design and implement the registry.

The enacting State, therefore, should set the date on which the new law enters into force at some reasonable period after the law is enacted.

379. On the other hand, excessive delay before the entry into force of the new law should be avoided as well. After all, the MLF is an economic statute, designed to bring about a beneficial effect on an enacting state's economy. Delaying the entry into force longer than necessary to accommodate the concerns listed in paragraph [375] will also delay the onset of those economic benefits.

Article 48 — Amendment and repeal of other laws

[1. [The enacting State to specify relevant laws] are repealed.]

[2. [The enacting State to specify relevant laws] are amended as follows [the enacting State to specify relevant amendments].]

Comment:

380. Legislation based on the MLF is intended to replace a law or laws that previously addressed the same issues, so the new law should repeal aspects of prior law that would be governed by a provision in MLF. Depending on the legal system of the enacting state, this could mean repeal of a comprehensive body of legislation that previously governed factoring transactions covered by the MLF. In some States, however, legislation governing such transactions may be scattered throughout the state's statutes. Paragraph 1 is presented with two sets of brackets. The outer brackets indicate that a State should enact paragraph 1 only if there are relevant laws of that State to repeal. The inner brackets indicate the place at which a State should designate the laws to repeal.

381. In some situations, an existing statute may govern not only factoring transactions within the scope of the new law but also other sorts of transactions. In those cases, that former law should not be repealed in its entirety but, rather, should be amended so as not to apply to transactions within the scope of the new law. The outer brackets indicate that a State should enact paragraph 2 only if there are relevant laws of that State to amend. The first set of inner brackets indicates the place at which a State should designate the laws to amend, and the second set of inner brackets provides a place for the enacting State to describe the amendments.

382. In many civil law jurisdictions, a new factoring law may implicate legal provisions and transactions governed by other laws, such as those governing the assignment of rights, assignment of contracts, "pledge of credits", etc. The enacting State may be required to amend those provisions to the extent it is needed to adapt their terminology with the terms introduced by the new factoring law. The location of this amendment and its formulation may depend on whether the new factoring law is enacted as a stand-alone statute or incorporated into a title, section, or chapter of a civil or commercial code.

383. In many common law jurisdictions, many or most of the legal rules governing factoring transactions are not found in statutes but, rather, in the decisions of courts. For those rules, there is no statute to repeal, yet it must be made clear that the enactment of the MLF pre-empts application of the court-made rules.

384. It should be noted that even repealed or amended prior law will remain relevant after the entry into force of the new law to govern situations described in Articles 50-54.

Article 49 — General applicability of this Law

1. For the purposes of this Chapter:

(a) "prior law" means the law applicable under the conflict-of-laws rules of [the enacting State] that applied to prior transfers immediately before the entry into force of this Law; and

(b) "prior transfer" means a right created by an agreement entered into before the entry into force of this Law that is a transfer within the meaning of this Law and to which this Law would have applied if it had been in force when the right was created.

2. Except as otherwise provided in this Chapter, this Law applies to all transfers, including prior transfers within its scope.

Comment:

385. Many transition rules for new legislation that apply in other contexts are quite simple. They state that the new law applies only to transactions entered into after the date on which the new law enters into force and that the old law does not apply to transactions entered into after that date. The transition rules in this chapter do not, however, follow that simple model. This is largely because factoring transactions often take place over a period of time, and thus may start under the prior legal regime with an initial agreement to transfer receivables, and continue with (i) one or more transfers of receivables that may take place before or after the date on which the new law enters into force, (ii) collection from obligors on the receivables before or after that date, and (iii) conflict with the rights of completing claimants whose rights may have arisen before or after that date. The result is a system where sometimes it is important to apply rules from the prior legal system to some issues even after the date on which the new law enters into force and other times it is important to apply the rules of the new legal system even to some actions that occurred before that date.

386. The result of this complexity of circumstances is a somewhat complex set of transition rules. Rather than starting with a simple rule that the new law applies only to transactions entered into after the date on which the new law enters into force, Article 49 starts with the opposite presumption – that the new factoring law applies to all transfers of receivables, both those entered into before the entry into force of the new law and those entered into afterward unless a transition rule provides to the contrary. See Article 49(2). Notwithstanding this presumption, which is presented in this form partly for ease of drafting, the exceptions provided in this Chapter result in a set of rules that are largely consistent with traditional transition rules except for those that address conflicts between interests arising before the entry into force of the new law and those that arise only after that date. The goal of the presumption and its exceptions is to protect settled expectations yet obtain benefits of new law as soon as possible. It should be noted that the definitions of "prior law" and "prior transfer" are nuanced. "Prior transfer" includes all rights created by agreement before date on which the new law enters into force that would constitute a transfer (as defined in Article 2(j)) under the new law, whether or not denominated as transfers under the previous legal regime. "Prior law" refers to the law that would have been applied by the courts of the enacting State to a particular transfer (as defined in Article 2(j)). Because, under the conflict of laws rules of the previous legal regime, the courts of the enacting state may have applied the law of a different State to a prior transfer, the definition of "prior law" takes that possibility into account.

Article 50 — Applicability of prior law to matters that are the subject of proceedings commenced before the entry into force of this Law

1. Subject to paragraph 2, prior law applies to a matter that is the subject of proceedings before a court or arbitral tribunal commenced before the entry into force of this Law.

2. If any step has been taken to collect a receivable or enforce a prior transfer before the entry into force of this Law, collection or enforcement may continue under prior law or may proceed under this Law.

Comment:

387. Article 50 provides the first two exceptions to the presumption stated in Article 49 that the new factoring law applies to all transfers, whether entered into before or after the date on which the

law enters into force. Article 50 (1) provides that, subject to paragraph (2), prior law applies to a matter that is already the subject of arbitral or judicial proceedings before that date. This is justified by a policy of freezing the rules applicable to a dispute once judicial or arbitral proceedings have commenced. It would be anomalous if legislation that went into effect only in the middle of a lawsuit changed the set of legal rules applicable to the dispute that is the subject of the lawsuit.

388. Article 50(2) provides two important qualifications to the exception in Article 50(1) from the general rule in Article 49(2). First, if steps have been taken by the transferee before the entry into force of the new factoring law to enforce a transfer, the transferee may continue to enforce under the prior law or may proceed under the new law. Second, if steps have been taken by the transferee to collect a receivable before the entry into force of the new factoring law, the transferee may continue to collect under the prior law or may proceed under the new law. While stated separately, "collection" and "enforcement" both spring from enforcement as described in Chapter VII. In the case of outright transfers, enforcement of the transfer consists of collection of payment from the obligor. By way of contrast, in the case of a security transfer, enforcement of the transfer upon the default of the transferor can consist of either collection of payment from the debtor or disposition of receivable by the transferee.

389. In keeping with a general policy of balancing the advantages of immediate application of the new law with the protection of existing rights, the transferee is thus given an option as to how to pursue pending enforcement rights, either continuing the enforcement or collection proceedings under prior law or commencing proceedings under the new law.

Article 51 — Applicability of prior law to effectiveness of a prior transfer between the parties

1. Prior law determines whether a prior transfer is effective between the parties.

2. A prior transfer remains effective between the parties even if it would not otherwise be effective between the parties under this Law.

Comment:

390. Article 51, which addresses only effectiveness of a transfer between the parties, provides stability for transfers that occurred before the entry into force of the new law. By indicating that prior law determines whether a transfer entered into before that date is effective between the parties to the transfer, it sets out an exception to general applicability of the new law to prior transfers under article 49, paragraph 2. Paragraph 2 confirms that a prior transfer that was effectively created under prior law remains effective between the parties after the new law enters into force even if the requirements for creation under the new law are not satisfied. This approach avoids the retroactive invalidation of prior transfers that were made in conformity with the law applicable to them when they were created. It also dispenses with the need for the transferee to obtain the cooperation of the transferor to take whatever additional steps may be necessary to conform to the requirements of the new law for an effective transfer. After all, such cooperation may not be forthcoming from a transferor that has already received all the value promised in exchange for the transferred receivable.

391. There is no parallel rule under which transfer entered into before the entry into force of the new law that was not effective between the parties under former law, but which satisfies the requirements for effectiveness under the new law, becomes effective on the date on which the new law enters into force. There is no policy promoting stability of results suggesting that a such a transfer should become effective when the new law enters into force.

Article 52 — Transitional rules for determining the third-party effectiveness of a prior transfer

1. A prior transfer that was effective against third parties under prior law at the time this Law entered into force continues to be effective against third parties under this Law until the earlier of:

(a) the time it would have ceased to be effective against third parties under prior law; and

(b) the expiration of [the enacting State to specify a period of time] after the entry into force of this Law.

2. If the third-party effectiveness requirements of this Law are satisfied before the third-party effectiveness of a prior transfer ceases in accordance with paragraph 1, the prior transfer continues to be effective against third parties under this Law from the time when it was made effective against third parties under prior law.

3. If the third-party effectiveness requirements of this Law are not satisfied before the third-party effectiveness of a prior transfer ceases in accordance with paragraph 1, the prior transfer is effective against third parties only from the time it is made effective against third parties under this Law.

4. A written agreement between a transferor and a transferee for a prior transfer is sufficient to constitute authorisation by the transferor for the registration of a notice covering the receivables described in that agreement under this Law.

[5. Subject to paragraph 6, if a prior transfer continues to be effective against third parties under this Law pursuant to paragraph 2, the time of third-party effectiveness under prior law is the time to be used for the purposes of applying the priority rules of this Law that refer to the time of registration of a notice relating to a transfer.]

[6. If a prior transfer that continues to be effective against third parties under this Law pursuant to paragraph 2 was made effective against third parties under prior law by the registration of a notice, the time of registration under that law is the time to be used for the purpose of applying the priority rules of this Law that refer to the time of registration of a notice relating to a transfer.]

Comment:

392. Article 52 provides a balance between stability of rights acquired against third parties under the prior legal regime and the benefits brought about by the adoption of the new factoring law, requiring publicly accessible registration of transfers in order to obtain third party effectiveness.

393. According to Art. 52(1), a transfer that is made effective against third parties under prior law by a method that would not suffice for third-party effectiveness under the new law continues to be effective for only a short period after the entry into force of the new law (until the earlier of the events delineated in subparagraphs (a) and (b) of Article 52(1) (the "grace period")). In order to obtain third-party effectiveness for such a transfer under the new law for periods after the expiration of the grace period, the transferee must take the actions necessary for third-party effectiveness under the new law. If the transferee satisfies those requirements for third-party effectiveness before

the expiration of the grace period, the transfer is treated as having been effective against third parties continuously since that status was obtained under prior law. See paragraph (2). If the transferee satisfies the requirements for third-party effectiveness under the new law only after expiration of the grace period, the transfer that pre-dates the entry into force of the new law is treated as being effective against third parties only from the time it was made effective against third parties under the new law.

394. Because authorisation for the registration of a notice is required by the new law, and a transferor who has already received payment for a receivable might refuse to provide that authorization after the entry into force of the new law, Article 52(4) indicates that a written agreement for a prior transfer suffices to constitute authorization required for registration under the new law.

395. Paragraphs (5) and (6) provide the nexus between third-party effectiveness achieved through this transition mechanism and the rules governing priority by specifying which date is to be used for purposes of the priority rule in Article 13(1). In situations in which the transfer was made effective against third parties under prior law by a method other than registration of a notice (such as by notification to the debtor), paragraph (5) augments the first-to-register rule of Article 13(1) by providing that the time of third-party effectiveness under prior law is to be treated as the time of registration under Article 13(1). If, on the other hand, the transfer was made effective against third parties under prior law by registration of a notice, paragraph (6) indicates that the time of registration under prior law is to be treated as the time of registration under Article 13(1). For purposes of paragraph 6, a prior transfer was made effective against third parties under prior law by registration even if, as is the case under the new law, in a transaction in which a notice is registered before the transfer is made, the transfer is not effective against third parties until it is made.

Article 53 — Applicability of prior law to the priority of a prior transfer as against the rights of competing claimants arising under prior law

1. The priority of a prior transfer as against the rights of a competing claimant is determined by prior law if:

(a) the transfer was made and the rights of all competing claimants arose before the entry into force of this Law; and

(b) the priority status of neither the prior transfer nor the rights of any of the competing claimants has changed since the entry into force of this Law.

2. For the purposes of paragraph 1(b), the priority status of a prior transfer has changed only if:

(a) it was effective against third parties when this Law entered into force but ceased to be effective against third parties; or

(b) it was not effective against third parties under prior law when this Law entered into force, and only became effective against third parties under this Law.

Comment:

396. The general rule of Article 49(2) makes the priority rules of the new factoring law applicable even to prior transfers unless an exception applies. One set of exception is provided in Article 52, which provides special rules about application of the elements of priority under the new factoring law. Article 53 provides a second exception to this general rule. In essence, Article 53 provides that, when

a transfer was made and a competing claim arose before the entry into force of the new law, the rank ordering of the transfer as against the competing claim should not be changed solely by the onset of the new law so long as there has been no change (other than that onset) in the factors that determine priority. So, for example, if two competing transfers were each effective against third parties under prior law and remained effective against third parties under the new law, their priority as against each other, as established under former law, will not change under the new law.

397. Under Article 53(1), prior law determines priority as between a transferee and competing claimant whose rights arose before the entry into force of the new law and as long as their "priority status" (as defined in Article 53(2)) has not changed since that . The priority status of a transfer changes only if it was effective against third parties under prior law but is not effective against third parties under the new law or vice versa.

398. Example: Assume that, according to the law in force in before the entry into force of the new law, transfers of receivables were effective against third parties when the debtor was notified of the transfer and priority as between competing transferees of the same receivable was determined according to the order in which the debtor was notified of each transfer. Assume further that, before the enactment and entry into force of the new law, TR transferred the same receivables to TE1 and then subsequently to TE2 but that TE2 notified the debtors on those receivables before TE1 did so, so that the claim of TE2 would have priority over that of TE1 under prior law. Subsequently, the new law was enacted and entered into force, and no other events (such as registration of a notice by either transferee) occur that would have an effect on priority. If a dispute arises before the expiration of the grace period under Article 52(a) and (b), application of Article 53 results in TE2's claim having priority over that of TE1. This is because that would be the case under the prior law and the priority status of neither claim has changed since the effective date.

399. If Article 53(1) does not apply, the priority rules of new law are applicable, even if one or more of the competing claims relate to transactions entered into before the entry into force of the new law. Example: Assume that, according to the law in force in before the entry into force of the new law, transfers of receivables were effective against third parties when the debtor was notified of the transfer and priority as between competing transferees of the same receivable was determined according to the order in which the debtor was notified of each transfer. Assume further that, before the enactment and entry into force of the new law, TR transferred the same receivables to TE1 and then subsequently to TE2 but that TE2 notified the debtors on those receivables before TE1 did so, so that the claim of TE2 would have priority over that of TE1 under prior law. Subsequently, the new law was enacted and entered into force. Before the expiration of the Article 52 grace period, TE1 registers a notice under the new law but TE2 does not do so, with the result that the transfer to TE2 ceased to be effective against third parties upon the expiration of the grace period. Two weeks after the expiration of the grace period, TE2 registers a notice under the new law. The priority status of the transfer to TE2 has changed because it was effective against third parties under prior law when the new law went into force and, thus, continued to be effective against third parties temporarily under the new law under Article 52, but ceased to be effective against third parties under the new law when the grace period expired. Because the priority status of one of the two competing transfers has changed, Article 53(1) does not apply and priority between the competing transfers is determined under Article 13(1) by the order of registration of notices relating to those transfers

Article 54 — Transitional rules for the rights and obligations of the debtor

If a contract giving rise to a receivable was entered into before the entry into force of this Law, the following matters are determined by the law applicable under the conflict-of-laws rules of [the enacting State] that applied immediately before the entry into force of this Law:

(a) Article 8(2);

(b) Article 25;

(c) Article 26;

(d) Article 27;

(e) Article 28;

(f) Article 29;

(g) Article 30; and

(h) Article 31.

Comment:

400. Under Article 54, when a receivable was created before the entry into force of the new law, the effectiveness of the new law does not change the rights and obligations of the debtor that appear in the listed Articles. Otherwise, the rights of debtors would be changed by a law that they could not have predicted would govern their rights. Thus, Article 54 can be seen as a corollary to Chapter VI, Section 2.

401. The reference to conflict-of-laws rules is needed because the law that governs the various rights and obligations of the debtor may not have been the law of the forum, particularly as a result of the party autonomy to select applicable law that is generally provided to parties to a contract under the conflict-of-laws rules of most States. Thus, stability of transactions requires that the reference here not be to the prior law of the forum but, rather, to the law that governed under the conflict of laws rules of the forum that were applicable before the entry into force of the new law, even if the new law implements different conflict of laws rules than were in effect before that date.

PART IV

ANNEXE A — REGISTRY PROVISIONS

Introduction

402. The registration system that is to be established under the Law, the rules for which are set out in Annexe A, lies at the very heart of the Law's operation. It serves three main purposes:

a. It provides a transferee of a receivable with a mechanism that they can use to make the transfer effective against third parties, by registering a notice in relation to the receivable with the Registry.[127]

b. It provides a mechanism for resolving priority disputes where a person transfers the same receivable to more than one transferee.

c. It provides transparency to third parties, by making it possible for anyone to search the public registry record – for example, where someone who is thinking of acquiring rights in a receivable from a person, they can search the registry record to determine whether that person may have already transferred the receivable to someone else.

403. The Registry system[128] allows for the registration of all types of transfers of receivables that are subject to the Law – that is, both outright transfers and transfers by way of security.

404. Traditional registry systems were paper-based, with information being submitted to the registry operator in paper form and then transcribed by registry staff into a physical record. More recent systems store information electronically rather than in a physical record, but still allow or require information to be submitted in paper form, with the information then being entered into the electronic record by registry staff.

405. Paper-based registry systems such as these can be slow, expensive and prone to error. For these reasons, paper-based systems are no longer considered to be good practice for modern registries.

406. Consistent with this, the provisions in Annexe A are drafted in the expectation that the Registry system under the Law will be fully electronic, and accessible only electronically – either through the Registry website, or by means of another electronic user interface that is made available by the Registry. Access should be available to any person who satisfies the conditions for access set out by the Registry in accordance with clause 5 (discussed in paragraphs XXX] below).

407. Unlike many traditional registries such as land registries, the registry record under the Law is not a record of actual property interests, or of transaction documents. Instead, the registry record is a database of notices, each lodged by or on behalf of a transferee against the name or other identifier of a transferor, that records the fact that the transferee may have taken (or in the future may take) a transfer of the receivables described in the notice from the transferor. If a searcher is considering acquiring rights in a receivable from a transferor, it can search the registry record to see whether the registry record contains any notices relating to that receivable. This can alert the

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[127] *BW: At WG2, it was said that we should distinguish consistently between the "Registry" (as the entity that runs the registry system), the "registrar" (the person who heads up the Registry) and the "registry record" (the information). I have endeavoured to do this. However, the Law itself doesn't seem to distinguish between the terms in the same way. In particular, art 2(h) defines the "Registry" to be the registration system, not the entity that manages it. How should we respond to this?

[128] *BW: I have used this term a bit in the discussion of Annexe A, because it is a convenient way of capturing the entirety of it all.

searcher to the fact that the transferor may not be able to give the searcher the rights in the receivable that it is wanting to acquire.

408. As the notices submitted to the Registry do not of themselves create property rights or even serve as evidence that property rights exist, there is no need for the notices to be vetted by Registry staff before they are uploaded into the registry record. Instead, if a registrant submits a properly-completed notice and pays the required fee (if any), the notice should be uploaded into the registry record almost immediately after it is submitted, without any intervention by Registry staff. It should then immediately become available for searching. This greatly enhances the reliability of the registry record, both by ensuring that it is up to date and by removing the risk of inaccuracies as a result of human error at the Registry.

409. Because the registration process is fully electronic and automatic, there is also no need to limit Registry operating hours to business hours in the place of the Registry. Instead, the Registry system should be available for both registrations and searches 24 hours a day and 365 days a year, apart from scheduled outages for maintenance or upgrades.

Further information

410. A number of publications can provide more information regarding the establishment and operation of registries such as the Registry system under the Law. For example, see:

a. [WBG publications from 2010 and 2019;][129]

b. UNIDROIT's Guide on Best Practices for Electronic Collateral Registries, available at https://www.unidroit.org/guide-on-best-practices-for-electronic-collateral-registries/; and

c. UNCITRAL's Guide on the Implementation of a Security Rights Registry, available at https://uncitral.un.org/en/texts/securityinterests/legislativeguides/security_rights_registry.

It should be noted, however, that these Guides address registry systems for fully-fledged secured transactions laws, and contain information that is not relevant to the more limited Registry system under the Law. It should also be noted that the UNCITRAL Guide was produced over a decade ago, and in some respects no longer represents modern best practice.[130]

Placement of the Annexe

411. The provisions in Annexe A have been drafted on the assumption that they would be included in the body of the Law, as Annexe A. Some States may prefer instead to enact the material in Annexe A in a separate Regulation or other legislative instrument. If a State takes this approach, however, it will need to ensure that the provisions of the separate Regulation or other instrument come into force at the same time as the Law itself, as allowing them to come into force at different times could create confusion and legal uncertainty.

[129] *BW: The WG has not yet come to a decision on whether or not to refer here to the WBG publications.

[130] *BW: It was suggested at WG2 that we should include a caution along these lines. Secretariat: Perhaps we should put the caution in a footnote instead?

A. GENERAL RULES[131]

Clause 1(a) — Address

For the purposes of this Annexe:

(a) "Address" means:

(i) a physical address or a post office box number, city, postal code and State; or

(ii) an electronic address.

Comment:

412. An initial notice must include the address of both the transferor and transferee. See clause 7, discussed in paragraphs [XXX] below.

Clause 1(b) — Amendment notice

For the purposes of this Annexe:

…

(b) "Amendment notice" means a notice submitted to the Registry to modify information contained in a registered notice.

Comment:

413. As its name suggests, an amendment notice is used to amend information in a notice that is already in the public registry record. The information that needs to be included in an amendment notice, and the manner in which it is to be submitted to the Registry, are set out in Parts C and D of Annexe A, and are discussed in paragraphs [XXX] below.

Clause 1(c) — Cancellation notice

For the purposes of this Annexe:

…

(c) "Cancellation notice" means a notice submitted to the Registry to cancel the effectiveness of a registered notice.

[131] BW: In the previous draft, we did not provide specific comments for each definition, but just noted compendiously that they were discussed in the context of the clauses in which they are used. It was pointed out though (by LG, I think) that this had the result, for some terms, that we didn't get around to explaining them until after we had already used them a few times. So I thought I would try this layout instead, and see what the WG thinks. There was also a suggestion that we should acknowledge that these terms derive in large part from the UNCITRAL Registry Guide. That's a bit harder to do in this format (without being repetitive). I also wonder whether we really need to say that - , the terms also come from the MLST, and we already acknowledge, somewhere earlier in the GtE, the extent to which the whole Law is modelled on that instrument.

Comment:

414. As its name suggests, a cancellation notice is used to cancel the registration of an initial notice and any associated amendment notices. Cancellation will remove those notices from the public registry record, so that they will no longer be discoverable by a search.[132] The information that needs to be included in an amendment notice, and the manner in which it is to be submitted to the Registry, are set out in Parts C and D of Annexe A, and are discussed in paragraphs [XXX] below.

Clause 1(d) — Designated field

For the purposes of this Annexe:

...

(d) "Designated field" means a field in a form available through the Registry's electronic user interface that is designated for entering a specified type of information.

Comment:

415. Clause 7 states that an initial notice must include specific types of information. Clause 13 sets out a corresponding rule for amendment notices. The forms that the Registry is to make available for each of these types of notice will need to identify specific fields into which each of these types of information is to be inserted. This is to ensure that the Registry software will then be able to collate and store the information in a systematic manner, so that it is reliably able to retrieve the information in response to a search. See the discussion of clauses 7 and 13 in paragraphs [XXX] below.

Clause 1(e) — Initial notice

For the purposes of this Annexe:

...

(e) "Initial notice" means a notice submitted to the Registry to achieve the third-party effectiveness of the transfer of a receivable to which the notice relates.

Comment:

416. Initial notices are the most important type of notice under the Registry system. As the text of the definition states, the primary purpose of an initial notice is to achieve the third-party effectiveness of a transfer of receivables to which the notice relates (f article 9, discussed in paragraphs [XXX] above). The order in which initial notices are registered is also relevant in the event of a priority dispute (article 13, discussed in paragraphs [XXX] above).

417. The information that needs to be included in an initial notice, and the manner in which it is to be submitted to the Registry, are set out in Part C of Annexe A, and are discussed in paragraphs [XXX] below.

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[132] *BW: Should we say "standard search" here? As I mention below in relation to clause 16, the Registry system will need to allow searches of the archive as well, even though Annexe A is silent on the point.

Clause 1(f) — Notice

For the purposes of this Annexe:

…

(f) "Notice" means an initial notice, an amendment notice and a cancellation notice.

Comment:

418. This definition is self-explanatory.

Clause 1(g) — Public registry record

For the purposes of this Annexe:

…

(g) "Public registry record" means that part of the registry record that is publicly accessible.

Comment:

419. The Registry system will need to retain a record of every transaction that affects the registry record, for the period of time required by clause 21(3) (see the discussion in paragraph [XXX] below). However, some of the information that is stored by the Registry system should not be available for routine searching by the public. As an example, a standard search of the Registry system should reveal only current registrations, not registrations that have been cancelled. The Annexe uses the term "public registry record" rather than "registry record" where it is necessary to draw this distinction.

Clause 1(h) — Registered notice

For the purposes of this Annexe:

…

(h) "Registered notice" means a notice the information in which has been entered into the registry record.

Comment:

420. The information that needs to be included in a notice, and the manner in which it is to be submitted to the Registry, are set out in Parts C and D of Annexe A, and are discussed in paragraphs [XXX] below. In a properly-designed Registry system, a notice that has been completed and submitted correctly should upload automatically and immediately into the registry record. At this point it becomes a registered notice, and available for search.

Clause 1(i) — Registrant

For the purposes of this Annexe:

…

(i) "Registrant" means a person who submits a notice to the Registry.

Comment:

421. Notices will usually be submitted to the Registry be the transferee. In some cases, however, they may be submitted on the transferor's behalf by a third party, such as the transferee's financial or legal advisers or a third-party service provider that specialises in interfacing with the Registry system on behalf of its customers..

Clause 1(j) — Registration

For the purposes of this Annexe:

…

(j) "Registration" means the entry of information contained in a notice into the registry record.

Comment:

422. The Registry system software should be designed so that the information in a properly completed and submitted notice is uploaded immediately and automatically into the registry record, without any checking or manual intervention by Registry staff.

Clause 1(k) — Registration number

For the purposes of this Annexe:

…

(k) "Registration number" means the unique number assigned to an initial notice by the Registry and permanently associated with that notice and any related notice.

Comment:

423. Each time an initial notice is entered into the registry record, the Registry system must assign it a unique identification number. That number then needs to be included in any amendment notice relating to the initial notice (see clause 13, discussed in paragraphs XXX] below). This allows the amendment notice to be linked to the initial notice in the Registry database in such a way that they will both be provided in a search result.

424. The registration number for an initial notice also needs to be included in a cancellation notice. This ensures that the correct initial notice is cancelled.

Clause 1(l) — Registry record

For the purposes of this Annexe:

…

(l) "Registry record" means the information in all registered notices stored by the Registry.

Comment:

425. This term is self-explanatory.

Clause 2 — Transferor's authorisation for registration

1. Registration of an initial notice is ineffective unless authorised by the transferor in writing.

2. Registration of an amendment notice that adds receivables or extends the period of effectiveness of the registration of a notice is ineffective unless authorised by the transferor in writing.

3. Registration of an amendment notice that adds a transferor is ineffective unless authorised by the additional transferor in writing.

4. Authorisation may be given before or after the registration of an initial or amendment notice.

5. A written transfer agreement is sufficient to constitute authorisation by the transferor for the registration of an initial or amendment notice covering a receivable described in that transfer agreement.

Comment:

426. Clause 2(1) protects transferors by providing that a registration of an initial notice will be ineffective if is not authorised in writing by the transferor. Clauses 2(2) and (3) similarly protect transferors, by providing that certain types of amendment notices will also be ineffective if they are not authorised in the same way. (Other types of amendment notices do not require transferor consent, because they will be of a more administrative nature.)

427. It would be good practice for a registrant to obtain the transferor's authorisation before it makes a registration. This is not essential, however, as clause 2(4) allows a transferee to register first and then obtain the transferor's consent later. If a transferee makes a registration without having first obtained the transferor's consent, though, then the registration will be ineffective, even though it appears in the registry record, until it has in fact been authorised. If a registration is made without the transferor's authorisation and the transferor does not want to authorise it, then the transferor can require that it be removed, under clause 14. See the discussion in paragraphs [XXX] below.

428. A transferor and transferee may have already entered into a written transfer agreement in relation to a receivable before a notice is submitted to the Registry. In that case, that agreement will be taken to provide the necessary authorisation, and the transferee does not need to get a separate written authorisation as well. In the same way, if a written transfer agreement is entered into after the notice is registered, then this will also be sufficient to authorise the (previously unauthorised) registration.

429. Because the Law allows a registrant to submit a notice to the Registry before it has obtained the transferor's consent, a registrant does not need to provide evidence of the transferor's consent as part of the registration

Clause 3 — One notice sufficient for multiple transfers

The registration of a single notice may relate to transfers under one or more than one transfer agreement.

Comment:

430. As explained in the Introduction to this Part IV of the Guide (see paragraph [XXX] above), the Registry system does not record actual transfers of receivables, but only notices that alert searchers to the fact that the receivables identified in the notice may have been (or in the future may be) transferred by the transferor to the transferee. For this reason, it is not necessary to register a separate notice for individual transfers, or even for individual transfer agreements, in order to make the transfers effective against third parties - one notice can achieve this for all transfers of all the receivables that it describes, whether they are transferred under just one transfer agreement, or several. This greatly simplifies the registration processes for transferees.

Clause 4 — Advance registration

A notice may be registered before a transfer or the entry into of a transfer agreement to which the notice relates.

Comment:

431. Traditional registries typically record property interests, or dealings in property interests. In these registries, it is necessarily the case that notices can only be registered in relation to a dealing after the dealing has taken place. Because the Registry system under the Law is a record of notices about actual or potential transfers, however, and not a record of the transfers themselves, there is no reason why registrations should only be able to be made after the relevant transaction has taken place. Indeed, it can be valuable for a transferee to be able to register a notice in relation to a transaction before the transaction closes, as this allows the transferee to fix its priority position ahead of committing its funding (see the discussion of article 8 in paragraphs [XXX]). Clause 4 accommodates this, by allowing a transferee to register an initial notice in advance of any transfer taking place. (The transferor is protected, however, by the fact that the notice will not be effective unless the transferor has authorised it in writing – see clause 2, discussed in paragraphs [XXX] above).

432. This flexibility is particularly important for factoring transactions. For example, it is common for businesses to finance their working capital needs by selling their receivables to a financier on an ongoing basis. Clauses 3 and 4, working together, facilitate this, by allowing one initial notice to cover multiple transfers, and by allowing that initial notice to cover transfers that are to be made in the future.

B. ACCESS TO REGISTRY SERVICES

Clause 5 — Conditions for access to registry services

1. Any person may submit a notice to the Registry, if that person:

(a) uses the form made available for that purpose through the Registry's electronic user interface;

(b) identifies itself in the manner specified by the Registry; and

(c) has paid or arranged to pay the prescribed fee.

2. A person may submit an amendment or cancellation notice if that person also satisfies the secure access requirements specified by the Registry.

3. Any person may submit a search request to the Registry if that person:

(a) uses the form made available for that purpose through the Registry's electronic user interface; and

(b) has paid or arranged to pay the prescribed fee.

Comment:

433. Any person can be a transferee of a receivable under the Law. For this reason, clause 5(1) establishes the important principle that any person may submit notices to the Registry, once they satisfy the requirements set out in the clause.

434. The experience in other jurisdictions with registry systems that are similar to the Registry system under the Law is that the risk of abuse of this flexibility is low, and that most registrations are made for proper purposes. If an unauthorised registration is made against a transferor for inappropriate reasons, however, it will not be effective (see clause 2, discussed in paragraphs [XXX] above), and the transferor will be able to require that the registration be removed (see clause 14, discussed in paragraphs [XXX] below).

435. In practice, the Registry may require a person to establish an account[133] with the Registry, and to satisfy some basic identification requirements, before they are able to register notices. Any such requirements should be kept as simple as possible, however, so that all transferees are able as a practical matter to access the Registry system.

436. Once a person has set up their account with the Registry (or satisfied any other identification requirements specified by the Registry), they can submit notices to the Registry, through their account, by:

a. completing a form that the Registry makes available through its website or other electronic user interface; and
b. paying (or arranging to pay) the relevant fee.[134]

437. Clause 5(2) recognises that the Registry system will need to include safeguards to limit the risk that an initial notice might be amended or cancelled without the transferee's consent. Commonly, this is achieved by requiring that any amendment notices or cancellation notices be submitted through the transferee's account, and by providing the transferee, at the time of registration of the initial notice, with a security code that will need also to be entered before the notice may be amended or cancelled.[135]

438. Clause 5(3) confirms that any person should be able to search the public registry record. A search does not change the contents of the registry record, but simply prompts the Registry to produce a report of information that is already contained in the public registry record. For this reason, a searcher is not required to set up an account or provide evidence of their identity. Any person may submit a search to the Registry, as long as they use the form that is accessible through the Registry's website or other electronic user interface, and they pay (or arrange to pay) the search fee (if any).

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133 *BW: At the previous WG meeting, we touched on whether we should say this, but I'm not sure that we reached a conclusion.

134 *BW: Should we cross-refer to a supporting publication for more detail, eg about the "arranging to pay" option?

135 *BW: Again, should we cross-refer to another publication for more detail?

Clause 6 — Acceptance of the registration of a notice or a search request

1. The Registry must not permit the registration of:

(a) a notice if no information is entered in one of the mandatory designated fields; or

(b) an amendment notice to extend the period of effectiveness of the registration of a notice if it is not submitted within the period referred to in clause 12(2).

2. The Registry must not accept a search request if no information is entered in one of the fields designated for entering a search criterion.

Comment:

439. Clause 6(1)(a) has the effect that notices may only be uploaded into the registry record if all the mandatory fields are filled in. This means, for example, that an initial notice will only be registered if information has been included in all the fields listed in clause 7. This rule is required because the functionality of the Registry system would be compromised if it were possible to register notices with incomplete information.

440. Clause 6(2) sets out a corresponding rule for searches.

441. Clause 6(1)(b) relates to clause 12(2). That clause allows the period of effectiveness of an initial notice to be extended through the registration of an amendment notice, as long as the notice is submitted within the period specified in that clause. Clause 6(1)(b) supports this by providing that the Registry software must only allow an amendment notice under clause 12(2) to be uploaded into the registry record if it is submitted within that period.

C. REGISTRATION OF A NOTICE

Clause 7 — Information required in an initial notice

An initial notice must contain the following information in the relevant designated field:

(a) the identifier and address of the transferor in accordance with clause 8;

(b) the identifier and address of the transferee or its representative in accordance with clause 9;

(c) a description of the receivables in accordance with clause 10; and

(d) the period of effectiveness of the registration in accordance with clause 12.

Comment:

442. Clause 7 sets out the information that needs be included an initial notice. Each item of information needs to be inserted into the relevant designated field. The details of what is required are set out in clauses 8 to 12.

443. The consequences of completing the information incorrectly are set out in clause 18.

444. Clauses 7(a) and (b) cross-refer to clauses 8 and 9 for the information to be included for the identifier and address of the transferor and transferee, respectively. In fact, clauses 8 and 9 provide rules in relation to the transferor and transferee's identifiers, but are silent as to what needs to be included in relation to their addresses. Each enacting State will need to develop its own rules for addresses, and ensure that the design of the form of initial notice will give effect to them.

445. The template form of initial notice will need to be made available by the Registry through its website or other electronic user interface. Importantly, the form should be made available in a format that automatically uploads correctly-completed forms directly into the registry record, without manual intervention by Registry staff. This maximises the integrity of the information in the registry record, and removes the risk that the Registry might be liable for staff errors.

Clause 8 — Transferor's identifier

1. Where the person to be identified in an initial or amendment notice as the transferor is a natural person, the transferor's identifier is [the enacting State to specify the name or other identifier of that person] as it appears in [the enacting State to specify the relevant official document].

[2. If the enacting State specifies more than one document under paragraph 1, it should designate the order in which each document should be used to determine that person's name or other identifier.]

3. Where the person to be identified in an initial or amendment notice as the transferor is a legal person, the transferor's identifier is [the enacting State to specify the name or other identifier of that person] as it appears in or is determined by [the enacting State to specify the relevant document, law or decree].

[4. The enacting State should specify which components of the transferor's name or other identifier determined in accordance with paragraphs 1 and 3 must be entered in an initial or amendment notice.]

[5. The enacting State should specify the manner in which the transferor's name or other identifier is determined if the name or other identifier is legally changed after the issuance of the relevant document, law or decree referred to in paragraphs 1,2 or 3.]

Comment:

446. Clause 8 is one of the most important provisions in the Registry rules, and needs to be completed by each enacting State with great care. Notices are indexed in the registry record against the transferor's name or other identifier, and searchers use a transferor's name or other identifier when conducting searches. If the Registry system is to operate properly and achieve its objectives, the rules for correctly identifying a transferor need to be clear, unambiguous and comprehensive.

447. Much of the text in clause 8 is in square brackets. This does not mean that the text is optional. Rather, this recognises that an enacting State will need to develop rules for these matters that reflect its domestic circumstances, and complete the text of clause 8 accordingly.

448. Clause 8 contemplates that there will be separate rules for natural person transferors on the one hand, and legal person transferors (e.g. companies) on the other. Where the transferor is a

natural person, clause 8(1) provides that the transferor's identifier is its name or other identifier as it appears in an official document. The enacting State needs to complete clause 8(1) to say whether the transferor's name (or some other identifier) is to be used, and which official document (eg driver's licence, State-issued identity card or birth certificate) is to be the authoritative source. If it is necessary to refer to more than one official document to ensure comprehensive coverage of all potential natural-person transferors, then the enacting State should use clause 8(2) to list them in order of authoritativeness.

449. Similarly, where the transferor is a legal person, clause 8(3) provides that that the transferor's identifier is the name or other identifier of the legal person as it appears in the relevant document, law or decree. The enacting State will need to specify, for each type of legal person, whether the identifier is to be its name or some other identifier (such as its registration number, if it has one), and the document, law or decree that is to be the authoritative source of that information. (It was not thought necessary to include a version of clause 8(2) for legal person transferors, because in their case there should only be one authoritative source of the information.)

450. It is possible that a transferor could change its name or other identifier after a registration is made. If a person searches the Registry at a later time using the new name or other identifier, the searcher may not find registrations that were made before the change. Clause 8(5) notes that an enacting State will need to include a rule to address this.[136]

Clause 9 — Transferee's identifier

1. Where the person to be identified in an initial or amendment notice as the transferee is a natural person, the transferee's identifier is [the enacting State to specify the name or other identifier of that person] as it appears in [the enacting State to specify the relevant official document].

[2. If the enacting State specifies more than one document under paragraph 1, it should designate the order in which each document should be used to determine that person's name or other identifier.]

3. Where the person to be identified in an initial or amendment notice as the transferee is a legal person, the transferee's identifier is [the enacting State to specify the name or other identifier of that person] as it appears in or is determined by [the enacting State to specify the relevant document, law or decree].

Comment:

451. An initial notice will also need to identify the transferee, so that it is clear who is to benefit from the registration. Similar to clause 8, an enacting State will need to complete clause 9 in a manner that is consistent with its domestic circumstances.

452. The rules for identifying transferees can be the same as the rules for identifying transferors (see the discussion of clause 8, above). Indeed, it would streamline the Registry system for users if this were the case. There are two ways, however, in which the rules for transferees are (or need to be) different.

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[136] *BW: Do we want to provide any guidance on the options? I'm not sure whether many enacting States will know by themselves how to respond to this.

a. Article 37 has the effect that the Law as adopted by an enacting State will only apply to a transfer of a receivable where the transferor is located in that State (see paragraphs [XXX] above). This means that the rules for identifying transferors only need to accommodate transferors of types found in the State. It is possible, however, that a transferee might be a natural person or legal entity that is located outside the State. This means that enacting States will need to ensure that the rules for identifying transferees are comprehensive enough to include not just natural persons or legal entities that are located within the enacting State, but also legal persons or legal entities that are located outside the enacting State as well.

b. It is not possible to search the Registry against the name of the transferee (only the name of the transferor). For this reason, it is not as important that the Law precisely specify the required elements of a transferee's name or other identifier, or that it deal with a situation where a transferee changes its name or other identifier after the registration is made. For this reason, clause 9 does not contain an equivalent of clauses 8(4) and (5).

Clause 10 — Description of receivables

1. The receivables must be described in an initial or amendment notice in a manner that reasonably allows their identification.

2. A description that indicates that the receivables consist of all of the transferor's receivables, or of all of the transferor's receivables within a generic category, satisfies the standard in paragraph 1.

Comment:

453. A registration can only be effective in relation to the receivables that are described in it. The description will usually be in an initial notice, but may also be added by an amendment notice that is submitted under clause 13 (see paragraphs [XXX] below).[137]

454. Receivables may be described in a notice in many ways. If so desired, the notice can describe each invoice individually (eg by invoice number, if that is sufficient to reasonably allow its identification). However, the description may also be more generic, as long as it reasonably allows the receivables to be identified.

455. The text of clause 10 mirrors the rule in article 5(2)(c) for the description of receivables in a transfer agreement, and it can simplify the registration process for transferees if they use the same description in both. However, it is not necessary to use the same description, and indeed in some situations it may not be possible. For example, clause 3 allows one notice to relate to transfers under more than one transfer agreement, and in that situation the description in the registration will need to be broader that the description in any one of the transfer agreements.

456. Clause 10(2) confirms, as an example of this principle, that a description will be sufficient if it refers to all of the transferor's receivables, or to all of the transferor's receivables within a generic category (such as "all receivables owing to the transferor" or "all receivables owing to the transferor by ABC Limited").

[137] *BW: It was suggested at the last WG meeting that we should cross-refer here to clause 18 . However, we mention clause 18 in the discussion of clause 7, and if we mention it again here then we should probably mention it in the discussion of clause 8 as well. I'm happy either way.

457. It should be remembered that the rules in the Law apply only to "receivables" as defined in the Law (see the discussion of article 2(g) in paragraphs [XXX] above). If the description in a notice is written in a way that also encompasses payment obligations that are not "receivables" as so defined, then the notice will have no legal effect (at least for the purposes of the Law) in relation to those other payment obligations. It can only make a transfer effective against third parties if the transfer is of a receivable.

Clause 11 — Time of effectiveness of the registration of a notice

1. The registration of an initial or amendment notice is effective from the date and time when the information in the notice is entered into the registry record so that it is accessible to searchers of the public registry record.

2. The registration of a cancellation notice is effective from the date and time when the information in the notice to which it relates is no longer accessible to searchers of the public registry record.

Comment:

458. Under Chapter 5 of the Law, the priority of one transfer of a receivable as against other transfers of the receivable, or as against judgment creditors, will turn on the time of registration of the transferee's notice.

459. Clause 11 states that the registration of an initial or amendment notice in the public registry record is effective from the date and time that it becomes available to searchers, rather than when the registrant submits the registration. This ensures that a person who searches the public registry record can be confident that they can rely on the information they obtain from the search.

460. The Registry system should be configured so that properly-submitted notices are uploaded automatically into the public registry record and so become available for search almost immediately after they are submitted to the Registry. This means that there should be little or no difference between the two times, in practice.

461. The same principle applies for cancellation notices. A cancellation notice takes effect when the information in the notice that it relates to is no longer available for search, rather than when the notice is submitted to the Registry. Again, in a well-designed electronic registry system, a correctly-submitted cancellation notice should result in an almost-immediate removal of the affected registration from the public registry record, so there should in practice be no difference between the two times.

Clause 12 — Period of effectiveness of the registration of a notice

1. The registration of an initial notice is effective for the period of time indicated by the registrant in the designated field of the notice, not exceeding [the enacting State to specify a maximum period of time].

2. The period of effectiveness of the registration of an initial notice may be extended within [the enacting State to specify a period of time] before its expiry by the registration of an amendment notice that indicates in the designated field a new period not exceeding the maximum period of time referred to in paragraph 1.

3. The period of effectiveness of the registration of an initial notice may be extended more than once.

4. The registration of an amendment notice in accordance with paragraph 2 extends the period of effectiveness for the period specified in the amendment notice beginning from the time when the current period would have expired if the amendment notice had not been registered.

Comment:

462. In a State that adopts the Law and is successful in developing a factoring market, it is likely that the public registry record will quickly accumulate many registrations. While it is important to ensure that registrations can remain on the public registry record for as long as they are needed, it is also important to not allow registrations to remain for longer than necessary in the public registry record, as this would complicate search results by forcing searchers to review registrations that are out-of-date, to determine whether they are still relevant.

463. Clause 12 strikes a balance between the needs of transferees and searchers. It starts by providing in clause 12(1) that a registration of an initial notice will be valid for the period of time specified by the registrant in the notice, but only up to a cap. Each enacting State can set its own cap, by inserting the relevant period of time (eg five years) in the clause, in place of the text in square brackets.

464. Clauses 12(2) to (4) then allow a transferee to extend the term of its registration beyond the cap set in clause 12(1), should it wish to do so, by submitting an appropriate amendment notice to the Registry before the current registration term ends. Each enacting State will need to decide how far in advance it is prepared to allow transferees to submit an amendment notice to extend the term of a registration (eg six months), and should then insert that period in clause 12(2) in place of the text in square brackets.

D. REGISTRATION OF AN AMENDMENT OR CANCELLATION NOTICE

Comment:

465. Part D of the Annexe sets out some specific rules for amendment notices and cancellation notices. An amendment notice amends the content of a registration that is already in the public registry record, but otherwise leaves the registration intact. The information that needs to be included in an amendment notice is set out in clause 13(1). In contrast, a cancellation notice does not amend a registration, but instead removes both the initial notice and any associated amendment notices from the public registry record entirely.

466. As a cancellation notice removes a registration from the public registry record rather than amend it, the only item of information that needs to be included in the notice should be the registration number of the initial notice that is to be cancelled.

467. As with initial notices (see clause 7, discussed in paragraphs [XXX] above), the template form of amendment notice and cancellation notice should be made available by the Registry through its website or other electronic user interface. Similarly, the forms should be made available in a format that automatically uploads correctly-completed forms directly into the registry record, without manual intervention by Registry staff.

468. A person wanting to submit an amendment notice or cancellation notice will also need to satisfy any secure access requirements that are imposed by the Registry – see clause 5, discussed in paragraphs [XXX] above.

Clause 13 — Information required in an amendment notice

1. An amendment notice must contain in the relevant designated field:

(a) the registration number of the initial notice to which it relates; and

(b) the information to be added or changed.

2. An amendment notice may modify one or more than one item of information in the registered notice to which it relates.

Comment:

469. Amendment notices should be submitted by completing the fields in the form of amendment notice provided by the Registry. An amendment notice does not need to restate all the information provided in the initial notice, but instead simply needs to set out the registration number of the initial notice that is being amended (so that the amendment notice can be linked to the initial notice in the registry record), and the information being added or changed. Linking the amendment notice with the initial notice will ensure that the documents will be retrieved together by a search of the registry record.

Clause 14 — Compulsory registration of an amendment or cancellation notice

1. The transferee must register an amendment notice deleting receivables from a description of receivables in a registered notice if:

(a) the transferor has not authorised the registration of a notice in relation to those receivables and the transferee has been informed by the transferor that it will not authorise that registration;

(b) the transferor authorised the registration of a notice covering those receivables but the authorisation has been withdrawn and no transfer agreement covering those receivables has been entered into; or

(c) the transfer agreement to which the registered notice relates has been revised to remove those receivables from the transfer agreement and the transferor has not otherwise authorised the registration of a notice covering those receivables.

2. The transferee must register a cancellation notice if:

(a) the registration of the initial notice was not authorised by the transferor and the transferee has been informed by the transferor that it will not authorise the registration of the initial notice;

(b) the transferor authorised the registration of the initial notice but the authorisation has been withdrawn and no transfer agreement has been entered into; or

(c) all receivables to which the initial and any amendment notice relate have been paid in full or have been transferred back to

the transferor or, in the case of a security transfer of a receivable, that security transfer has been extinguished.

3. The transferee may not charge or accept a fee or expense for complying with its obligation in accordance with paragraph 1(a), 1(b), 2(a) or 2(b).

4. If the conditions set out in paragraph 1 or 2 have been met, the transferor may request the transferee in writing, reasonably identifying itself and the related initial notice, to register the appropriate amendment or cancellation notice. The transferee may not charge or accept any fee or expense for complying with the transferor's request.

5. If the transferee does not comply with the transferor's request made in accordance with paragraph 4 within [the enacting State to specify a short period of time] after its receipt, the transferor may seek an order for the registration of an amendment or cancellation notice through [the enacting State to specify a summary judicial or administrative procedure].

6. Where an order for the registration of an amendment or cancellation notice is issued in accordance with paragraph 5, the Registry must register the notice without delay upon receipt of a request with a copy of the relevant order.

Comment:

470. The Registry system allows a transferee to register a notice unilaterally, without the involvement of the person who is designated in the notice as being the transferor. Transferors are protected from the consequences of unauthorised registrations, however, by clause 2 (discussed in paragraphs [XXX] above), which states that a registration is not effective, even if it appears in the public registry record, if it has not been authorised in writing by the transferor.

471. Clause 14 provides transferors with an important additional protection. It requires a transferee to amend or cancel a notice to the extent that it is not authorised. The situations in which this could arise are set out in clauses 14(1) and (2). Clause 14(3) then states that the transferee may not charge the transferor a fee for submitting the amendment or cancellation notice if the registration was never authorised, or if it was authorised but the transaction never proceeded.

472. A transferee must submit the amendment or cancellation notice on its own initiative. If it does not do this, however, the transferor may require the transferee to do so, under clause 14(4). In this case, the transferee may not charge a fee in any circumstances.

473. Finally, if a transferee does not comply with a request from the transferor within a short period of time, the transferor may take legal proceedings against the transferee to have the registration amended or removed. An enacting State will need to complete clause 14(5) by specifying what the short period of time is to be (eg 14 days). The enacting State will also need to complete clause 14(5) by identifying a suitable summary judicial or administrative procedure that transferors can use for this purpose. If a suitable summary procedure does not already exist in the enacting State, the State should consider introducing one that is appropriate for this purpose.[138]

[138] *BW: To be discussed, in the context of the Best Practices for Effective Enforcement project

Clause 15 — Effectiveness of the registration of an amendment or cancellation notice not authorised by the transferee

The registration of an amendment or cancellation notice is effective regardless of whether it is authorised by the transferee.

Comment:

474. It is important for the integrity of the Registry system that searchers be able to rely on the accuracy and legal effect of search results. For this reason, clause 15 states that an amendment or cancellation notice that is entered into the registry record is effective whether or not it was authorised by the transferee. This enhances reliability of the registry record for searchers, such as prospective transferees.

475. Each enacting State's Registry system will need to include procedural safeguards that protect transferees against the risk of registration of unauthorised amendment or cancellation notices – see the discussion of clause 5(2) in paragraphs [XXX] above. Transferees should also implement internal protocols to enhance their protection - for example, by limiting access to their Registry accounts, and through the careful storage of any passcodes or other security information that is provided by the Registry as part of the registration process.

E. SEARCHES

Clause 16 — Search criteria

A search of the public registry record may be conducted according to:

(a) the identifier of a transferor; or

(b) the registration number of an initial notice.

Comment:

476. Clause 5(3) sets out the important principle that the public registry record[139] may be searched by anyone who wishes to do so. Clause 16 sets out the ways in which searches may be conducted.

477. In almost all cases, searchers will search the public registry record against a transferor's identifier. The rules that determine the correct identifier for searches are the same as the rules for making registrations, set out in clause 9 (see paragraphs [XXX] above).

478. Clause 7 requires the registrant of an initial notice to include both the transferor's identifier and the transferor's address in the registration. When making a search, however, a searcher need only insert the transferor's identifier. The transferor's address will then appear in the search result. Should more than one transferor have the same identifier (whether this is possible will depend on the rules for identifying transferors that an enacting State develops under clause 8), the addresses shown in the search result may help the searcher to determine which of the transferors (if any) is relevant to the purpose of their search.

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[139] *BW: We don't say anything at the moment about searches of the archive (eg where a priority dispute has arisen between historical transfers). Should we?

479. A search against the registration number of an initial notice will usually only be undertaken by the transferee of that notice. This is because the transferee will usually be the only person who has this number. These types of searches are unlikely to be common.

Clause 17 — Search results

1. Upon receipt of a search request, the Registry must provide a search result that indicates the date and time when the search was performed and:

(a) sets out all information in each registered notice that contains information matching the search criterion; or

(b) indicates that no registered notice contains information matching the search criterion.

2. A search result that purports to have been issued by the Registry is proof of its contents in the absence of evidence to the contrary.

Comment:

480. Clause 17 describes the information that is to be provided in a search result.

481. A well-designed Registry system should be able to produce a search result almost immediately after the search is made. For example, the search result could appear directly to the searcher's screen, in a downloadable format. [In the case of a search against a transferor's identifier, the search result should either set out all the information that was contained in any notice that had been registered against that identifier (including any associated amendment notices), or state that there are no registrations against that identifier.][140]

482. Clause 17(2) states that a search result provided by the Registry is prima facie proof of its contents. This means that a search result should itself be acceptable in legal proceedings as evidence of the information that it contains.

F. ERRORS AND POST-REGISTRATION CHANGES

Clause 18 — Registrant errors in required information

1. An error in the transferor's identifier entered in an initial or amendment notice does not render the registration of the notice ineffective if the information in the notice would be retrieved by a search of the public registry record using the transferor's correct identifier as the search criterion.

2. An error in information required to be entered in an initial or amendment notice other than the transferor's identifier does not render the registration of the notice ineffective unless the error would seriously mislead a reasonable searcher.

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[140] *BW: It was suggested at WG2 that we provide some examples here, rather than just parrot the text of the clause. That raises a question for me: Are we expecting that the search result will simply be a copy of the initial notice(s) together with any amendment notices, so that the searcher themself needs to work out what the current position is? Or will the Registry software produce a "current composite" of the registration, by updating the initial notice (so to speak) each time an amendment notice is submitted?

Comment:

483. Clause 6(1) states that the Registry must only permit the registration of a notice if information has been included in all the mandatory designated fields. If a notice contains information in all the mandatory designated fields and the registrant has complied with the access requirements in clause 5, then the notice should be automatically uploaded into the public registry record, without any checking or other intervention by Registry staff.

484. Even though a notice will only appear in the public registry record if all its mandatory designated fields have been completed, it does not necessarily follow that all the information provided in the notice will be correct. Clause 18 explains whether an initial notice or an amendment notice can still be effective even if it contains an error. (The only information in a cancellation notice is the registration number of the initial notice being cancelled, so it was not necessary to extend clause 18 to cancellation notices as well.)

485. Clause 18(1) states that an error in the transferor's identifier will not invalidate the registration if a search using the correct identifier would still retrieve the notice. If the error is such that a searcher would not find the notice, however, then it will be invalid.

486. To give an example, assume that the identifier for a company is its 8-digit registration number (eg 12345678). A registrant registers an initial notice that accidentally inserts a blank space into the transferor's number (eg 1234 5678), even though the correct number has no space in it. This error is unlikely to render the registration invalid, because search algorithms typically ignore blank spaces. However, the result would be different if the registrant accidentally transposed two of the digits (eg 21345678), as the search algorithm is unlikely to associate this number with the correct one. It is likely that an error of this type would indeed render the notice invalid.[141]

487. Clause 18(2) says that an error in other information that is required to be included will only invalidate the registration if the error would seriously mislead a reasonable searcher. To give another example, if a transferee takes a transfer of a receivable owed by Ignacio Tirado, but in the description of the receivables instead inserts "Ignacio Tisado", this error might invalidate the notice (eg if the transferor has separate customers with each of these names). Whether it does, however, is a question of fact that would need to be looked at in light of the particular circumstances.[142]

Clause 19 — Post-registration change of transferor's identifier

1. Subject to paragraph 2, the third-party effectiveness and priority of a transfer that is effective against third parties by registration of a notice are not affected by a change in the identifier of the transferor after the notice is registered.

2. If the identifier of the transferor changes after a notice is registered, a competing transfer made by the transferor that is made effective against third parties after the change has priority over the transfer to which the notice relates, unless an amendment notice disclosing the new identifier of the transferor is registered:

[141] *BW: I have a recollection that we discussed developing a consistent format for examples. I can reshape this in due course, as needed.

[142] *BW: I fully accept that this example will not survive the editing process. That doesn't stop me from putting it in the draft, though!

(a) before the expiry of [the enacting State to specify a short period of time] after the change; or

(b) after the expiry of the period referred to in paragraph 2(a) but before the competing transfer is made effective against third parties.

Comment:

488. A transferor's identifier may change after an initial notice is registered against them. In this situation a transferee that registered an initial notice against the transferor's old name will want to know whether it needs to take any action to preserve the third-party effectiveness of its transfer after the name change.

489. Clause 19 explains what happens in this situation.

490. The general principle is set out in clause 19(1). It states that a notice that was registered against the transferor's old identifier will continue to be valid despite the change of identifier.

491. This provides valuable protection for the transferee that registered before the change. However, it has the potential to produce unfair outcomes for future transferees. If a potential future transferee is not aware that the transferor has changed its identifier, then it will only know to search against the transferor's new one. This means that it will not discover the first transferee's registration, even though that registration continues to be valid and will in principle have priority under article 13.

492. Clause 19(2) modifies the operation of clause 19(1) to deal with this. It provides, broadly, that the first transferee will lose the priority that it would otherwise have, unless it registers an amendment notice within a specified grace period to update the transferor's identifier in its registration (so that a person searching against the new identifier will now be able to discover the registration). Paragraphs (a) and (b) set out the grace period in which the first transferee needs to do this. An enacting State will need to decide what an appropriate grace period is in the context of its domestic circumstances (eg 90 days), and insert that period into paragraph (a) in place of the text in square brackets.

493. As a practical matter, one effect of this clause is that transferees will need to monitor their customers on a regular basis, so that they can become aware of any relevant change to the customer's identifier so that they can update their registrations before the end of the grace period.

494. It should be noted that a transferee may still register an amendment notice, even the grace period in paragraphs (a) and (b) has expired. However, it will lose priority to a competing transfer that was made effective against third parties after the change but before the amendment notice was registered.

495. It should also be noted that clause 19(2) only affects a transfer's priority as against later transfers. The transfer will continue to be effective against third parties, and will retain its priority as against all other competing claimants, such as judgment creditors (see article 17, discussed in paragraphs [XXX] above).

G. ORGANISATION OF THE REGISTRY AND THE REGISTRY RECORD

Clause 20 — The registrar

The [the enacting State to specify the appropriate authority] has the power to appoint and dismiss the registrar, and to determine the registrar's duties and monitor their performance.

Comment:

496. Article 2(h) of the MLF states that the Registry is to be established by an authority chosen for this purpose by the enacting State (e.g. its central bank).[143]

497. Clause 20 allows an enacting State to specify which authority is to be responsible for appointing and supervising the registrar (i.e. the individual who is to be in charge of Registry operations). Logically, this authority should be the same as the authority specified in article 2(h). [Cross-refer to other relevant literature?]

Clause 21 — Integrity of information in the registry record

1. Except as provided in clauses 22 and 23,[144] the Registry may not amend or remove information contained in a registered notice from the registry record.

2. The Registry must preserve all information contained in the registry record and reconstruct the registry record in the event of loss or damage.

Comment:

498. It is integral to the successful operation of the Registry system that data, once entered in the registry record, should only be able to be changed or removed in clearly specified and limited circumstances. This ensures that users of the Registry system can have confidence in its accuracy and integrity.

499. A transferee can change or remove data from the public registry record (but not the archive) by submitting an amendment notice or cancellation notice under clause 13 or 14, discussed in paragraphs [XXX] above. In contrast, clause 21(1) prohibits the Registry itself from amending or removing information from any of the registry record (whether the public registry record or the archive), except in the very limited circumstances described in clauses 22 and 23 (see paragraphs [XXX] below).

500. Clause 21(2) reinforces the importance of maintaining the integrity of the registry record, by requiring the Registry to preserve information in the registry record (i.e. both the public registry

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[143] *BW: See the question in the footnote at the start of the Introduction to Part IV (reproduced below). I can update this text after we have discussed the question at our upcoming WG meeting.

At our last WG meeting, it was said [Meeting Transcript, GtE chapter order - paras 1250-1] that we should distinguish consistently between the "Registry" (as the entity that runs the registry system), the "registrar" (the person who heads up the Registry) and the "registry record" (the information). I have endeavoured to do this. However, the Law itself doesn't seem to distinguish between the terms in the same way. In particular, art 2(h) defines the "Registry" to be the registration system, not the entity that manages it. How should we respond to this?

[144] *BW: Strictly speaking, clause 23 does not deal with the amendment or removal of information by the Registry, but the opposite. I don't think that this matters, though, and wasn't planning on commenting on it.

record and the archive). In practice, this obliges the Registry to maintain backups that enable it to reconstruct the registry record if necessary. [Cross-refer to other literature for more detail.][145]

Clause 22 — Removal of information from the public registry record and archival

1. The Registry must remove information in a registered notice from the public registry record upon the expiry of the period of effectiveness of the registration of a notice in accordance with clause 12, or upon the registration of a cancellation notice, including any cancellation notice registered in accordance with clause 14(2) or (6).

2. Except as provided in paragraph 1, the Registry may not remove information contained in a registered notice from the public registry record.

3. The Registry must archive information removed from the public registry record in accordance with paragraph 1 for [the enacting State to specify a period of time] in a manner that enables the information to be retrieved by the Registry.

Comment:

501. It is important that the Registry system be as easy to use as possible, including for searchers. If expired notices and cancelled information were to remain on the public registry record, this would add unnecessary complexity to search results, creating uncertainty and potentially hindering a transferor's ability to grant a new transfer. For this reason, clause 22 requires the Registry to remove information in a registered notice from the public registry record when its period of effectiveness has expired or when it has been cancelled by a cancellation notice. These are the only circumstances in which the Registry may remove information from the public registry record.

502. If information is removed from the public registry record, it will no longer be visible to searchers of the Registry. However, clause 22(3) states that the Registry will still need to store the information in its archive, for a specified period of time. Each enacting State will need to complete the clause by inserting into the clause a period of time that suits its domestic circumstances. The period chosen by an enacting State should be long enough to cover the maximum period of prescription under local law, plus an appropriate additional period for relevant legal proceedings to be completed.

Clause 23 — Correction of errors made by the Registry

1. If the Registry discovers that it erroneously removed from the public registry record information contained in a registered notice, a notice must be registered by the Registry without delay to restore the erroneously removed information. The Registry must send a copy of the information in the registered notice to the persons identified in the notice as the transferor and the transferee.

[145] *WG: We have yet to come to a landing on the extent to which we want to cross-refer to other publications.

2. The registration of a notice referred to in paragraph 1 is effective as of the time it would have been effective if the information had never been erroneously removed.

3. Notwithstanding paragraph 2, a transfer to which the notice relates is subordinate to the right of a competing claimant that acquired a right in the transferred receivable in reliance on a search of the public registry record made before the notice was registered, provided the competing claimant did not have knowledge of the erroneous removal of the information at the time it acquired its right.

Comment:

503. The Registry system under the Law should allow notices to be registered and uploaded into the public registry record automatically, without any supervision or other manual intervention by Registry staff. It is therefore highly unlikely that circumstances could arise where the Registry might itself erroneously remove information from the public registry record. If this does happen, however, then clause 23 states that the Registry must register a notice to rectify the public registry record without delay, and inform the transferor and the transferee.

504. Under clause 23(2), once the notice has been registered the registry record takes effect as if the information had never been removed.

505. Clause 23(3) contains one exception to the rule in clause 23(2). It says that a transfer that is the subject of the notice registered by the Registry under clause 23(1) may rank behind a right of a competing claimant, if the competing claimant acquired that right in reliance on a search that was made before the Registry registered its notice.[146]

506. It is important to emphasise that clause 23 relates only to information removed in error from the public registry record by the Registry. It is not engaged where information is removed from the public registry record by any other person. In particular, it does not apply where a transferee has mistakenly removed information from the public registry record by means of an amendment or cancellation notice. In such a situation, the transferee will itself need to correct its error by making a further registration, and the further registration will only take effect from the time it is made – that is, it will not have any retroactive effect.

Clause 24 — Limitation of liability of the Registry

Any liability that the Registry may have in accordance with other law for loss or damage caused by an error or omission in the administration or operation of the Registry is limited to [the enacting State to specify a maximum amount].

Comment:

507. The fully electronic nature of the Registry system makes it unlikely that the Registry could be liable to third parties as a result of an error or omission in the administration or operation of the Registry. Nevertheless, it is possible that the Registry could be operated in a way that caused a loss

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[146] *BW: Clause 23(3) is a bit more complicated than this, but I didn’t think we needed to spell out all the nuances.

e.g. if there is a malfunction in the Registry software, or if the Registry erroneously removes information from the public registry record (see clause 23, discussed in paragraphs [XXX] above).

508. Clause 24 allows an enacting State to set a cap on the amount for which the Registry could be liable for such an error or omission, by inserting the cap in place of the text in square brackets. The cap could be formulated in a number of ways. For example, it could be an annual global cap, or a cap for each error. The enacting State will need to decide what is most appropriate for its domestic circumstances.

509. It is important to note that the Law itself does not impose liability on the Registry for loss or damage caused by errors or omissions in the administration or operation of the Registry. Any such liability will need to flow from other law of the enacting State. If there is no principle of domestic law in an enacting State that could impose liability of this type on the Registry, then the State could consider deleting clause 24 entirely.

Clause 25 — Registry fees

> **1. Fees may be charged for Registry services in the amounts to be specified by [the enacting State to specify the authority pursuant to clause 20].**
>
> **2. [The enacting State to specify the appropriate authority pursuant to clause 20] may modify the fee schedule from time to time.**

Comment:

510. Clause 25 allows fees to be charged for Registry services. The fees should be set by the authority that is also responsible under clause 20 for the appointment of the registrar, and an enacting State will need to complete the clause by inserting the name of that authority in place of the text in square brackets.

511. The overarching objective of the Law is [to assist States to strengthen their economies through the development of markets for the financing of receivables, particularly for small businesses, in a way that increases the availability of credit and reduces its cost (see [cross-ref to some other part of the Guide] for a discussion of this).[147] If the Law is to achieve this objective, the fees that are charged for registering notices and making searches should be kept as low as possible, as fees inevitably get passed on to customers, raising their cost of credit. High fees would act as a disincentive to use the Registry system, and could compromise the success of the reform. Modest fees, in contrast, would maximise the use of the Registry system by encouraging transferees to properly register notices, and by encouraging others to conduct searches.

512. In order to maximise this potential, an enacting State might decide to charge no fees at all, or at least no fees for some services (e.g. not for the registration of cancellation notices, or for searches). Even if a State does decide to charge fees, however, it should resist the temptation to use the Registry as a revenue-raising tool, and should set the fees at a level that is no higher than is necessary to cover the costs of establishing and operating the Registry system.

[147] *BW: This may need to be aligned in due course with the discussion of this elsewhere inf the GtE.

ANNEXE I

UNIDROIT WORKING GROUP RESPONSIBLE FOR THE PREPARATION OF THE GUIDE TO ENACTMENT

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DIGITAL ECONOMY SUPPLEMENT TO THE MODEL LAW ON FACTORING

First Edition [date of issue]

(to be added to the electronic PDF version of the Guide)

1. This Supplement covers various aspects of the 'Digital Economy' that may affect factoring This Supplement covers various aspects of the 'Digital Economy' that may affect factoring transactions. The MLF is technology-agnostic and enables the use of various types of technologies in factoring transactions. It is divided into four Sections that provide guidance on (1) the issuance and transfer of 'digital receivables', (2) monetary sum and money to include virtual currencies, (3) platforms and exchanges for receivables, and (4) other technological applications, such as Artificial Intelligence (AI) and the Internet of Things (IoT). The Supplement is directed at a) legislators, particularly concerning the desirability of enacting other laws that may recognize some digital records as effectively embodying the receivable, b) factors, particularly to appreciate the potential application of multiple laws to the same receivable that could create priority conflicts, and c) exchange/platform software providers and operators with respect to the legal effect of transactions they enable.

A. 'Digital receivables'

2. The MLF applies to receivables defined in Article 2(g) as contractual rights to payment. Receivables are intangible assets. However, when the right to payment is embodied in a negotiable instrument or linked with a digital asset, it will likely cease to be a receivable. The MLF does not apply to transactions with negotiable instruments, whether issued in paper or electronically, other than as proceeds of receivables [see Section XXX of the Guide to Enactment]. If the debtor tenders a bill of exchange or promissory note in payment of the debt, then the negotiable instrument may be referred to as a "documentary receivable" with the effect that the transfer of the negotiable instrument also transfers the receivable.[1] Likewise, if a State has enacted a law governing digital assets, including those that effectively link the receivable to a digital record, that law will govern transfers of those assets. Under such laws, non-fungible tokens (NFTs) may be linked to a receivable that is transferred with the NFT. As illustrated below, some supply chain finance products contemplate using "tokenized receivables," but the legal effect of transferring such tokens is uncertain.

3. Some States have amended their laws to recognise specific types of receivables linked to digital assets – "electronically recorded monetary claims"[2] and "controllable accounts"[3] – that may be transferred by registration or control. The underlying reason for both of these reform initiatives was to address some inefficiencies in the law governing negotiable instruments without actually undertaking a lengthy reform of that body of law. When such reforms are implemented, it is important for the legal framework to include clear rules that determine when a receivable arises and continues to exist as a purely intangible asset or when it becomes effectively linked to some record constituting a digital asset governed by another law. Other aspects, especially concerning priorities and applicable law, must also be addressed. Unlike the MLF, under these regimes receivables are transferred individually as registries require invoice-by-invoice registration and every receivables

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1 See Sealy and Hooley's Commercial Law Text, Cases, and Materials Edited by David Fox (Oxford University Press, 2024).

2 See Electronically Recorded Monetary Claims: A New Financial Means for Raising Business Funds (Financial Services Agency of Japan), https://www.fsa.go.jp/ordinary/densi02-en.pdf.

3 Controllable account is defined in UCC 9-102(a)(27A) as "an account evidenced by a controllable electronic record that provides that the account debtor undertakes to pay the person that has control […] of the controllable electronic record."

linked to a digital record must be subject to control, which makes them less suitable for transfers of receivables in bulk.

4. The form in which the right to payment is presented affects its characterisation under law. Depending on that form, a law that implements the MLF, the UNCITRAL Model Law on Electronic Transferable Records (MLETR), or the UNIDROIT Principles on Digital Assets and Private Law (DAPL) may govern the transfer of the relevant right to payment. The purpose of this Section is not to examine the potential application of these standards but to illustrate the different nature of rights to payment to enable enacting States to consider various aspects of digitalisation in the reform process.

5. Commercial transactions that generate receivables are typically documented in an invoice that describes the goods, services, data, or license of intellectual property rights. Under most domestic laws, the invoice is only evidence that a receivable has been generated, documenting the description of goods, the purchase price, and other aspects of the transaction. Factors may require invoices to verify various aspects of the commercial transaction, such as payment terms. Invoices may also be used to notify debtors of the transfer of a receivable when an appropriate notation is inserted therein. Under some domestic laws, especially in Latin America, an invoice may embody a receivable with the effect that the transfer of the invoice also transfers the receivable.[4] In the markets that operate under these laws, the factor and other financiers of receivables routinely take possession of invoices to ensure an effective transfer of the "linked" receivable. Invoices are thus functionally treated as negotiable instruments that represent an irrevocable promise to pay.

6. Invoices are increasingly issued and transferred electronically. The digital invoice may be a simple attachment to an email, routed through an Extensible Markup Language (XML) system or an Application Program Interface (API), or embedded in an integrated finance solution made available to clients of a financial institution. In some industries, such as utilities, it may be delivered to the user, typically a consumer, through a web portal, but such receivables are not typically used to obtain financing under a factoring arrangement. Yet another mechanism is for an intermediary to provide a digital solution for e-invoicing.

7. Digitalisation of invoices is driven both by market practice and statutory requirements, such as the collection of taxes and reducing fraud. Some States in the Americas have enacted laws to make the use of e-invoicing mandatory to increase transparency in the tax collection system.[5] In such systems, digital invoices may be authenticated and validated by tax authorities that operate 'invoice registries'. A registered invoice must be electronically confirmed by the debtor, which is reflected in the registry. A transfer of the invoice is also recorded in the registry, precluding its 'double-selling'. Some laws require a digital endorsement by the transferor. Accordingly, a digital invoice is issued and transferred by entries in a registry.

8. In the systems where the invoice does not embody the related receivable, digitalisation facilitates various factoring processes, but does not impact the effectiveness of a transfer. DAPL includes the following illustration (adapted for this Supplement):

> In State X, an invoice is not seen as an embodiment of the underlying right to payment. Factor A regularly takes control of digital invoices for due diligence purposes. This would neither transfer the receivable nor make it effective against third parties. Factor B regularly acquires receivables documented in invoices, which are issued in the form of digital assets. Both factors must make a registration in the MLF Registry to make a transfer effective against third parties. Because there is no effective link between the receivable and invoice, a transfer of the digital invoice would not have any value in a

[4] See Negotiable Invoice (Government of Peru, 2023), https://www.gob.pe/7848-factura-negociable. See also https://leyes.congreso.gob.pe/documentos/leyes/29623.pdf and https://www.mef.gob.pe/en/por-instrumento/decreto-supremo/12989-anexos-01-02-03-escolaridad/file.

[5] IFC Handbook on Technology and Digitalization in Supply Chain Finance, p. 43.

similar way to the delivery of possession of a paper invoice that does not embody a right to payment.

9. However, in the systems where the invoice embodies the receivable, digitalisation generates legal challenges where the law must recognise an equivalent to possession, such as an entry in a registry or control, to transfer the digital invoice. The receivable may thus become a type of digital asset that links the record to the receivable (see further Principle 4 of the DAPL).[6]

10. Some States have amended their laws to recognise specific types of receivables linked to digital assets – "electronically recorded monetary claims"[7] and "controllable accounts"[8] – that may be transferred by registration or control. The underlying reason for both of these reform initiatives was to address some inefficiencies in the law governing negotiable instruments without actually undertaking a lengthy reform of that body of law. When such reforms are implemented, it is important for the legal framework to include clear rules that determine when a receivable arises and continues to exist as a purely intangible asset or when it becomes effectively linked to some record constituting a digital asset governed by another law. Other aspects, especially concerning priorities and applicable law, must also be addressed.

B. Monetary Sum, Money, and Currencies

11. The MLF in Article 2 defines a receivable by referencing a 'monetary sum.' It also includes 'money' within the definition of 'proceeds'. Finally, Article 24(2)(a) refers to the 'currency of payment' in relation to a receivable. None of these terms is further defined, as this is a matter of laws other than the MLF. Other laws of the State may define money, monetary sum, and currency narrowly to include only legal tender or, more expensively, to include 'virtual currencies,' which may be issued by private companies (e.g., Tether).[9] This Section does not explore the various types of virtual currencies, such as stablecoins, which are not material to the MLF.

12. There do not appear to be any factoring platforms and/or exchanges that support dealings in receivables denominated in virtual currencies. However, some FinTechs claim to be working on technology solutions that would enable this type of transaction and offer accounting solutions for managing receivables denominated in virtual currencies. Tax authorities and tax preparers have issued guidance on the treatment of receivables denominated in virtual currency for tax and accounting purposes, which suggests this type of transaction might be happening in practice. However, it is not clear whether that is the case for receivables covered by the MLF.

13. Monetary sum is not typically defined in other laws but its meaning may be inferred from the definitions of monetary obligations, which arise where the debtor is 'bound to pay a fixed, certain, or liquidated sum of money.'[10] Other laws of States may define monetary obligations excluding means of payment that do not have 'legal tender status,' such as virtual currency.[11] In those jurisdictions, the law thus provides that monetary obligations may only be settled in national

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[6] The Commentary to Principle 4 states, in section 4.4, that "[t]he operation of linked assets depends on two distinct questions: (1) whether there is any link at all between the digital asset and the other asset; and (2) whether the link has a legal effect on the parties' rights in relation to the other asset. Both questions depend on the other law of the State."

[7] See Electronically Recorded Monetary Claims: A New Financial Means for Raising Business Funds (Financial Services Agency of Japan), https://www.fsa.go.jp/ordinary/densi02-en.pdf.

[8] Controllable account is defined in UCC 9-102(a)(27A) as "an account evidenced by a controllable electronic record that provides that the account debtor undertakes to pay the person that has control […] of the controllable electronic record."

[9] For an illustration of virtual currency, see DAPL, Principle 2, para 2.8.

[10] See Charles Proctor, Mann and Proctor on the Law of Money, 8th Edition (Oxford, 2023).

[11] See Wouter Bossu et al, Legal Aspects of Central Bank Digital Currency: Central Bank and Monetary Law Considerations (IMF, 2020), https://www.imf.org/en/Publications/WP/Issues/2020/11/20/Legal-Aspects-of-Central-Bank-Digital-Currency-Central-Bank-and-Monetary-Law-Considerations-49827.

currencies, whether domestic or foreign.[12] Under these narrower definitions, the obligor of a monetary obligation, including a debtor that owes the receivable must, by law, pay in legal tender.[13]

14. Money may be defined in monetary, commercial, secured transactions, or other laws. For instance, the UNCITRAL Model Law on Secured Transactions defines money as 'currency authorised as legal tender by any State.' This and similar definitions would include central bank digital currencies (CBDC), which is a virtual representation of fiat money.[14] CBDC may be issued as account or token-based, which is not material to the MLF. CBDC may also constitute a digital asset, and its transfers are governed by the special law on digital assets, such as DAPL.[15] The Uniform Commercial Code of the United States defines money, in 9-102(a), as a medium of exchange currently authorised or adopted by a domestic or foreign government. The term includes a monetary unit of account established by an intergovernmental organisation or by agreement between two or more States. It defines electronic money as 'money in an electronic form' and 'tangible money.'

15. Money that is legal tender has co-existed with 'private money' in the form of bank deposits issued by depository financial institutions.[16] Such 'money' is treated and defined separately, including for the purposes of the definition of proceeds in the MLF that covers money and the right to payment of funds credited to an account with an authorized deposit-taking institution. It is questionable whether virtual currency credited to an account with an authorised deposit-taking institution would fall under the definition of proceeds in the MLF, which would depend on the definition of 'funds' in other laws of the Enacting State. Other laws must thus recognise the possibility for receivables to be denominated in virtual currencies and for proceeds to encompass them.

16. Currency may be defined similarly to money as a medium of exchange authorized by the government. The MLF precludes the transferee to change the currency in which the receivable is payable without the consent of the debtor. The debtor may thus not be required to settle a receivable, originally denominated in the Euro, in the U.S. dollar or Bitcoin. The former is a different currency and the latter is generally not considered currency at all. However, the debtor may settle the receivable by paying the Euro by a wire transfer from a bank account or transferring a Euro CBDC.

C. Receivables platforms and exchanges

17. Various types of platforms and exchanges have been established to facilitate transactions with receivables. Both infrastructures can reduce the cost of factoring transactions, enable more effective management of relationships and various processes, and facilitate other supply chain financing products. This Supplement distinguishes platforms and exchanges from one another because they are organised differently, and the legal effect of the transactions that they record may vary. One of the main distinguishing features between a platform and an exchange (for purposes of this Supplement) is that the former facilitates financing between suppliers and a single financier, typically a financial institution that operates the platform. In contrast, the latter facilitates financing between suppliers and multiple financiers, including FinTechs, wealth managers, pension funds, and individuals.

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[12] See https://www.hka.com/can-a-contract-price-be-paid-in-bitcoin/.

[13] Id. See also Official Comment 12A to UCC 9-102.

[14] See Central bank digital currencies (CBDCs) in emerging market economies (EMEs) – India (BIS), https://www.bis.org/publ/bppdf/bispap123_j.pdf. At least 6 central banks have launched a CBDC: the Central Bank of The Bahamas (Sand Dollar), the Eastern Caribbean Central Bank (DCash), the Central Bank of Nigeria (e-Naira), the Bank of Jamaica (JamDex), People's Bank of China (Digital renminbi), the Reserve Bank of India (Digital Rupee), and Bank of Russia (Digital Ruble).

[15] See further DAPL, Principle 2, para 2.11-13.

[16] See Tobias Adrian and Tommaso Mancini-Griffoli, Public and Private Money Can Coexist in the Digital Age (IMF, 2021), https://www.imf.org/en/Blogs/Articles/2021/02/18/blog-public-and-private-money-can-coexist-in-the-digital-age.

18. The MLF does not include special rules for platforms and exchanges, but its private law framework and the regulatory guidance included in the Guide to Enactment are important building blocks for their efficient functioning. Some factoring laws expressly contemplate the establishment of exchanges. Terms and conditions of use or master agreements typically govern the relationship between the parties who transact on exchanges and platforms.[17] Such terms and conditions of use and master agreements should satisfy the requirements of Article 5 of the MLF applicable to the effectiveness of a transfer as between the transferor and transferee.

19. Since their operations are not anchored in the MLF, any recording of a transfer of a receivable would not achieve third-party effectiveness, such that the transferee must register a notice in an appropriate registry established pursuant to the MLF. Alternatively, the exchange or platform may be connected to the registry and automatically effectuate registrations reflecting the completed transaction.

20. Some platforms and exchanges offer only particular types of factoring products, such as reverse factoring or non-recourse factoring. The MLF is not limited to a particular type of factoring transaction. Platforms and exchanges may impose qualification criteria on the receivables, such as upper limits on the duration of receivables (e.g., up to 360 days) and trade single receivables or portfolios. While platforms may be used for both outright and security transfers, exchanges generally support only outright transfers.

21. In addition to facilitating factoring, platforms and exchanges often provide onboarding, client identity verification, transaction and payment record-keeping, and other functions. While these additional functions are outside the scope of the MLF, they can make factoring more efficient.

22. This section outlines the core functional features of platforms and exchanges and examines how those features might be affected by the MLF.

1. Platforms

23. Financial institutions offer conventional platforms as software solutions to finance and manage receivables owed by their clients. In some cases, a financial institution may operate a platform that facilitates transactions between suppliers and buyers, such as in the case of dynamic discounting platforms that, however, do not provide any financing solutions. These platforms are not subject to the MLF because they do not facilitate the transfer of a receivable but rather a settlement of payments. They act as 'brokers'. In contrast, if a platform is used to transfer a receivable for the purposes of financing or collection, that transaction will be governed by the MLF.

24. Recently established platforms engage a broader range of supply chain participants, enabling financial institutions to deploy more integrated solutions that, for instance, finance tiers of participants within the supply chain. Platforms are critical for 'deep-tier supply chain finance,' which reaches tiers of suppliers, often located in multiple jurisdictions.[18]

25. The software solution enabling these platforms may be developed by the financial institution or provided by a partner, such as a FinTech or other solutions provider. Some FinTech providers specialise in supply chain management and offer software to partnering financial institutions that may be customised to meet the specific needs of their clients.

26. There are several reasons for parties to use platforms, including the efficient management of client relationships in reverse factoring, where it would be administratively cumbersome for the

[17] See, e.g., Supplier Chain Finance Platform Agreement / Terms & Conditions (Commercial Bank of Dubai), https://www.cbd.ae/docs/librariesprovider2/default-document-library/scf-platform-agreement-cum-terms-conditions_click-through.pdf?sfvrsn=c4f1786b_2.

[18] ADB, Deep-Tier Supply Chain Finance, Unlocking the Potential, 12 (May 2024).

factor to disburse individual payments to hundreds of small suppliers transacting with the anchor buyer. In reverse factoring platforms, anchor buyers register and invite their suppliers to join. As financial institutions and large corporates are held more accountable for environmental, social, and governance aspects of the participants in the supply chains, they seek visibility through the tiers that also facilitate receivables finance.[19] Another reason for the use of platforms is to match the payment terms to the needs of the parties, where the anchor buyer might prefer to pay the receivable, for instance, 90 days after receipt of goods, while the supplier might prefer to collect the payment in 45 days or less.

27. Platforms provide various services, including digital invoice delivery, settlement of payments, and extension and management of credit facilities. They are generally automated and powered by a range of technologies, including distributed ledgers (DLT), such as blockchain. DLT may create a transparent, secure, and tamper-proof record of all invoice details and transactions between the supplier, the buyer, and the financial institution, streamlining the process by automatically updating the ledger with each transaction.[20] Interested parties can view the status of each invoice in real time, as the ledger is shared across the network, reducing the risk of discrepancies or fraud. The immutable nature of the ledger provides a reliable audit trail, enabling better risk assessment for financial institutions.

28. DLT-powered platforms[21] may provide the following services: (1) invoice creation and upload, when the supplier issues an invoice and digitally records it on the platform, including the invoice number, amount, due date, and buyer information; (2) invoice verification, where the buyer confirms all of the invoice details; (3) transfer, when the receivables reflected in the invoice are digitally transferred to the financial institution;[22] and (4) funding, where the financial institution advances a percentage of the invoice amount. When the buyer pays the invoice, the funds are automatically transferred to the financial institution via the platform-initiated settlement.

29. Smart contracts can be designed to disburse payments automatically if pre-determined conditions are satisfied. They may contain data, such as NFTs representing invoices, that can be programmed to release funds.[23]

30. As noted above, a platform may be provided by a third party to a financial institution. Sometimes, the third-party platform provider may purchase the receivables but subsequently transfer a proportional interest (e.g., 90%) to the financial institution. It retains a partial 10% stake in each receivable, a type of transfer recognised by the MLF in Article 5(4). A guarantee by an export-credit agency for trade receivables or other public guarantee scheme may support a facility of this nature. The provider registers notices against the individual transferors (there may not be any special interface between the platform and a factoring or secured transactions registry that would facilitate automated registration), but the financial institution does not register its own notices or assignments of the notices registered by the provider.

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[19] Id., 2.

[20] See Distributed Ledger Technology (Trade Finance Global, 2024), https://www.tradefinanceglobal.com/tradetech/distributed-ledger -technology-dlt/#:~:text=On%20such%20platforms%2C%20the%20distributed,and%20a%20defined%20transaction%20process.

[21] See, e.g., DLTledgers, https://dltledgers.com/the-app-hub/banking-finance/multi-party-and-multi-tier-supply-chain-finance-digitalization-app/.

[22] See IFC Handbook on Technology and Digitalization in Supply Chain Finance, p. 45.

[23] See Invoice factoring through Blockchain: harnessing technology dividends (Africa Finance Forum Blog, 2022), https://www.mfw4a.org/blog/invoice-factoring-through-blockchain-harnessing-technology-dividends.

2. Exchanges

31. Digitalisation of invoices is expected to incentivise the establishment of exchanges for receivables.[24] Exchanges may be established and operated by public or private sector entities. Governmental institutions have established exchanges that allow any qualified supplier to offer their receivables for sale to multiple institutions that compete against one another in an auction. One such exchange is Mexico's Nacional Financiera (NAFIN), a national development bank that pioneered reverse factoring services through the "Cadenas Productivas."[25] Exchanges may also facilitate factoring of receivables owed by government entities. They may benefit from the support of development banks and international finance institutions. While the operations of these exchanges are not governed by factoring laws, more recent reform initiatives seek to establish national exchanges for the trading of receivables. If so, transfers of receivables on such exchanges without a corresponding registration in an MLF registry may achieve third-party effectiveness, which is not a mechanism recognised by the MLF. If so, it is important for such legislation to include appropriate priority rules to resolve conflicts between transfers of the same receivable made effective against third parties by recording on an exchange and registration in an MLF registry.

32. Some exchanges enable only a particular type of supplier (e.g., MSMEs) to register as a seller of receivables.[26] Exchanges may also impose specific requirements on the registration of debtors of receivables.[27] Interested parties must typically register and satisfy KYC requirements. Sellers sign a single agreement (e.g., the NAFIN platform usage agreement) that allows them to transfer their receivables to various financiers that compete to provide the best financing terms.

33. Recently, FinTechs have begun establishing "crowdfactoring" exchanges, enabling suppliers to sell receivables to various private parties in a similar fashion to other peer-to-peer (P2P) financing facilities such as crowdfunding.[28] A full or partial interest in receivables may be purchased. Crowdfactoring may be carried out on a recourse basis. While such transfers will be subject to the MLF, typically, the amounts financed are low, which may be the reason for such financiers not to register notices in an MLF Registry.

34. Depending on the type of factoring, either the seller or buyer uploads the invoice to the exchange, and then the counterparty confirms it. After the confirmation through the exchange, the invoice may be auctioned off to the highest bidder. The seller may receive payment within 24 hours, and the buyer (debtor of the receivable) pays the financier on the due date. The seller may set some parameters, such as the maximum discount fees and minimum pre-payments it is willing to accept. Alternatively, these parameters may be set by the exchange. Upon conclusion of the auction, the exchange 'allocates' the receivable to the buyer. Receivables may also be transferred partially to multiple transferees.[29] The MLF recognises the transfer of partial interests in receivables and provides a mechanism for their collection, protecting the debtor against increased administrative costs if/when required to effectuate multiple payments – see Article 26(6).

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[24] Monkey operates an auction-based marketplace for receivables owed by large buyers. With the new regulation, any supplier that has issued an invoice will be able to transform it into a financial asset. It will be enough to register it and then use it as a credit guarantee through the registers. This will ensure that the invoice is valid and has not been anticipated by any other financier before. See https://braziljournal.com/monkey-exchange-faz-rodada-com-a-b3-de-olho-nas-duplicatas-escriturais/?ref=thisweekinfintech.com.

[25] See further https://blogs.worldbank.org/en/psd/supply-chain-financing-effective-way-development-banks-support-small-entrepreneurs.

[26] See India's Micro, Small and Medium Enterprises Development Act, 2006.

[27] An anchor buyer at Mexican NAFIN must be a private corporation with annual sales over US$12.5 million.

[28] See, e.g., ZWEBB FinTech, https://www.zwebb.com/trading-platform and Inverse FinTech, https://www.inversa.es.

[29] Salinger on Factoring (eds. Mills & Ruddy, 6th edition, 2020), pp. 22-23.

D. Other technological applications

35. Artificial intelligence (AI) has profoundly affected finance products, processes, and applications, and is having an impact on factoring. The Internet of Things (IoT) facilitates various processes that indirectly support factoring. The MLF does not include any rules that would affect these functions or applications.

36. In general, including in factoring transactions, AI facilitates due diligence and credit scoring, especially for businesses with opaque credit history, and assists in identifying risks and compliance with anti-money laundering (AML) regulations or detecting fraud. The key applications of AI in factoring include: (1) invoice verification and data extraction, reducing the need for manual data entry, (2) credit risk assessment, enabling analysis of a company's financial data, payment history, and other information to generate a credit score and predict the likelihood of default, (3) fraud detection, identifying suspicious patterns in transaction data, such as unusual payment amounts or inconsistencies in invoice details, (4) predictive analytics of future payment behaviour, allowing financial institutions to proactively manage collection efforts and prioritise receivables with higher risk of non-payment, (5) client onboarding and qualification, by quickly evaluating potential clients based on their financial data, reducing the time needed for manual review, (6) portfolio monitoring, identifying potential issues with specific receivables and providing real-time alerts to take necessary actions, and (7) dynamic pricing, through analysis of market conditions and client data to determine optimal factoring rates for individual transactions.

37. IoT, for instance, enables the tracking of the movement of goods, confirming their delivery, which may trigger the obligation of the debtor to pay the receivable a specified number of days after their delivery. By monitoring conditions in real-time, IoT can identify potential issues like delayed deliveries or damaged goods early on, allowing businesses to take proactive measures and minimise losses.[30] Accurate data from IoT sensors can improve a company's creditworthiness by demonstrating greater transparency and control over its supply chain operations, potentially leading to better financing terms.[31]

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[30] See IoT in Supply Chain: Enhancing Efficiency and Sustainability in Logistics (Cognitive Clouds, 2023), https://www.cognitiveclouds.com/insights/iot-in-supply-chain#:~:text=The%20IoT%20(Internet%20of%20Things,late%20deliveries%2C%20and%20product%20integrity.

[31] Id.