



British Institute of
International and
Comparative Law

BIICL Study Assignment and the Rome I Regulation

Effectiveness of an Assignment of a Claim
against Third Parties and Priority of the
Assigned Claim

Dr Eva Lein

Herbert Smith Freehills
Senior Research Fellow in
Private International Law,
BIICL

BIICL Study

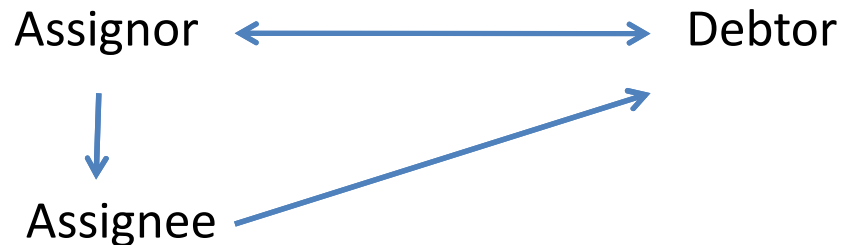
- Drafted in 2011
- Legal, Statistical and Empirical Analysis
 - National reports on conflict of laws rules and relevant substantive law in 12 Member States and 6 Third States
 - Data on assignments in different sectors (transaction volumes, costs etc.)
 - Questionnaire to assess problems in practice, need for legislation, preferred solution for third party effects of an assignment
- Sectors involved
 - Factoring, securitisation, loans, guarantees, insurance
 - Financial institutions, financial and legal associations, legal practitioners, academics from different Member States
 - 36 participants (including associations representing several thousand members)
- Expert group (11)
 - Different Member States and Sectors
 - Including representatives of financial sector (factoring, securitisation, derivatives, banking), lawyers, academics

Assignment and Rome I

1.) Debt between Assignor and Debtor, subject to law X

Assignor  Debtor

2.) Assignment of this debt to an assignee:



3.) Which law applies?

- Relationship Assignor – Assignee: Art. 14 (1);
- Relationship Assignee – Debtor: Art. 14 (2);
- “Third parties”? E.g. creditors of the assignor; competing assignees etc. – not regulated

Art. 14 Rome I Regulation

Voluntary assignment and contractual subrogation

1. The **relationship between assignor and assignee** under a voluntary assignment or contractual subrogation of a claim against another person (the debtor) shall be governed by the **law that applies to the contract between the assignor and assignee under this Regulation**.

2. The **law governing the assigned or subrogated claim** shall determine its assignability, the **relationship between the assignee and the debtor**, the conditions under which the assignment or subrogation can be invoked against the debtor and whether the debtor's obligations have been discharged.

3. The concept of assignment in this Article includes outright transfers of claims, transfers of claims by way of security and pledges or other security rights over claims.

Recital 38 Rome I Regulation

In the context of voluntary assignment, the term 'relationship' should make it clear that Article 14(1) also applies to the **property aspects** of an assignment, **as between assignor and assignee**, in legal orders where such aspects are treated separately from the aspects under the law of obligations...

Original **COM Proposal** for Rome I: included a rule on third party effects (law of habitual residence of assignor) which was deleted

Coverage of Art. 14 (1)

Relationship assignor – assignee

Contractual and other aspects as between assignor and assignee of a failure to assign or perfect the assignment

Art. 14(1), Recital (38)

Property aspects as between assignor and assignee

Recital (38)

- Note: difference in meaning between property aspects as between the parties and in relation to third parties -> artificial and contrary to *erga omnes* effect of property law

Coverage of Art. 14 (2)

Relationship assignee-debtor and other aspects affecting the debtor

Assignability

(E.g. effects of restrictions on assignment in the contract between assignor and debtor)

Defences of the debtor against assignor

(Can the debtor rely, as against the assignee, on the defences that he had against the assignor?)

Additional defences of the debtor

(Can the debtor rely on any additional defences against the assignee (e.g. set-off with a claim the debtor has against the assignor))

Conditions under which the assignment can be invoked against the debtor

(including any notice requirement, form of notice etc.)

Discharge of the debtor's obligations

(whether payment by the debtor to the assignor/assignee after the assignment results in an effective discharge)

Not included in Art. 14

- Effectiveness of an assignment or a subrogation of a claim against “third parties” (“proprietary issues”)
 - “Third parties”
 - The assignor's unsecured creditors (including judgment creditors)
 - other persons dealing with the assignor (including competing assignees)
 - creditors of the assignee
 - Unclear: status of insolvency representatives
- Priority of the rights of the assignee over the rights of another person
 - i.e. the question whether an the assignee can assert an entitlement over a claim against a prior or subsequent assignee or judgment creditor

Uncertain Issues

- Claim of assignee against assignor to recover the proceeds or value of the claim, where the debtor has discharged his duties to the assignor (or *vice versa*)
- Claims under contracts not yet in existence, for which the law applicable to the claim cannot be identified at the date of assignment.
- Effectiveness of an assignment vis-à-vis successors in title and other representatives of the assignor and assignee, including heirs and insolvency representatives.

Problems

- 47% of stakeholders confirm problems regarding the effectiveness of an assignment as to third parties
- 80% confirm a need for legislation
- Divergent views as to which law should govern third party effects of an assignment
- Need for reduction of potentially applicable laws to reduce complexity
- Should there be a new rule *in addition* to the existing Art. 14(1) and (2)?
- Should Art. 14 be revisited entirely?
 - Is the construction of Art. 14(1) based on the *relationship* assignor-assignee (and not based on a distinction between contractual and property aspects of the assignment) the right one?
 - Should Art. 14(1) be restricted to the legal effects of an assignment given that contractual aspects between assignor and assignee are covered by Arts. 3-8 Rome I?
 - Should there be *one* rule for *all* proprietary aspects (between assignor and assignee *and* as to third parties)?
- Should there be sector specific rules? Complexity and characterisation problems?

Possibly applicable laws to the proprietary aspects of the assignment

- Law applicable to the contract between assignor and assignee
- Law of the underlying claim
- Law of the habitual residence of the assignor

LAW APPLICABLE TO THE CONTRACT BETWEEN ASSIGNOR AND ASSIGNEE

Advantages

Flexibility through party autonomy

Reduction of applicable laws and of complexity

Solution adaptable to different market sectors, no need for specific sectoral rules

Increased legal certainty in case of future claims

Disadvantages

**Prejudice to third parties
in case of free choice,
Potential for abuse
(limited choice?)**

**Conflict of connecting
factors (priority);
Competing assignments
governed by different laws**

**Unsuitability for financial
claims**

Limited Party Autonomy

- To mitigate disadvantages:
 - Restricted choice available to the assignor and assignee can combine flexibility with greater foreseeability for third parties.
 - e.g. limited choice of either the law of the assigned claim or the law of the assignor's habitual residence

Support for this solution

- **Adopted in The Netherlands and Switzerland:**
 - party autonomy based solution for the third party effects of an assignment.
 - Example of **the Netherlands**:
 - Law applicable to the contract between assignor and assignee is applicable to the effectiveness of an assignment, i.e. to all its property aspects.
 - Priority of multiple (competing) assignments: the law governing the second assignment should decide upon the protection of bona fide second acquirers.
 - The solution is reported to work well:
 - no cases of abuse to defraud third parties;
 - typical choice: law of the assignor's habitual residence or law of the underlying debt assigned
- Supported by
 - 11 % of the stakeholders overall
 - 20% of financial institutions
 - 3 out of 11 experts

LAW OF THE UNDERLYING CLAIM ASSIGNED

Advantages

**Consistency of
connecting factor
(priority)**

**Reduction of applicable
laws and of complexity**

**Suitability for financial
claims**

Disadvantages

**Unsuitability for
“future claims” under
contracts not yet
concluded**

**Complexity and
inefficiency for bulk
assignments**

**Conflict of connecting
factors (change of
applicable law by
parties, but Art. 3(2)
Rome I)**

Support for this solution

- The solution is the most frequent: adopted in several EU Member States (Luxemburg, Poland, Spain, Italy, United Kingdom, Germany) and third States (Australia, Canada, Japan and the Russian Federation).
- Supported by
 - 30 % of stakeholders
 - 43% of legal practitioners
 - 26 % of financial institutions

LAW OF THE ASSIGNOR'S LOCATION (HABITUAL RESIDENCE)

Advantages

**Easily
ascertainable
connecting factor**

**Synergies with Art.
22 UNCITRAL
Receivables
Convention**

**Suitability for bulk
assignments**

**Synergies with the
Insolvency
Regulation (COMI)**

Disadvantages

Complexity (adds a third applicable law to the current Art. 14)

Conflict of connecting factors (chain of assignments or change of habitual residence (SPVs, offshore companies))

Determination of connecting factor under Art. 19 Rome I

Inflexibility (rigid connecting factor)

Support of this solution

- Solution is adopted in one EU Member State (Belgium) and one third State (USA)
- Corresponds to Art. 22 of the UNCITRAL Receivables Convention.
- Was originally favoured by the European Commission in the Rome I Proposal, but was deleted.
- Supported by
 - 44 % of stakeholders overall
 - 75% of the representatives of the factoring sector
 - Most academic participants

Sector-Specific Solutions

- **Problems of definition and characterisation** (e.g. definition of “factoring”)
- **Piecemeal approach:** Rome I tends to avoid it, with the exception of the provisions protecting weaker parties (consumers, employees).
- **Conflict of connecting factors** in circumstances where only one of two competing assignments was occasioned by a transaction subject to a sectoral rule (e.g. factoring).

Conclusions

- **A clear solution** is needed
- The solution should balance the interests of **all parties** involved
- **Contractual aspects** of the assignment should be covered by **Art. 3 ff. Rome I directly**, while Art. 14 only addresses the assignment itself, i.e. its legal effects.
- Preferable that **all** property aspects of assignment are governed by **one** rule.
- Sector specific rules **add complexity and encourage characterisation problems** and are to be avoided
- The **solution should reduce complexity and the number of applicable laws under Art. 14**
 - Law of the assignor's habitual residence is overall most favoured but would increase applicable laws
 - Law of the assigned debt would reduce applicable laws
 - Limited party autonomy (choice of the law of the underlying debt assigned or of the assignor's habitual residence) would enable flexibility for all sectors while limiting the problem of unforeseeability as to third parties.