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Draft Legislative Guide on Secured Transactions

Security rights in receivables: definitions and recommendations

Note by the Secretariat*

Contents

* This document is submitted two weeks later than the required ten weeks prior to the start of the meeting because of the need to complete consultations and to finalize consequent amendments.

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Security rights in receivables

I. Definitions (A/CN.9/WG.VI/WP.22/Add.1, para. 21 (n)-(v))

(a) "Security right" means a consensual property right in movable property and fixtures that secures payment or other performance of one or more obligations. References to a "security right" in this Guide also refer to the "right of an assignee of receivables".

(d) "Secured creditor" means a creditor that has a security right. References to the "secured creditor" in this Guide also refer to the "assignee".

(f) "Grantor" means a person that creates a security right in one or more of its assets in favour of a secured creditor to secure either its own obligation or that of another person (see debtor). References to the "grantor" in this Guide also refer to the "assignor".

[*Note to the Working Group: The Working Group may wish to note that the second sentence in the definitions of "security right, "secured creditor" and "grantor" is intended to ensure that the general recommendations apply to security rights in receivables and to outright transfers of receivables, unless otherwise provided.*]

(n) "Claim" means a right to the performance of a non-monetary obligation other than a right in tangibles under a negotiable document.

[*Note to the Working Group: The Working Group may wish to consider whether limited special rules are required for transactions in which a "claim" is an encumbered asset.*

As defined in the terminology chapter (see A/CN.9/WG.VI/WP.22/Add.1, para. 21 (n)), "claim" means "a right to the performance of a non-monetary obligation other than a right in tangibles under a negotiable document." For example, if a grantor has entered into a contract with another party pursuant to which the other party (the "obligor") has agreed to transfer goods to the grantor or perform services for the grantor, the grantor's right to the other party's performance is a "claim." This definition does not include rights granted by a government or a private party that owes no performance obligation with respect to those rights, such as may be the case with a State-granted licence to sell alcoholic beverages. It is not clear, though, whether this definition covers other rights, such as the right of a franchisee under a franchise agreement in which the franchisor owes no positive performance of an obligation to the franchisee (but has agreed not to sue the franchisee for using the franchisor's name) or the right of a licensee under an intellectual property licence in which the licensor owes no positive performance of an obligation to the licensee. The Working Group may wish to consider whether, in light of the discussion below concerning issues about security rights in "claims" that might require special rules, the definition of "claim" should include rights as to which the only performance obligation is to refrain from taking an action (as in the case of a franchise or license) or as to which there is no performance obligation owed to the grantor at all (as in the case of a State-granted licence to sell alcoholic beverages).

In determining whether any special rules are required for security rights in claims, several issues must be considered: (i) the rules governing creation of a security right in the claim, (ii) the rules governing the steps required for a security right in the claim to be effective against third parties, (iii) the rules governing priority of a security right in the claim over the rights of competing claimants, (iv) the rules governing enforcement of a security right in the claim as against the grantor and other parties that may have an interest in the claim deriving from the grantor, and (v) the rules governing the right of the secured creditor, or a party to which the claim has been transferred in a disposition under the enforcement procedures, to enforce the claim against the obligor. With respect to issue (v), consideration must also be given to the source of substantive law governing the rights and duties of the obligor on the claim with respect to the enforcing secured creditor or other party. With respect to all of the issues, conflict-of-laws rules that determine the State whose law is applicable must also be considered.

It would appear that the existing recommendations in the draft Guide that address security rights in other intangible movable property are sufficient to govern the first four issues with respect to security rights in claims.

Resolution of the fifth issue: the right of the secured creditor to enforce the claim against the obligor likely depends, in part, on whether, under other law, the claim is assignable (or may be enforced by an assignee). Limitations on assignment of a claim (or on the enforceability of a claim by an assignee) may result from limitations on assignment in a contract between the obligor on the claim and the obligee/grantor that is enforceable under applicable law or may arise directly by rule of law that limits assignment of certain claims even in the absence of a contractual prohibition. It should be noted in this regard that in some cases such rules of law exist for the protection of the obligor while in other cases such rules of law exist for the protection of the obligee. While the draft Guide recommends limits on the effectiveness of certain contractual anti-assignment provisions with respect to receivables, the Working Group may conclude that the economic justifications for limiting the effectiveness of those anti-assignment provisions in the case of receivables are not present when the obligation of the obligor is not monetary. Accordingly, the Working Group may conclude that the ability of the secured creditor to enforce a claim directly against the obligor may be limited by contract.

With respect to the source of substantive law governing the fifth issue, the Working Group may wish to conclude that, as in the case of security rights in other types of movable property consisting of a claim against a third party (such as receivables and negotiable instruments), the body of law that governs the claim determines the nature of the obligations of the obligor (and the extent to which contractual anti-assignment provisions or other legal anti-assignment rules are applicable).

With respect to conflict-of-laws rules, the recommendations in the conflict-of-laws chapter seem well suited to address the first four issues listed above. With respect to the fifth issue, the Working Group may wish to conclude that the State whose law governs the claim should govern.]

(o) "Receivable" means a right to the payment of a monetary obligation, excluding, however, rights to payment evidenced by a negotiable instrument, the

obligation to pay under an independent undertaking and the obligation of a bank to pay funds credited to a bank account.

[*Note to the Working Group: The Working Group may wish to note that the definition of "receivable" in the draft Guide is broader than the definition of "receivable" in article 2 (a) of the Convention in that it covers even non-contractual receivables, such as receivables arising by operation of law (e.g. tort receivables, receivables arising in the context of unjust enrichment or tax receivables), or receivables confirmed in court judgements or arbitral awards (unless incorporated in a settlement agreement). The Working Group may wish to limit the definition of "receivable" in the draft Guide to contractual receivables or consider whether the recommendations in this document should apply, with any necessary modifications, to non-contractual receivables as well.*]

(p) "Assignment" means the creation of a security right in a receivable or the outright transfer of a receivable.

[*Note to the Working Group: The Working Group may wish to note that the commentary will explain that the creation of a security right in a receivable includes an outright transfer of receivables by way of security, which is treated in the draft Guide as a security right.*]

(q) "Assignor" means the person that makes an assignment of a receivable.

[*Note to the Working Group: Article 2 (a) of the United Nations Assignment Convention.*]

(r) "Assignee" means the person to which an assignment of a receivable is made.

[*Note to the Working Group: Article 2 (a) of the United Nations Assignment Convention.*]

(s) "Subsequent assignment" means an assignment by the initial or any other assignee. In the case of a subsequent assignment, the person that makes that assignment is the assignor and the person to which that assignment is made is the assignee.

[*Note to the Working Group: Article 2 (b) of the United Nations Assignment Convention.]*

(t) "Account debtor" means a person liable for payment of a receivable.

[*Note to the Working Group: Article 2 (a) of the United Nations Assignment Convention. "Account debtor" includes a "guarantor", as an accessory guarantee is a receivable.*]

(u) "Notification of the assignment" means a communication in writing that reasonably identifies the assigned receivables and the assignee.

[*Note to the Working Group: Article 5 (d) of the United Nations Assignment Convention. According to recommendations 11 and 12 (see A/CN.9/WG.VI/WP.21), "writing" includes electronic communications and "signature" includes electronic signature. The Working Group may wish to consider including recommendations 11 and 12 in the definitions.*]

(v) "Original contract" in the context of an assignment means the contract between the assignor and the account debtor from which the assigned receivable arises.

[*Note to the Working Group: Article 5 (a) of the United Nations Assignment Convention.*]

II. Recommendations

Parties, security rights, secured obligations and assets covered (A/CN.9/WG.VI/WP.21, recs. 3 (d) and (f))

3. In particular, the law should provide that it applies to:

(d) All types of movable assets and fixtures, tangible or intangible, present or future, not specifically excluded in the law, including inventory, equipment and other goods, receivables, negotiable instruments, negotiable documents, rights to payment of funds credited to bank accounts, rights to drawing proceeds from independent undertakings, and intellectual property rights;

...

(f) Generally, outright transfers of receivables;

[*Note to the Working Group: The Working Group may wish to note that, as the definition of "receivable" in para. 21 (o) of A/CN.9/WG.VI/WP.22/Add.1 excludes rights to payment under a negotiable instrument, the obligation to pay under an independent undertaking and the obligation of a bank to pay funds credited to a bank account, recommendation 3 (f) does not apply to an outright transfer of a negotiable instrument, an independent undertaking or a right to payment of funds credited to a bank account (however, the recommendations apply to transfers of such assets for security purposes, as they are treated as secured transactions; for example, the transfer for security purposes of a right to payment of funds in a bank account is covered as a method of achieving control; see definition of "control" in A/CN.9/WG.VI/WP.26/Add.1). The Working Group may wish to consider whether the outright transfer of a negotiable instrument should be included within the scope of the draft Guide.*

There are several reasons to include such transfers. Providing clear rules for the creation, effectiveness against third parties and priority of an outright transfer of a negotiable instrument might assist financing transactions, securitizations and sales of loan participations that involve the outright transfer of negotiable instruments. Inclusion also recognizes that, since the draft Guide already includes the outright transfer of receivables within its scope, it would be a logical extension to include in the scope rights to payment that would have been receivables had they not been evidenced by negotiable instruments.

However, there are also reasons not to include outright transfers of negotiable instruments within the scope of the draft Guide. The main reason is that the benefits of inclusion may be outweighed by the burdens of adding to the draft Guide rules dealing with outright transfers of negotiable instruments. The benefits of inclusion may not be significant in those States in which the law relating to the outright transfer of negotiable instruments is already clear. The greater the number of States

that are satisfied with their current law on this subject, the less the benefits that would be provided by inclusion in the draft Guide. Moreover, the volume of financing transactions actually involving the outright transfer of negotiable instruments and the need to give the transferee sufficient protective rights in law other than the negotiable instrument law may differ from country to country.

The burdens of inclusion would be several. The Working Group would need to examine the entire draft Guide in order to determine what special rules will need to be added on such issues as creation, effectiveness against third parties and priority. In addressing effectiveness against third parties, the Working Group would need to consider whether, for the outright transfer of a negotiable instrument to be effective against third parties, the buyer must take possession of the negotiable instrument or register in the general security rights registry a notice of the outright transfer, or whether effectiveness against third parties is achieved automatically upon creation. Parties that extend credit secured by security rights in negotiable instruments may favour a possession/registration third-party effectiveness rule, while parties that buy negotiable instruments in bulk and customary buyers and sellers of loans and loan participations, may prefer an automatic third-party effectiveness rule.

A final reason to exclude outright transfers of negotiable instruments is that, as a technical matter, outright transfers of negotiable instruments concern the law of sale more than the law of secured transactions. Although the draft Guide does include outright transfers of receivables within its scope, it does so largely to protect reliance upon the registration system, which would be of little utility in establishing priority for the financing of receivables if outright transfers of receivables were excluded from the registration requirement. Similar concerns may not apply to an outright transfer of a negotiable instrument since the lender or buyer would usually have the option to obtain priority under recommendation 74 (b) (see A/CN.9/WG.VI/WP.24/Add.4) by taking possession of the negotiable instrument.

Even if the Working Group does decide that transfers of negotiable instruments should be included within the scope of the draft Guide as a general matter, the Working Group may nevertheless wish to consider whether certain exclusions are appropriate. For example, it may make sense to exclude transfers of cheques from the scope of the draft Guide even if transfers of other negotiable instruments are included. Financing transactions that involve transfers of cheques may be far less common and may be expected to remain far less common than financing transactions involving transfers of other negotiable instruments.]

Creation of a security right in receivables (see A/CN.9/WG.VI/WP.21, recs. 13, 14 and 15)

Assets and obligations subject to a security agreement

13. The law should specify that a security right may secure all types of obligation, including future, conditional and fluctuating obligations. It should also specify that a security right may be given in all types of asset, including parts of assets and undivided interests in assets and assets which, at the time of the security agreement, the grantor may not yet own or have the power to dispose of, or which may not yet exist, as well as in proceeds. Any exceptions to these rules should be limited and described clearly in the law.

Effectiveness of a bulk assignment and an assignment of future, parts of and undivided interests in receivables

14. The law should provide that:

(a) The assignment of receivables that are not specifically identified, future receivables and parts of or undivided interests in receivables is effective as between the assignor and the assignee and as against the account debtor, as long as, at the time of the assignment or, in the case of future receivables, at the time they arise, they can be identified to the assignment to which they relate; and

(b) Unless otherwise agreed, an assignment of one or more future receivables is effective without a new act of transfer being required to assign each receivable.

[*Note to the Working Group: Article 8 of the United Nations Assignment Convention. The Working Group may wish to note that the commentary will explain that the general recommendations apply unless modified by asset-specific recommendations.*]

Effectiveness of an assignment made despite an anti-assignment clause

15. The law should provide that:

(a) An assignment is effective as between the assignor and the assignee and as against the account debtor notwithstanding an agreement between the initial or any subsequent assignor and the account debtor or subsequent assignee limiting in any way the assignor's right to assign its receivables;

[*Note to the Working Group: The Working Group may wish to note that the commentary will explain that recommendation 15 (a) makes ineffective only an agreement between an obligor and an obligee that limits the obligee's right to assign a receivable owed by the obligor to the obligee. If such a receivable is assigned, the obligor is the "account debtor" and the obligee is the "assignor".*

For example, if an agreement for the lease of goods limits the lessor's right to assign the rents due to it under the lease, recommendation 15 (a) makes the limitation on assignment ineffective, because the agreement is between the obligor (the lessee) and the obligee (the lessor) of the receivable (the rent arising from the lease agreement) By way of contrast, if the lease agreement between the lessor and the lessee limits the lessee's right to assign a receivable consisting of the lessee's claim to rents due to the lessee from the sublessee under a sublease, recommendation 15 (a) has no application, and nothing in this Guide makes the limitation ineffective. That is because the agreement limiting the right of the lessee to assign its claim for rents due to it from the sublessee under the sublease is not an agreement between the lessee (sublessor and obligee in a sublease) and the sublessee (obligor in the sublease). Whether the limitation in the lease is enforceable against the lessee would be determined by the law other than the law recommended in this Guide.

The same analysis would apply if the restriction on transfer was contained in a licence of intellectual property. Recommendation 15 (a) would render ineffective a term in the licence agreement that restricted the licensor from assigning fees due from the licensee. However, it would not render ineffective a term in the licence agreement restricting the licensee from assigning sublicence fees. Whether the latter

term would be effective would be determined by law other than that recommended in the draft Guide.]

(b) If other law creates any obligation or liability of the assignor for breach of such an agreement, the other party to such an agreement may not avoid the contract from which the assigned receivables arise or the assignment contract on the sole ground of that breach. A person who is not a party to such an agreement is not liable on the sole ground that it had knowledge of the agreement;

[(c) This recommendation applies only to assignments of receivables:

(i) Arising from an original contract that is a contract for the supply or lease of goods or services other than financial services, a construction contract or a contract for the sale or lease of real property;

(ii) Arising from an original contract for the sale, lease or licence of industrial or other intellectual property or of proprietary information;

(iii) Representing the payment obligation for a credit card transaction;

(iv) Owed to the assignor upon net settlement of payments due pursuant to a netting agreement involving more than two parties.]

[*Note to the Working Group: The Working Group may wish to note that the commentary will clarify that contract avoidance referred to in paragraph (b) means contract termination in general.*]

Creation of a security right in a right that secures an assigned receivable, a negotiable instrument or any other obligation (see A/CN.9/WG.VI/WP.24/Add.2)

16. The law should provide that upon creation of a security right in a receivable, a negotiable instrument or any other obligation covered as an encumbered asset by this Guide, a security right is automatically created, without further action by either the grantor or the secured creditor, in any personal or property right that secures payment or performance of that receivable, negotiable instrument, or other obligation. If, under the law governing a right that secures payment of a receivable, negotiable instrument or other obligation covered as an encumbered asset by this Guide, a security right in that securing right may be created only after a separate act of creation, the grantor is obligated to take such action. When an independent undertaking secures payment or performance of a receivable, a negotiable instrument or any other obligation covered as an encumbered asset by this Guide, a security right in a right to drawing proceeds from the independent undertaking is created without a separate act of creation by the grantor.

[*Note to the Working Group: The Working Group may wish to note that the second sentence of recommendation 16 refers to " law governing a right". The law recommended in the draft Guide may be this domestic law. The Working Group may also wish to note that the second sentence of recommendation 16, which is based on the second sentence of article 10 (1) of the United Nations Assignment Convention, was intended to refer to independent rights so as to safeguard the interests of the obligor of an independent right, such as an independent undertaking (see Analytical commentary on the draft Convention, A/CN.9/489, para. 105). This result may be better achieved in a domestic law, such as the law recommended in the draft Guide, by language along the following lines: "This recommendation does not create a*

security right in an independent right, such as an independent undertaking, and does not affect the rights and obligations of an obligor of an independent right, such as a guarantor/issuer of or nominated person in an independent undertaking." If the Working Group adopts this wording, the second sentence of recommendation 16 could be deleted. As the third sentence of recommendation 16 is intended to carve out of the second sentence rights to receive payment under an independent undertaking, the third sentence could also be deleted.

Financing transactions that fall under the first sentence of recommendation 16 would thus be facilitated. Such transactions include securitizations of pools of loans secured by security rights in movables and immovables. In these cases the buyer of the loans will want to be able to look to the security rights securing the loans but would not want to incur, at the outset of the purchase, the additional expense of a separate act of transfer (if required under law other than the law recommended in the draft Guide) for each loan in the pool of loans, that could number in the hundreds or thousands. Separate acts of transfer, if any, would be necessary (if required under other law) to enforce only those loans that are later in default, typically a small proportion of the loans in the pool actually purchased. The buyer could decide whether to accept the expense of separate acts of transfer at the time of enforcement, whether voluntarily from the seller or with the assistance of a court. But, in deciding whether to purchase the loans and at what price, the buyer would take into account the expense of separate acts of transfer only for the small portion of the loans expected to be in default, not for the entire pool of loans. As a result of the expense savings, the seller should be able to obtain a higher purchase price, thereby making more funds available to the seller.

The Working Group may wish to consider whether: (i) recommendation 16 apply to outright transfers of receivables (but not of negotiable instruments or other obligations as the draft Guide generally applies only to outright transfers of receivables), since, even in the case of an outright transfer of a receivable, rights securing payment of the receivable should follow); and (ii) recommendation 16 should be supplemented by recommendations along the lines of paras. (2) to (6) of article 10 of the Convention (for para. (2) to (4) see rec. 15 above; for paras. (5) and (6), see below).

"The creation of a security right in [or the outright transfer of] a possessory property right under paragraph 1 of this recommendation does not affect any obligations of the assignor to the account debtor or the person granting the property right with respect to the relevant property existing under the law governing that property right."

According to this wording, if the security right in or the transfer of a security right involves the delivery of possession of an asset and such delivery causes loss or prejudice to the account debtor or the person granting the right, any liability that may exist under law applicable outside the law recommended in the draft Guide is not affected. This may arise, for example, in the case of a delivery of possession of an item of valuable tangible property if the secured creditor or transferee damages or loses the property.

"This recommendation does not affect any requirement under law other than this law relating to the form or registration of the creation of security rights in [or

the outright transfer of] any rights securing payment of the assigned receivable, negotiable instrument or other obligation."

This wording makes it clear that, the form of transfer of a security right in an asset outside the scope of this law (e.g. an immovable) is left to law other than this law. Accordingly, a notarized document and registration may be necessary for the transferee of a mortgage to obtain various rights under immovables law, such the right to enforce the mortgage.]

Pre-default rights and obligations of the assignor and the assignee

[*Note to the Working Group: The Working Group may wish to include recommendations dealing with the rights and obligations of the assignor and the assignee in the chapter on the pre-default rights and obligations of the parties. These recommendations could be based on articles 11 to 14 of the United Nations Assignment Convention.*]

Rights and obligations of the assignor and the assignee

16 bis The law should provide that:

(a) The mutual rights and obligations of the assignor and the assignee arising from their agreement are determined by the terms and conditions set forth in that agreement, including any rules or general conditions referred to therein;

(b) The assignor and the assignee are bound by any usage to which they have agreed and, unless otherwise agreed, by any practices they have established between themselves[;

(c) In an international assignment, the assignor and the assignee are considered, unless otherwise agreed, implicitly to have made applicable to the assignment a usage that in international trade is widely known to, and regularly observed by, parties to the particular type of assignment or to the assignment of the particular category of receivables].

[*Note to the Working Group: The Working Group may wish to consider whether paragraph (c) would fit in a domestic law. If paragraph (c) were to be included, "international assignment" might need to be defined.*]

Representations of the assignor

16 ter The law should provide that:

(a) Unless otherwise agreed between the assignor and the assignee, the assignor represents at the time of conclusion of the contract of assignment that:

(i) The assignor has the right to assign the receivable;

(ii) The assignor has not previously assigned the receivable to another assignee; and

(iii) The account debtor does not and will not have any defences or rights of set off;

(b) Unless otherwise agreed between the assignor and the assignee, the assignor does not represent that the account debtor has, or will have, the ability to pay.

Right to notify the account debtor

16 quater The law should provide that:

(a) Unless otherwise agreed between the assignor and the assignee, the assignor or the assignee or both may send the account debtor notification of the assignment and a payment instruction, but after notification has been sent only the assignee may send such an instruction; and

(b) Notification of the assignment or a payment instruction sent in breach of any agreement referred to in paragraph (a) of this recommendation is not ineffective for the purposes of recommendation 19 by reason of such breach. However, nothing in this recommendation affects any obligation or liability of the party in breach of such an agreement for any damages arising as a result of the breach.

Right to payment

16 quinquiens The law should provide that:

(a) As between the assignor and the assignee, unless otherwise agreed and whether or not notification of the assignment has been sent:

(i) If payment in respect of the assigned receivable is made to the assignee, the assignee is entitled to retain the proceeds and goods returned in respect of the assigned receivable;

(ii) If payment in respect of the assigned receivable is made to the assignor, the assignee is entitled to payment of the proceeds and also to goods returned to the assignor in respect of the assigned receivable; and

(iii) If payment in respect of the assigned receivable is made to another person over whom the assignee has priority, the assignee is entitled to payment of the proceeds and also to goods returned to such person in respect of the assigned receivable;

(b) The assignee may not retain more than the value of its right in the receivable.

Rights and obligations of the account debtor and the assignee (see A/CN.9/WG.VI/WP.21, recs. 17-23)

Principle of account debtor protection

[*Note to the Working Group: Recommendations 17 to 23 are based on articles 15-21 of the United Nations Assignment Convention.*]

17. The law should provide that:

(a) Except as otherwise provided in this law, an assignment does not, without the consent of the account debtor, affect the rights and obligations of the account debtor, including the payment terms contained in the original contract;

(b) A payment instruction may change the person, address or account to which the account debtor is required to make payment, but may not change:

(i) The currency of payment specified in the original contract; or

(ii) The State specified in the original contract in which payment is to be made to a State other than that in which the account debtor is located.

[*Note to the Working Group: The Working Group may wish to consider whether subparagraph (b)(ii) should refer to "place" rather than "State", so as to preclude a change in the place of payment even in a single State. The Working Group may also wish to note that references to "the original contract" would need to be adjusted if the Working Group decides that these recommendations should apply even to non-contractual receivables (see Note after the definition of "receivable" above).*]

Notification of the account debtor

18. The law should provide that:

(a) Notification of the assignment or a payment instruction is effective when received by the account debtor if it is in a language that is reasonably expected to inform the account debtor about its contents. It is sufficient if notification of the assignment or a payment instruction is in the language of the original contract; and

(b) Notification of the assignment or a payment instruction may relate to receivables arising after notification and that notification of a subsequent assignment constitutes notification of all prior assignments.

Discharge of the account debtor by payment

19. The law should provide that:

(a) Until the account debtor receives notification of the assignment, it is entitled to be discharged by paying in accordance with the original contract;

(b) After the account debtor receives notification of the assignment, subject to paragraphs (c) to (h) of this recommendation, it is discharged only by paying the assignee or, if otherwise instructed in the notification of the assignment or subsequently by the assignee in a writing received by the account debtor, in accordance with such payment instruction;

(c) If the account debtor receives more than one payment instruction relating to a single assignment of the same receivable by the same assignor, it is discharged by paying in accordance with the last payment instruction received from the assignee before payment;

(d) If the account debtor receives notification of more than one assignment of the same receivable made by the same assignor, it is discharged by paying in accordance with the first notification received;

(e) If the account debtor receives notification of one or more subsequent assignments, it is discharged by paying in accordance with the notification of the last of such subsequent assignments;

(f) If the account debtor receives notification of the assignment of a part of or an undivided interest in one or more receivables, it is discharged by paying in accordance with the notification or in accordance with this recommendation as if the account debtor had not received the notification. If the account debtor pays in accordance with the notification, it is discharged only to the extent of the part or undivided interest paid.

(g) If the account debtor receives notification of the assignment from the assignee, it is entitled to request the assignee to provide within a reasonable period

of time adequate proof that the assignment from the initial assignor to the initial assignee and any intermediate assignment have been made and, unless the assignee does so, the account debtor is discharged by paying in accordance with this recommendation as if the notification from the assignee had not been received. Adequate proof of an assignment includes but is not limited to any writing emanating from the assignor and indicating that the assignment has taken place.

(h) This recommendation does not affect any other ground on which payment by the account debtor to the person entitled to payment, to a competent judicial or other authority, or to a public deposit fund discharges the account debtor.

Defences and rights of set-off of the account debtor

20. The law should provide that:

(a) In a claim by the assignee against the account debtor for payment of the assigned receivable, the account debtor may raise against the assignee all defences and rights of set-off arising from the original contract, or any other contract that was part of the same transaction, of which the account debtor could avail itself as if the assignment had not been made and such claim were made by the assignor;

(b) The account debtor may raise against the assignee any other right of set-off, provided that it was available to the account debtor at the time notification of the assignment was received by the account debtor;

(c) Notwithstanding paragraphs (a) and (b) of this recommendation, defences and rights of set-off that the account debtor may raise pursuant to recommendations 15 and 16 against the assignor for breach of an agreement limiting in any way the assignor's right to make the assignment are not available to the account debtor against the assignee.

[*Note to the Working Group: The Working Group may wish to note that, under recommendation 3 (a) (see A/CN.9/WG.VI/WP.21), the draft Guide applies to consumers but does affect the rights of consumers under consumer-protection law.*]

Agreement not to raise defences or rights of set-off

21. The law should provide that:

(a) The account debtor may agree with the assignor in a writing signed by the account debtor not to raise against the assignee the defences and rights of set-off that it could raise pursuant to recommendation 20. Such an agreement precludes the account debtor from raising against the assignee those defences and rights of set-off;

(b) The account debtor may not waive defences:

(i) Arising from fraudulent acts on the part of the assignee; or

(ii) Based on the account debtor's incapacity;

(c) Such an agreement may be modified only by an agreement in a writing signed by the account debtor. The effect of such a modification as against the assignee is determined by recommendation 22, paragraph (b).

[*Note to the Working Group: Recommendation 21 is based on article 19 of the United Nations Assignment Convention, which refers to a signed writing only for a waiver of defences or its modification. If the Working Group decides not to refer to*

signature in recommendation 8 (see A/CN.9/WG.VI/WP.21) but rather to evidence that the grantor intended to grant a security right, it may wish to reconsider the reference to signature in recommendation 21. If reference to signature is retained in recommendation 8, an electronic signature should be sufficient (see note after definition (u).]

Modification of the original contract

22. The law should provide that:

(a) An agreement concluded before notification of the assignment between the assignor and the account debtor that affects the assignee's rights is effective as against the assignee, and the assignee acquires corresponding rights;

(b) An agreement concluded after notification of the assignment between the assignor and the account debtor that affects the assignee's rights is ineffective as against the assignee unless:

(i) The assignee consents to it; or

(ii) The receivable is not fully earned by performance and either the modification is provided for in the original contract or, in the context of the original contract, a reasonable assignee would consent to the modification.

(c) Paragraphs (a) and (b) of this recommendation do not affect any right of the assignor or the assignee arising from breach of an agreement between them.

Recovery of payments

23. The law should provide that failure of the assignor to perform the original contract does not entitle the account debtor to recover from the assignee a sum paid by the account debtor to the assignor or the assignee.

[*Note to the Working Group: The Working Group may wish to note that the commentary will explain that recommendation 23 does not affect any liability of the assignor towards the account debtor for breach of contract.*].

Third-party effectiveness of a security right in receivables (see A/CN.9/WG.VI/WP.24/Add.3, rec. 37)

37. The law should provide that the right of an assignee under an outright assignment of receivables becomes effective against third parties by registration of a notice of the right in the general security rights registry.

[*Note to the Working Group: The Working Group will recall that at its ninth session it decided that text of recommendation 37 should be placed in the commentary as it repeats the general third-party effectiveness rule (see A/CN.9/593, para. 18).*]

Priority of security rights in receivables (A/CN.9/WG.VI/WP.24/Add.4, recs. 80 and 81)

[*Note to the Working Group: The Working Group may wish to note that the commentary will explain that the general priority recommendations apply to security rights in receivables, as well as to outright transfers of receivables.*]

Enforcement of a security right in receivables (A/CN.9/WG.VI/WP.24/Add.1, recs. 88, 102 and 103)

Application of this chapter to outright transfers of receivables

88. The law should provide that this chapter applies to the enforcement of the rights of a transferee of receivables acquired by means of an outright transfer only to the extent that, pursuant to the terms of the transfer, there is recourse to the transferor for a payment default of the account debtor.

[*Note to the Working Group: The Working Group may wish to note that recommendation 88 is intended to clarify that, although the Guide applies generally to outright transfers of receivables, this chapter applies to transfers of receivables only if there is recourse to the transferor.*]

Collection of receivables

102. With respect to a receivable that is an encumbered asset, the law should provide that after default or before default with the agreement of the assignor the secured creditor may collect or otherwise enforce the receivable.

[*Note to the Working Group: The Working Group may wish to note that the commentary will explain that the secured creditor may, as an alternative, elect to dispose of or retain a receivable pursuant to recommendations 93 (d), (e), 110 and 113 (see A/CN.9/WG.VI/WP.24/Add.1). The commentary will also explain that the assignee may send a notification and a payment instruction even in breach of an agreement with the assignor (see rec. 16 quater bis above).*]

103. The law should provide that the secured creditor's right to collect or otherwise enforce a receivable includes the right to collect or otherwise enforce any personal or property right that secures payment of the receivable (such as a guarantee or security right).

[*Note to the Working Group: The Working Group may wish to note that the commentary will discuss how other recommendations of the chapter on enforcement may apply to the enforcement of a right securing payment of an assigned receivable.*]

Law applicable to security rights in intangible property (A/CN.9/WG.VI/WP.24)

137. The law should provide that the creation, the effectiveness against third parties and the priority over the rights of competing claimants of a security right in intangible property are governed by the law of the State in which the grantor is located. [However, with respect to security rights in intangible property that is subject to a title registration system, the law should provide that such issues are governed by the law of the State in which […].]

[137 bis The law should provide that the law of the State in which the assignor is located governs the creation, third-party effectiveness and priority of a security right in a receivable arising from a sale or lease of, or a security agreement relating to, an immovable over the rights of competing claimants. However, a priority conflict involving the rights of a competing third party registered in the immovables registry of the State in which the immovable is located is governed by the law of that State.]

[*Note to the Working Group: The Working Group may wish to consider adding a new recommendation along the lines of recommendation 137 bis, which is designed to address the law applicable to assignments of receivables owing to the grantor under an agreement for the sale or lease of an immovable or under a security agreement over an immovable. In a number of States, it is not possible to create rights in such receivables independently of the related immovable with the result that the effectiveness as between the parties, the third- party effectiveness and the priority of a security right in the receivables is governed by the law (and, in particular, the registry regime) that applies to the related immovable. In other States, it is possible to grant a security right in such receivables independently of the related immovable but the secured creditor is subordinated to third-party rights that are registered against the related immovable in the immovables registry. The second sentence of recommendation 137 bis is designed to preserve the application of the law of the State where the related immovable is located in order to protect third parties who rely on the registration in the immovables registry of that State. Reference is made to rights of a competing third party as the term "competing claimant" is defined by reference to security rights in movables. Reference is also made to "rights" of such parties, since rights of third parties could include not just competing mortgagees but also assignees or buyers of the immovable or the related intangible and indeed any class of third party right for which the immovables regime makes provision for registration. In addition, reference is made to a right "registered in the immovables registry" rather than "that became effective against third parties by registration", since: (i) some immovables registries do not distinguish between inter-parties and third party effectiveness, and (ii) immovables registries do not necessarily require registration for general third-party effectiveness but only for effectiveness against third parties whose rights are also registrable in the immovables registry (e.g. registration may not be needed for effectiveness against an insolvency administrator or a judgment creditor.*]

Law applicable to the rights and obligations of the grantor and the secured creditor

146. The law should provide that the mutual rights and obligations of the grantor and the secured creditor with respect to the security right, whether arising from the security agreement or by law, are governed by the law chosen by them and, in the absence of a choice of law, by the law governing the security agreement.

Law applicable to the rights and obligations of the account debtor and the assignee, the obligor under a negotiable instrument or the issuer of a negotiable document and the secured creditor

147. The law should provide that the following matters are governed by the law of the State whose law governs an assigned receivable, or a negotiable instrument or a negotiable document in which a security right has been created:

(a) The relationship between an account debtor and an assignee of the receivable, between an obligor under a negotiable instrument and a creditor with a security right in that instrument or between an issuer of a negotiable document and a creditor with a security right in that document;

(b) The conditions under which the assignment of the receivable, the transfer of the negotiable instrument or the transfer of the negotiable document can be

invoked against the account debtor, the obligor on the negotiable instrument or the issuer of the negotiable document; and

(c) The determination of whether the obligations of the account debtor, the obligor on the negotiable instrument or the issuer of the negotiable document have been discharged.

[*Note to the Working Group: The Working Group may wish to note that the commentary will explain that: (i) recommendation 148 applies to the enforcement of a security right in a receivable (A/CN.9/WG.VI/WP.24); and (ii) the recommendations on the impact of insolvency on the law applicable, as well as the other general recommendations in the conflict-of-laws chapter (A/CN.9/WG.VI/WP.24), apply to security rights in receivables.*]