

**DPhil Thesis**

**Establishing an International Registration System for the  
Assignment and Security Interest of Receivables**

Supervisor:

Professor Louise Gullifer  
Harris Manchester College

Woo-Jung Jon

St Antony's College  
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# Establishing an International Registration System for the Assignment and Security Interest of Receivables

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## **ABSTRACT**

Legal systems around the world vary widely in how they deal with the assignment of receivables. This legal variety makes it difficult for financiers to conduct their international receivables financing business. This thesis suggests an International Registration System for the Assignment and Security Interest of Receivables ('IRSAR') and proposes a model international convention for the IRSAR ('proposed IRSAR Convention'), which could help financiers to overcome the obstacles they currently encounter. Under the proposed IRSAR Convention, the international assignment of receivables would be regulated by a unified legal system with respect to priority and perfection. The IRSAR would facilitate international project financing. Furthermore, the IRSAR would enable companies to raise finance from greater ranges of investors around the world through international receivables financing and to dispose of non-performing loans more easily.

The proposed IRSAR Convention would succeed the UN Convention on the Assignment of Receivables in International Trade in the attempt of establishing a registration system for international assignments of receivables. The proposed IRSAR Convention confines its scope of application by defining the assignor (or the security provider), inventing the concept of ‘Vehicle for the International Registration System’ (‘VIRS’). The proposed IRSAR Convention applies where the assignor or security provider is a VIRS. An assignment of a receivable where the assignor is a VIRS and a security interest in a receivable where the security provider is a VIRS could be registered in the IRSAR. Under the proposed IRSAR Convention, priority of assignments of and security interests in receivables is determined by the order of registration in the IRSAR.

The proposed IRSAR Convention would be a receivables version of the Cape Town Convention. With respect to the contents and effect of registration, it would prescribe a notice-filing system along the lines of that adopted in the UCC Article 9. With respect to the operation of the registration, it would adopt an automatic online registration system operating 24 hours a day, 365 days a year like the International Registry under the Cape Town Convention.

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I studied at Seoul National University College of Law in Seoul, Korea, Peking University Law School and Tsinghua University Law School in Beijing, China, Tokyo University Faculty of Law in Tokyo, Japan, and researched at the United Nations Commission on International Trade Law (UNCITRAL) in Vienna, Austria, the International Institute for the Unification of Private Law (UNIDROIT) in Rome, Italy and the Max Planck Institute for Comparative and International Private Law in Hamburg, Germany.

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Austria Personal Property Securities Register

<http://www.ppsr.gov.au>

Japanese Assignment Registration

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Wisconsin UCC Filing

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## **PART 1. INTRODUCTION**

### **1-1. Purpose of this Thesis**

This thesis proposes an international registration system to facilitate international assignments of receivables. The assignment of receivables is critical in raising finance and there are various problems involved in international assignments. It is proposed that the best way to such problems is an international register of assignments of receivables. An international registration system for the assignment of receivables could be an effective method to facilitate international capital movements. The purpose of this thesis is to propose a model international registration system for the assignment of receivables. This introduction will review the use of receivables in financing. It will make clear that this proposal is focused on receivables other than tangible movable assets. Furthermore, it will present the structure of this thesis.

The term, a 'receivable' is a generic description of a right to payment of a monetary obligation. It includes rights to payment for goods sold or leased, facilities made available or services rendered.<sup>1</sup> Receivables form an integral part of the assets of every trading company, for example, insurance premiums, credit card debts, freights, and real and personal property rentals. Receivables may be used to provide working capital by outright sale with discounting or as security for a loan. Therefore receivables are generally considered an ideal basis for short-term finance.<sup>2</sup> Receivables financing also helps small and mid-sized companies that do not have sufficient real estate to mortgage

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<sup>1</sup> Fidelis Oditah, *Legal Aspects of Receivables Financing* (Sweet & Maxwell, London 1991) 19.

<sup>2</sup> *ibid* 2-3.

for a loan. Receivables are potentially the single largest category of assets transferred in cross-border financing transactions.<sup>3</sup>

With respect to assignments of and security interests in receivables, a domestic registry and an international registry have different purposes. The main purpose of a domestic registry for the assignment of receivables is to help companies (especially small and mid-sized companies which do not have enough collateral) to finance using their receivables as collateral.

The main purpose of an international registry for the assignment of receivables, which would include both outright assignments and security assignments, is to facilitate international receivables financing that could solve national financial crises. Where the effect of a financial crisis is within a national boundary, domestic receivables financing could not help to solve such a crisis because all companies in the nation are affected. In this case, international receivables financing can help eliminate non-performing loans in the affected nation. Receivables financing could help disposal of non-performing loans and mitigate liquidity risk. International receivables financing is particularly important when a financial crisis affects a country. During a financial crisis, an influx of foreign capital is necessary to combat the frozen cash-flow circulation.

For example, after the collapse of the bubble economy in Japan in 1991, Japan disposed of non-performing loans to foreign investors through securitisation. At that time, many American and European investment companies created branch offices or Special Purpose Companies ('SPCs') in Japan for the sole purpose of perfecting the

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<sup>3</sup> Steven L. Schwarcz, 'Towards a Centralized Perfection System for Cross-border Receivables Financing' (Fall 1999) 20 *University of Pennsylvania Journal of International Economic Law* 455, 455.

assignment of receivables under Japanese law. After the financial crisis of Korea in 1997, Korea disposed of non-performing loans to foreign investors through securitisation. Subsequently, a number of Korean financial institutions created SPCs both in Korea and in Hong Kong to sell securitisations in the Hong Kong financial markets. Today, Japan has a domestic registration system for the assignment of receivables. Nevertheless, in international assignments of receivables between Japan and the United State, legal practitioners would usually register the assignment of receivables both in Japan and in the US in order to ensure the perfection of the assignment.<sup>4</sup>

Under the international registration system this thesis proposes, foreign investors (assignees) would only have to register the assignment of receivables at the international registry in the case of cross-border assignments of receivables. An assignor could directly dispose of its receivables to foreign investors. A foreign investor could directly purchase the receivables without concerning itself with perfection requirements under domestic laws. If an investor (assignee) registers the assignment of receivables in an international registry, the investor would be entitled to enforce his priority based on the registration in any state that has joined the international convention for it.

Furthermore, an international registration system would facilitate international bank loans using receivables as collateral. A company could easily obtain loans using its receivables as collateral from a foreign bank of a neighbouring country or international banks such as the IMF. For example, a Spanish company could easily obtain loans using

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<sup>4</sup> Email from Takashi Asada (Head of Legal Engineering Group, Legal Department, Sumitomo Mitsui Banking Corporation) to author (25 August 2008)

its receivables as collateral from a German bank. A Korean company could easily obtain loans using its receivables as collateral from a Chinese bank.

If it were regulated by a single international legal system, international financiers would not need to give notice to debtors of receivables or register their security interests in a domestic registry of a foreign country. All they would have to do is to register their security interests in receivables with an international registration system for perfection against third parties. This would substantially reduce transaction costs in international financing.

Under the proposed international registration system, companies located in states with no established capital market would be able to raise funds from established capital markets across national borders through international receivables financing including factoring and securitisation. Factoring, block discounting without recourse and securitisation are receivables financing structures using outright assignments of receivables.

The IRSAR would pave the way for the cross-border assignment of receivables and could help receivables financing to cross national borders, enabling entrepreneurs to raise funds from a greater range of investors around the world **without** needing to heed foreign domestic laws or coping with foreign languages. It would ultimately result in a more efficient distribution of capital at a global level.

The IRSAR would also facilitate international project financing. For example, in the case of a power station construction project in a country in Africa, the power station would provide a stable cash flow of future receivables. A foreign investor could perfect assignments of or security interests in the future receivables of the power station by

registering them in the IRSAR without having to be concerned with the domestic laws of the country involved.

The purpose of this thesis is to propose an international registration system for assignments of and security interests in receivables to facilitate such international receivables financing.

## **1-2. Assignments of Receivables**

### 1-2-1. International Assignments of Receivables

International assignments of receivables are important in disposal of non-performing loans, securitisation and factoring. Today, with rapid globalisation, goods and services are traded across national borders, specifically, capital moves across national borders. Capital mobility enables the total savings of the world to be distributed among countries that have the highest investment potential. Under these circumstances, one country's growth is not constrained by its own domestic savings.<sup>5</sup> International capital movements have been made mostly through stock and bond markets. However, this was one of the causes of financial crisis as stock markets are quite unstable. The volatility in stock markets and the ease with which funds can be withdrawn from countries and following liquidity risk have often created financial crises. Assignments of receivables

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<sup>5</sup> C. Rangarajan, 'Responding to Globalization: India's Answer', 4th Ramanbhai Patel Memorial Lecture on Excellence in Education (New Delhi, February 25, 2006) 3 <[http://eac.gov.in/aboutus/chspe/55GLOBALIZATION%20AND%20CHALLENGES%20BEFORE%](http://eac.gov.in/aboutus/chspe/55GLOBALIZATION%20AND%20CHALLENGES%20BEFORE%20)> accessed 5 January 2011.

can mitigate such liquidity risk since by selling outstanding receivables a company may get immediate cash influx.

Receivables are the objects of investment through factoring, block discounting, securitisation, and other similar methods. Receivables financing such as factoring, block discounting or securitisation provides liquidity and prevents insolvency from temporary cash-flow shortage or liquidity risk.<sup>6</sup> However, there are various problems involved in international assignments of receivables.

## 1-2-2. Securitisation

Securitisation is defined as creating tradable financial instruments from a number of non-tradable financial assets.<sup>7</sup> In a typical securitisation transaction, the originator sells rights to payment from income-producing financial assets, such as credit card receivables, loans or lease, to a special purpose vehicle ('SPV'). The SPV issues securities to capital market investors and uses the proceeds of the issuance to pay the originator for the receivables. The investors in the securities are repaid from collection of the receivables. Thus, they buy the securities based on their assessment of the value of the receivables. The function of securitisation is the transfer and dispersion of risk.

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<sup>6</sup> 'Cash flow insolvency' is described in Insolvency Act 1986, s 123(1)(e) as follows: 'A company is deemed unable to pay its debts - ... (e) if it is proved to the satisfaction of the court that the company is unable to pay its debts as they fall due.' The opposite concept of 'cash flow insolvency' is 'balance sheet insolvency' which is described in Insolvency Act 1986, s 123(2): 'A company is also deemed unable to pay its debts if it is proved to the satisfaction of the court that the value of the company's assets is less than the amount of its liabilities, taking into account its contingent and prospective liabilities.'

<sup>7</sup> Steven L. Schwarcz, 'Securitisation Post-Enron' (2004) 25 *Cardozo Law Review* 1539, 1540

Financial markets promote the availability of capital and credit at optimal rates.<sup>8</sup> Currently, however, if companies in countries without established capital markets wish to raise funds from established capital markets such as New York, London, Hong Kong and other major financial centres,<sup>9</sup> those companies will have to structure deals that cross national borders through securitisation. For this reason, securitisation has an increasingly international focus.<sup>10</sup> Securitisations are often used for cross-border fund raising because the cross-border assignment of receivables confronts difficult legal issues due to the different legal systems of each jurisdiction.

### 1-2-3. Factoring

A company may also enter into factoring on the strength of their receivables, where it has the receivables to be assigned. As a result, receivables are no longer simply claims and contractual obligations between the two parties who made the original contract, but become reified objects that could be bought or sold as assets in the financial markets.

In factoring, a business sells its accounts receivable at a discount. Factoring<sup>11</sup> is classified according to whether a factor provides a debt collection service and whether a factor offers the acceptance of the risk of debtor's non-payment.<sup>12</sup>

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<sup>8</sup> UNCITRAL 'Explanatory note on the United Nations Convention on the Assignment of Receivables in International Trade' A/CN.9/557, 3.

<sup>9</sup> Steven L. Schwarcz, 'The Universal Language of International Securitization' (2002) 12 *Duke Journal of Comparative & International Law* 285, 288 n 10.

<sup>10</sup> *ibid* 288.

<sup>11</sup> This terminology is used in English law. Internationally 'factoring' has a wider meaning.

Non-recourse factoring is the traditional method of factoring and puts the full risk of debtor's non-payment on the factor. If the debtor cannot pay the debt, it is the factor's responsibility and the factor cannot seek payment from the seller. The factor will only purchase solid credit worthy invoices and often turns away average credit quality customers. The cost for the seller is typically higher with this factoring process since the factor assumes a greater risk.

On the other hand, an assignor who is not concerned about risk will sell on a recourse basis, giving a factor the right to resell debts that go into default to the seller (original creditor). Here, the credit risk that the factor might not be able to collect the debt due to the debtor's default or bankruptcy does not transfer to the factor. Recourse factoring is similar to the security assignment of receivables. Recourse factoring is typically the lowest cost for the seller because the risk for the factor on the funding transaction is lower.<sup>13</sup>

For such factoring, differing perfection requirements and priority criteria with respect to the assignment of receivables in each jurisdiction are problems.<sup>14</sup> This thesis proposes that the best way to solve such problems is an internationally unified registration system for the assignment of receivables.

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<sup>12</sup> Roy Goode and Ewan McKendrick, *Goode on Commercial Law* (4th edn Penguin Books 2010) 788-90

<sup>13</sup> UNCITRAL, 'Receivables financing: analytical commentary on the draft Convention on Assignment of Receivables in International Trade' (A/CN.9/489, UNCITRAL 2001) [10].

<sup>14</sup> See Section 3-5-1-2

### **1-3. Security Interests in Receivables**

Using receivables as security is useful in raising finance. Creating a security interest in receivables is better for the debtor than encumbering movable assets or real estate. This is because movable assets and real estate are commonly essential for manufacturing goods or providing services. If a secured creditor enforces the security interest, a debtor would lose encumbered movable assets and real estate, and consequently would not be able to operate the business. Receivables are different. Even though a debtor grants security over the receivables, it can continue to operate the business. Also, receivables provide extra collateral.<sup>15</sup> An international registration system for security interests in receivables will assist international financiers with obtaining security interests internationally.

### **1-4. Security Assignment of Receivables**

In addition to an outright assignment of receivables and a security interest in receivables, there is a hybrid security interest i.e. a security assignment of receivables. The international registration system this thesis proposes should cover all these three categories of receivables transactions.

A security assignment of receivables is an assignment of receivables for security purposes. The difference between a security assignment and an outright assignment is that in a security assignment the assignor may get back his right to the receivables after fulfilling the debt payment to the assignee, which the receivables secured. Nevertheless, a

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<sup>15</sup> Many lenders would want all assets encumbered.

security assignment of receivables functions to induce economically similar result as an outright assignment of receivables with recourse. In an assignment of receivables with recourse, if debtors of receivables fail to pay the receivables to the assignee, the assignee can request the assignor to buy back the receivables.

For example, in an English mortgage (security assignment) on receivables, the receivable is assigned to the assignee (secured creditor). This means that the assignee (secured creditor) may collect the proceeds directly from the debtor of the receivable. For example, V may borrow money from B and assign its receivable to B as security. If V pays the debt to B before the due date, V has the right to have the receivable reassigned to V. If V fails to pay the debt to B before the due date, B may give notice of the assignment to the account debtor of the receivable and collect the receivable directly from the account debtor, returning the remainder to V after satisfying the debt.

An assignment with recourse functions in the same way as a security assignment. In an assignment with recourse, V may assign its receivable to C with recourse and obtain the price of the receivable as consideration. C may give notice of the assignment to the account debtor of the receivable and collect the receivable directly from the account debtor. If the account debtor fails to pay the receivable to C, C may ask V to repurchase the receivable from C at the same price as sold.

In some jurisdictions, a security assignment of receivables is treated as an outright assignment of receivables because a security assignment is an assignment.<sup>16</sup> In other

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<sup>16</sup> Germany. See Appendix II. 12 Q2-2 .

jurisdictions, a security assignment of receivables is treated as a security interest in receivables because both of them serve the same economic function.<sup>17</sup>

<Table 1> Receivables Financing

		Notice of the assignment to the account debtor (usually)	Debt collection	Account debtor default risk
Sale	Factoring without recourse	At the outset	Assignee (factor)	
	Factoring with recourse	At the outset	Assignee	Assignor
	Block discounting without recourse	In / before assignor's insolvency	Assignor	Assignee
	Block discounting with recourse	In / before assignor's insolvency	Assignor	
Trust / Sale	Securitisation	In / before assignor (originator)'s insolvency	Assignor (originator)	General investors
Security purpose	Security assignment (assignment for the purpose of security)	After assignor (debtor)'s default	Assignee (secured creditor)	Assignee (secured creditor) / assignor (debtor)
	Security interest	After security provider (debtor)'s default	Secured creditor	Secured creditor / security provider (debtor)

## 1-5. Assignments rather than Security Interests

An outright assignment of receivables and a security interest in receivables appear differently on the balance sheet in the financial statement. A business balance sheet consists of two vertical columns. Assets are set out on the one column, and liabilities and

<sup>17</sup> France. See Appendix II. 8 Q2-1

equity are set out on the other column. An outright assignment of receivables eliminates the receivables on the asset column and instead a cash income for the consideration will appear on the asset column. By contrast, a security interest in receivables does not eliminate the receivables on the asset column, but the debt that the receivables are encumbered will appear on the liability column and a cash income from the debt will appear on the asset column.

For a bank to increase the capital adequacy ratio under the Basel III, an outright assignment of receivables is more advantageous than a security interest in receivables. The capital adequacy ratio is measured by the percentage of a bank's core capital divided by its risk-weighted assets. Since in calculating risk weighted assets, cash is to be multiplied by zero, a cash income from selling receivables or borrowing has nothing to do with the capital adequacy ratios. However, decreasing bad receivables results in decreasing risk weighted assets, and thus has the effect to increase the capital adequacy ratio.

Considering potential reorganisation proceedings of a debtor (a security provider or assignor), an outright assignment of receivables is more advantageous than a security interest in receivables. In potential reorganisation proceedings of a debtor (a security provider or assignor), secured creditors with security interests might be pressured to sacrifice for the reorganisation of the debtor, whereas an assignee is not involved with the reorganisation proceedings of the assignor.<sup>18</sup> In this aspect, creditors sometimes prefer an assignment of receivables.

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<sup>18</sup> Under English law, an assignment by way of security could mean a mortgage, where the security taker is very much involved in a reorganisation. It is only when there is an assignment that the assignee can sue the account debtor without having to account to the security provider for the surplus, and

Among security interests in receivables, a floating charge over receivables in English law is quite powerful. A floating charge usually covers both receivables and tangible movable assets since receivables continuously become proceeds by payment of the account debtor. Thus, a floating charge over all existing and future assets of a debtor has a strong point.

## **1-6. An International Registration System should cover both Assignments and Security Interests**

Even though assignments of receivables are used more than creating security interests in receivables, an international registration system should cover both assignments of and security interests in receivables due to the following reasons.

For the court to determine the priority among competing assignments or security interests, the court must compare all assignments of and security interests in the receivable. There could be a security interest in and an assignment of the same receivable, where an assignor creates a security interest in the receivable and later assigns the receivable to a third party, or vice versa. If the secured creditor perfected the security interest prior to the assignee, the secured creditor will trump the assignee when the debtor (assignor) defaults.

When a potential assignee purchases a receivable, it must investigate whether there is any prior assignment of or security interest in the receivable in order to secure priority

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so is completely outside the reorganisation. Hugh Beale, Michael Bridge, Louise Gullifer and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) 326 [7.09]

over any prior assignment of and security interest in the receivable. In order to investigate any prior assignment of and security interest in a receivable at once through the register and determine the priority among competing assignments of and security interests in a receivable clearly, an international registration system should cover both assignments of and security interests in receivables.

## **1-7. Proposed IRSAR Convention**

### **1-7-1. IRSAR**

This thesis proposes an international registration system for the assignment of and security interest in receivables, which is referred to as ‘IRSAR’ in this thesis. The IRSAR includes outright assignments of receivables, security assignments of receivables and security interests in receivables in its registration scheme.

This thesis proposes a set of rules to realise the IRSAR. To explain the details of the proposal, this thesis drafts a model international convention for the IRSAR, ‘The Draft Convention on Priority of Assignments of and Security Interests in Receivables’ (‘proposed IRSAR Convention’). This thesis includes it as Appendix I.<sup>19</sup>

Under the proposed IRSAR Convention, international assignment of receivables would be regulated by a unified legal system with respect to priority and perfection. The IRSAR could help financiers to overcome the obstacles they currently encounter and thus

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<sup>19</sup> This is attached at the end of this thesis as Appendix I. See 386. Each article of the proposed IRSAR Convention is drafted with reference to existing international conventions, legislative guides and national laws including the UN Receivables Convention, the Cape Town Convention and its Regulations and Procedures for the International Registry, the UNCITRAL Legislative Guide on Secured Transactions and the New Zealand PPSA.

facilitate international assignments of receivables, international project financing and international finance using security interests in receivables. Furthermore, the IRSAR would enable companies to raise finance from greater ranges of investors around the world through international receivables financing and to dispose of non-performing loans more easily.

Since under current private international laws, it is not clear which national law on priority among competing assignees should be applied in international assignments of receivables,<sup>20</sup> it could be expected that the parties who wish certainty of priority would choose to register in the IRSAR. In this thesis, ‘registration of an assignment of, or a security interest in, a receivable in the IRSAR’ is referred to as ‘**IRSAR registration**’.

## 1-7-2. Receivables

Under the proposed IRSAR Convention, ‘receivable’<sup>21</sup> does not cover cheques, bonds and other debt securities. Many jurisdictions have their own laws regulating cheques, bonds and debt securities. In most, priority of the right in a cheque, a bond or other debt securities is determined by possession.

Under the proposed IRSAR Convention, ‘receivable’ does not include bank accounts. This is because when a bank account is assigned, the bank account is controlled by the assignee. In most jurisdictions, priority is determined by the order of

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<sup>20</sup> See Section 3-4-2

<sup>21</sup> Draft IRSAR Convention, art 1(g). See 315

control of the bank account, and upon the assignee's control of the bank account, the assignment is perfected against third parties.

### 1-7-3. Assignment

An 'assignment' is a transaction between the person entitled to the benefit from a contract (assignor) and a third party to that contract (assignee), as a result of which the third party becomes entitled to sue the person liable under the contract (debtor).<sup>22</sup>

The UN Receivables Convention stipulates that 'assignment' means the transfer by agreement from one person (assignor) to another person (assignee) of an interest in the assignor's contractual right to payment of a monetary sum (receivable) from a third person (the debtor of the receivable).<sup>23</sup> The proposed IRSAR Convention adopts this definition of 'assignment'.<sup>24</sup>

In the assignment of receivables, a debtor may set-off against an assignee the counter claims that the debtor had against the assignor until notified of the assignment.<sup>25</sup> Notice of the assignment to the debtor of the receivable prevents the debtor from setting-off any claims that the debtor had against the assignor that arise after notice.

By contrast, in a novation, an old agreement is extinguished and a new agreement is created. A novation replaces the old creditor by a new creditor with agreement. A

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<sup>22</sup> Guenter Treitel, *The Law of Contract* (London: Sweet & Maxwell, 2003) 672

<sup>23</sup> UN Receivables Convention, art 2

<sup>24</sup> Draft IRSAR Convention, art 1(a). See 314

<sup>25</sup> It is not a mandatory rule, and thus a debtor may voluntarily waive any defences or rights of set-off before or even after notified of the assignment. The Cape Town Convention, art 31(4) and its Space Protocol, art X(3) stipulate the obligor's waiver of defences and rights of set-off by agreement in writing.

contract which is transferred by novation transfers all duties and obligations from the old creditor to a new creditor. Thus, the debtor cannot set up against the new creditor any set-off available against the old creditor.

#### 1-7-4. Security Interest

In the proposed IRSAR Convention, ‘security interest’ means a property right in a receivable that is created by agreement and secures payment, regardless of whether the parties have denominated it as a security interest. The term does not include a personal right against a guarantor or other persons liable for the payment of the secured obligation.<sup>26</sup>

The proposed IRSAR Convention uses the term ‘security interest’ in receivables. However, there is a noticeable difference in the terminology of security interests in receivables as between English common law and French and German civil law. For a security interest in receivables, English law uses the term, ‘**charge**’ over receivables.<sup>27</sup> UCC Article 9 and the Personal Property Security Acts (‘PPSAs’) of Canada, New Zealand and Australia use the term, ‘**security interest**’ in receivables.<sup>28</sup>

German law and French civil law use the term, ‘**pledge**’ of receivables. The English translation of the German Civil Code provided by the Federal Ministry of Justice

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<sup>26</sup> Draft IRSAR Convention, art 1(j). See 316

<sup>27</sup> For example, ‘charge on book debts of the company’ in Companies Act 2006. ‘Charge’ in Companies Act 2006 includes ‘mortgage’. Under English law only tangible property may be pledged.

<sup>28</sup> Hugh Beale, Michael Bridge, Louise Gullifer, and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) 328 n 33. By comparison, a pledge under English law is called a ‘security interest perfected by possession’ in UCC Article 9 and in the PPSAs of Canada, New Zealand and Australia.

(*Bundesministerium der Justiz*) of Germany uses the term, ‘pledge’ rather than ‘charge’ for a security interest in receivables.<sup>29</sup> Likewise, the English translation of the French Civil Code provided by *Légifrance*, the official website of the French government for the publication of legislation, regulations and legal information, uses the term ‘pledge’ rather than ‘charge’ for a security interest in receivables.<sup>30</sup> From the English law point of view, one cannot have a ‘pledge’ of receivables since one cannot have physical possession with receivables. Nonetheless, the pledge (*Pfandrecht*)<sup>31</sup> of a claim under the German Civil Code<sup>32</sup> and the pledge (*nantissement*)<sup>33</sup> of a debt under the French Civil Code<sup>34</sup> use the term ‘pledge’ which generally signify security interests over movable personal property, the creation of which is made public by physical transfer of the object. This shows slightly different understating or approach toward security interests in receivables in English law and in German and French laws.

With respect to security interests, one of the most recent trends is to make a comprehensive registration system which covers every type of security interests. Registration systems in many jurisdictions are not separately provided for each type of security interests, instead these countries adopt comprehensive security rights registration systems which include any type of security interests. For example, the Uniform Commercial Code (‘UCC’) Article 9 filing of the United State covers any type of security

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<sup>29</sup> <[http://www.gesetze-im-internet.de/englisch\\_bgb/englisch\\_bgb.html#Section%20405](http://www.gesetze-im-internet.de/englisch_bgb/englisch_bgb.html#Section%20405)> accessed 10 January 2010.

<sup>30</sup> <<http://195.83.177.9/code/liste.phtml?lang=uk&c=22&r=7815>> accessed 10 January 2010.

<sup>31</sup> <<http://www.gesetze-im-internet.de/bgb/BJNR001950896.html>> accessed 10 January 2010.

<sup>32</sup> German Civil Code, ss 1279-1290

<sup>33</sup> <[http://www.legifrance.gouv.fr/affichCode.do;jsessionid=10CE907B0C1018B38E574A6B23720541.tpdj\\_o01v\\_3?idSectionTA=LEGISCTA000006150366&cidTexte=LEGITEXT000006070721&dateTexte=20090220](http://www.legifrance.gouv.fr/affichCode.do;jsessionid=10CE907B0C1018B38E574A6B23720541.tpdj_o01v_3?idSectionTA=LEGISCTA000006150366&cidTexte=LEGITEXT000006070721&dateTexte=20090220)> accessed 10 January 2010.

<sup>34</sup> French Civil Code, ss 2356–2366

interest arrangements. The parties can make special arrangement freely. This trend was initiated from the UCC Article 9 registry of the US. The UNCITRAL Legislative Guide on Secured Transactions (UNCITRAL 2007) also recommends this approach. The IRSAR adopts this comprehensive security rights registration system. Thus, any type of security interests should be registered in the IRSAR in order to be perfected against third parties.

## **1-8. Overview of this Thesis**

### 1-8-1. Overview

This thesis consists of seven parts. Part 1 is the introduction. Part 2 explores current general security rights registries in the world, and finds the need for an international registration system for security interests in receivables. Part 3 is general analysis on current laws of priority and perfection with respect to assignments of and security interests in receivables. Parts 4, 5 and 6 show a model for the IRSAR. Part 4 creates limitation of the scope of the IRSAR. Part 5 designs priority rules of the proposed IRSAR Convention. Part 6 illustrates how to operate the IRSAR. Part 7 is the conclusion.

### 1-8-2. Research Methods

This thesis conducts a comparative analysis on perfection against third parties, priority and registration systems of multiple jurisdictions. Chapter 2-3 compares laws on security interests in common law jurisdictions. Chapter 2-4 compares laws on security

interests in civil law jurisdictions. Chapter 3-2 analyses such laws in each jurisdiction answering the same six questions about effectiveness and perfection of assignments and security interests. Section 6-2-5 compares the information required for registration in each jurisdiction. Section 6-3-2 compares the cooperation of the registrant and the other counterparty to the assignment (or security interest) agreement in the registration procedure in each jurisdiction. Chapter 6-6 compares the system of searching the registry in each jurisdiction.

The purpose of this comparative analysis is to suggest a desirable model of the regulatory system on the assignment of receivables that best fits an international convention. The system should be functionally efficient as well as widely acceptable. There are two different aspects for a successful international model: efficiency and universality. The first is to find the most efficient system among the legal systems of each jurisdiction. The second is to find the legal system, which is most widely acceptable. The most efficient legal system is not always the most widely acceptable for States vary in the degree of their legal sophistication. The lesson of the UN Receivables Convention shows that the most efficient model is not necessarily the best strategy for an international convention if it is not widely acceptable. Even though the UN Receivables Convention presents an ideal model for the assignment of receivables, the model has not been widely accepted.<sup>35</sup> For a successful international convention, wide acceptability is one of the most important considerations.

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<sup>35</sup> It is because each State does not want to revise its domestic laws, especially basic laws such as Civil Codes in civil law jurisdictions. In order to adopt the UN Receivables Convention, many States need to revise their domestic Civil Codes.

## **PART 2. CURRENT GENERAL SECURITY RIGHTS REGISTRIES**

### **2-1. INTRODUCTION**

The IRSAR covers both assignments of and security interests in receivables. In Part 1, it is reviewed that in receivables financing, assignments of receivables are used more than creating security interests,<sup>36</sup> but because of determining priority and perfecting an assignment or security interest against any other assignments or security interests, the IRSAR should cover both assignments of and security interests in receivables.<sup>37</sup>

Part 2 attempt to answer the question of why we need an international registration system for assignments of and security interests in receivables. It analyses the merits of a registration system for security interests in receivables. Before designing an international registration system for assignments of and security interests in receivables, Part 2 reviews existing registration systems under current laws in different jurisdictions. The UK, the US, Canada, New Zealand, Australia, Japan, Korea, China have registration systems. No registration system exists for assignments of and security interests in only receivables (without tangible movable assets) in any jurisdiction.

Chapters 2-2 to 2-4 comparatively analyse national laws on security interests, registration systems for movable assets and receivables. Chapters 2-3 and 2-4 compare the difference between common law jurisdictions and civil law jurisdictions with respect to registration with the focus on why a registration system for the assignment of

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<sup>36</sup> See Section 1-5

<sup>37</sup> See Section 1-6

receivables has not been developed in European civil law jurisdictions. Chapter 2-4 also investigates how China, Korea and Japan compromised between the civil law jurisdiction and the common law jurisdiction. China, Korea and Japan have hybrid systems where they adopted the registration systems influenced by the common law countries, on top of their civil law legal systems.

Chapter 2-5 reviews global movements to harmonise laws on a general security rights registry facilitating security interests in movable assets and receivables as well as to try establishing international registries for each specific type of assets including receivables. Chapter 2-6 analyses pros and cons of a general security rights registry and seek to show the economic value of a general security rights registry. Chapter 2-7 explains the reason that this thesis limits its research to establishing an international registration system for security interests in and assignments of receivables. It also examines why we need to create security interests in receivables. Chapter 2-8 is the conclusion.

## **2-2. PUBLICITY**

Before investigating the general security rights registry of each jurisdiction, this section examines whether publicity is required for perfection of a security interest against third parties in order to explain the function of a general security rights registry.

### **2-2-1. Methods of Publicity**

Registration is one method of obtaining publicity. With respect to tangible movable assets, there are four methods of publicity. The steps that must be taken for perfection of security interests in tangible movable assets fall into the following four categories: (1) filing a notice in a public records system established for that purpose; (2) taking possession of collateral; (3) taking control of collateral by means of the stakeholder's agreement to hold for the secured creditor; or (4) posting a notice on the property or where it will be seen by persons dealing with the property.<sup>38</sup>

With respect to assignments of and security interests in receivables: (1) registration or filing is required in some jurisdictions; and (2) notice of the assignment to the debtor is required in some jurisdictions.

### **2-2-2. Function of Publicity**

There are two main functions of publicity. First, it allows the public to be aware of the existence of an assignment of, or a security interest in, a receivable. Second, it publically certifies the existence of an assignment of, or a security interest in, a receivable.

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<sup>38</sup> Lynn M. Lopucki and Elizabeth Warren, *Secured Credit: A Systems Approach* (6th ed, Aspen Publishers 2009) 280. In England, the United States and France, because there are registries for security interests in movable assets, a third party can check the status of a movable asset by referring to the relevant registry. In Germany, there is no security rights registry where a third party can check the status of a movable asset. As such, a potential secured creditor could only ask the debtor or the security provider for that information.

### 2-2-2-1. Informing the Public

Informing the public dispels any incorrect assumptions of the financial health of a company,<sup>39</sup> and also prevents double assignments. With respect to assignments of and security interests in receivables, publicity gives information on the status of a certain receivable to third parties interested in purchasing or taking security interests in the receivable. Both notification to the debtor and registration are good publicity. In the jurisdictions where registration is form of publicity, potential investors can refer to a registry. Alternatively, in the jurisdictions where giving notice of the assignment to the debtor is the form of publicity, potential investors can enquire of the debtor whether there has been a prior assignment of the receivable. However, for future receivables for which debtors would not yet be specified, giving notice of the assignment is impossible. Furthermore, for bulk receivables for which there are numerous account debtors, giving notice of the assignment is impractical, time-consuming and costly.<sup>40</sup> As a result, registration is a more desirable system of publicity than notification.

In addition, a registration system for security interests in movable assets facilitates non-possessory security interests in movable assets. Under traditional civil law, the transfer of an *in rem* right should be publicised since it is effective *erga omnes* (enforceable against all). Therefore, for the pledge of a tangible movable asset, delivery of possession is required. With respect to non-possessory security interests, since a security provider is still in possession of the encumbered asset, third parties cannot easily determine whether there is a security interest in that asset. Traditionally in civil law, non-

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<sup>39</sup> UNCITRAL Legislative Guide on Secured Transactions, 47 [69].

<sup>40</sup> See Section 3-5-1

possessory security interests in tangible movable assets depend on exceptional legal conceptualisation because there is no physical delivery of possession. Because it is not publicised, a non-possessory security interest creates uncertainty about its existence since there is no physical delivery for a third party to 'see'. A lender might be able to do an extensive search to minimize the uncertainty of any hidden prior security interests in the encumbered asset, but this is time consuming, costly, and increases the cost of credit. A registration system can publicise the security interest in a tangible movable asset without possession, and therefore it facilitates non-possessory security interests in tangible movable assets.

#### 2-2-2-2. Evidence

A second purpose of publicity for some jurisdictions is to provide a mechanism for secured creditors to prove, as an evidentiary matter, the existence and effective date of their security interests.<sup>41</sup> Publicity is useful for a secured creditor to verify the effective date of a security interest in order to preserve priority of such right.

Publicity ensuring the veracity of the timing and the existence of a security interest could eliminate the possibility that a debtor and a secured creditor could conspire to claim that a security interest was created earlier than it actually was.<sup>42</sup> In the

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<sup>41</sup> *ibid* 47 [70]. In some jurisdictions, publicity is a requirement for creation of a security interest. But, under the UCC Article 9, parties may file the financing statement even before a security agreement has been executed. Then, when the security interest is created by a security agreement, priority dates back from the earlier of the time when a filing covering the security interest is first made. UCC, s 9-322(a)

<sup>42</sup> Charles W. Mooney, Jr., 'The Mystery and Myth of Ostensible Ownership and Article 9 Filing: A Critique of Proposals to Extend Filing Requirements to Leases', 39 *Alabama Law Review* 683 (Spring 1988) 752

jurisdiction where priority is generally determined by the order of registration, there is little risk that collusion concerning the time of creation might affect priority.<sup>43</sup>

Moreover, publicity allows the debtor of a receivable to have greater trust in an unknown assignee once the assignee shows publically certified evidence of the assignment to him, such as a certificate of registration or a notarized assignment contract. Thus, providing public evidence of the assignment might reduce the cost of credit.

## **2-3. SECURITY INTERESTS SYSTEM OF COMMON LAW JURISDICTIONS**

### **2-3-1. Security Rights Registries in English Law**

#### 2-3-1-1. English Courts of Equity allowing Non-Possessory Charges

Registration of charges over movable assets and receivables were first developed under English law. England has a relatively long history of non-possessory security interests, namely charges and mortgages. Although English law does not formally limit the permissible categories of security interest, there are broadly four categories of consensual security known to English law: ① the pledge, ② the contractual lien, ③ the mortgage and ④ the charge.<sup>44</sup> Whereas mortgages require transfer of ownership, charges require neither transfer of possession nor transfer of ownership,<sup>45</sup> and all charges are

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<sup>43</sup> *ibid* fn 264

<sup>44</sup> Roy Goode and Louise Gullifer, *Goode on Legal Problems of Credit and Security* (4th edn, Sweet & Maxwell, 2008) 30-31, fn 153 [1-42]

<sup>45</sup> *Carreras Rothmans Ltd v Freeman Mathews Treasure Ltd* [1985] ch 207 (Ch).

equitable.<sup>46</sup> The scope of charges includes equitable mortgages and therefore all equitable mortgages are charges.<sup>47</sup> Thanks to equity in English law, non-possessory security interests could develop without the formality of *in rem* rights of the civil law,<sup>48</sup> and accordingly its registration system could develop under English law first. Common law jurisdictions could adopt registration systems without changing their existing laws.

### 2-3-1-2. Publicity Problem of Non-Possessory Charges

In England, the original reason for the development of a registration system was to prevent hidden non-possessory security interests. *Twyne's Case*<sup>49</sup> shows us the problem of a hidden non-possessory security interest. In 1601 Pierce was indebted to Twyne and was also indebted to C. However, in secret, Pierce disposed by deed of all his goods to Twyne in satisfaction of his debt. Pierce continued in possession of the goods. Pierce sold some of the goods to third parties. Pierce then sheared the sheep and branded them with his own mark. C subsequently brought an action of debt against Pierce. C obtained a judgment against Pierce and had a *feri facias* directed to the Sheriff of Southampton. When the Sheriff came to make execution of the goods by force of the writ, Twyne resisted the sheriff with force. Twyne claimed that he owned the goods by

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<sup>46</sup> Roy Goode and Louise Gullifer, *Goode on Legal Problems of Credit and Security* (4th edn, Sweet & Maxwell, 2008) 5

<sup>47</sup> *Shea v Moore* [1894] I.R.158 (CA), per Walker L.C. 168. Mortgages are divided into legal mortgages, which require transfer of ownership, and equitable mortgages.

<sup>48</sup> In contrast, in civil law jurisdictions, because security interests are *in rem* rights, the *numerus clausus* principle applies to security interests and therefore the parties may not freely create a new type of security interest. It prevented the development of non-possessory security interests in civil law jurisdictions until the economic demand of non-possessory security interests increased unbearably.

<sup>49</sup> *Twyne's Case* [1558-1774] All ER Rep 303; 3 Co Rep 80 b; Moore KB 638; 76 ER 809 (Court of Star Chamber).

force of the gift, and it was a gift made on a good and lawful consideration. Twyne was criminally convicted of fraud according to the Fraudulent Conveyances Act 1571.<sup>50</sup> This case was a criminal action involving imputed fraud.<sup>51</sup> One way to understand fraudulent or hidden non-possessory security interests was as an affront to community norms.<sup>52</sup>

The problem with fraudulent or hidden non-possessory security interests appears to have had a significant influence on the development of a registration system, which functions as an information proxy for possession that could deter or correct the problems of hidden non-possessory security interests like those in *Twyne's Case*.<sup>53</sup>

### 2-3-1-3. Registration as an Ex Ante Method

A creditor may recover his loan in so far as the debtor can be brought under the jurisdiction of the court and recovery of the fraudulent transaction can be performed *ex post*. However, at that time, England had colonies around the world and English merchants travelled the world to places like Australia, New Zealand, Hong Kong, Singapore, Shanghai, India, and Africa. Therefore it would have been easy for an English merchant to effectively 'run away'. Because of this historical circumstance, there was vital need to prevent fraudulent or hidden non-possessory security interests by an *ex ante* method.

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<sup>50</sup> 13 Eliz I Cap 5.

<sup>51</sup> Charles W. Mooney, Jr., 'The Mystery and Myth of Ostensible Ownership and Article 9 Filing: A Critique of Proposals to Extend Filing Requirements to Leases', 39 *Alabama Law Review* 683 (Spring 1988) 727

<sup>52</sup> Jonathan C. Lipson, 'Secrets And Liens: The End Of Notice In Commercial Finance Law' (2005) 21 *Emory Bankruptcy Developments Journal* 421, 438.

<sup>53</sup> *ibid* 437

Registration of company charges can function as an *ex ante* method. Under a transparent registration system, a debtor cannot hide non-possessory security interests. By checking the registry, a creditor can *ex ante* avoid those debtors who have created non-possessory security interests. Since if a security interest is not registered, it is not effective, a creditor may rely on the registry. An unregistered charge created by a company is not perfected against the insolvency representative.<sup>54</sup> An unregistered security bill of sale is completely ineffective.<sup>55</sup>

#### 2-3-1-4. Origin of Security Rights Registries in English Law

The English courts of equity allowing non-possessory charges accelerated the creation of a registration system for company charges. In England, a general security rights registry was invented for non-possessory security interests in the late nineteenth century. The Bills of Sale Act 1878 provides for the registry of written chattel mortgages created by individuals. Registration of charges created by companies was introduced by the Companies Act 1862 but it required each company to maintain a registry of all mortgages and charges affecting the properties of the company.<sup>56</sup> A centralised registry that is searchable by any member of the public was introduced for company charges over

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<sup>54</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, s 859H. Still, it is valid against the company itself since registration is a perfection requirement for a company charge. Registration is required for validity against other secured creditors and against unsecured creditors on insolvency, but not against the debtor of the receivable.

<sup>55</sup> Bills of Sale Act (1878) Amendment Act 1882, s 8. It is because registration is a creation requirement for a security bill of sale.

<sup>56</sup> Hugh Beale, Michael Bridge, Louise Gullifer and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) 324 [7.03]

certain types of assets stipulated in the Company Charges Act 1890.<sup>57</sup> The scheme for registering company charges dates from the Companies Act 1900.<sup>58</sup> Originally, this registration system was for tangible personal property such as equipment and goods. Companies often create non-possessory security interests in factory machines or inventory. Companies also create charges over company receivables and create floating charges over future and present properties. The Companies Act 2006 provides for the register of charges created by companies.<sup>59</sup> The company charges register is a general security rights registry which covers various types of assets unless the asset is exempt or regulated by other laws.<sup>60</sup> In addition, there are other kinds of registries for specific types of assets such as mortgages or charges of registered ships,<sup>61</sup> registered aircraft<sup>62</sup> and intellectual property<sup>63</sup> that is able to be registered.

### 2-3-1-5. Debtor-Based Indexed Registration System

A general security rights registry can hardly be systemised as an asset-indexed registry, but needs to be designed as a debtor-indexed registry. In addition, a debtor-indexed registry is suitable for floating charges (universal charges) because a creditor

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<sup>57</sup> *ibid.* Following the report of the Davey Committee on Company Law Amendment (C 7779, 1895), paras 46-50.

<sup>58</sup> Companies Act 1900 (63 & 64 Vict Cap 48), s 14.

<sup>59</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, ss 859A-G

<sup>60</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, s 859A(6)

<sup>61</sup> Merchant Shipping Act 1995, s 16 and Schedule 1

<sup>62</sup> The Mortgaging of Aircraft Order 1972, SI 1972/1268.

<sup>63</sup> Patents Act 1977, ss 30-33; Trade Marks Act 1994, s 25; Registered Designs Act 1949, s 19. There is no registration of copyright.

with floating charges only knows his debtor (security provider) and does not know potentially encumbered assets.

In contrast, asset-indexed registries are exemplified by the land registry and special registries for particular movable assets such as cars, ships and airplanes. In most modern countries, each tract of land is assigned a unique number on a map, and thus one can find the number of the land in question on the maps and search the index under the tract number in the land registry. Also, each car, each ship and each airplane is assigned a registration number.

In England and Wales, there are two existing parallel systems of providing title to land and investigating third party rights in land. **Unregistered land** is governed by the older system of title deeds and the Land Charges Registry under the Land Charges Act 1925. Title deeds, where titles are recorded genealogically, evidence ownership of lands,<sup>64</sup> whereas the Land Charges Registry records all equitable interests in land.<sup>65</sup> The Land Charges Registry is indexed by the owner of the land (the debtor) at the time the charge is created, and therefore a debtor-indexed registry.

**Registered land** is governed by the newer system under the Land Registration Act 1925, which provides for the Land Registry.<sup>66</sup> The Land Registration Act 2002 has increased the number of interests which must be registered, to make the Land Registry as self-contained and all-encompassing as possible, and accordingly, all creation, change and discharge of ownership of and security interests in each piece of land need to be

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<sup>64</sup> Elizabeth Cooke, *The New Law of Land Registration* (Hart Publishing 2003) 5-9

<sup>65</sup> Land Charges Act 1972, s 2

<sup>66</sup> It is title registration and contains a tabular wherein the state of the title can be seen and thus a searcher need not look behind the final registration. Elizabeth Cooke, *The New Law of Land Registration* (Hart Publishing 2003) 5-9

registered.<sup>67</sup> The Land Registry is indexed by the land, and therefore an asset-indexed registry.

## **2-3-2. Uniform Commercial Code Article 9**

### **2-3-2-1. Historical Background**

The US established the financial statement filing system under Article 9 of the US Uniform Commercial Code ('UCC')<sup>68</sup> in 1952. The scope of the filing system has been expanded from charges over personal property including receivables to include outright assignments of receivables. This is because of historical reasons. Before the enactment of UCC Article 9, different rules had been developed by the various state courts. For example, in California and Pennsylvania, courts followed the English rule but in New York, courts followed the German rule. In 1943, in *Corn Exchange National Bank v Klaunder*,<sup>69</sup> the US Supreme Court held that assignees, who engaged in non-notification financing of accounts receivable in a state following the English *Dearle v. Hall* rule,<sup>70</sup> were not protected in the insolvency of the assignor. As a result, in interstate transactions of receivables, the assignor or the assignee had to give notice of the assignment to the debtor for the assignee to be protected from the insolvency of the assignor. However,

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<sup>67</sup> Elizabeth Cooke, *The New Law of Land Registration* (Hart Publishing 2003) 9-12

<sup>68</sup> The United States Uniform Commercial Code is a set of standardized business laws, created by the National Conference of Commissioners on Uniform State Laws ('NCCUSL') and the American Law Institute ('ALI'), and first published in 1952. The UCC has been adopted by most states of the United States with a few modifications. Its purpose is to harmonise, and further unify, the laws of business and commercial transactions throughout the United States. The latest version of UCC Article 9 has an effective date of 1 July 2001.

<sup>69</sup> 63 S.Ct. 679, 318 U.S. 434 (1943).

<sup>70</sup> *Dearle v. Hall* (1828) 3 Russ 1

giving notice of the assignment to the debtor is costly and time-consuming. After this decision, a codification of these various priority rules was accelerated.<sup>71</sup> In 1952, UCC Article 9 unified all these rules, and now the assignor and the assignee only have to file a financing statement for an assignment of a receivable to be perfected against the insolvency representative of the assignor. As a result, UCC Article 9 includes both security interests in receivables and outright assignments of receivables. All the states have adopted UCC Article 9 with some amendments.

### 2-3-2-2. Notice-Filing System

The US invented a notice-filing system significantly different from the commonly accepted concept of registration systems, where the state guarantees the contents.<sup>72</sup> Since land registries in the US differ by county and the application criteria varied and could be lax, the concept of a notice-filing system under UCC Article 9 could be implemented.<sup>73</sup> The goal of notice-filing under UCC Article 9 was to replace the cumbersome document-filing system with the registration of a simple notice containing only basic details about the security interest to which it related.<sup>74</sup> In a notice-filing system, ‘a registrant need not

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<sup>71</sup> Hein Kötz, ‘Rights of Third Parties. Third Party Beneficiaries and Assignment’ in Arthur von Mehren (ed), *International Encyclopedia of Comparative Law*, vol 7 ch 13 (Möhr, Tübingen, 1992) 56

<sup>72</sup> UNCITRAL Legislative Guide on Secured Transactions, 111

<sup>73</sup> In the US, with respect to the financing statement filing under UCC Article 9, one registry exists in each state in the state level. But land registries exist at the county level. The contents of the land registration are more detailed than the contents of the financing statement filing under UCC Article 9. The registry officers do not examine the substance of a filing. They only examine and reject filings that are not in the proper form. For example, omission of required data results in rejection of an Article 9 filing. Omission of a notarisation or tax stamps might result in rejection of a real estate filing. With respect to land registries, deeds are recorded and deeds evidence the ownership of land.

<sup>74</sup> UNCITRAL Legislative Guide on Secured Transactions, 111 [32]

submit the underlying security documentation or provide other evidence of the security interest to which the registration relates in order to register a notice'.<sup>75</sup>

Its main function is to confirm that a debtor has made full disclosure and to provide warning of the need for further investigation.<sup>76</sup> In addition, a general security rights registry could also support due diligence and the discovery of potentially competing secured creditors.<sup>77</sup>

### **2-3-3. Personal Property Security Acts**

In Canada, all provinces following the common law have had registration requirements with respect to a general assignment of receivables since the 1920s and each has its own registry. The current Canadian registry provisions are merged in the provincial PPSAs but the basic principles remain the same.

New Zealand enacted the PPSA in 1999, which came into force on 1 May 2002 when the Personal Property Securities Register ('PPS Register') became operational.<sup>78</sup> The New Zealand PPSA provides for the PPS Register, a registration system for security interests in personal property including the assignment of receivables. The registration

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<sup>75</sup> UNCITRAL Legislative Guide on Secured Transactions, 174 [98]

<sup>76</sup> Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Tangibles* (Sellier 2007) 43.

<sup>77</sup> *ibid* 42.

<sup>78</sup> <[http://www.med.govt.nz/templates/StandardSummary\\_\\_\\_15299.aspx](http://www.med.govt.nz/templates/StandardSummary___15299.aspx)> accessed 10 January 2011.

system is operated online on the official website, where security interests over personal property may be registered and can be searched.<sup>79</sup>

The Australian PPSA was passed in December 2009 and entered into force in May 2011. Since May 2011, there is one national personal property securities law and one national online PPS Register under the PPSA 2009.<sup>80</sup> The Insolvency and Trustee Service Australia will assume responsibility for the PPS Register and Customer Contact Centre.<sup>81</sup>

## **2-4. SECURITY INTERESTS SYSTEM OF CIVIL LAW JURISDICTIONS**

### **2-4-1. Numerus Clausus Principle**

In civil law jurisdictions, there has been a big mountain before the development of registration system for security interests, i.e. the *numerus clausus* principle. The civil law countries explicitly restrict the available range of *in rem* rights and set up a closed list, known as the *numerus clausus* principle.<sup>82</sup>

Merrill and Smith argue that the *numerus clausus* principle strikes a balance between a proliferation of *in rem* rights and a 'one size fits all' system of *in rem* rights.<sup>83</sup>

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<sup>79</sup> The official website for the PPS Register of New Zealand is: <<http://www.ppsr.govt.nz/cms>> accessed 7 June 2010.

<sup>80</sup> The official website for the PPS Register of Austria is:< <http://www.ppsr.gov.au>> accessed 7 June 2010.

<sup>81</sup> < <http://www.ag.gov.au/pps>> accessed 7 June 2010.

<sup>82</sup> Bernard Rudden, 'Economic Theory v Property Law: The Numerus Clausus Problem' in Eekelaar and Bell (eds), *Oxford Essays in Jurisprudence* (Third series) (Clarendon Press, 1987)

<sup>83</sup> Thomas Merrill and Henry Smith, 'Optimal Standardization in the Law of Property: the *Numerus Clausus* principle' *Yale Law Journal* (October 2000) 69

On the one hand, a 'one size fits all' system of *in rem* rights would frustrate those legitimate objectives that can be achieved only by using different *in rem* rights that fall short of full ownership. On the other, permitting free customization of new forms of *in rem* rights is a problem because third parties must ascertain and measure the legal dimensions of *in rem* rights in order to avoid violating the rights of others and to assess whether to acquire the rights, and it would impose significant transaction costs. The *numerus clausus* principle pertains to protect all third parties from novel *in rem* rights.

*In rem* rights require publicity. In the past, the methods of publicity were costly and time-consuming. However, with the development of the internet technology, publicity through internet registration becomes very convenient. As a result, today, the *numerus clausus* principle might be relaxed. It is because third parties can easily and clearly check the contents of the contract arrangement of the parties through the internet registration system. Thanks to the development of internet technology, people can use many internet registration systems. People can search the internet registry at home and in the office without visiting the registry office in person. The technical change could result in changes in the property law systems including security interests. Traditionally, in the civil law jurisdictions, the types of *in rem* rights are restricted because of the *numerus clausus* principle. However, nowadays, with the use of internet technology, the *numerus clausus* principle might be relaxed.

There is a critical view towards the *numerus clausus* principle based on the historical background. Hansmann and Kraakman argue that the *numerus clausus* principle results from a 'unitary theory of property rights' of the civil law. They observe the historical background of the French Revolution that the *numerus clausus* doctrine was

born. At that time, since divided property rights came to be associated with feudal social relations, it was argued that divided property rights must be closely regulated and restricted.<sup>84</sup> Since then, that the civil law countries of Europe have adhered to a ‘unitary theory of property rights’ under which all *in rem* rights in an asset must be concentrated in the hands of a single owner rather than divided into partial rights shared among two or more persons; and only a relatively small, closed number (*‘numerus clausus’*) of specifically defined exceptions are permitted.<sup>85</sup>

Anyhow, both Merrill and Smith and Hansmann and Kraakman agree that the *numerus clausus* principle is more strictly valued in civil law jurisdictions than in common law jurisdictions.<sup>86</sup>

There is strong principle that *in rem* rights require publicity since they are effective *erga omnes*. Without publicity, an agreement to create a security interest in an asset is not effective against third parties. As for real estate, registration is required to satisfy the publicity requirement.<sup>87</sup> Under the Pandecten system, security interests belong

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<sup>84</sup> Henry Hansmann and Reinier Kraakman, ‘Property, Contract, and Verification: the Numerus Clausus Problem and the Divisibility of Rights’, *The Journal of Legal Studies* (2002) 37

<sup>85</sup> *ibid* 2. Such exceptions includes mortgages on real property and security interests in personal property.

<sup>86</sup> Thomas Merrill and Henry Smith, ‘Optimal Standardization in the Law of Property: the *Numerus Clausus* principle’ *Yale Law Journal* (October 2000) 69; Henry Hansmann and Reinier Kraakman, ‘Property, Contract, and Verification: the Numerus Clausus Problem and the Divisibility of Rights’, *The Journal of Legal Studies* (2002) 38

<sup>87</sup> In civil law jurisdictions, registration is required either for the creation of a title or at least for third party effectiveness. In Germany and Korea, registration in a title registry is required for the creation or change of a title. This approach is called formalism (*Formalismus* in German) because this approach requires strict formality for the creation of a title that registration is a creation requirement (*Entstehungsvoraussetzung* in German). In France and Japan, registration in a title registry is required for the third party effectiveness of a title. This approach is called the legal will theory (*Rechtwillentheorie* in German) because a title is created by just the parties’ will or intention, and registration is only a perfection requirement (*Einwendungsvoraussetzung* in German). Mortgages on real estate are registered in the real estate registry, and mortgages in aircraft are registered in the aircraft registry.

to *in rem* rights, and thus governed by the *numerus clausus* principle. Mortgages<sup>88</sup> must be perfected by registration, and pledges must be perfected by delivery of possession. A lien is not a contractual security interest, but a statutory security interest, which arises automatically once the requirements stipulated by law are fulfilled. These core concepts of three basic types of security interests are common in civil law jurisdictions. Due to the *numerus clausus* principle, the types of *in rem* rights are strictly limited in civil law jurisdictions and parties may not create a new type of *in rem* right.

The pledge (*pignus* in Latin) is the oldest security interest and was well known from Roman law.<sup>89</sup> In civil law jurisdictions, pledges are divided into two types: pledges of tangible movable assets and pledges of intangible rights.<sup>90</sup> A pledge of a tangible movable asset is perfected by delivery of the possession. A pledge of an *in personam* right requires transfer of that right. Thus, with respect to movable assets, a pledge is a possessory security interest.<sup>91</sup> For this reason, a non-possessory security interest in movable assets could not be incorporated into civil codes. In civil law jurisdictions, non-

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<sup>88</sup> A mortgage is a non-possessory security interest, which must be registered. A mortgage in Chinese, Korean and Japanese laws is not exactly a mortgage in English law in that the former is not involved with the transfer of ownership of the encumbered asset to the secured creditor. In Chinese, Korean and Japanese laws, a mortgage is registered in the title registry of the relevant asset as a mortgage, but the ownership title of the encumbered asset is not influenced by a mortgage. For example, a mortgage in land is registered in the land registry, and a mortgage in airplane is registered in the aircraft registry. An asset, which cannot be registered, cannot be an object of a mortgage.

<sup>89</sup> This Roman institution has spread over Europe and has been incorporated into all continental civil codes. Ulrich Drobnig, 'Security interests in Movables' (January 15, 2010) 2. Available at SSRN: <http://ssrn.com/abstract=1537137> accessed on 5 September 2010.

<sup>90</sup> In Korea, any rights other than the right to use and take profits from immovables may be the subject of pledges. Korean Civil Code, art 345. In China, the Property Law and the Security Law stipulate types of rights that can be objects of pledges. Chinese Property Law, art 180; Chinese Security Law, art 34.

<sup>91</sup> In common law jurisdictions, secured transactions law have always recognised the possessory pledge, and it traditionally explained that possessory of the collateral by the pledgee provides publicity. Harry C. Sigman, Eva-Maria Kieninger (eds), *Cross-Border Security over Tangibles* (Sellier 2007) 40.

possessory security interests were almost non-existent in the nineteenth century and therefore do not appear in the civil codes of the nineteenth century and only appear in the last decade of the twentieth century.<sup>92</sup>

#### **2-4-2. Fiduciary Transfer of Title for Security Purposes**

In Germany, due to the increasing economic demand for non-possessory security interests, the court acknowledges a non-possessory security interest in practice, developing the fiduciary transfer of title for security purposes, which is called ‘*Sicherungsübereignung*’. Title may be transferred without a change in actual possession, and no publicity is required. The fiduciary transfer of title for security purposes allows the parties to agree on their preferred enforcement mechanism outside insolvency proceedings and gives the secured creditor a preferential right to liquidation proceeds in the insolvency of the debtor (security provider).<sup>93</sup> This principle also applies to receivables.<sup>94</sup>

Japan and Korea adopted the fiduciary transfer of title for security purposes from Germany, and the courts in Japan and Korea acknowledge non-possessory security interests as ‘*YangDoTamBo*’<sup>95</sup> in practice.

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<sup>92</sup> Ulrich Drobni, ‘Security Interests in Movables’ working paper (15 January 2010) 5. <<http://ssrn.com/abstract=1537137>> accessed on 5 September 2010

<sup>93</sup> Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Tangibles* (Sellier 2007) 69.

<sup>94</sup> See Appendix II. 12 Q2-2

<sup>95</sup> Fiduciary transfer of title for security purposes is ‘讓渡擔保’ in Chinese character. The pronunciation of ‘讓渡擔保’ is *YangDoTamBo* in Korean and *JyouToTanPo* in Japanese. In this thesis, for convenience of reference, ‘讓渡擔保’ is referred to as *YangDoTamBo*.

In China, the legal regime has not introduced specific provisions on transfer of title to the creditor as an alternative approach to security interest.<sup>96</sup> However, it is possible to arrange such contracts.<sup>97</sup> Under Chinese law, financial leases and reservation-of-title arrangements are allowed, but they are treated as contractual arrangements, and thus not subject to the general rules on security interests, such as requirements of form, publicity and effects.<sup>98</sup>

### **2-4-3. Special Registers**

#### 2-4-3-1. Germany

In Germany, in addition to the non-possessory security device of fiduciary transfer of title, a few very specific statutes for registration were enacted in the 20th century. There are only registration systems for real estate and some movable assets that can be easily identified and specified. Germany has three special statutes of limited practical importance: agricultural tenants' inventories of 1951, agricultural fruits of 1949; and overseas cables of 1925.<sup>99</sup> A security rights registry for general personal property including receivables does not exist in Germany.

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<sup>96</sup> John Hou, Cherry Chow, and Zhen Zhao, International Secured Transactions (People's Republic of China Section), in Dennis Campbell (ed), International Secured Transactions, Binder 1 (Oceana Publications, Inc., Dobbs Ferry, NY , 2008) CHI-7

<sup>97</sup> *ibid*

<sup>98</sup> *ibid* CHI-7 - CHI-8

<sup>99</sup> Ulrich Drobnig, Security interests in Movables (January 15, 2010) 6fn 27. Available at SSRN: <http://ssrn.com/abstract=1537137> accessed on 5 September 2010.

## 2-4-3-2. France

France developed many special registers for each type of movable assets and enacted the *Dailly* Act for assignments of receivables. In France, there are special registers for security interests in: ships,<sup>100</sup> airplanes,<sup>101</sup> motor vehicles,<sup>102</sup> motion picture,<sup>103</sup> and patents,<sup>104</sup> trademarks<sup>105</sup> and rights in computer software.<sup>106</sup> Furthermore, there are special regulations for the security interests in: pledges of hotel equipment and furniture,<sup>107</sup> warrants for oil,<sup>108</sup> charges over tooling and equipment;<sup>109</sup> pledges of securities accounts,<sup>110</sup> and financial leases.<sup>111</sup>

In addition, the French Commercial Code allows charges over businesses as a going concern.<sup>112</sup> Registration must take place within 15 days of the date of the memorandum and articles of association.<sup>113</sup> Priority among secured creditors shall be determined by the date of their registrations.<sup>114</sup>

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<sup>100</sup> *loi n°67-5 du 3 janvier 1967 relative au statut des navires et autres bâtiments de mer*, arts 43 and 48.

<sup>101</sup> French Civil Aviation Code (*Code de l'aviation civile*), arts 121-2 and 122-7.

<sup>102</sup> French Civil Code, arts 2351, 2352 and 2353.

<sup>103</sup> French Industrial Cinema Code (*Code de l'industrie cinématographique*), art 33

<sup>104</sup> French Intellectual Property Code (*Code de la Propriété Intellectuelle*), art L613-9.

<sup>105</sup> French Intellectual Property Code (*Code de la Propriété Intellectuelle*), art L714-7.

<sup>106</sup> French Intellectual Property Code (*Code de la Propriété Intellectuelle*), art L132-34.

<sup>107</sup> French Commercial Code, arts L523-1 - L523-15.

<sup>108</sup> French Commercial Code, arts L524-1 - L524-21.

<sup>109</sup> French Commercial Code, arts L525-1 - L525-20.

<sup>110</sup> French Monetary and Financial Code, art L211-20

<sup>111</sup> French Monetary and Financial Code, arts L133-7 - L133-11

<sup>112</sup> French Commercial Code, arts L142-1 - L143-23.

<sup>113</sup> French Commercial Code, art L142-4

<sup>114</sup> French Commercial Code, art L142-5

### 2-4-3-3. China

#### ***2-4-3-3-1. Registries of Mortgages***

The Chinese Property Right Law stipulates types of property that can be objects of mortgages, which includes certain types of real estate, rights to real estate and movable assets.<sup>115</sup> Mortgages on buildings or land use right, etc. are created upon registration of the mortgage.<sup>116</sup>

Mortgages on manufacturing facilities, raw materials, semi-manufactured products, finished products;<sup>117</sup> ships under construction, aircrafts under construction;<sup>118</sup> or means of transportation<sup>119</sup> are created upon the mortgage agreement of the parties.<sup>120</sup> Such mortgages are perfected against third parties by registration. If not registered, they are not effective against *bona fide* third parties.<sup>121</sup> Registration of such mortgages should be conducted with the county-level administrative department for industry and commerce of the address of the mortgagor.<sup>122</sup>

The Chinese Property Right Law introduces mortgages on future assets. Companies, individual industrial and commercial households and agricultural producers may mortgage manufacturing equipment, raw materials, semi-manufactured products or

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<sup>115</sup> Chinese Property Right Law, art 180; Chinese Security Law, art 34

<sup>116</sup> Chinese Property Right Law, art 187

<sup>117</sup> Chinese Property Right Law, arts 180(1)(iv)

<sup>118</sup> Chinese Property Right Law, arts 180(1)(v)

<sup>119</sup> Chinese Property Right Law, arts 180(1)(vi)

<sup>120</sup> Chinese Property Right Law, art 188

<sup>121</sup> Chinese Property Right Law, art 188

<sup>122</sup> Measures for Registration of the Mortgage on Movable Assets (Order No.30 of the State Administration for Industry and Commerce), art 2

finished products, which they own at present or in the future.<sup>123</sup> Such mortgages shall be registered in the administrative department for industry and commerce at the place where the mortgagor resides.<sup>124</sup>

<Table 2> Effect of registration of Mortgages in China

Objects of Mortgages under the Chinese Property Right Law <sup>125</sup>	Registration
(1) buildings and other things firmly fixed on the land	creation requirement <sup>126</sup>
(2) land use right for construction	
(3) land management right for barren land, etc. contracted by the mortgagor by way of bidding, auction and public consultation, etc.	
(5) buildings under construction	
(4) manufacturing equipment, raw materials, semi-manufactured products or finished products (existing or future) <sup>127</sup>	perfection requirement <sup>128</sup>
(5) ships and aircrafts that are under construction	
(6) means of transportation	
manufacturing facilities, raw materials, semi-manufactured goods and products <sup>129</sup>	

#### 2-4-3-3-2. Registries of Pledges of Movable Assets

In China, the Property Right Law and the Security Law stipulates types of rights that can be objects of pledges.<sup>130</sup> The Chinese Property Right Law provides creation requirements of pledges of several types of rights. Pledges of bills of exchange, cheques, promissory notes, bonds, certificates of deposit, warehouse receipts and bills of lading are

<sup>123</sup> Chinese Property Right Law, arts 189 and 181

<sup>124</sup> Chinese Property Right Law, art 189

<sup>125</sup> Chinese Property Right Law, art 180

<sup>126</sup> Chinese Property Right Law, art 187

<sup>127</sup> Chinese Property Right Law, arts 181 and 189

<sup>128</sup> Chinese Property Right Law, art 188

<sup>129</sup> Chinese Property Right Law, art 181

<sup>130</sup> Chinese Property Right Law, art 180; Chinese Security Law, art 34

created by delivery of such negotiable instrument or document.<sup>131</sup> If there is no title certificate, pledges are created by registration.<sup>132</sup> Pledges of shares are created by registration in the securities depository and clearing institution.<sup>133</sup> Pledges of intellectual properties are also created by registration in the relevant department.<sup>134</sup>

<Table 3> Creation Requirements of Pledges in China

Objects of Pledges of Rights under the Chinese Property Right Law <sup>135</sup>	Creation requirement
bills of exchange, cheques, promissory notes	Delivery of possession or Registration <sup>136</sup>
bonds, certificates of deposit	
warehouse receipts, bills of lading	
shares of stocks or certificates of stocks which are transferable	Registration in the securities depository and clearing institution <sup>137</sup>
exclusive trademark rights, patent rights, copyrights or other property rights in intellectual property which are transferable according to law	Registration in the relevant department <sup>138</sup>
account receivables	Registration in the Credit Information Centre of the People's Bank of China <sup>139</sup>

#### **2-4-3-3. Registry of Pledge of Receivables**

In 2007, the Chinese Property Right Law has greatly expanded the range of movable collateral available to borrowers and lenders in secured finance transactions to include receivables. Accordingly, account receivables can be used as pledges.<sup>140</sup>

<sup>131</sup> Chinese Property Right Law, art 224

<sup>132</sup> Chinese Property Right Law, art 224

<sup>133</sup> Chinese Property Right Law, art 226

<sup>134</sup> Chinese Property Right Law, art 227

<sup>135</sup> Chinese Property Right Law, art 223

<sup>136</sup> Chinese Property Right Law, art 224

<sup>137</sup> Chinese Property Right Law, art 226

<sup>138</sup> Chinese Property Right Law, art 227

<sup>139</sup> Chinese Property Right Law, art 228

Under the Chinese Property Right Law, the pledge of receivables must be registered in the Credit Centre of the People's Bank of China.<sup>141</sup> Registration is required for the creation of pledges of receivables. Without registration, the pledge is not effective even as between the parties to the pledge agreement.<sup>142</sup> Article 228 of the Chinese Property Right Law stipulates that, where receivables are pledged, the pledgor (creditor) and the pledgee (debtor) shall conclude a contract in writing and the pledge shall become effective upon registration with the Credit Information Centre. Such registration is compulsory.

In order to provide the registration system for pledge of receivables in accordance with Article 228 of the Chinese Property Right Law, the People's Bank of China, which is China's central bank, made the Measures for Registration of the Pledge of Receivables ('MRPR'),<sup>143</sup> and established the Credit Information Centre. The MRPR addresses this issue by introducing a centralized registration system for pledges of account receivables. A pledge of account receivables is perfected by registering it in the Credit Information Centre. The Credit Information Centre establishes a system for publicizing the registration of pledge receivables to handle the registration of pledge receivables and provide inquiry services for the general public to search registration.<sup>144</sup>

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<sup>140</sup> Chinese Property Right Law, art 223(6)

<sup>141</sup> Chinese Property Right Law, art 228

<sup>142</sup> In comparison, under the Chinese Contract Law, if the creditor assigns its claim, it shall notify the debtor of the claim; such assignment is not binding upon the debtor of the claim if notice was not given; and a notice of the assignment of the claim given by the creditor may not be revoked, except with the consent of the assignee. Chinese Contract Law, article 80

<sup>143</sup> adopted in 2007, Order No.4 [2007] of the People's Bank of China, entered into force as of 1 October 2007

<sup>144</sup> MRPR, s 2

China has the registration system for the pledge of receivables under the MRPR. The MRPR provides a centralized scheme and system for registration of security interests over account receivables. This is welcomed especially by small and mid-sized companies and other enterprises engaged in manufacturing with high levels of account receivables and inventory.<sup>145</sup> It is important because lenders or other parties are able to access a centralized system in order to obtain information about a borrower or registered pledges of receivables.<sup>146</sup>

In China, the MRPR define account receivables as the right to ask the debtor to make payments which is obtained by the creditor for offering goods, services or facilities, including existing and potential money claim and the proceeds thereof, but not including the right to claim a payment incurred from bills or other negotiable securities.<sup>147</sup> It further provides that account receivables are included.<sup>148</sup> Still, there is the registration system for only pledges of receivables, and there is not any registration system for assignments of receivables in China.

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<sup>145</sup> Joshua T. Klein, “Recent Legal Changes That Affect Secured Financing In The People’s Republic Of China”, 27-JAN Am. Bankr. Inst. J. 38 (2009) 73

<sup>146</sup> *ibid* 72

<sup>147</sup> MRPR, s 4

<sup>148</sup> MRPR, s 4

## 2-4-4. General Security Rights Registry

### 2-4-4-1. France

Under the revised French Civil Code of 2006, a non-possessory pledge of movable assets may be perfected by registration. Since 2006, a pledge is perfected by publicity,<sup>149</sup> which is achieved by transfer of the encumbered asset to the creditor or a third party,<sup>150</sup> or by registration in a special registry.<sup>151</sup> Where the same asset has been the subject of several non-possessory pledges, priority is determined by the order of their respective registrations.<sup>152</sup>

### 2-4-4-2. Optional Registration

In Korea and Japan, as receivables financing develops, the problem with notice to debtors became unbearable. Under the Korean and the Japanese Civil Codes, an assignment of receivables is perfected against third parties only if an assignor gives notice to a debtor by means of a certified document with a fixed date stamp.<sup>153</sup> Notice to debtors in receivables financing takes time and costs, and is simply impracticable. To circumvent this notification requirement, Japan and Korea have developed registration systems for the assignment of receivables in specified types of receivables financing.

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<sup>149</sup> French Civil Code, art 2337.

<sup>150</sup> French Civil Code, art 2337.

<sup>151</sup> French Civil Code, art 2338. The details of the special registry are regulated by a decree in *Conseil d'Etat*.

<sup>152</sup> French Civil Code, art 2340.

<sup>153</sup> Korean Civil Code, art 450(2); Japanese Civil Code, art 467(2)

In Korea and Japan, the pledge of a right becomes effective by the method of the assignment of the right. Under the Korean and the Japanese Civil Codes, the assignment of an ordinary claim<sup>154</sup> (other than claims embodied in negotiable instruments or negotiable documents) may not be effective against the debtor of the claim or other third parties, unless the assignor notifies the debtor of the claim of the assignment or the debtor of the claim consents the assignment.<sup>155</sup> Such a notice to the debtor or the debtor's consent must be done by a certified document with a fixed date stamp, in order for the assignment of the claim to be effective against third parties other than the debtor of the claim.<sup>156</sup>

A claim embodied in a negotiable instrument or a negotiable document may be assigned by means of endorsement on and delivery of the instrument or document.<sup>157</sup> A pledge of a claim embodied in a negotiable instrument or a negotiable document is perfected by endorsement of the instrument or document and its delivery to the secured creditor.<sup>158</sup> A debt payable to bearer may be assigned by means of delivery of the bearer instrument.<sup>159</sup> A pledge of a bearer instrument is effected by delivery of the instrument to the secured creditor.<sup>160</sup>

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<sup>154</sup> It means the claim that should be performed to the specific creditor who is a party to the agreement from which the claim arises or an assignee of the claim, the assignment to whom the debtor is notified of or consents to.

<sup>155</sup> Korean Civil Code, art 450(1); Japanese Civil Code, art 467(1)

<sup>156</sup> Korean Civil Code, art 450(2); Japanese Civil Code, art 467(2)

<sup>157</sup> Korean Civil Code, art 508; Japanese Civil Code, art 469

<sup>158</sup> Korean Civil Code, art 350; Japanese Civil Code, art 365

<sup>159</sup> Korean Civil Code, art 523; Japanese Civil Code, art 473

<sup>160</sup> Korean Civil Code, art 351

Korea and Japan initially adopted registration systems with respect to the assignment of receivables to facilitate securitisation for the purpose of disposing non-performing loans. In Japan, it expanded to include pledges of receivables and the assignment of movable assets, abolishing the original law for securitisation. In Korea, registration of security interests in movable assets and receivables was adopted without abolishing the law for securitisation. When adopting registration systems, the legislators in Korea and Japan did not want to revise their respective Civil Codes because it would trigger costs and confusion. For this reason, they adopted alternative optional registration systems that co-exist with existing laws.

### 2-4-4-3. Japan

#### ***2-4-4-3-1. Specified Claims Act***

After the collapse of Japanese bubble economy in 1991,<sup>161</sup> Japan enacted the Act Concerning Restrictions on Businesses in Specified Claims<sup>162</sup> ('Specified Claims Act') in 1992 with the aim of helping lease companies and credit card companies to raise funds through securitisations.<sup>163</sup> The Specified Claims Act provided for the reporting system of securitisation plans to the Finance Committee and public notice of such a report in a daily newspaper, which could replace notice of the assignment to the debtor under the Japanese

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<sup>161</sup> At that time, many real estate brokers in Japan became bankrupt and consequently many banks which lent money to those real estate brokers also went bankrupt.

<sup>162</sup> Act No. 77 of 1992, enacted on 5 June 1992 and entered into force 1 June 1993. This Act is also translated as 'Business Asset Securitisation Act'.

<sup>163</sup> This Act covers auto loans and lease receivables e.g. industrial lease, computer lease, etc. Japanese Specified Claims Act, art 2(1).

Civil Code. However, the Specified Claims Act was abolished as of 30 December 2004.<sup>164</sup>

#### ***2-4-4-3-2. Special Act for the Assignment of Receivables***

After the financial crisis in Asia in 1997 and the moratorium of Russia in 1998, worries about insolvency due to temporary cash-flow shortage prevailed. Therefore how to change receivables to cash on a balance sheet was an important issue. Securitisation was encouraged. In June 1998, Japan enacted the Act Prescribing Exceptions to the Civil Code Requirements for Perfection of the Assignment of Receivables ('Special Act for the Assignment of Receivables'),<sup>165</sup> which provides that the assignment of receivables can also be perfected against third parties by registering it in the registration system administrated by the Ministry of Justice.<sup>166</sup> This is an alternative to notification of the assignment to the debtor under the Japanese Civil Code.<sup>167</sup> It only applies to the assignment of receivable where the assignor is a legal person.<sup>168</sup> Under the Special Act for the Assignment of Receivables, the scope of registration includes general receivables in addition to lease receivables and credit card receivables covered by the Specified Claims Act. It was seen as a way to promote securitisations,<sup>169</sup> which in turn would

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<sup>164</sup> Although the Specified Claims Act was still valid until 2004, it was not often used after 1998 because assignments covered by the Specified Claims Act were also applicable to the Special Act for the Assignment of Receivables enacted in 1998 which provides for the registration system for general receivables. Finally, the Specified Claims Act was repealed on 30 December 2004.

<sup>165</sup> Act No. 104 of 1998, enacted on 12 June 1998 and entered into force on 1 October 1998.

<sup>166</sup> Japan has been operating the electronic registration system since 1 October 1998.

<sup>167</sup> See Appendix II. 7 Qs1,2,3,4-2

<sup>168</sup> See Section 4-8-3

contribute to improving financial strength in markets through diversification of the methods by which companies could raise funds.<sup>170</sup>

#### ***2-4-4-3. Japanese Assignment Registration Act***

In 2005, Japan amended the Special Act for the Assignment of Receivables, and it was renamed the ‘Act on the Exceptions to the Civil Code Requirements for Perfection of the Assignment of Movable Assets and Receivables’ (‘Japanese Assignment Registration Act’).<sup>171</sup> The Japanese Assignment Registration Act expands the scope of registration to include assignments of movable assets, and provides a registration system for the assignment of movable assets and receivables.<sup>172</sup> Furthermore, the Japanese Assignment Registration Act provides for registration of the assignment of future receivables against unspecified debtors. Also, perfection of the assignment of a pool of receivables or movable assets could be achieved with one registration.

Under the Japanese Assignment Registration Act, the assignment of receivables, whose assignor is a legal person, may be registered. The Ministry of Justice is in charge of the management of the registration system for the assignment of movable assets and

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<sup>169</sup> Because there are a great number of account debtors in securitisation, it is impracticable to send notice of the assignment to all of the account debtors.

<sup>170</sup> Kazumoto Kitamura, ‘Perfection Law Clears Way for Financing Opportunities’, *The IFLR Guide to Japan 2006*, January 2006.

<sup>171</sup> Act No. 104 of June 12, 1998, amended on 26 July 2005 and entered into force on 3 October 2005.

<sup>172</sup> It was intended to cover primarily fiduciary transfer of title for security purposes (*JyouToTanPo* in Japanese), which is regarded as a transfer in Japan. According to Japanese Civil Code, art 178, the transfers of real rights concerning movables may not be perfected against third parties, unless the movables are delivered. For this delivery, Japanese Assignment Registration Act, art 3(1) stipulates that, when a registration of assignment is made in a movable assets registry with regard to the assignment of the movable assets, it shall be deemed that the movable assets have been delivered as set forth in Japanese Civil Code, art 178. Thus, if a non-possessory security interest is registered, it is perfected against third parties.

receivables under the Japanese Assignment Registration Act. An assignor and an assignee may request the registration of an assignment to the Assignment Registry Office, which is the Registration Department, Civil Administration Division of the Tokyo Legal Affairs Bureau. In Japan, there is only one centralized Assignment Registry Office in Tokyo.

Under the Japanese Assignment Registration Act, only assignments of movable assets<sup>173</sup> and receivables<sup>174</sup> and security interests in receivables<sup>175</sup> can be registered. A security interest in movable assets cannot be registered under the Japanese Assignment Registration Act. It is said that this is because Article 345 of the Japanese Civil Code stipulates that a pledgee may not allow a pledgor to possess the movable asset pledged on behalf of the pledgee.<sup>176</sup>

In Japan, the Japanese Assignment Registration Act has been enacted mainly for fiduciary transfer of title for security purposes (“*JyouToTanPo*” in Japanese), and *JyouToTanPo* in Japan is regarded as an outright assignment.<sup>177</sup> Accordingly, other acquisition financing that is not regarded as an outright assignment such as retention of title and financial lease cannot be registered under the Japanese Assignment Registration Act.

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<sup>173</sup> Japanese Assignment Registration Act, art 3

<sup>174</sup> Japanese Assignment Registration Act, art 4(1). Receivables are limited to nominative claims for monetary payment.

<sup>175</sup> Japanese Assignment Registration Act, art 14. With respect to receivables, the Japanese Assignment registration Act is *mutatis mutandis* applied to the pledge of receivables.

<sup>176</sup> Katsuhiro UEKAKI (植垣勝裕) and Hideki OGAWA (小川秀樹), *Ichimon Ichi Tou Dousan Saiken Jouto Tokurei Hou* (『一問一答・動産・債権譲渡特例法』) (3rd edn, Shouji Houmu (商事法務) 2008) 15-16. In fact, the same provision exists in the Korean Civil Code as well. Korean Civil Code, art 332 stipulates that a pledgee cannot let the pledgor hold possession of the pledged article on his behalf. However, the Korean Security Registration Act enables security interests in movable assets to be registered and makes them non-possessory security interests in movable assets.

<sup>177</sup> *ibid*

Under the Japanese Assignment Registration Act, registration is a creation requirement for an assignment of movable assets, but a perfection requirement for an assignment of and a security interest in receivables. Such registration is optional in that if an assignment of movable assets or an assignment of or a security interest in receivables is not registered, it would be regulated by the Japanese Civil Code.

#### 2-4-4-4. Korea

##### ***2-4-4-4-1. Asset-Backed Securitisation Act***

After the financial crisis in Korea in late 1997, which resulted in the sudden halt of corporate bond circulation, the government swiftly codified the Asset-Backed Securitisation Act ('ABS Act')<sup>178</sup> in September 1998. The purpose of the ABS Act was to facilitate the restructuring of financial institutions through efficient resolution of non-performing loans ('NPLs').

The ABS Act provides a filing system for the assignment of receivables in asset-backed securitisations,<sup>179</sup> where an originator is a financial institution or public corporation stipulated in Article 2(2) of this Act. The ABS Act does not apply to securitisations where an ordinary private company is the originator. It is because the legislators thought preferential exceptions imposed by this Act might be misused.<sup>180</sup>

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<sup>178</sup> Act No. 5555, enacted on 16 September 1998 and entered into force on 16 September 1998.

<sup>179</sup> Korean ABS Act, art 3.

<sup>180</sup> Chae-Jin Lee, 'Study on Development and Evolving Process of Securitisation Laws in Korea', (2005.06) Vol.18, No.2, *Commercial Case Study (Sang Sa Pan Rye Yeon Gu)* 208-9.

Facilitating such receivables financing is very important because it could prevent insolvencies caused by a temporary cash-flow shortage. The rapid enactment in 1998 of the ABS Act helped the Korean economy to recover from the crisis quickly. Under the ABS Act, a SPV can perfect an assignment of receivables against third parties by filing the securitisation plan and the assignment of receivables at the Financial Services Commission.<sup>181</sup>

#### ***2-4-4-4-2. Mortgage-Backed Securitisation Company Act***

Subsequently, in 1999, the Korean government codified the Mortgage-Backed Securitisation Company Act ('MBS Company Act')<sup>182</sup> to facilitate mortgage-backed securitisations. The MBS Company Act has many provisions that parallel the ABS Act. The MBS Company Act provides for the filing system for the assignment of receivables in mortgage-backed securitisations.<sup>183</sup>

#### ***2-4-4-4-3. Korean Security Registration Act***

Since the financial crisis in 1998, many banks in Korea have been privatized, and foreign investors have taken over the management of many Korean banks. As a result, it

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<sup>181</sup> Korean ABS Act, art 7(2). See Appendix II. 6 Q1,3-2

<sup>182</sup> Act No. 5692, enacted on 29 January 1999 and entered into force on 29 April 1999.

<sup>183</sup> Korean MBS Company Act, art 4.

became more difficult for small and mid-sized companies, especially those that do not have sufficient real estate to satisfy a bank's collateral requirements.<sup>184</sup>

To help these small and mid-sized companies with their financing, and pave a way for companies to use receivables and tangible movable assets as collateral, on 10 June 2010, Korea enacted the Act concerning Security Interests in Movable Assets and Receivables, etc. ("Korean Security Registration Act").<sup>185</sup> This Act provides for another convenient method to perfect security interests in movable assets or receivables against third parties. The Act provides for the registration system for security interests in movable assets and receivables.<sup>186</sup> The Act entered into force on 11 June 2012. The Supreme Court of Korea is in charge of the management of the registration system for the security interests in movable assets and receivables under the Korean Security Registration Act. There are many registration offices around Korea.<sup>187</sup> Those registration offices are linked with each other online and thus information is searchable at any of the registration offices.

Under the Korean Security Registration Act, only security interest in movable assets and receivables<sup>188</sup> can be registered. The registration system under the Korean Security Registration Act does not cover an outright assignment of movable assets or

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<sup>184</sup> It is because foreign investors tend to avoid the risks of small and mid-sized companies and will not provide them with long-term policy loans.

<sup>185</sup> *DongSan-ChaeKwon DeungEui DamBoE GwanHan BeobLyul* (동산·채권등의담보에관한법률) in Korean, enacted 10 June 2010, entered into force 11 June 2012.

<sup>186</sup> It provides for two kinds of registry: the movable assets registry and the receivables registry. Security interests in movable assets should be registered in the movable assets registry, and security interests in receivables should be registered in the receivables registry.

<sup>187</sup> Korean Security Registration Act, arts 39(1) and (2)

<sup>188</sup> It covers, among claims, only nominative claims for payment of money. Korean Security Registration Act, art 34(1)

receivables. The reason why the Korean Security Registration Act does not include the assignment of receivable is that the drafters did not want to change the Civil Code regime of the assignment of receivables. In addition, assignments of receivables in Asset-Backed Securitizations and Mortgage-Backed Securitizations will still be regulated by the Korean ABS Act and the Korean MBS Company Act, under which the assignment of receivables is perfected by filing with the Financial Services Commission even after the operation of the Korean Security Registration Act, whereas Japan abolished the Specified Claims Act<sup>189</sup> after adopting the registration system for general receivables.

Outright assignments of movable assets and receivables are regulated by the Civil Code.<sup>190</sup> For an outright assignment of a movable asset, delivery of possession is required. The Korean Civil Code stipulates that the assignment of a real right over a movable asset takes effect by delivery of the movable asset.<sup>191</sup> For an outright assignment of a receivable, notice of the assignment to, or consent of, the debtor is required.<sup>192</sup> For securitisation, assignments of receivables in securitisation assets are regulated by the ABS Act or the MBS Company Act.

Acquisition financing including fiduciary transfer of title for security purposes, reservation of title and financial lease can be registered under the Korean Security Registration Act, so far as it is an agreement to create security interests in movable assets

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<sup>189</sup> *Tokutei Saiken Tou Kakaru Jigyō no Kisei nikansuru Houritsu* (特定債権等に係る事業の規制に関する法律) enacted on 5 June 1992, Act No. 77 of 1992, entered into force 1 June 1993

<sup>190</sup> For movable assets, Korean Civil Code, arts 188 and 189; for receivables, Korean Civil Code art 450

<sup>191</sup> Korean Civil Code, art 188(1)

<sup>192</sup> Korean Civil Code, art 450(1). Under the Korean Civil Code, which stipulates that the assignment of a receivable cannot be set up against the debtor of the receivable or third parties, unless the assignor has given notice thereof to the debtor of the receivable or the debtor of the receivable has consented thereto.

or receivables.<sup>193</sup> The Korean Security Registration Act stipulates, ‘security agreement’ means the agreement to create security interests in movable assets, receivables or intellectual property according to this Act regardless of the title such as *YangDoDamBo* (fiduciary transfer of title for security purposes).<sup>194</sup> A financial lease right can be registered by the lessor as a secured creditor and the lessee as a security provider.<sup>195</sup> A reservation-of-title right can be registered by the seller as a secured creditor and the buyer as a security provider.

If a legal person encumbers movable assets or receivables according to a security agreement (either pledge or fiduciary transfer), it can register its security interest.<sup>196</sup> The parties may decide whether to register a financial lease right or a reservation-of-title right and be treated as a secured creditor under the Korean Security Registration Act, or not to register it and remain in an uncertain status as before.<sup>197</sup>

Once *YangDoDamBo* is registered, it should be regulated under the Korean Security Registration Act regardless of the content of the *YangDoDamBo* contract,<sup>198</sup> and it would be not a real *YangDoDamBo* anymore. *YangDoDamBo* does not have to be registered. If it is not registered, it would be regulated by uncertain case laws as it used to be. Once a financial lease right or a reservation-of-title right is registered in the security

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<sup>193</sup> Korean Security Registration Act, art 2(1)

<sup>194</sup> Korean Security Registration Act, art 2(1)

<sup>195</sup> Kwang-Hyun Suk and Woo-Jung Jon, International Secured Transactions (South Korea Section), in Dennis Campbell (ed), *International Secured Transactions* Binder 2 (Oceana Publications, Inc., Dobbs Ferry, NY, 2010)

<sup>196</sup> For a movable asset, Korean Security Registration Act, art 3(1); and for a nominative claim for the purpose of monetary payment, Korean Security Registration Act, art 34(1)

<sup>197</sup> *ibid* `

<sup>198</sup> Jae Hyung KIM, ‘Organisation and Contents of the draft of the Act concerning Security interests in Movable Assets, Receivables, etc.’, *Jurist* Vol.638 (November 2009) 12

rights registry under the Korean Security Registration Act, it is treated as a security interest and regulated by the Korean Security Registration Act.<sup>199</sup> Still, a financial lease or a reservation-of-title transaction can be created and used by an agreement of parties without registration. Then, it is regulated by the Korean Civil Code and case laws.

Under the Korean Security Registration Act, registration is a creation requirement for a security interest in movable assets, but a perfection requirement for a security interest in receivables. Such registration is optional in that if a security interest in movable assets or receivables is not registered, it would be regulated as a pledge of movable assets or receivables under the Korean Civil Code.

**<Table 4> Comparison of Chinese, Korean and Japanese Registration Systems for Movable Assets and Receivables**

	China	Korean Security Registration Act	Japanese Assignment Registration Act
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<sup>199</sup> *ibid*

Transfer of movable assets	Not registered	Not registered	Registrable (optional) <sup>200</sup>
Pledge (or mortgage) of movable assets	manufacturing facilities, raw materials, semi-manufactured goods and products <sup>201</sup>	Registrable (optional)	Not registered <sup>202</sup>
Retention of title	Not registered		
Financial lease	Not registered		
A pool of movable assets Future movable assets	Registrable (compulsory) <sup>203</sup>	Registrable (optional) <sup>204</sup>	no provision
Outright transfer of receivables	Not registered	Not registered <sup>205</sup>	Registrable (optional) <sup>206</sup>
Pledge of receivables	Registrable (compulsory) <sup>207</sup>	Registrable (optional) <sup>208</sup>	Registrable (optional) <sup>209</sup>
Future receivables	Registrable (compulsory) <sup>210</sup>	Registrable (optional) <sup>211</sup>	no provision

<sup>200</sup> Japanese Assignment Registration Act, art 3

<sup>201</sup> Chinese Property Right Law, art 180(1)(iv)

<sup>202</sup> Katsuhiko UEKAKI (植垣勝裕) and Hideki OGAWA (小川秀樹), *Ichi Mon Ichi Tou Dousan Saiken Jouto Tokurei Hou* (『一問一答・動産・債権譲渡特例法』) (3rd edn, Shouji Houmu (商事法務) 2008) 15-16. Japanese Civil Code, art 345: ‘A pledgee may not allow a pledgor to possess the movable asset pledged on behalf of the pledgee.’

<sup>203</sup> Chinese Property Right Law, arts 181 and 189

<sup>204</sup> Korean Security Registration Act, art 3(2)(i). However, a group of movable assets and receivables cannot be registered together. Movable assets and receivables should be separated from each other. Security interests in movables assets cannot be registered in the receivables registry, and security interests in receivables cannot be registered in the movable assets registry.

<sup>205</sup> Korean Security Registration Act, art 2(3)

<sup>206</sup> Japanese Assignment Registration Act, art 4(1)

<sup>207</sup> Chinese Property Right Law, art 223(vi)

<sup>208</sup> Korean Security Registration Act, art 34(1)

<sup>209</sup> Japanese Assignment Registration Act, art 14

<sup>210</sup> Chinese Measures for Registration of the Pledge of Receivables, art 4

<sup>211</sup> Korean Security Registration Act, art 34(2)

## **2-5. INTERNATIONAL EFFORTS OF HARMONISATION**

A security rights registry was created for non-possessory security interests in England in the late nineteenth century. A notice-filing system was created in the US in 1952. Ever since, many countries have established a national domestic security rights registry. Establishing an international registry is much more difficult than establishing a national domestic registry even though they share similar basic principles. A major barrier is language, including legal terminology, which results in accessibility difficulties for lay persons, and problems with identification of registrants and specification of encumbered objects. As international efforts of harmonisation, there have been soft laws and international conventions.

### **2-5-1. Soft Laws**

There have been soft laws that recommend establishing a security rights registry at national level. They include the UNCITRAL Legislative Guide on Secured Transactions,<sup>212</sup> the European Bank for Reconstruction and Development ('EBRD') Model Law on Secured Transactions<sup>213</sup> and the Organization of American States ('OAS')

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<sup>212</sup> The UNCITRAL Legislative Guide on Secured Transactions was prepared by the United Nations Commission on International Trade Law ('UNCITRAL'), and the General Assembly of the United Nations adopted the Guide on 11 December 2008.  
< [http://www.uncitral.org/uncitral/en/uncitral\\_texts/payments/Guide\\_securedtrans.html](http://www.uncitral.org/uncitral/en/uncitral_texts/payments/Guide_securedtrans.html)> accessed 5 January 2011.

<sup>213</sup> The European Bank for Reconstruction and Development ('EBRD') published the EBRD Model Law on Secured Transactions in early 1994.

Model Inter-American Law on Secured Transactions.<sup>214</sup> The Draft Common Frame of Reference ('DCFR')<sup>215</sup> of the European Union also proposes the European registry for proprietary rights in movable assets.

#### 2-5-1-1. EBRD Model Law on Secured Transactions

The EBRD published the EBRD Model Law on Secured Transactions in early 1994. Many central and eastern European countries referred to the EBRD Model Law on Secured Transactions, and established registration systems for security interests in personal property.<sup>216</sup> The EBRD Model Law shows a model law regarding the registration system for security interests. Furthermore, the EBRD established the Guiding Principles for the Development of a Charges Registry in 2004.

The philosophy of the EBRD Model Law on Secured Transactions was to target first and foremost security transactions, and thus the EBRD Model Law does not apply to the assignment of receivables, even if it may serve the same function as security transactions.<sup>217</sup>

The EBRD Model Law on Secured Transactions produced a text compatible with the civil law concepts which many central and eastern European legal systems are based

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<sup>214</sup> The Organization of American States ('OAS') made the Model Inter-American Law on Secured Transactions.

<sup>215</sup> The Draft Common Frame of Reference is presented by the Study Group on a European Civil Code and the Research Group on Existing EC Private Law, commissioned by the European Commission in 2005. Part of the work is funded by the European Commission's Research Directorate-General. See *DCFR Outline Edition* (Sellier 2009) 3-4

<sup>216</sup> Jan-Hendrik Röver, *Secured lending in Eastern Europe : comparative law of secured transactions and the EBRD model law* (OUP, 2007)

<sup>217</sup> Email from Frédérique Dahan (Lead Counsel and Head of Financial Law Unit, European Bank for Reconstruction and Development) to author (24 February 2011)

upon and, at the same time, to draw on common law systems that have developed solutions to accommodate modern financing techniques.<sup>218</sup>

Under the EBRD Model Law on Secured Transactions, a charge may be only (i) a registered charge; or (ii) an unpaid vendor's charge; or (iii) a possessory charge. A charge on a receivable can only fall into the first category,<sup>219</sup> and therefore a charge on receivables must be registered. Thus, the EBRD Model Law on Secured Transactions does not require notice to the account debtor for perfection against third parties.

## 2-5-1-2. OAS Model Inter-American Law on Secured Transactions

The Organization of American States ('OAS') made the Model Inter-American Law on Secured Transactions, and recently incorporated the registration for security interests regime. There are conflicts between the common law and the civil law among American States. North American States follows the common law. However, Central and South American States follows the civil law tradition. In addition, Louisiana State in the US and Québec State in Canada follows the civil law tradition. The OAS Model Inter-American Law shows the efforts to harmonise the common law and the civil law.

Nonetheless, the OAS Model Inter-American Law on Secured Transactions is much closer to the American UCC Article 9 in substance as well as terminology than the EBRD Model Law on Secured Transactions.<sup>220</sup> Perfection of a security interest against

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<sup>218</sup> Introduction, *EBRD Model Law on Secured Transactions* (London, EBRD, 1994)

<sup>219</sup> EBRD Model Law on Secured Transactions, art 6(1)

<sup>220</sup> Gerard McCormack, *Secured Credit and the Harmonisation of Law: The UNCITRAL Experience* (Edward Elgar 2011) 120

third parties requires the security interest to be publicised by registration or by delivery of possession or control of the encumbered asset to the secured creditor or to a third person on its behalf.<sup>221</sup>

The OAS Model Inter-American Law covers an assignment of receivables as well as a security interest in receivables. Article 13 of the OAS Model Law stipulates that, if the assignment is not for security it must comply only with the publicity provisions of the OAS Model Law; if it fails to so comply, it will be subject to the priority rules of the OAS Model Law.

In practice, there are problems with respect to establishing the security rights registry in American States.<sup>222</sup> First, civil law jurisdictions are not familiar with notice-filing system. In civil law jurisdictions, registry officers are supposed to examine and review the content of registration applications, and registrants should submit contract documents. Another problem is description of encumbered assets. In civil law jurisdictions, usually more detailed description is required. For these reasons, it is not common to have security rights registries in Central and South American States.

### 2-5-1-3. UNCITRAL Legislative Guide on Secured Transactions

The UNCITRAL Legislative Guide on Secured Transactions contains commentary and legislative recommendations on all issues that need to be addressed in a

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<sup>221</sup> OAS Model Inter-American Law on Secured Transactions, art 10

<sup>222</sup> Telephone Interview with John M Wilson, Senior Legal Advisor, Department of International Law, Organization of American States (UNCITRAL, Austria, Vienna, 22 September 2010)

modern law on security interests in all types of movable asset, tangible or intangible.<sup>223</sup> The UNCITRAL Legislative Guide follows a modern approach to secured transactions that can be described as a functional, integrated and comprehensive approach, relying on a notice-based public registry for third-party and priority effects.<sup>224</sup> The UNCITRAL Legislative Guide also applies to outright assignments of receivables although they are not secured transactions.<sup>225</sup> In broad terms, the UNCITRAL Legislative Guide follows the UCC Article 9 functional approach towards security.<sup>226</sup> Under the UCC Article 9, notice of all non-possessory security interests in tangible movable assets and all assignments of receivables must be filed in order to be perfected against third parties including the insolvency representative.<sup>227</sup> Likewise, the UNCITRAL Legislative Guide on Secured Transactions recommends that all non-possessory security interests in tangible movable assets and all assignments of receivables must be registered to be perfected against third parties.<sup>228</sup> Such a functional, integrated and comprehensive approach to secured transactions is clear and simple.

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<sup>223</sup> Spiros V. Bazinas, 'The Work of UNCITRAL on Security Interests: An Overview' [2010] *Uniform Law Review* 315, 319

<sup>224</sup> UNCITRAL Legislative Guide on Secured Transactions, 55-58 [101]-[112]. Spiros V. Bazinas, 'The Work of UNCITRAL on Security Interests: An Overview' [2010] *Uniform Law Review* 315, 320.

<sup>225</sup> Spiros V. Bazinas, 'The Work of UNCITRAL on Security Interests: An Overview' [2010] *Uniform Law Review* 315, 320

<sup>226</sup> Gerard McCormack, *Secured Credit and the Harmonisation of Law: The UNCITRAL Experience* (Edward Elgar 2011) 152

<sup>227</sup> Under the UCC Article 9, one of three perfection methods is required: (1) filing of a financing statement, (2) possession or (3) control. UCC, ss 9-310 - 9-314 .

<sup>228</sup> Recommendation 37

#### 2-5-1-4. Draft Common Frame of Reference ('DCFR')

The Draft Common Frame of Reference ('DCFR') is an effort to accomplish a unified European Civil Code. The Study Group on a European Civil Code and the Research Group on Existing EC Private Law, commissioned by the European Commission in 2005, presented the Draft Common Frame of Reference in 2009.<sup>229</sup> Part of the work is funded by the European Commission's Research Directorate-General.

Because most European countries are the civil law antecedents, it is often voiced that the DCFR would involve marginalising the common law canon of experience in favour of the civil law.<sup>230</sup> Notwithstanding, the DCFR adopts a registration system for priority of security interests. The DCFR states that the priority between several security interests and between a security interest and other limited proprietary rights in the same asset is determined according to the order of the time of registration, possession or control for security interests.<sup>231</sup> This rule applies to security interests in receivables. However, the rule does not apply to assignments of receivables. The DCFR states that, where there are successive purported assignments by the same person of the same right to performance, the purported assignee whose assignment is first notified to the debtor has priority over any earlier assignee if at the time of the later assignment the assignee under that assignment neither knew nor could reasonably be expected to have known of the earlier assignment.<sup>232</sup>

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<sup>229</sup> *Draft Common Frame of Reference, Outline Edition* (Sellier 2009) 3-4  
<[http://ec.europa.eu/justice/contract/files/european-private-law\\_en.pdf](http://ec.europa.eu/justice/contract/files/european-private-law_en.pdf)> accessed 10 March 2012

<sup>230</sup> Gerard McCormack, *Secured Credit and the Harmonisation of Law: The UNCITRAL Experience* (Edward Elgar 2011) 187

<sup>231</sup> *DCFR Outline Edition* (Sellier 2009) 478, arts IX-4:101(1) and (2).

<sup>232</sup> *DCFR Outline Edition* (Sellier 2009) 265, art III-5:121.

## 2-5-2. International Conventions

There have been many international conventions addressing matters of public international law, such as human rights. But it appears to be more difficult to harmonise numerous legal systems and create a unified international convention in areas of private law. There have been only two international conventions relating to international registration systems: the UN Receivables Convention and the Cape Town Convention.

### 2-5-2-1. UN Convention on the Assignment of Receivables in International Trade

The UN Convention on the Assignment of Receivables in International Trade ('UN Receivables Convention')<sup>233</sup> was the first international effort to harmonise the laws on the assignment of receivables around the world. In order to facilitate international assignments of receivables, the UN Receivables Convention provides three options for Contracting States to adopt. The UN Receivables Convention proposes the registration system as one of the three options. It offers alternative priority rules based on registration<sup>234</sup> and model provisions for an international registration system.<sup>235</sup>

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<sup>233</sup> (adopted 31 January 2002, open for signature 31 December 2003). The Convention will enter into force upon ratification by five Member States (ibid art 45(1)). However, to date, the UN Convention has been signed by only three States and acceded to by only one: Luxembourg signed on 12 June 2002; Madagascar signed on 24 September 2003; the United States signed on 30 December 2003; and Liberia acceded to the UN Convention on 16 September 2005.  
<[http://www.uncitral.org/uncitral/en/uncitral\\_texts/payments/2001Convention\\_receivables\\_status.html](http://www.uncitral.org/uncitral/en/uncitral_texts/payments/2001Convention_receivables_status.html)> accessed 10 October 2011.

<sup>234</sup> Annex to the Convention, Section I.

In addition, the UN Receivables Convention removes statutory prohibitions from the assignment of future receivables and bulk assignments,<sup>236</sup> and prevents contractual prohibition on the assignment of trade receivables.<sup>237</sup>

However, the UN Receivables Convention, adopted January 2002 has not been successful despite presenting a desirable model for the assignment of receivables regime.

The proposed IRSAR Convention differs from the UN Receivables Convention in that, under the proposed IRSAR Convention, priority of assignments of and security interests in receivables is determined by the order of registration in the IRSAR uniformly.<sup>238</sup>

## 2-5-2-2. Convention on International Interests in Mobile Equipment

The Convention on International Interests in Mobile Equipment (Cape Town, 2001) of UNIDROIT, called the ‘Cape Town Convention’<sup>239</sup> established the first example of an international registration system for mobile equipment such as aircraft and railway

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<sup>235</sup> Annex to the Convention, Section II.

<sup>236</sup> UN Receivables Convention, art 8

<sup>237</sup> UN Receivables Convention, art 9

<sup>238</sup> The assignment or security interest registered first in the IRSAR prevails over other assignments or security interests which are subsequently registered or not registered.

<sup>239</sup> The Convention on International Interests in Mobile Equipment (‘Cape Town Convention’) and the Protocol to the Convention on International Interests in Mobile Equipment on Matters specific to Aircraft Equipment (‘Aircraft Protocol’) were adopted jointly in Cape Town on 16 November 2001. The Cape Town Convention entered into force on 1 March 2006. As of 11 May 2013, the Cape Town Convention has been ratified by 57 States and the Aircraft Protocol by 51 States. In order for the Cape Town Convention to be enforced completely in a Member State of the European Union (‘EU’), both the Member State and the EU must join the Cape Town Convention. Even though the EU joins the Cape Town Convention, if a Member State does not, it does not give the Convention any effect whatsoever in the Member State. The Convention and the Protocol can only be ratified in its entirety, subject to permitted reservations or declarations. Adoption of the Cape Town Convention by the EU merely frees Member States to ratify the Convention. With respect to key insolvency provisions in the Aircraft Protocol, over which the EU has exclusive competence, the EU has made no declaration, which leaves it to Member States as to what declaration, if any, to make under Article XI (Remedies on insolvency) of the Aircraft Protocol.

rolling stock. This demonstrates that an international registration system for the assignment and security interest of receivables is also possible.<sup>240</sup>

## **2-6. PROS FOR & CONS AGAINST GENERAL SECURITY RIGHTS REGISTRY**

### **2-6-1. Pros**

#### **2-6-1-1. Use Movable Assets as Security**

For finance, a company may borrow money from banks. Banks usually request security or collateral for loans. Historically, security interests in tangible movable assets are essentially possessory i.e. pledges. Security interests in real estate are non-possessory because they can be registered in the real estate registry. Because of the economic need for security providers' use of encumbered assets, non-possessory security interests in tangible movable assets have developed by registering the movable assets. Since non-possessory security interests are not visible to third parties, for non-possessory security interests in movable assets, a security rights registry is needed. Creating security interests in movable assets and receivables enables small and middle sized companies that do not have sufficient real estate to pledge for a loan to finance, and thus provides entrepreneurs greater chances and opportunities.

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<sup>240</sup> The International Registry of Mobile Assets under the Cape Town Convention and its Aircraft Protocol exemplifies the problems caused by the language barrier including the specification of encumbered objects, identification of registrants and interested parties, incentive of registration, enforcement regime, conflict of laws issues and registration fee.

Lord Scott, in *Re Spectrum Plus Ltd.*,<sup>241</sup> observed the preponderance of circulating capital within enterprises such as inventory and receivables stating as follows:

By the middle of the 19th century industrial and commercial expansion in this country had led to an increasing need by companies for more capital. Subscription for share capital could not meet this need and loan capital had to be raised. But the lenders required security for their loans. Traditional security, in the form of legal or equitable charges over the borrowers' fixed assets, whether land or goods, could not meet the need. The greater part of most entrepreneurial companies' assets would consist of raw materials, work in progress, stock-in-trade and trade debts. These were circulating assets, replaced in the normal course of business and constantly changing.

## 2-6-1-2. Civil Law Jurisdiction v Common Law Jurisdiction

In order to estimate and compare the rights of secured creditors in each jurisdiction, Rafael La Porta and others use four variables: (a) no automatic stay on assets; (b) secured creditors first paid; (c) restrictions for going into reorganization; and (d) management does not stay in reorganization.<sup>242</sup> They take the perspective of senior secured creditors rather than unsecured creditors for concreteness and because much of the debt in the world has that character.<sup>243</sup> Their conclusion is that common law jurisdictions protect investors the most, and French civil law jurisdictions protect them the least; and German civil law jurisdictions are in the middle though closer to the civil law group.<sup>244</sup> Rafael La Porta and others argue that civil law countries which have

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<sup>241</sup> [2005] UKHL 41 (HL), [2005] 2 AC 680 para 95. Also see Robert R. Pennington, 'The Genesis of the Floating Charge' (1960) 23 MLR 630, 634-38

<sup>242</sup> Rafael La Porta and others, 'Law and Finance', *Journal of Political Economy*, vol. 106(6) (University of Chicago Press December 1998) 1135

<sup>243</sup> *ibid* 1134

<sup>244</sup> *ibid* 1139

weaker investor protections, measured by the character of legal rules and the quality of law enforcement, have less developed credit markets than common law countries.<sup>245</sup>

A general security rights registry makes it easy for a debtor to create a security interest in movable assets and receivables by registering it and for a creditor to become a secured creditor. Thus, a general security rights registry would strengthen investor protections and ultimately develop credit markets.

### 2-6-1-3. World Bank Report

Empirical studies by the Center for the Economic Analysis of Law with the World Bank show that the lack of a security rights registration system accounts for higher interest rates in Guatemala<sup>246</sup> than in the US, and that it results in limited access to credit in the agriculture sector of Nicaragua.<sup>247</sup> The Centre for the Economic Analysis of Law also concluded that adopting a security rights registration system would increase the GDP of Argentina and Bolivia.<sup>248</sup> This is on the basis that businesses could obtain the cash necessary to purchase additional inventory and generate additional sales by using their portfolios of assets as collateral. Where such financing is possible, it allow an increased

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<sup>245</sup> Rafael La Porta and others, 'Legal Determinants of External Finance' (1997) 52(3) *Journal of Finance* 1131-50

<sup>246</sup> Steven L. Schwarcz, 'Towards a Centralized Perfection System for Cross-border Receivables Financing' (Fall 1999) 20 *University of Pennsylvania Journal of International Economic Law* 455, 467-468, citing 'Heywood W. Fleisig and Nuria de la Peña, Guatemala: How Problems in the Framework for Secured Transactions Limit Access to Credit' (Nov. 1998) <<http://www.ceal.org>>.

<sup>247</sup> Heywood W. Fleisig and Nuria de la Peña, 'Nicaragua: How Problems in the Framework for Secured Transactions Limit Access to Credit' (Center for the Economic Analysis of Law February 1998). <[http://www.ceal.org/papers/Nicaversion26\(cealp039\)CovPage&ExecSum,v2.htm](http://www.ceal.org/papers/Nicaversion26(cealp039)CovPage&ExecSum,v2.htm)> accessed 10 November 2010 .

<sup>248</sup> Heywood W. Fleisig and Nuria de la Peña, 'Guatemala: How Problems in the Framework for Secured Transactions Limit Access to Credit' (Center for the Economic Analysis of Law February November 1998) 44. <<http://www.ceal.org>> accessed 10 November 2010.

line of credit for the company so that it could better respond to the needs of its business.<sup>249</sup>

For example, research by the World Bank shows that movable property accounts for approximately 60% of company's capital stock in the US in 2004.<sup>250</sup> Among movable property: intellectual property was 30%; accounts receivable 20%; inventory 10%; automobiles 1%; and other equipment 39%.<sup>251</sup> To take one example, in Nigeria, due to the lack of a registration system, nearly 99% of movable property that could serve as collateral for a loan in the US would likely be unacceptable to a lender.<sup>252</sup> In some jurisdictions, there is a great disparity between the assets that firms possess or will need to possess, and the assets lenders will accept as collateral.<sup>253</sup> The data from surveys conducted by the World Bank Group in more than sixty low- and middle-income countries from 2001 to 2005 shows this disparity (figure 1).

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<sup>249</sup> Steven L. Schwarcz, 'Towards a Centralized Perfection System for Cross-border Receivables Financing' (Fall 1999) 20 *University of Pennsylvania Journal of International Economic Law* 455, 466-68

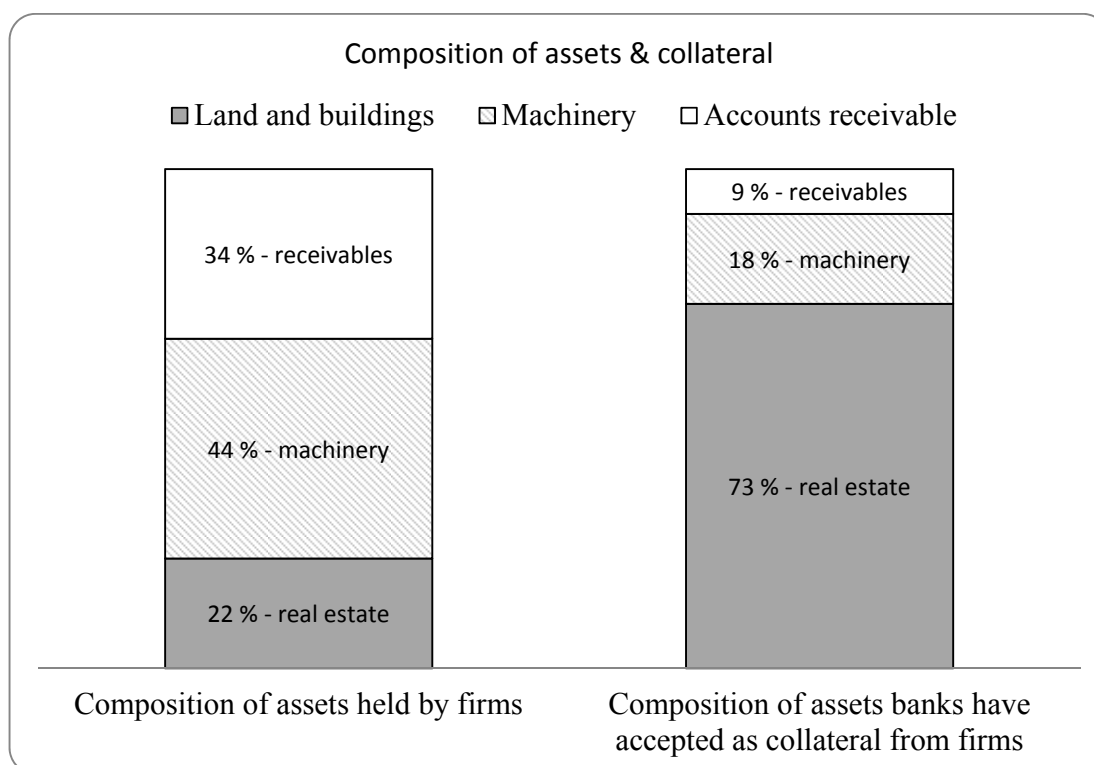
<sup>250</sup> Heywood Fleisig, Mehnaz Safavian and Nuria de la Peña, 'Reforming Collateral Laws to Expand Access to Finance' (World Bank, August 2006)  
<[http://www.ifc.org/ifcext/sme.nsf/AttachmentsByTitle/BEE+Collateral+Access+to+Finance/\\$FILE/Reforming\\_Collateral.pdf](http://www.ifc.org/ifcext/sme.nsf/AttachmentsByTitle/BEE+Collateral+Access+to+Finance/$FILE/Reforming_Collateral.pdf)> accessed 10 November 2010.

<sup>251</sup> *ibid* 8.

<sup>252</sup> *ibid* 7.

<sup>253</sup> *ibid* 8.

<Figure 1> The assets firms hold are a poor match for those banks accept as collateral.<sup>254</sup>



There are several reasons why banks accept less machinery and account receivables as collateral from firms in the jurisdictions where a registration system is not developed. With respect to machinery, since companies need to use the machinery for production, a non-possessory security interest must be used. However, if the security provider (debtor) still has possession of the machinery, it is quite difficult to perfect the security interest in the machinery. With respect to account receivables, giving notice of the assignment to all account debtors is costly and time-consuming. Moreover,

<sup>254</sup> Mehnaz Safavian, Heywood Fleisig, and Jevgenijs Steinbuks, ‘Unlocking Dead Capital: How Reforming Collateral Laws Improves Access to Finance’, *Private Sector Development Viewpoint*, No. 307 (World Bank, March 2006) 2. Data are from surveys conducted in more than 60 low- and middle-income countries in 2001–05. The source is World Bank Group, Enterprise Surveys database. [http://rru.worldbank.org/documents/publicpolicyjournal/307Safavian\\_Fleisig\\_Steinbuks.pdf](http://rru.worldbank.org/documents/publicpolicyjournal/307Safavian_Fleisig_Steinbuks.pdf) accessed 10 November 2010.

sometimes the security provider (assignor) does not wish to let account debtors know that their receivables are assigned.

The World Bank data below shows that many firms in low- and middle-income countries cannot meet collateral requirements for loans because of a lack of security interest registries for movable assets and receivables. Thus, it is recommendable for such countries to have security interest registries.

<Table 5> World Bank Group, Enterprise Surveys<sup>255</sup>

	Firms that are rejected because they have insufficient collateral (as a percent of all firms that are rejected for credit)	Firms that do not apply for credit because the collateral requirements are too high (as a percent of all firms that do not apply for credit)
Africa	51%	19%
East Asia	70%	20%
Eastern Europe & Central Asia	72%	13%
Latin America & the Caribbean	39%	23%
South Asia	72%	31%

<sup>255</sup> Heywood Fleisig, Mehnaz Safavian, Nuria de la Peña, 'Reforming Collateral Laws to Expand Access to Finance' (World Bank, August 2006) 9. Data are from surveys conducted in more than 60 countries in 2001-05.  
<[http://www.ifc.org/ifcext/sme.nsf/AttachmentsByTitle/BEE+Collateral+Access+to+Finance/\\$FILE/Reforming\\_Collateral.pdf](http://www.ifc.org/ifcext/sme.nsf/AttachmentsByTitle/BEE+Collateral+Access+to+Finance/$FILE/Reforming_Collateral.pdf)> accessed 10 November 2010.

## 2-6-2. Cons

### 2-6-2-1. Over-Leverage

Most of the soft laws and international conventions recommend a registration system for security interests. However, there are also criticisms against these global movements.

Secured credit law reform is generally promoted on the basis that it will foster market-based decision making on credit issues. It is often seen as part of an overall growth and development strategy.<sup>256</sup> One of the presumptions is that markets will intrinsically lead to efficient outcomes. However, the recent global financial crisis has highlighted the possibility of desirable government intervention that can guide economic growth and make everyone better off.<sup>257</sup>

When a debtor may use its movable assets and receivables as collateral, it might get excessive loans from creditors. Such over-leverage increases risks. With the excessive loans, the debtor would try greater business. Such expansion of credit might introduce a source of error in the calculations of the entrepreneurs, and thus causes them to misjudge business projects and to embark upon businesses which previously had been regarded as unprofitable.<sup>258</sup> If the business would be successful the debtor would be well off, but if the business would fail the debtor would lose more.

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<sup>256</sup> Gerard McCormack, *Secured Credit and the Harmonisation of Law: The UNCITRAL Experience* (Edward Elgar 2011) 71

<sup>257</sup> *ibid* 72

<sup>258</sup> Ludwig von Mises, *Interventionism: An Economic Analysis*, Edited with a Foreword by Bettina Bien Greaves (Indianapolis: Liberty Fund, 2011). Ch. 2.: Credit Expansion  
<<http://oll.libertyfund.org/title/2394/226152>> accessed 10 May 2013

Expansion of credit increases demand for land and accordingly raises the price of land. Price appreciation enlarges the amount that can be borrowed based on the collateral of land. This further expansion of credit may in turn raise land prices.<sup>259</sup> Over all, it could create economic bubbles in a society.

All of a sudden, people may discover that land is overvalued relative to the real economy sector cash flows, e.g. businesses cannot pay escalating rents.<sup>260</sup> Then, land prices start to drop to the extent that land price becomes insufficient to cover the loans. As a result, debtors default on loans and dispose of land. Simultaneous sales of land accelerate price drop.

## 2-6-2-2. Secured Creditor v. Unsecured Creditor

Security runs counter to fairness in that it may involve secured creditors being paid whereas unsecured creditors remain unpaid.<sup>261</sup> In case of a default, secured creditors may have a simple interest in getting possession of collateral no matter what happens to the debtor company, whereas unsecured creditors may wish to preserve the debtor company as a going concern so that they can hope to get some of their money back if the company turns a profit.<sup>262</sup> It might restrict vibrant economic activities of companies and cause adverse effects on the development of economy. Bebchuk argues that full priority

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<sup>259</sup> Jeffrey N. Gordon and Christopher Muller, 'Confronting Financial Crisis: Dodd-Frank's Dangers and the Case for a Systemic Emergency Insurance Fund', 28 *Yale Journal on Regulation* 151 (Winter 2011) 169

<sup>260</sup> *ibid*

<sup>261</sup> Gerard McCormack, *Secured Credit and the Harmonisation of Law: The UNCITRAL Experience* (Edward Elgar 2011) 70

<sup>262</sup> Rafael La Porta and others, 'Law and Finance', *Journal of Political Economy*, vol. 106(6) (University of Chicago Press December 1998) 1134

of secured creditors over unsecured creditors, distorting the monitoring functions of companies, reduces the incentive of companies to take adequate precautions, and therefore causes excessive use of security interests.<sup>263</sup>

### **2-6-3. Analysis**

Security rights registry enables a company to use its movable assets and receivables as collateral and raise more finance. It might cause vicious circles of expansion of credit and market bubble and collapse. However, collateralising receivables has different aspects from collateralising real estate. The latter could be more risky than the former since the price of real estate could fluctuate much more dramatically than the value of receivables. It is because the supply of land is limited, and there is a gap between its use value and exchange value. Collateralising real estate contains the risk of market bubble and collapse, which are quite unpredictable. For example, MBS which caused the subprime mortgage crisis in 2008 is based on mortgages on real estate which is susceptible to market bubble and collapse.

In contrast, receivables do not have use value since one does not utilise receivables for other production. Receivables have only exchange value. Therefore, receivables cannot be overvalued relative to its use value, and thus have less risk of market bubble and collapse. With respect to receivables, the risk is debt default, which is calculated and reflected in discounting the value of receivables. For this reason, receivables could be safer to use as collateral than real estate.

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<sup>263</sup> Lucian A Bebhuk and Jesse M Fried, 'The Uneasy Case for the Priority of Secured Claims in Bankruptcy', 105 *Yale Law Journal* 857 (1996) 895-904

The problem of secured creditors' tendency of liquidation of the debtor company due to full priority of secured creditors over unsecured creditors could be solved by national insolvency laws stipulating automatic stay on assets in insolvency.

## **2-7. SCOPE OF REGISTRATION - RECEIVABLES**

This thesis proposes an international registration system focused on assignments of and security interests in only receivables. With respect to national general security rights registry, almost all registries cover both receivables and tangible movable assets.<sup>264</sup> However, this thesis argues that establishing a general security rights registry at an international level would be impractical and not practicable because of translation difficulties and identification problems. These difficulties are now discussed.

### **2-7-1. Translation**

With respect to security interests, encumbered assets must be identified.<sup>265</sup> Types of tangible movable assets are so unlimited and varied that translation of their descriptions in English would be very difficult. Descriptions, and their translations, of all types of encumbered items in an international registry would be prohibitively expensive

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<sup>264</sup> There are a few examples of national registration systems applicable only to receivables. One example is the filing system of securitisation plans including the assignment of securitised receivables under the Korean ABS Act and Korean MBS Company Act. See Appendix II. 6 Q1,3-2 and Q1,3-3. In Japan, the registration system was only for the assignment of receivables from 1998 until the revision of the Japanese Assignment Registration Act in 2005. See Appendix II. 7 Q1,2,3,4-2

<sup>265</sup> Many jurisdictions do not acknowledge the legal concept of universal charges where individual assets do not have to be identified.

and, even though possible, would still produce uncertainty. It might be possible only among English-speaking States or among countries of a similar linguistic family.

## 2-7-2. Identification

Identification of an encumbered asset is a problem. For example, in Japan, there are two ways to identify tangible movable assets: (i) a detailed description of the asset,<sup>266</sup> or, (ii) a brief description of the asset and its location.<sup>267</sup> The first method requires too much detailed information of an individual asset. The second method is for a pool of assets, but it also has a weakness. If the registered assets are moved to another location, the registration becomes invalid.<sup>268</sup> For this reason, in Japan, registration of security interests in movable assets is not used as much as fiduciary transfer of title for security purposes,<sup>269</sup> while registration of security interests in receivables is frequently used.

For this reason, international registries have only been established for specific mobile equipment under the Cape Town Convention. The International Registry of Mobile Assets under the Cape Town Convention is relatively successful. However, such

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<sup>266</sup> Japanese Assignment Registration Rules, art 8(1)(i).

<sup>267</sup> Japanese Assignment Registration Rules, art 8(1)(ii).

<sup>268</sup> For example, in Japan, a secured creditor (P) registered his security interests in a pool of assets with a brief description and their current location (X). Then, once the registered assets are moved to another location (Y), the registration identifying the assets by a brief description and their old location (X) is no longer valid. Meanwhile, if another secured creditor (Q) registers security interests in the assets with the new location (Y), only the new registration is valid. As a result, P will lose his security interest in the assets, and Q's registration will prevail over P's registration.

<sup>269</sup> Fiduciary transfer of title for security purposes is a kind of acquisition financing. The secured creditor takes the ownership title of the encumbered asset *erga omnes*. However, in between the security provider and the secured creditor, they agree that the security provider still retains the true ownership title of the encumbered asset. Fiduciary transfer of title for security purposes can be perfected by purely fictitious constructive transfer of possession. Thus, the security provider may retain possession of, and make use of, the encumbered asset.

an international registry might not be successful when applied to other types of property. It was relatively simple to establish an international registry for aircraft because there was already a registry for aircraft in every state in accordance with the Convention on International Civil Aviation ('Chicago Convention').<sup>270</sup> It is true that if there is already a national registry for a certain type of property, it is easier to make an international one. In addition, the internet-based International Registry for aircraft uses a down-drop menu bar, provided by aircraft manufacturing companies, to identify the object of security interests.<sup>271</sup> Such an object specific approach makes registration and searches for particular assets very specific in the International Registry for aircraft.

### **2-7-3. Separate International Registry for Each Type of Property**

To harmonise the laws of security interests in movable assets and receivables around the world, the most suitable approach would be different for each type of assets. It is very difficult to find only one method applicable to all types of property. The Cape Town Convention has established International Registries for aircraft equipment, railway rolling stock<sup>272</sup> and satellite.<sup>273</sup> It is convenient for a potential secured creditor to search

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<sup>270</sup> Signed on 7 December 1944 by 52 States. The Provisional International Civil Aviation Organization functioned from 6 June 1945 until 4 April 1947. By 5 March 1947 the 26th ratification was received, and International Civil Aviation Organization ('ICAO') came into being on 4 April 1947. In October 1947, ICAO became a specialized agency of the United Nations linked to Economic and Social Council (ECOSOC). <[www.icao.int/icao/net/dcs/7300.html](http://www.icao.int/icao/net/dcs/7300.html)> accessed on 1 July 2011

<sup>271</sup> Answer to Frequently Asked Question No. 11 on the International Registry on Mobile Assets website <<https://www.internationalregistry.aero/irWeb/showFAQs.do>> accessed 17 September 2011. See also Regulations and Procedures for the International Registry, Regulations, s 5.1.

<sup>272</sup> Luxembourg Protocol to the Convention on International Interests in Mobile Equipment on Matters specific to Railway Rolling Stock, adopted in Luxembourg on 23 February 2007

<sup>273</sup> Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Space Assets, adopted in Berlin on 9 March 2012

any prior security interests in an object because these registries are particular to the type of mobile equipment. Thus, establishing an international and general security rights registry covering all types of personal properties might not be feasible at this stage. First, the international registry for each type of asset such as aircraft, rail way stock, satellite, and construction and agricultural equipment can be established, and in the near future it would be feasible to consolidate them into one general international security rights registry.

Among other assets, this thesis focuses on receivables. Currently, there is no international registry for the assignment of receivables. Given the importance of receivables in international finance, harmonising the law regarding the assignment of receivables (outright sale or security interests) is of great importance practically. A receivable could be identified simply by identifying the assignor, the assignee, a list of debtors or a general description of the debtors of the receivables, the amount of monetary obligation and the due date. In addition, a receivable may be easily translated in different languages. Thus, establishing an international registration system for assignments of and security interests in receivables would be feasible.

## **2-8. CONCLUSION OF PART 2**

A registration system for security interests in movable assets and receivables was originally developed in common law jurisdictions. England invented the general security rights registry. The US invented a notice-filing registration. Owing to the strict principle

of *numerus clausus*, civil law jurisdictions could not develop registration systems for security interests in movable assets and receivables until the increasing economic demand of non-possessory security interests becomes unbearable. Today, many civil law countries e.g. Korea and Japan established registration systems for security interests in movable assets and receivables. Korea and Japan invented optional registration.

Furthermore, there have been global movements to establish a general security rights registry to facilitate creating security interests in movable assets and receivables and to try establishing international registries for each specific type of assets including receivables.

In an international level, establishing a general security rights registry which covers all movable assets and receivables might not be recommendable due to over-leverage and credit expansion problems, and would be impractical because of translation and identification problems. For these reasons, this thesis focuses on the registration system for assignments of and security interests in receivables.

## **PART 3. CURRENT LAWS ON ASSIGNMENTS OF & SECURITY INTERESTS IN**

### **RECEIVABLES**

#### **3-1. INTRODUCTION**

Part 3 comparatively analyses current laws on priority and perfection of assignments of and security interests in receivables and private international laws. These comparative analyses have three purposes: First, it is to show how different various systems are and thus to demonstrate the need for an international registration system. Second, it is to demonstrate the complexity of investigations that have to be made by a potential assignee under the current law. Third, it is to survey possible models for an international convention and to determine the most widely acceptable legal system.

Chapter 3-2 examines current laws in the following jurisdictions: the US, Canada, New Zealand, Australia, Korea, Japan, France, Belgium, England, China, Germany, Austria and the Netherlands. These jurisdictions have been selected partly because they represent different legal systems and partly because it was impossible to study additional jurisdictions due to the limited capacity of this thesis. It compares the receivables assignment systems of the jurisdictions and considers whether a registration system is more desirable than other systems.

Chapter 3-3 categorises these jurisdictions into five groups according to perfection methods and potential assignee's check point.

Chapter 3-4 examines private international laws of these jurisdictions in order to simulate which national law would be applied in international receivables financing. The simulation shows that unifying choice-of-laws rules cannot solve the current situation and rather a unified substantive rule is needed to facilitate international receivables financing. These researches shows many problems hindering international receivables financing such as different governing laws for priority, different rules for perfection and uncertainty of private international law rules.

Chapter 3-5 tries to find a solution, and concludes that an international registration system could be a solution.

## 3-2. COMPARATIVE ANALYSIS ON PRIORITY & PERFECTION

### 3-2-1. Preliminary Review

#### 3-2-1-1. Definition of Perfection

Priority is determined by the order of perfection against third parties. Let us first analyse the term, ‘perfection’. ‘Perfection’ is the step required to make an assignment or a security interest effective against third parties and in the case of insolvency of the assignor or the security provider.<sup>274</sup> It is different from the creation of a security. In some cases, an additional step beyond the creation of a security must be taken for perfection. For example, under the UK Companies Act 2006 an unregistered charge is not perfected against third parties or in insolvency,<sup>275</sup> but it is valid against the company itself. This is because registration is a perfection requirement for a company charge. In other cases, the creation requirement is also the perfection requirement.<sup>276</sup> The UNCITRAL Legislative Guide does not use the term ‘perfection’. Under the Guide, a security interest either has ‘third party effectiveness’ or there is no priority contest at all.<sup>277</sup>

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<sup>274</sup> Hugh Beale, Michael Bridge, Louise Gullifer and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) 327 [7.13].

<sup>275</sup> See Appendix II. 10 Q2

<sup>276</sup> For example, the situation referred to as ‘automatic perfection’ under the UCC Article 9. An assignment of accounts that does not transfer a significant part of the outstanding accounts of the assignor is automatically perfected upon attachment under UCC, s 9-309(2).

<sup>277</sup> Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border security over Tangibles* (Sellier 2007) 37

Perfection against third parties means third party effectiveness, which preserves priority over another assignee.<sup>278</sup> Perfection of an assignment of receivables is regulated by the law on assignments of receivables. Perfection of a security interest in receivables is regulated by the law on security interests in receivables. Thus, this thesis examines assignments and security interests separately.

Third parties include insolvency representatives. However, perfection against an insolvency representative will be examined separately because it is regulated by insolvency laws of each state. Perfection of an assignment against an insolvency representative of an assignor requires a step to make it effective in case of the assignor's insolvency, which means that the assignee can enforce against the insolvency representative and the assigned receivable is not included in the insolvency estate.

Chapter 3-2 analyses priority of assignments of receivables vis-à-vis third parties (Section 3-2-2), and separately analyses priority of security interests in receivables vis-à-vis third parties (Section 3-2-3), because in many jurisdictions priority of assignments and priority of security interests are regulated differently. Furthermore, Chapter 3-2 analyses perfection of an assignment of receivables against the insolvency representative (Section 3-2-4) and perfection of a security interest in receivables against the insolvency representative (Section 3-2-5).

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<sup>278</sup> There are exceptions to this principle. The followings are examples of where perfection does not secure priority. Under English law, the exceptions are subordination of a floating charge to a fixed charge (See Section 5-5-2-1) and a *bona fide* purchaser (See Section 5-4-3-2). Under UCC Article 9, a secured creditor who has his security interest perfected can be subordinated to a buyer in the ordinary course of business (See Section 5-4-4-2).

### 3-2-1-2. Case Scenario

Chapter 3-2 analyses the laws with respect to assignments of and security interests in receivables in the following jurisdictions: the US, Canada, New Zealand, Australia, Korea, Japan, France, Belgium, England, China, Germany, Austria and the Netherlands. To provide a direct comparison of the laws in each jurisdiction, the same six questions are asked of each. The six questions relate to priority vis-à-vis third parties and perfection against the insolvency representative with respect to an assignment of a receivable and a security interest in a receivable.

These questions are for the analysis from the following two aspects: (1) the first aspect is to determine for each jurisdiction what an assignee must do to achieve perfection against third parties and priority over other assignees or secured creditors in receivables financing. There could be a security interest in a receivable as well as an assignment of that same receivable.<sup>279</sup> In other words, an assignor may create a security interest in his receivable for a creditor and later sell the same receivable to a third party, or vice versa. In such situations, to determine the priority, the court must compare both perfection of an assignment of the receivable and perfection of a security interest in the receivable. This aspect is examined in Section 3-2-6.

(2) The second aspect is to determine where a potential assignee should investigate before executing an assignment or security contract in order to secure his priority over any prior assignee or secured creditor in the receivable. It demonstrates the complexity of investigations that have to be made under the current law by a potential assignee. This aspect is examined in Section 3-2-7.

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<sup>279</sup> See Section 1-6

The six questions are based on the following case scenario:

C is a company. In this case scenario, C who is an assignor and a security provider is a legal person (company) not a natural person.

C is a creditor of D. C has a receivable R owed by D. D is the debtor of the receivable R. C sells its receivable to E for receivables financing such as factoring, block discounting or securitisation. C assigns the receivable to E. E is an assignee of the receivable.

C arranges for a loan from S using its receivables as security. S is a secured creditor with a security interest in C's receivables, including the receivable R owed by D and assigned to E. E2 is another assignee of the receivable R. S2 is another secured creditor with a security interest in the receivable R.

P is a potential assignee of the receivable R or a potential secured creditor with a security interest in the receivable R.

### 3-2-1-3. Six Common Questions

Q1. How is priority between E and E2 determined?

Q2. How is priority between S and S2 determined?

Q3. What should assignee E do to be perfected against the insolvency representative of the assignor C in the case of C's insolvency?

Q4. What should the secured creditor S do to be perfected against the insolvency representative of C in the case of C's insolvency?

Q5. How is priority between E and S determined?

Q6. What should a potential assignee P check before executing the assignment contract or security interest contract in order to secure priority over any prior assignment of or security interest in the receivable R?

#### 3-2-1-4. Table of Preliminary Answers

<Table 6> below shows the answers to the six common questions asked for the thirteen jurisdictions listed above. Details of the answers to the six common questions are elaborated upon in the Appendix II (Answers to the Six Common Questions).<sup>280</sup> Each Section of Appendix II answers the same six questions regarding the requirements for perfection against different parties. This allows direct comparisons to be made among the different jurisdictions.

<Table 6> below simplifies the answers and uses abbreviations for the answers. ‘Notice’ means notice to the debtor of the receivable. For example, in most jurisdictions, effectiveness against a debtor of a receivable is achieved by notice to the debtor of the receivable. In particular, in Korea, Japan and France, notice to the debtor requires specific formality stipulated by law. Such notice with specific formality under the law is indicated as ‘formal notice’.

‘Registration’ means registration. In Korea especially, there are two methods of registration for assignments of receivables and security interests in receivables. The first registration at the Financial Services Commission of Korea is indicated as ‘securitisation

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<sup>280</sup> Appendix II (Answers to the Six Common Questions) See 329-396

registration’ and the second registration in the Korean Security Registry Act is indicated as ‘registration’.

‘Contract’ means conclusion of the contract. ‘Notarised contract’ means notarisation of the contract or registration of the contract at the Tax Registration Department (*Belastingdienst/Registratie en successie*) in the Netherlands. ‘Transfer deed’ means a transfer deed (*bordereau*) in France. ‘Company book’ means recordation in the company book of the assignor in Austria, which is a perfection method for a pledge of receivables.

‘Debtor’ means enquiring of the debtor of the receivable whether it received notice of a prior assignment or security interest. In the jurisdictions where priority is determined by the order of notice to the debtor of the receivable, to check whether there is any prior assignment of or security interest in a receivable, a potential assignee should ask the debtor of the receivable. Even though in Germany, Austria and the Netherlands, enquiring of the debtor won’t give a complete picture, a potential assignee had better ask the debtor of the receivable.

<Table 6> Summary Table of Answers

	Group R				Group RN		Group N		Group SR		Group C		
	USA	Canada	New Zealand	Australia	Korea	Japan	France	Belgium	England	China	Germany	Austria	Netherlands
Q1	registration	registration	registration	registration	securitisation registration, formal notice	registration, formal notice	formal notice, transfer deed	notice	notice	notice	contract	contract	notarised contract, notice
Q2	registration	registration	registration	registration	registration, formal notice	registration, formal notice	contract, transfer deed	notice	notice	registration	notice	company book, notice	notarised contract, notice
Q3	registration	registration	registration	registration	securitisation registration	registration	formal notice, transfer deed	contract	contract	contract	contract	contract	notarised contract, notice
Q4	registration	registration	registration	registration	registration	registration	contract, transfer deed	contract	registration	registration	notice	company book, notice	notarised contract, notice
Q5	registration	registration	registration	registration	securitisation registration, registration, formal notice	registration, formal notice	formal notice, contract, transfer deed	notice	notice	registration, notice	contract, notice	contract, company book, notice	notarised contract, notice
Q6	registration	registration	registration	registration	securitisation registration, registration, debtor	registration, debtor	debtor	debtor	registration, debtor	registration, debtor	debtor	debtor	debtor

## **3-2-2. Priority of Assignments vis-à-vis Third Parties (Question 1)**

### 3-2-2-1. Priority

Section 3-2-2 analyses priority of only absolute assignments. Priority of security interests are addressed in Section 3-2-3. In Korea, France, China, Germany and Austria, the perfection of an assignment of receivables against third parties is different from the perfection of a security interest in receivables against third parties. In the other jurisdictions they are the same.

If an assignment of a receivable is perfected against third parties, it has priority over third parties. Perfection against third parties preserves priority among competing assignees and secured creditors. In principle, the assignee that first achieves perfection against third parties has priority over other assignees.

Perfection against third parties can be achieved by publicity such as (i) notice of the assignment to the debtor or (ii) registration or (iii) conclusion of the assignment.

### 3-2-2-2. Notice to the Debtor

In many jurisdictions, priority between competing assignees is determined by the order in which a debtor receives notice of the assignment. Accordingly, notification to the debtor is required for perfection of the assignment. In Korea, Japan, France, Belgium, England and China, priority between competing assignees is determined by the order in which the account debtor receives notice of the assignment.

In Korea, Japan and France, an assignor or an assignee must give notice of the assignment to the debtor to perfect the assignment against competing assignees, the insolvency representative and a judgment creditor of the assignor. If the assignor becomes insolvent and no notice of the assignment has been given to the debtor, the insolvency representative prevails over the assignee and therefore the assignment is void and ineffective.

The French Civil Code stipulates that an assignment is perfected against third parties only by giving notice of the assignment with an official letter (*signification*) to the debtor.<sup>281</sup> It also stipulates that, alternatively, the assignment may be made effective against third parties by the debtor's acceptance of the assignment in a notarised deed (*acte authentique*).<sup>282</sup> Such notification is also required for effectiveness against the debtor. Until notification, the debtor may discharge the debt by paying the assignor (original creditor) regardless of any actual knowledge of the assignment on the part of the debtor.<sup>283</sup> Korea and Japan follow this approach of the French Civil Code except they generally omit the formality requirements.

In Korea and Japan, the assignment of a receivable is not effective against the debtor of a receivable, unless the assignor gives notice of the assignment to the debtor or the debtor has consented to the assignment.<sup>284</sup> Furthermore, for perfection against third parties and priority, such notification requires formality of a certified document with a

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<sup>281</sup> French Civil Code, art 1690. See Appendix II. 8 Q1-1

<sup>282</sup> French Civil Code, art 1690.

<sup>283</sup> James Leavy, France, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 129.

<sup>284</sup> Korean Civil Code, art 450(1); Japanese Civil Code, art 467(1)

fixed date stamp.<sup>285</sup> However, for suing the debtor, notice of the assignment to the debtor does not require any formality.

English law is the opposite of the situation in Korea and Japan with respect to the formality of notification for priority and for suing the debtor. According to the holding of *Dearle v. Hall*,<sup>286</sup> priority between competing assignees is determined by the order that the debtor receives notice of the assignment. It is the ‘first in time’ rule. Therefore notice of the assignment to the debtor is required for priority. Such notice does not require any formality. However, to sue the debtor, notification to the debtor must be in writing.<sup>287</sup>

But under English law, notification is not required for perfection against the insolvency representative. An assignment without notice to the debtor is still valid as an equitable assignment.<sup>288</sup> The concept of ‘equitable assignment’ of English law which does not require notice to the debtor<sup>289</sup> does not exist in many civil jurisdictions including France, Korea and Japan.

In France,<sup>290</sup> Korea<sup>291</sup> and Japan,<sup>292</sup> priority of competing assignees and perfection in the insolvency of the assignor are determined by the order in which the debtor of the receivable receives notice of the assignment. In France, Korea and Japan, if

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<sup>285</sup> Korean Civil Code, art 450(2); Japanese Civil Code, art 467(2)

<sup>286</sup> *Dearle v. Hall* (1828) 3 Russ 1. In fact, the decision of *Dearle v. Hall* relates to interests held in trust. According to the decision, if the equitable owner of an asset purports to dispose of his equitable interest on two or more occasions, the claimant who first notifies the trustee or legal owner of the asset shall have priority.

<sup>287</sup> In English law, the benefit of a contract may be transferred to a third party by a process called ‘assignment’ under Section 136(1) of the Law of Property Act 1925.

<sup>288</sup> See Appendix II. 10 Q3-2

<sup>289</sup> See Appendix II. 10 Q1-1

<sup>290</sup> French Civil Code, art 1690.

<sup>291</sup> Korean Civil Code, art 450.

<sup>292</sup> Japanese Civil Code, art 467.

the debtor of the receivable has not received notice of the assignment, the assignment is null and void and cannot be protected in the insolvency of the assignor. The English law principle that an equitable assignee may defeat a trustee in bankruptcy has no equivalent in these jurisdictions. These indicate how essential giving notice of the assignment to the debtor of the receivable is in these jurisdictions. However, giving notice of the assignment to debtors of receivables is time-consuming and costly. Thus, it had been an obstacle to receivables financing, especially to assignments of future receivables and bulk assignments of receivables.<sup>293</sup>

Under *Dearle v. Hall* there is an exception to the first in time rule. If a subsequent assignee knew of the prior assignment at the time of his assignment, even if the subsequent assignee gave notice of the assignment to the debtor earlier than the prior assignee, the subsequent assignee cannot have priority over the prior assignee.<sup>294</sup> Thus, under English law, priority is influenced by the subsequent assignee's knowledge of the prior assignment.

This is different to the approach of France, Korea and Japan. In these states, even though a subsequent assignee knew of the prior assignment at the time of his assignment, the subsequent assignee may have priority over the prior assignee by giving notice of his assignment earlier than the prior assignee. This is because under the French, Korean, and Japanese civil codes, an assignment of receivables is not perfected against third parties unless the debtor is notified of the assignment. Therefore, prior assignment without notification to the debtor is not perfected against the subsequent assignee.

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<sup>293</sup> See Section 3-5-1

<sup>294</sup> *Dearle v Hall* (1828) 3 Russ 1. Hugh Beale, Michael Bridge, Louise Gullifer and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) 437 [13.09]. See Appendix II. 10 Q3

### 3-2-2-3. Registration

The meaning of a registration system for the assignment of receivables is related to the different cultures of assignment in common law jurisdictions and civil law jurisdictions. In the US, Canada, New Zealand and Australia, priority is determined by the order of registration. Under registration systems such as UCC Article 9 and the PPSAs of Canada, New Zealand and Australia, the assignment of receivables is perfected against third parties by registration, and priority between competing assignees is determined by the order of registration. In these jurisdictions and in Japan, the registration system covers both assignments of receivables and security interests in receivables. In contrast, in the UK, Korea and China, the registration system covers only security interests in receivables.

In the US, the filing system includes both security interests in and outright assignments of receivables.<sup>295</sup> In 1952, UCC Article 9 was drafted with the intent of unifying the rules regarding perfection of assignments of receivables that varied between the states. UCC Article 9 includes not only security interests in receivables but also outright assignments of receivables.<sup>296</sup> Thus, the assignor and the assignee only have to file a financing statement for the assignee to be perfected against the insolvency representative of the assignor. Most of the law on the assignment of receivables is

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<sup>295</sup> UCC, s 9-109(a)(3).

<sup>296</sup> UCC, s 9-310(a). UCC Article 9 applies to the assignments of accounts, chattel paper, payment intangibles and promissory notes (s 9-109(a)(3)) as well as all security interests in personal property (s 9-109(a)(1)). 'Payment intangible' refers to general intangibles where the debtor's primary obligation is monetary. UCC, s 9-102(a)(61)

stipulated not in general contract law but in UCC Article 9. As a result, the law on the assignment of receivables appears to be treated as a subsection of the broader law regarding transfers of personal property security under UCC Article 9.<sup>297</sup>

The PPSAs of Canada, New Zealand and Australia also include both security interests in receivables and outright assignments of receivables. Under the PPSAs, registration of an assignment of a receivable is required for perfection of the assignment against third parties.<sup>298</sup> Priority between competing assignees is determined by the order of filing or registration of the assignment.

In Japan, there is a registration system for the assignment of movable assets and receivables under the Japanese Assignment Registration Act. It also covers pledges of receivables.<sup>299</sup>

### 3-2-2-4. Time of Creation Doctrine

#### ***3-2-2-4-1. Neither Notice Nor Registration***

In Germany,<sup>300</sup> Austria and the Netherlands, priority between competing assignees is determined by the order of conclusion of the assignment contract regardless

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<sup>297</sup> Hein Kötz, 'Rights of Third Parties. Third Party Beneficiaries and Assignment' in Arthur von Mehren (ed), *International Encyclopedia of Comparative Law*, vol 7 ch 13 (Möhr, Tübingen, 1992) 56

<sup>298</sup> Saskatchewan PPSA, s 35(2); Ontario PPSA, s 30(1)1; New Zealand PPSA, s 66; Australian PPSA, ss 267, 267A

<sup>299</sup> Japanese Assignment Registration Act, art 14.

<sup>300</sup> In Germany, if the assignee demands, the assignor must issue the assignee with a publicly certified document on the assignment, and the assignee must bear and advance the costs. German Civil Code, s 403. This is to verify the time of conclusion of the assignment contract. See Appendix II. 12 Q1-1

of notification to the debtor of the receivable. In Germany,<sup>301</sup> Austria and the Netherlands, notice to the debtor is not required for an assignment (*Zession*) of a receivable to be perfected in the insolvency of the assignor. Therefore an assignment without notice is absolutely valid. The distinction between the statutory assignment and the equitable assignment under English law does not work in these jurisdictions. The assignee prior in time of the assignment agreement has priority regardless of notification.

Until the debtor receives notice of the assignment, the debtor of the receivable may discharge the debt by paying the original creditor (the assignor). In the case of double assignments, the debtor that did not receive notice of the first assignment from the assignor may also discharge the debt by paying the second assignee if the second assignee presents the document evidencing the assignment issued by the assignor.<sup>302</sup> However, the second assignee must surrender the money to the first assignee once the second assignee has collected the debt from the debtor. This is even though the second assignee gave proper consideration to the assignor and knew nothing of the first assignment.<sup>303</sup> The second assignee may cancel the assignment contract with the assignor and make a claim for damages from the assignor. In Germany, the date of the assignment is verified by a publicly certified document evidencing the assignment (if it is issued), which an assignor must issue upon demand.<sup>304</sup>

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<sup>301</sup> German Civil Code, s 398. In contrast, for a pledge of a receivable to be effective against third parties, the debtor of the receivable must be notified of the pledge. German Civil Code, s 1280. However, because of the inconvenience of notification, pledges of receivables are seldom used in practice in Germany.

<sup>302</sup> German Civil Code, s 410(1)

<sup>303</sup> See Appendix II. 12 Q3

<sup>304</sup> German Civil Code, s 403 stipulates that the assignor must, upon demand, issue the assignee with a publicly certified document on the assignment. The assignee must bear and advance the costs.

In a jurisdiction following the German approach where notice to debtors is not required for the assignment, priority between an assignee, the insolvency representative and a judgment creditor is determined according to the order of conclusion of the assignment contract, bankruptcy adjudication and attachment notice.

The German concept of the assignment of receivables is peculiar in that it has an *in rem* (*dingliche* in German) nature. Once a receivable is assigned to an assignee (A), the assignor no longer has a right in the receivable and a later assignment gives the subsequent assignee (B) no right in the receivable.<sup>305</sup> An assignment is effective *erga omnes* even if particular formalities are not required.<sup>306</sup> The German Civil Code does not require any publicity for the assignment of receivables. For this reason, there is not strong need to develop a registration system for the assignment of receivables. In Germany, an assignor functions as the information centre since the law requires that a potential assignee consult with the assignor regarding the status of a receivable. This is sensible because the assignor is in the best position to report on the status of his receivable.

How then could the law prevent an assignor from attempting double assignments of receivables? The German view on double assignments or fraudulent non-possessory security interests is that such conduct is a tort or breach of contract, so that the assignor who sells a receivable twice, or sells a receivable that has been pledged as security, will be liable for the damages incurred by third parties and will be punished criminally.

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<sup>305</sup> Julia Klauer Rakob, Germany, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 112.

<sup>306</sup> Lina Aleknaitė, 'Why the Fruits Of Capital Markets Are Less Accessible In Civil Law Jurisdictions Or How France And Germany Try To Benefit From Asset Securitisation' (Winter 2007) 5 *DePaul Business & Commercial Law Journal* 191, 219.

#### **3-2-2-4-2. Delivery of Transfer Deed (*Bordereau*)**

Under the French Monetary and Financial Code, an assignment of receivables may be perfected against third parties by simple delivery of a transfer deed (*bordereau*).<sup>307</sup> An assignor must sign on a transfer deed (*bordereau*) and the assignee must date it. The date of a *Dailly* assignment is indicated on a transfer deed (*bordereau*). A transfer deed (*bordereau*) is made between an assignor and an assignee without any involvement or verification of a third party or even the debtor of the receivable. Delivering a transfer deed (*bordereau*) is not publishing it. Neither is it a notice to a debtor nor registration. A transfer deed (*bordereau*) is simply a written document, the provisions of which are stipulated by law, evidencing the date of the conclusion of the relevant contract.

#### **3-2-2-4-3. Comparative Analysis**

The priority rule under the French Monetary and Financial Code is, from a functional point of view, close to the German law, where no notification is required for third party effectiveness. To the extent the Monetary and Financial Code apply and a transfer deed (*bordereau*) could perfect an assignment of receivables,<sup>308</sup> the French regime for the assignment of receivables has almost the same effect as the German system.

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<sup>307</sup> French Monetary and Financial Code, art L313-23 to L313-34

<sup>308</sup> See Appendix II. 8 Q1-2

First, in both the situation where no competing creditor gives notice to a debtor of the receivable and the situation where all competing creditors give notice to a debtor, the priority rule is the same in France and Germany. Priority is determined by the order of conclusion of the relevant contract.

For comparison, under Korean and Japanese law, if neither competing creditor gives notice of the assignment of a receivable, the debtor of the receivable may pay the assignor (original creditor), and competing creditors could only claim against the assignor.

In the situation where one competing assignee gives notice to the debtor of the receivable, and the others do not, in France, the assignee giving notice has priority over the other assignee. This is different from the priority rules under German law.

In Germany, where X is an assignor, Y1 and Y2 are assignees and the assignment to Y1 is prior in time to the assignment to Y2, if Y2 asks the debtor of the receivable to pay the debt to him and shows the assignment contract, the debtor without knowing of the prior assignment to Y1 could discharge the debt by paying Y2. Still, Y1 has priority and Y1 could sue Y2 for unjust enrichment.

In France, if no other assignee has given notice of the assignment to the debtor of the receivable, Y2 may claim against the debtor of the receivable, and the debtor may discharge the debt by paying Y2. This is the same as Germany. However, in France, Y2 who gave notice of the assignment to the debtor of the receivable has priority over Y1 who has not given notice. Therefore, unlike in Germany, Y1 without giving notice is not entitled to claim against Y2 for unjust enrichment.<sup>309</sup>

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<sup>309</sup> If in theory, Y1 could be allowed to give notice to the debtor, even after the debtor of the receivable paid, Y1 might be able to have priority over Y2 and then accordingly sue Y2 for unjust enrichment.

In comparison, under Korean and Japanese law, if Y2 first gives notice of the assignment to the debtor of the receivable, Y2 has priority over Y1 because only the assignment to Y2 is effective against the debtor of the receivable as well as third parties.<sup>310</sup>

The primary difference between French law and German law is the scope of this priority regime focused on the time of creation and supplemented by notice. In France, it only applies to assignments and pledges under the Monetary and Financial Code and pledges of receivables under the revised French Civil Code. By contrast, in Germany, this priority regime applies generally to the assignment of receivables under the German Civil Code but not to pledges of receivables under the German Civil Code. In Germany, because of notification difficulties, a pledge of receivables is rarely used, but rather a security assignment is used. Notification is not required for a security assignment in Germany<sup>311</sup> since a security assignment is not a pledge, and therefore Section 1280 of the German Civil Code does not apply to a security assignment of receivables.<sup>312</sup>

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<sup>310</sup> Appendix II. 6 Q1,3-1 and 3-3-7 Q1,2,3,4-1

<sup>311</sup> Julia Klauer Rakob, Germany, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 96-97.

<sup>312</sup> See Appendix II. 12 Q2-2

<Table 7> Comparison of Outright Sale of and Security Interest in Receivables (where the assignor is a company)

		Requirement for Perfection against Third Parties	
		Outright Sale of Receivables	Security interest in Receivables
R	US, Canada, New Zealand, Australia	Registration	
RN	Korea	Notice or Filing at the Financial Services Commission	Notice or Registration
	Japan	Notice or Registration	
N	France	Notice	No publicity
	Belgium	No publicity	
SR	UK	No publicity for equitable assignment	Registration in the Companies House
		Notice for statutory assignment	
	China	Notice	Registration in the Credit Reference Centre
C	Germany	No publicity	Notice
	Austria	No publicity	Notice or Recording in the company book of the assignor
	Netherlands	Notice, Notarisation of the deed or Registration with TRD <sup>313</sup>	

### 3-2-3. Priority of Security Interests vis-à-vis Third Parties (Question 2)

Section 3-2-3 analyses the perfection of security interests in receivables, comparing the difference between a security interest in receivables and an outright assignment.

In the US, Canada, New Zealand, Australia, Japan, Belgium and the Netherlands, the requirement for perfection of an assignment of a receivable is **the same** as the requirement for perfection of a security interest in a receivable.

<sup>313</sup> Tax Registration Department (*Belastingdienst/Registratie en successie*).

In contrast, in France, England, China, Germany and Austria, the requirement for perfection of a security interest in a receivable is **different** from the requirement for perfection of an assignment of a receivable. This difference means a potential assignee should check both the perfection of an assignment and the perfection of a security interest.

Under UCC Article 9 and the PPSAs of Canada, New Zealand and Australia and in England and China, registration is required for perfection of a security interest in a receivable. Most existing registration systems are for security interests in movables assets and receivables. Under UCC Article 9 of the US and PPSAs of Canada, New Zealand and Australia and in Japan, the registration system covers security interests in movable assets and receivables, and assignments of receivables. In the US, Canada, New Zealand and Australia, the scope of the registration system has been expanded from charges over personal property including receivables to include outright assignments of receivables. Japan has the registration system for assignments of movable assets and receivables, and assignments of receivables.

In contrast, in England, Korea and China, the registration system covers only security interests in movable assets and receivables, and includes only security interests in (and not assignments of) receivables.

In England, Companies Act provides for registration of company charges. Under the Companies Act 2006 (Amendment of Part 25) Regulations 2013, all charges (including charges over receivables) created by a company can be registered in the Registrar of Companies at Companies House. Under English law, registration of charges

created by a company does not guarantee priority.<sup>314</sup> Priority of competing charges is determined by the usual priority rules established at common law for the particular type of asset in question.<sup>315</sup> According to *Dearle v Hall*,<sup>316</sup> priority is determined by the order in which the debtor receives notice of the charge. If fixed charge F1 is registered, fixed charge F2 will take subject to F1 because of constructive notice.<sup>317</sup> *Dearle v Hall* does not apply to floating charges.

Korea has the registration system for security interests in movable assets and receivables. The Korean Security Registration Act provides for a registration system for security interests in movable assets and receivables. This Act applies to only security interests in receivables and it does not apply to outright assignments of receivables.

China adopted registration systems for security interests in specified types of movable assets and receivables separately. Under the Chinese Property Law, a pledge of an account receivable becomes effective upon its registration in the Credit Reference Centre.<sup>318</sup> It must be registered to be perfected against third parties. Notification to the debtor is not required for the creation of a pledge.<sup>319</sup> The registration system is only for pledges of receivables and not for outright assignment of receivables. Outright assignments do not have to be registered.

In Germany, notice to the debtor is required for a pledge of receivables, and not for the assignment of receivables. For this reason, transfer of title for security purposes

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<sup>314</sup> Roy Goode and Ewan McKendrick, *Goode on Commercial Law* (4<sup>th</sup> edn Penguin Books 2010) 705.

<sup>315</sup> *ibid.*

<sup>316</sup> (1828) 3 Russ 1.

<sup>317</sup> Second limb of *Dearle v Hall* (1828) 3 Russ 1.

<sup>318</sup> Chinese Property Law, arts 228 and 223(6).

<sup>319</sup> William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 644.

*(Sicherungsabtretung)* is used more frequently for security interests in receivables than the pledge of receivables to circumvent the notification requirement.<sup>320</sup> In France, notice to the debtor is not required for a pledge of receivables since 2006.<sup>321</sup> As such, the German and French Civil Codes have contrasting approaches with respect to requirements for assignments and pledges. Nevertheless, in both German law and French law, notice to the debtor is not required for security assignments of receivables.

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<sup>320</sup> See Appendix II. 12 Q2-2

<sup>321</sup> See Appendix II. 8 Q2-1

<Table 8> Perfection Requirements (Priority) for the Assignment of Receivables (a: assignment, security: security interest, sec: securitisation, cc: charges over company book debts)

Perfection against		Competing Assignee	Judgment Creditor	Insolvency Representative
USA		Filing of the financing statement		
Canada		Registration		
New Zealand		Registration	Equitable Assignment	
Australia		Registration		
Korea	a	Notice		
	sec <sup>322</sup>	Filing at Financial Services Commission		
	Security	Notice or Registration		
Japan		Notice or Registration		
France	a	Notice		
	d <sup>323</sup>	Delivery of a transfer deed ( <i>bordereau</i> )		
	Security	Conclusion of pledge contract		
Belgium		Notice	Conclusion of the contract	
England		Notice	Equitable Assignment	
	cc <sup>324</sup>	Registration		
China	assignment	Notice	not certain	
	security	Registration in the Credit Reference Centre		
Germany	assignment	Conclusion of the assignment contract		
	security	Notice		
Austria	assignment	Conclusion of the assignment contract		
	security	Notice or Recording on the company book of the assignor		
Netherlands		Notice or Notarisation of the deed or Registration with TRD <sup>325</sup>		

### 3-2-4. Perfection of Assignments against the Insolvency Representative (Question 3)

#### 3-2-4-1. Perfection

The most critical perfection is that against the insolvency representative of the assignor.<sup>326</sup> It depends on the insolvency law of the jurisdiction. With respect to outright

<sup>322</sup> Korean Asset-Backed Securitisation Act, Korean Mortgage-Backed Securitisation Act.

<sup>323</sup> *Dailly* Act, French Monetary and Financial Code.

<sup>324</sup> Charges over company book debts under the Companies Act 2006.

<sup>325</sup> Tax Registration Department (*Belastingdienst/Registratie en successie*).

assignments of receivables, in England, New Zealand, Belgium, China, Germany and Austria, an assignment of receivables is perfected against an insolvency representative of the assignor upon the conclusion of the assignment contract. In the US, Canada and Australia for assignments and security interests, filing or registration is required for perfection against the insolvency representative of the assignor.

Under English and New Zealand law, in order for an assignment to be perfected against the insolvency representative, perfection against third parties is not required.<sup>327</sup> In the other jurisdictions, the method of perfection against the insolvency representative is the same as the method of perfection against third parties.

### 3-2-4-2. Insolvency Representative $\subset$ Third Parties

In order for an assignment of a receivable to be perfected against an insolvency representative of the assignor, the assignment must be perfected against third parties prior to the insolvency adjudication in most jurisdictions other than England and New Zealand. If an assignment is perfected against third parties prior to the insolvency adjudication and an attachment, it is deemed perfected against the insolvency representative and a judgment creditor.

In France, Korea and Japan, upon the insolvency adjudication of the assignor, every right and every obligation of the assignor is considered transferred to the insolvency representative of the assignor. Therefore an insolvency representative of the

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<sup>326</sup> See Section 3-5-4

<sup>327</sup> See Section 3-2-3-2

assignor is regarded as similar to a kind of assignee. This is a critical difference between civil law jurisdictions and common law jurisdictions.<sup>328</sup> As a result, priority between an assignee and an insolvency representative is determined according to the order in which the debtor receives notice of the assignment or the insolvency of the assignor is adjudicated. For example, suppose that X assigned its receivables against D to Y, and X subsequently filed for bankruptcy. T was appointed as insolvency representative. The perfection rule determines priority between Y and T. The assignment of the receivables must be perfected against third parties before the insolvency adjudication in order for Y to win against T.

Under UCC Article 9, a financing statement must be filed for the assignment to be perfected against third parties including the insolvency representative.<sup>329</sup> If parties have not filed a financing statement, the assignee might lose his rights upon the assignor's insolvency. Likewise, under the PPSAs of Canada and Australia, the assignment of receivables must be registered to be perfected against the insolvency representative.<sup>330</sup> If the assignment is not registered, the assignee might lose his rights upon the assignor's insolvency. This is a punishment for not having filed the financing statement. It is a policy decision.

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<sup>328</sup> Upon attachment, the attached receivable is considered transferred to a judgment creditor. So, a judgment creditor is also regarded as a kind of assignee. As a result, priority between an assignee and a judgment creditor is determined according to the order in which the debtor receives a notice of the assignment or an attachment notice.

<sup>329</sup> See Appendix II. 2 Q1,2

<sup>330</sup> See Appendix II. 3 Q1,2 and 3-3-5 Q1,2

In the jurisdictions where publicity is not required such as Germany and Belgium, an assignee can assert the assignment of receivables against the insolvency representative if the assignment contract is concluded before the insolvency adjudication.<sup>331</sup>

### 3-2-4-3. Insolvency Representative ≠ Third Parties

Under English law, notice of the assignment to the debtor is not required for perfection against an insolvency representative and a judgment creditor. Perfection against third parties differs from perfection against the insolvency representative. Perfection against third parties is not required for an equitable assignment to be perfected against an insolvency representative. Unless it is a security assignment that must be registered, an assignee can assert an equitable assignment against the insolvency representative even before the debtor has been notified of the assignment.

Under English law, an insolvency representative<sup>332</sup> is not a third party. An insolvency representative must fulfil every obligation that the insolvent assignor should have fulfilled. The assignment contract is valid between the assignor and the assignee regardless of whether notice of the assignment is given to the debtor. Before notice of the assignment is given to the debtor, the assignor must collect the debt from the debtor and give the money to the assignee. Therefore an insolvency representative is also obliged to collect the debt from the debtor for the account of the assignee. The receivables assigned to the assignee are separated from the insolvency assets of the

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<sup>331</sup> See Appendix II. 12 Q1-1 and 3-3-9 Q1

<sup>332</sup> Alternative titles for this position are an insolvency administrator or a liquidator in common law jurisdictions.

assignor. The assignor or the insolvency representative holds the proceeds on trust for the assignee. An equitable assignee as well as a statutory assignee prevails against the insolvency representative of an assignor, and the receivables assigned to an assignee are not included in the assignor's insolvency assets.<sup>333</sup>

For this reason notice of the assignment is not normally given to the debtors of the receivables initially, even though England does not have a registration system for the outright assignment of receivables. An equitable assignment is still perfected against the insolvency representative without notice of the assignment to the debtor. In addition, the assignor generally wishes to maintain its relationship with its customers (debtors of receivables) and continue to collect the receivables. In the case of the assignor's insolvency or reneging on the debt, the assignee himself could give notice of the assignment to the debtors. An assignee factor may give notice of the assignment to the debtors if and when necessary.

New Zealand has a registration system under the New Zealand PPSA, which covers both security interests in and assignments of receivables. Therefore an assignment of a receivable is perfected against third parties upon registration in the registry. However, New Zealand does not have provisions that declare unregistered interests to be void against the insolvency representative or a company liquidator.<sup>334</sup> Thus, an unperfected security interest is still effective against the debtor (security provider) and its

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<sup>333</sup> See Appendix II. 10 Q1-1

<sup>334</sup> Roger Fenton, *Garrow & Fenton's Law of Personal Property in New Zealand: Volume 2 Personal Property Securities* (7th edn, LexisNexis 2010) 49 [2.2.18].

insolvency representative as an equitable security interest.<sup>335</sup> This is different from the PPSAs of Canada and Australia.

### **3-2-5. Perfection of Security Interests against the Insolvency Representative (Question 4)**

In order for a security interest in a receivable to be perfected against an insolvency representative of the security provider, it must be perfected against third parties by registration or notice to the debtor or by creation of the security interest prior to the insolvency adjudication in most jurisdictions other than New Zealand.

Under registration systems such as UCC Article 9 and the PPSAs of Canada and Australia, the perfection method of a security interest in receivables is the same as the perfection method of an assignment of receivables. Both of them are registration.

In England, charges created by a company are required to be registered in the Company Charges Registry for perfection against the insolvency representative of the chargor.<sup>336</sup> A security interest in receivables must be registered to be perfected against the insolvency representative.

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<sup>335</sup> See Australian Attorney-General's Department, *Personal Property Securities Discussion Paper 2 - Extinguishment, Priorities, Conflict of Laws, Enforcement, Insolvency* (March 2007) 85 [342]. <[http://www.ag.gov.au/www/agd/agd.nsf/Page/PersonalPropertySecurityReform\\_PPSTDownloads#papers](http://www.ag.gov.au/www/agd/agd.nsf/Page/PersonalPropertySecurityReform_PPSTDownloads#papers)> accessed on 10 January 2011.

<sup>336</sup> See Appendix II. 10 Q2. In addition, a general assignment of book debts by a person must be registered under the Bills of Sale Act 1878 to be perfected in the insolvency of the assignor. Insolvency Act 1986, s 344

In New Zealand, a security interest in a receivable is perfected against third parties upon registration in the PPS Register. Nevertheless, unregistered interests are perfected against the insolvency representative.<sup>337</sup>

### **3-2-6. Priority between Assignments & Security Interests (Question 5)**

In the US, Canada, New Zealand, Australia, Japan, England, Belgium and the Netherlands, the same requirements apply to both determining priority of assignments of receivables and determining priority of security interests in receivables.

In the US, Canada, New Zealand, and Australia, priority of both assignments and security interests is determined by the order of filing or registration.

In Japan, priority of both assignments and security interests is determined by the order of notice or registration.<sup>338</sup>

Under English law, priority of both assignments and security interests is determined by the *Dearle v Hall* rule. Thus, priority is determined by the order of notification to the debtor of the receivable. In addition, registration of charges over company book debts in the Registrar of Companies influences constructive knowledge of the second assignee about the first assignment. So, if the first assignment is registered, the second assignee does not have priority even though the second assignee gave notice of the second assignment to the debtor first.<sup>339</sup>

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<sup>337</sup> Roger Fenton, *Garrow & Fenton's Law of Personal Property in New Zealand: Volume 2 Personal Property Securities* (7th edn, LexisNexis 2010) 49 [2.2.18].

<sup>338</sup> See Appendix II. 7 Q1,2,3,4

<sup>339</sup> *ibid.*

In Belgium, even though the notification requirement for perfection against third parties has been abolished, priority is determined by the order in which the debtor of the receivable receives notice with respect to both assignments and security interests.<sup>340</sup>

In the Netherlands, priority is determined by the order of notarisation of the contract, registration in the Tax Registration Department (*Belastingdienst/Registratie en successie*) or notification to the debtor of the receivable with respect to both assignments and security interests.<sup>341</sup>

In the other jurisdiction, priority of assignments is different from priority of security interests. For example, under the French Civil Code, for an outright assignment of a receivable notification is required, but for a pledge of a receivable notification is not required. It is the opposite under the German Civil Code, where for an outright assignment of a receivable notification is not required, but for a pledge of a receivable notification is required. In these jurisdictions, to determine priority between assignments of and security interests in a receivable, both perfection of assignments and perfection of security interests must be compared.

In Korea, priority of assignments is determined by the order of notice or registration under the Korean ABS Act or MBS Company Act,<sup>342</sup> and priority of security interests is determined by the order of notice or registration under the Korean Security Registration Act.<sup>343</sup>

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<sup>340</sup> See Appendix II. 9 Q3,4,5

<sup>341</sup> See Appendix II. 14 Q3,4,5

<sup>342</sup> See Appendix II. 6 Q1,3

<sup>343</sup> See Appendix II. 6 Q2,4

### 3-2-7. Potential Assignee's Check Points (Question 6)

When a potential assignee purchases a receivable, there must be an investigation to determine whether there was any prior assignment of the receivable and whether there was any prior security interest in the receivable. Question 6 asks what an intending assignee should investigate and check before concluding the assignment or security contract in order to secure priority over any prior assignment of or security interest in the receivable.

<Table 9> below shows the answers to this question. This table combines the information centre for perfection of an outright assignment of receivables and the information centre for perfection of a security interest in receivables. In most cases, publicity is required for perfection, but there are exceptions where perfection is not published.<sup>344</sup> Unpublished perfection produces hidden priority, which causes uncertainty in transactions with receivables. Still, it is the best course for a potential assignee to check all of the published perfections.

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<sup>344</sup> For example, registration in the Tax Registration Department (*Belastingdienst/Registratie en successie*) in the Netherlands, conclusion of a contract in Germany, delivery of a transfer deed (*bordereau*) in France

<Table 9> Potential Assignee's Check Points for Prior Assignments and Security Interests (Answers to Q6)

	Country	Potential Assignee's Check Points	Unpublished Perfection
R	US	UCC Registry	
	Canada	PPS Register	
	New Zealand	PPS Register	
	Australia	PPS Register	
RN	Korea	security Registry Financial Services Commission account Debtors	
	Japan	assignment Registry account Debtors	
N	France	account Debtors	Delivery of a transfer deed ( <i>bordereau</i> ) Conclusion of pledge Contract
	Belgium	account Debtors <sup>345</sup>	Conclusion of the Contract
SR	England	account Debtors	
		c <sup>346</sup> Company Charges Registry account Debtors	
	China	Credit Reference Centre	
C	Germany	account Debtors	Conclusion of assignment Contract
	Austria	account Debtors	Conclusion of assignment Contract
	Netherlands	account Debtors	Notarisation of a deed, Registration with TRD <sup>347</sup>

<sup>345</sup> Assignments and pledges of receivables are perfected by conclusion of the contract, but priority is determined by the order of notice to the account debtor.

<sup>346</sup> Charges over company's book debts.

<sup>347</sup> Tax Registration Department (*Belastingdienst/Registratie en successie*)

### 3-3. CLASSIFICATION OF JURISDICTIONS

#### 3-3-1. Classification

<Table 10> Classification of Jurisdictions

Group		The assignor or security provider is a company (legal person).		
		Perfection		Check Point
		What should an assignee (or secured creditor) do to achieve third party effectiveness and priority over any other assignees or secured creditors?		Where should a potential assignee check before concluding the assignment contract (or the security contract) in order to secure his priority over any prior assignee of or secured creditor in the receivable?
		assignment	security interest	
R	USA, Canada, New Zealand, Australia	Registration	Registration	Registry
RN	Korea, Japan	Registration or Notice	Registration or Notice	Registry & account Debtor
N	France ('bordereau')	Notice to the debtor	Conclusion of the Contract	account Debtor
	Belgium		Notice to the debtor	
SR	UK, China	Notice to the debtor	Registration	Registry & account Debtor
C	Germany	Conclusion of the Contract	Notice to the debtor	account Debtor
	Austria (recording in the book of the assignor company)	Conclusion of the Contract	Recording in the book of the pledgor company	
	Netherlands	Registration with TRD	Registration with TRD	

This thesis categorises jurisdictions into five groups according to the perfection method of assignments of and security interests in receivables where the assignor is a

legal person and according to the points that a potential assignee should check before concluding the assignment contract in order to ensure that there are no prior assignees or secured creditors of the receivable.

In the jurisdictions of Groups R and RN, a financier may perfect an assignment of receivables by registering them. The difference between Group R and Group RN is that in the jurisdictions of Group R, registration is the only method to perfect the assignment of receivables. In contrast, in the jurisdictions of Group RN, both registration and notice of the assignment to the debtor of the receivable are available methods to perfect the assignment of receivables. Therefore to be certain that there is no prior assignment of or security interest in the receivable, a potential assignee should both check the registry and ask the debtor of the receivable whether it received notice of a prior assignment of or security interest in the receivable.

In the jurisdictions of Groups N and SR, a financier may perfect an assignment of receivables by giving notice of the assignment to the debtors of the receivables. The difference between Group N and Group SR is that in the jurisdictions of Group N, there is no registration system for assignments or security interests of movable assets or receivables. In contrast, in the jurisdiction of Group SR, there is a security rights registration system and security interests in the receivable are registered with the registry. Therefore to ensure that there is no prior assignment of or security interest in the receivable, a potential assignee should both check the registry and ask the debtor of the receivable whether it received notice of a prior assignment of or security interest in the receivable.

In the jurisdiction of Group C, a financier may perfect an assignment of receivables by the conclusion of the assignment contract. However, due to German law regarding pledges of receivables, notice of the pledge to the debtor of the receivable is required. A potential assignee should ask the debtor of the receivable whether the debtor received notice of a prior pledge of the receivable to ensure that there is no other prior pledge of the receivable. Austria law with respect to the assignment of receivable is the same as German law. In addition, Austria has the recording system of pledges in the book of the pledgor company. Under Dutch law, there are disclosed and undisclosed assignments of receivables and pledges of receivables. For a disclosed assignment or pledge of a receivable, notice of the assignment or pledge to the debtor of the receivable is required. Therefore a potential assignee should ask the debtor of the receivable whether it received notice of a prior assignment or pledge of the receivable to ensure that there is not any prior disclosed assignment or pledge of the receivable.

### **3-3-2. Information Centre**

One question to think about is which party should be the information centre where third parties may obtain information about a particular receivable. In the jurisdictions where publicity is required, a potential assignee may seek the status of a receivable through a neutral third party (the registry, an account debtor, etc.) other than the direct counterparty to the contract. Publicity evidences the existence of the assignment of or security interest in receivables through a neutral third party's confirmation.

A **registry** can be a neutral third party to confirm the assignment of or security interest in receivables.<sup>348</sup> A neutral third party serves as an information centre for the public. In the jurisdictions of Groups R and RN, where the assignment of receivables needs to be registered or filed to be perfected against third parties, the law designates the registry as an information centre for security interests. For example, in the US, filing is required for perfection of the assignment of receivables, and therefore a third party can check the status of a receivable by referring to the filing registry.

A **debtor** of a receivable can also be a neutral third party to confirm the assignment or security interest. It is because the parties to a contract for the assignment of a receivable are the assignor and the assignee, and thus a debtor of a receivable is not a direct party to an assignment contract. In the jurisdictions of Groups RN, N and SR, where notice of the assignment to a debtor is required for perfection of an assignment of receivables against third parties, the law intends for a debtor of a receivable to be an information centre so that anyone may seek the status of a receivable from the debtor. A potential assignee may inquire as to the status of a receivable by asking the debtor of the receivable, who must have been notified if there was any prior assignment of the receivable. In these jurisdictions, priority is determined by the order in which a debtor receives notice of the assignment.

In the jurisdictions of Group C, where publicity is not required, for example, in Germany, an assignment of receivables does not have to be confirmed by a third party

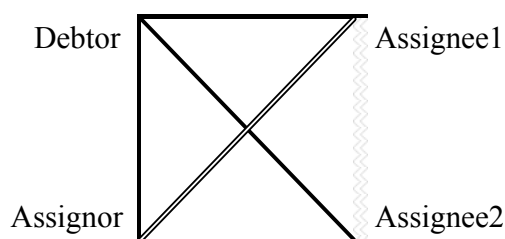
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<sup>348</sup> ‘Registry’ refers to the institution which fulfils the registration function. ‘Register’ refers to the physical file or database that contains all the information that has been registered, and ‘registrar’ refers to the person responsible for operating the registry (including the agent or the representative of the registrar with whom a user has contact). See EBRD, *Publicity of Security interests - Guiding Principles for the Development of a Charges Registry* (2004) 4, fn 10.  
<<http://www.oas.org/dil/ebd-publicity.pdf>> accessed 20 October 2011.

outside the parties to the contract. Priority among claimants is determined by the order of the conclusion of the assignment contracts, rather than depending on publicity. Therefore a potential assignee is not able to check the status of a receivable other than by asking the assignor. In these jurisdictions, investors have to trust and rely on the direct counterparty (assignor) in the contract. Thus, an **assignor** can function as an information centre.

### 3-4. CHOICE OF LAW DIFFICULTIES

#### 3-4-1. Governing Law



The assignment of receivables is a triangular relationship: between the assignor and the assignee; between the assignor and the debtor; and between the assignee and the debtor. In the assignment of receivables, each relationship between different parties is governed by different choice-of-law rules.

##### 3-4-1-1. Assignor v Assignee

The relationship between the assignor and the assignee is governed by the governing law of the assignment contract. For example, formality of the contract, rights and obligations of the parties and the effect of an assignment of future receivables are governed by the governing law of the assignment contract. Article 14(1) of the Rome I Regulation<sup>349</sup> stipulates the same rule.

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<sup>349</sup> Regulation (EC) No 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I) [2008] OJ L 177/6

If the receivable has been collected by the assignor, the assignor has the obligation to transfer the proceeds to the assignee. The assignee's right on the proceeds is governed by the governing law of the assignment contract.<sup>350</sup> If the assignee claims for the proceeds on the basis of unjust enrichment, Article 10 of the Rome II Regulation<sup>351</sup> will apply. In any case, the result is the same that it is governed by the governing law of the assignment contract.<sup>352</sup>

### 3-4-1-2. Assignor v Debtor, Assignee v Debtor

The relationship between the assignor and the debtor is governed by the governing law of the contract generating the receivable between the assignor and the debtor. The relationship between the assignee and the debtor is also governed by the governing law of the contract generating the receivable.<sup>353</sup> For example, assignability of the receivable, validity of assigned obligation, the effect of an anti-assignment clause vis-à-vis the debtor,<sup>354</sup> discharge of the receivable are governed by the law of the obligation of the debtor.

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<sup>350</sup> Rome I Regulation, art 14(1) The Rome I Regulation applies to contractual obligations. However, Recital 38 of the Rome I Regulation stipulates that Article 14(1) also applies to the property aspects of an assignment as between assignor and assignee.

<sup>351</sup> Regulation (EC) No 864/2007 of the European Parliament and of the Council of 11 July 2007 on the law applicable to non-contractual obligations (Rome II) [2007] OJ L 199/40. The Rome II Regulation applies to non-contractual obligations.

<sup>352</sup> Rome II Regulation, art 10(1)

<sup>353</sup> Rome I Registration, art 14(2)

<sup>354</sup> However, where the assignment is invalid due to an anti-assignment clause, the remedy of the assignee to the assignor is governed by the governing law of the assignment contract.

### 3-4-1-3. Insolvency Representative v Assignee

In insolvency of the assignor, the relationship between the insolvency representative and the assignee is governed by the law of the state where the insolvent assignor is located.<sup>355</sup> It is because the insolvency proceeding is opened in the state where the assignor is located.

### 3-4-1-4. Attachment Creditor v Assignee

The relationship between the assignee and an attachment creditor of the assignor is not stipulated in the Rome Regulation.

In *Raiffeisen Zentralbank Osterreich AG v. Five Star General Trading LLC*,<sup>356</sup> where an insurance policy is assigned to an assignee under English law and later the insurance policy is attached by a creditor of the assignor in a court in France, the English Court of Appeal decided that since the insurance policy had been validly assigned to the assignee under English law before the attachment, the assignor was no longer the owner of the insurance policy and therefore the creditor of the assignor cannot attach the insurance policy.

It is thought that if the insurance policy were first attached and then assigned to the assignor, it might be an issue of priority and thus French law might be the governing law. Under both French and English private international laws, priority between competing assignees is governed by the law of the state in which the debtor is located.

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<sup>355</sup> Council regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings [2000] OJ L 160/1, arts 4(1) and 4(2)(m)

<sup>356</sup> [2000] EWCA Civ 68, [2001] QB 825 (CA)

### 3-4-1-5. Assignee1 v Assignee2

The relationship between competing assignees is not stipulated in the Rome Regulation. There are four choice-of-law rules: the law of the state in which the debtor is located ('Rule D'), the governing law of the assignment contract between the assignor and the assignee ('Rule C'), the governing law of the contract generating the receivable between the assignor and the debtor ('Rule R'), and the law of the state where the assignor is located ('Rule A').

The Rule C has serious disadvantage in the case where there are different assignees competing each other, because different assignment contracts may be governed by different governing laws. Each of these would have to be examined.

The Rules D and R have serious disadvantage in receivables financing which contains various receivables, since there would be various account debtors of receivables and different receivable contracts governed by different governing laws. Each of these would have to be investigated.

The Rule A is desirable because there is only one single assignor in the case of competing assignees and in receivables financing. In addition, if the proceeds are already collected by the assignor, it is a matter of unjust enrichment between the assignor and the assignees. According the Rome II Regulation, the governing law may be the law of the

state where the unjust enrichment took place,<sup>357</sup> which is the law of the state in which the assignor is located.

### **3-4-2. Governing Law for Priority**

#### **3-4-2-1. Rome I Regulation**

Under Article 14(1) of the Rome I Regulation, which governs the choice of law in the European Union ('EU'), the relationship between an assignor and an assignee is governed by the law that applies to the contract between the assignor and assignee. Furthermore, Article 14(2) of the Rome I Regulation only stipulates that the law governing the assigned receivable between the assignor (original creditor) and the debtor determines the relationship between the assignee and the debtor, and thus is the governing law for the legal obligation between the assignee and the debtor.

The EC Commission's proposal for the Rome I Regulation<sup>358</sup> suggested that the law of the assignor's State should be the governing law for the priority among competing assignees or claimants of the assigned receivable.<sup>359</sup> However, unfortunately the EU

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<sup>357</sup> Rome II Regulation, art 10(3)

<sup>358</sup> Proposal for a Regulation of the European Parliament and the Council on the law applicable to contractual obligations (Rome I) (COM/2005/0650 final - COD 2005/0261), art 13(3).

<sup>359</sup> The benefit of this approach is that there would be only one governing law for all assignments. An assignee would only have to look at the laws of one jurisdiction for bulk assignments. In bulk international assignments of receivables for international receivables financing, though there might be multiple debtors, there will only be one assignor. Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 60-62. However, the law of the State of an assignor might not be enforceable in the State of the debtor. If a debtor does not pay the debt, the assignee must use the domestic court in the debtor's State to enforce payment. The court would decide priority and make judgments according to that State's law. Even if the governing law of the assignment contract is the law of the assignor's State, it is not clear that the applicable court in the debtor's State would apply the foreign law of the assignor's State.

Member States did not reach an agreement on this issue, and this proposal has not been accepted. As a result, there is no clear regulation on the governing law for third party effectiveness and priority in the Rome I Regulation at the moment.

### 3-4-2-2. Private International Law

At present, private international laws regarding priority vary from state to state. In international assignments of receivables, it is not always clear which state's law is the governing law for priority. According to the private international law of the jurisdiction, the governing law of priority can be considered, but there is still uncertainty depending on the court involved.

<Table 12> below displays the governing law of the relationship of each parties in the assignment of receivables according to private international laws of each jurisdiction. The governing law of priority is related to the information centre where a potential assignee can check whether there is any prior assignment or security interest.

<Table 11> Governing Law in the Assignment of Receivables

		Assignee v Assignor	Assignor v Debtor, Assignee v Debtor	Insolvency Representative v Assignee	Priority between competing assignees
R	USA	Rule C	Rule R	Rule A	Rule A <sup>360</sup>
	Canada				Rule A <sup>361</sup>
	New Zealand				Rule A <sup>362</sup>
	Australia				Rule A <sup>363</sup>
RN	Korea	Rule C	Rule R	Rule A	Rule R <sup>364</sup>
	Japan				Rule R <sup>365</sup>
N	France	Rule C	Rule R	Rule A	Rule D <sup>366</sup>
	Belgium				Rule A <sup>367</sup>
SR	England	Rule C	Rule R	Rule A	Rule D <sup>368</sup>
	China				not known <sup>369</sup>
C	Germany	Rule C	Rule R	Rule A	Rule R <sup>370</sup>
	Austria				Rule R
	Netherlands				Rule C <sup>371</sup>

In the jurisdictions of Group R, where priority is determined by the order of registration, the **registry** is an information centre. Registration of the assignment of

<sup>360</sup> US UCC, s 9-301(1)

<sup>361</sup> Ontario PPSA, s 7(1)(a)(i); Saskatchewan, s 7(2)(a)(i).

<sup>362</sup> New Zealand PPSA, s 30(a)

<sup>363</sup> Australian PPSA, ss 239(2) and 77(2).

<sup>364</sup> Korean Private International Act, art 34(1).

<sup>365</sup> Japanese Act on General Rules for Application of Laws (法の適用に関する通則法), art 23.

<sup>366</sup> CA Paris, 26 March 1986, D. 1986, 374 2°, note *Vasseur*.

<sup>367</sup> Belgian Private International Law, art 87(3).

<sup>368</sup> *Re Queensland Mercantile and Agency Co* [1892] 1 Ch 219 (CA). Roy Goode and Ewan McKendrick, *Goode on Commercial Law* (4<sup>th</sup> edn Penguin Books 2010) 1242, citing James Fawcett, Janeen Carruthers and Peter North, *Private International Law* (14<sup>th</sup> edn OUP 2008) 1234-35.

<sup>369</sup> The governing law of priority of competing assignees is not stipulated in the Law of the Application of Law for Foreign-related Civil Relations (涉外民事关系法律适用法).

<sup>370</sup> BGH 20 June 1990, BGHZ 111, 376, at 379; BGH 26 November 1990, NJW 1991, 1414. In Germany, Convention on the law applicable to contractual obligations opened for signature in Rome on 19 June 1980 [1980] OJ L 266/1 ('Rome Convention'), art 12(2) was applied.

<sup>371</sup> Property Law (Conflict of Laws) Act (*Wet Conflictenrecht Goederenrecht*) of 25 February 2008; HR 16 May 1997 Brandsma q.q./Hansa Chemie, NJ 1998, 585; JOR 1997,77. In the Netherlands, Rome Convention, art 12(1) was applied.

receivables must be done in the registry of the assignor's state, because the registry is indexed by assignor (or security provider). The assignor's state is where registrants register their assignments or security interests and searchers seek to discover them.<sup>372</sup> Thus, in these jurisdictions, the law of the assignor's state is the governing law for perfection and priority, but subject to the exceptions discussed in the next paragraph.

Under UCC Article 9, if an assignor is located in a foreign country that has a central filing system meeting the UCC's requirements, the law of the assignor's country is the governing law with respect to perfection and priority of security interests.<sup>373</sup> If an assignor is located in a foreign country, but that country does not have a central filing system meeting the UCC's requirements, the assignor is considered for the purposes of the UCC to be located in Washington D.C. for filing purposes.<sup>374</sup> If an assignor is incorporated in a foreign country but has a place of business or a chief executive office in the US, the filing should be made in the US at its place of business or chief executive office as applicable.<sup>375</sup>

Under the Australian PPSA as interpreted by Australian courts, if the law of the jurisdiction that governs the priority does not provide for public registration,<sup>376</sup> the assignment of receivables, perfected by registration under Australian PPSA before the

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<sup>372</sup> Lynn M Lopucki, *The Systems Approach to Law*, 82 *Cornell Law Review* 479 (1996-1997) 512; Maria Kieninger, 'General Principles on the Law Applicable to the Assignment of Receivables in Europe' in Jürgen Basedow, Harald Baum and Yuko Nishitani (eds), *Japanese and European Private International Law in Comparative Perspective* (Mohr Siebeck, 2008) 162.

<sup>373</sup> UCC, ss 9-307(b),(c) and 9-301(1).

<sup>374</sup> UCC, s 9-307(c).

<sup>375</sup> UCC, ss 9-307(b)(2) and (3). Elizabeth A Roff, New York (Ch 26) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 372.

<sup>376</sup> Australian PPSA, s 77(1).

other interest attaches to the receivables, has priority over the other assignment in proceedings.<sup>377</sup>

In the jurisdictions of Groups N and SR (except Belgium), where priority is determined by the order in which the debtor of the receivable receives notice of the assignment, the law of the account debtor's state is generally the governing law for priority. It is because the **debtor** of the receivable is an information centre. A potential assignee would be expected to ask the debtor regarding a prior assignment or security interest.<sup>378</sup> Moreover, the state where the debtor of the receivable is located is the place where the courts have control over the debtor and thus recovery of the debt.<sup>379</sup> Thus, potential assignees will naturally turn to the rules of the jurisdiction where the debtor is located.

Exceptionally, under the French Monetary and Financial Act, notice of assignment to the debtor is not required.<sup>380</sup> An assignment or pledge of receivables is perfected against third parties from the date indicated on the transfer deed (*bordereau*) when it is handed over, regardless of the law applicable to the receivables and the law of the debtor's country of residence.<sup>381</sup> The same principle applies to assignments to the

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<sup>377</sup> Australian PPSA, s 77(2).

<sup>378</sup> Roy Goode and Ewan McKendrick, *Goode on Commercial Law* (4<sup>th</sup> edn Penguin Books 2010) 1242, citing James Fawcett, Janeen Carruthers and Peter North, *Private International Law* (14<sup>th</sup> edn OUP 2008) 1234-35.

<sup>379</sup> *ibid.*

<sup>380</sup> See Appendix II. 8 Q1-2

<sup>381</sup> French Monetary and Financial Code, art L.313-27

*Fonds Communs de Créances* ('FCC')<sup>382</sup> in securitisation.<sup>383</sup> Priority is also determined by the order of the date indicated on the transfer deed (*bordereau*) when it is handed over.

In the jurisdictions of Group RN, where priority is determined by the order of registration or notice of the assignment to the debtor, both the **debtor** of the receivable and the **registry** are information centres that a potential assignee should check. In these jurisdictions, the governing law for perfection and priority is the law governing the receivable, which is determined according to the characteristics of the contact generating the receivable.

For example, if the receivables assigned are trade receivables, the law of the seller's state is the law governing the receivable because it is the most closely related state. The seller of the goods is the assignor (original creditor) of the receivables. As a result, the law of the assignor's state would be the governing law for priority of the assignment of trade receivables. This is suitable because in trade receivables, the parties would opt to register the assignment rather than give notice to all of the small account debtors. For trade receivables, there are usually a number of small account debtors and it is very costly and time-consuming to give notice of the assignment to all of the account receivables.

In the jurisdictions of Group C, where neither notice nor registration is required for perfection, the **assignor** is an information centre. In these jurisdictions, e.g. if the

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<sup>382</sup> The French Monetary and Financial Code provides for the use of FCC, which can be either an incorporated entity (*société de titrisation*) or an unincorporated co-ownership between the holders of the participation interests in it (*fonds commun de titrisation*). The latter form does not have legal personality. James Leavy, France, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 142.

<sup>383</sup> See Appendix II. 8 Q1-3

receivables assigned are trade receivables, the governing law for perfection and priority is the law of the assignor's state because it is the law governing the receivable. In the Netherlands, parties may choose the governing law for priority.<sup>384</sup> If not, priority is determined by the governing law of the assignment contract.<sup>385</sup>

### **3-4-3. Perfection Methods & Check Points**

#### **3-4-3-1. What to do for Perfection in International Assignments**

The governing law for priority in international assignments of receivables would be determined mostly by Rule R, Rule A or Rule D. Although the law governing the receivable (Rule R) varies according to the characteristics of the receivable, it is either the law of the assignor's state or the law of the account debtor's state. As a result, the governing law would be either the law of the state of the assignor (Rule A) or the law of the account debtor's state (Rule D). Thus, it is the best strategy to perfect the assignment of receivables both under the law of the assignor's state and under the law of the account debtor's state. In practice, it has become the custom. <Table 12> below shows what an assignee should do in order to perfect an assignment of a receivable against third parties in international receivables financing where the assignor is a company under the current laws.

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<sup>384</sup> Rome Convention, art 3(1).

<sup>385</sup> Property Law (Conflict of Laws) Act (*Wet Conflictenrecht Goederenrecht*) of 25 February 2008; HR 16 May 1997 Brandsma q.q./Hansa Chemie, NJ 1998, 585; JOR 1997,77. In the Netherlands, Rome Convention, art 12(1) was applied.

<Table 12> What should an assignee do in order to perfect an assignment against third parties in international receivables financing where the assignor is a company? (Groups R, RN, N, SR and C refer to the classification of jurisdictions in Section 3-3.)

Debtor Assignor	Group R	Group RN	Group N	Group SR	Group C
Group R	Registration in R	Registration in R Registration in RN	Registration in R Notice to the debtor in N	Registration in R Notice to the debtor in N	Registration in R
Group RN	Registration in RN	Registration in RN or Notice to the debtor in RN	Registration in RN Notice to the debtor in N	Registration in RN Notice to the debtor in SR	Registration in RN
Group N	Registration in R Notice to the debtor in R	Notice to the debtor in RN	Notice to the debtor in N	Notice to the debtor in SR	Notice to the debtor in C
Group SR	Registration in R Notice to the debtor in R	Notice to the debtor in RN	Notice to the debtor in N	Notice to the debtor in SR	Notice to the debtor in C
Group C	Registration in R	Registration in RN or Notice to the debtor in RN	Notice to the debtor in N	Notice to the debtor in SR	Conclusion of the contract

The grey boxes in the <Table 12> above indicate international assignments of receivables where the assignor has to give notice of the assignment to the debtor of the receivable. If notice of the assignment to the debtor is required under either the law of the assignor's state or the law of the account debtor's state, the parties would give notice of the assignment to the debtor in order to be certain of priority. Currently, in many international assignments of receivables, notice of the assignment to the debtor is required. In block assignments of receivables and assignments of future receivables, giving notice to account debtors is too costly and time-consuming and impractical. This could be a barrier to free international assignments of receivables.

For example, if the assignor is an American company (Group R) and the debtor is a French company (Group N), it is safest to file the assignment in the US in accordance with the US law and give notice of the assignment to the French company in accordance with the French law. By doing so, the assignee will have priority regardless of whether US law or French law governs priority.

If the assignor is a French company (Group N), and the debtor is an American company (Group R), it would be safest to give notice of the assignment to the American company in accordance with the French law, and file the assignment in accordance with the US law. However, it is impossible to file the assignment in France because there is no filing system for the assignment of receivables. If priority is considered by a US court, since under UCC Article 9 the law of the assignor's state is the governing law for priority,<sup>386</sup> French law would be the applicable governing law for priority. As a result, priority will be determined by the order of notification of the assignment to the American company. By contrast, if priority is considered under French private international law, which stipulates that the law of the debtor's state is the governing law for priority,<sup>387</sup> US law is the governing law for priority. As a result, priority will be determined by the order of filing. Since France does not have a registration system for the assignment of receivables, the assignment would have to be registered in Washington D.C.<sup>388</sup> Thus, the parties might wish to both give notice of the assignment to the American company and file the assignment of receivables in the US.

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<sup>386</sup> UCC, ss 9-307(b),(c) and 9-301(1).

<sup>387</sup> CA Paris, 26 March 1986, D. 1986, 374 2°, note *Vasseur*.

<sup>388</sup> UCC, s 9-307(c) See Section 4-3-2-2

If the assignor is a German company (Group C) and the debtor is a Japanese company (Group RN), it is safest to register the assignment or give notice of the assignment to the Japanese company in accordance with the Japanese law. In Japanese law, there are two perfection methods: registration and notice of the assignment to the debtor. A foreign legal person can also register the assignment of receivables as an assignor under the Japanese Assignment Registration Act.<sup>389</sup> Thus, it is safest to register the assignment in Japan.

Under the Korean ABS Act, a foreign legal person may file securitisation plans including the assignment of receivables with the Financial Services Commission as an originator (assignor) even if the foreign legal person does not have an office in Korea.<sup>390</sup> Thus, if the assignor is a German company and the debtor is a Korean company and if the transaction is securitisation, it is safest to file the assignment and the securitisation plan in Korea in accordance with the Korean ABS Act. Furthermore, under the Korean Security Registration Act, a foreign legal person can also register security interests in receivables as a security provider or a secured creditor.<sup>391</sup>

As seen above, currently in many international assignments of receivables, notice of the assignment to debtors of the receivables is required, which hampers international assignments of receivables. Hence, the IRSAR that liberates financiers from the notification requirement could facilitate international assignments of receivables.

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<sup>389</sup> Japanese Assignment Registration Act, art 7(2)(iii).

<sup>390</sup> Korean ABS Act, art 3(1).

<sup>391</sup> Korean Security Registration Act, art 47(2)(iv); Korean Security Registration Rules, art 34.

### 3-4-3-2. Potential Assignee's Check Point

In order for a potential assignee to secure priority over other assignments of or security interests in a receivable, the potential assignee must ensure that there is no prior assignment of or security interest in the receivable. <Table 13> below indicates information centres that a potential assignee should check before concluding an assignment contract under the current law, i.e. without implementation of the proposed IRSAR Convention.

**<Table 13> Where should an intending assignee check before concluding an agreement for an assignment of a receivable or a security interest in a receivable in order to secure his priority over any prior assignment of or security interest in the receivable?**

Debtor Assignor	Group R	Group RN	Group N	Group SR	Group C
Group R	Registry in R	Registry in R Debtors in RN	Registry in R Debtors in N	Registry in R Debtors in SR	Registry in R Debtors in C
Group RN	Registry in RN	Registry in RN Debtors in RN	Registry in RN Debtors in N	Registry in RN Debtors in SR	Registry in RN Debtors in C
Group N	Debtors in R	Debtors in RN	Debtors in N	Debtors in SR	Debtors in C
Group SR	Registry in SR Debtors in R	Registry in SR Debtors in RN	Registry in SR Debtors in N	Registry in SR Debtors in SR	Registry in SR Debtors in C
Group C	Debtors in R	Debtors in RN	Debtors in N	Debtors in SR	Debtors in C

In most of the cases, the parties have to search both the registry of the assignor's state and ask the debtor whether it received notice of any prior assignment of or security interest in the receivable. In block assignments of receivables and assignments of future

receivables, enquiring of account debtors is too costly and time-consuming and impractical. Under the current laws, priority issues in international assignments of receivables are very complicated, unsettled, and often involve notification of the assignment to the debtor, which is often difficult or undesirable.

#### **3-4-4. Experience of the UN Receivables Convention**

The UN Receivables Convention proposes that the law of an assignor's State should be applied to international assignments of receivables.<sup>392</sup> However, the UN Receivables Convention, adopted in January 2002, has not yet entered into force.<sup>393</sup> It is said that European States hesitated to join the UN Receivables Convention because of the current uncertain situation whether the rule under the UN Receivables Convention might or might not be identical to, or at least compatible with, future European regulations.<sup>394</sup>

One of the reasons for the UN Receivables Convention's lack of success might be that priority issues are not adequately resolved by the choice-of-laws rule. The UN Receivables Convention attempts to resolve priority issues with the choice of law rule that the law of the assignor's State determines priority disputes for international assignments.<sup>395</sup>

As analysed in Section 3-4-2-2 above, the choice-of-laws rule for priority issues is affected by where the information centre is under the substantive law on determining

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<sup>392</sup> UN Receivables Convention, art 30(1)

<sup>393</sup> See Section 1-7-1

<sup>394</sup> Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 55.

<sup>395</sup> UN Receivables Convention, art 30(1).

priority between competing assignees, and the substantive laws on priority differ by jurisdictions.<sup>396</sup> Thus, States which have different substantive laws on priority would not agree on a unified choice-of-laws rule for priority issues. Even within Europe, it is challenging to unify domestic choice-of-laws rules for priority. It would be even more difficult to unify these rules worldwide. Thus, a unified substantive rule (rather than choice-of-laws rule) is needed to facilitate international receivables financing.

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<sup>396</sup> See Section 3-4-2-2

## **3-5. REGISTRATION IS THE SOLUTION**

### **3-5-1. Problems of Notification Requirement**

In the jurisdictions of Groups RN, N and SR, where notice of the assignment to the debtor is required for the assignment of receivables, notification has always hampered receivables financing.<sup>397</sup> As receivables financing developed, the problem of notification requirement became unbearable in these jurisdictions. Even though an assignee in a receivables financing does not usually intend to immediately collect the debt from the debtor, the assignor or the assignee has to give notice of the assignment to the debtor for perfection against third parties including the insolvency representative or a judgment creditor of the assignor.

However, as explained in the following two subsections, sending notifications to debtors in receivables financing is impractical, costly and time-consuming to give notice of the assignment to all debtors of bulk receivables. Moreover, it is impossible to give notice of the assignment to the debtors of future receivables. Because of this pressure, many jurisdictions have adopted registration systems. One registration can replace innumerable notifications.

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<sup>397</sup> Despite that, the assignee in a receivables financing does not usually intend to immediately collect the debt from the debtor, the assignee has to give notice of the assignment to the debtor for perfection against the insolvency representative or a judgment creditor of the assignor.

### 3-5-1-1. Facilitating Assignments of Future Receivables

To assist companies (especially small and mid-sized companies with insufficient collateral) in using their receivables as collateral, the ability to assign future receivables is important. Long-term receivables and future receivables are recommended for receivables financing. It takes a long time to liquidate long-term receivables and future receivables. Thus, using long-term receivables and future receivables for receivables financing would be helpful to companies.

A registration system for security interests in receivables facilitates the assignments of future receivables. Under traditional civil law, notification of the receivable to the debtor is required for the assignment of receivables. However, with respect to future receivables, the debtor of the receivable is not yet ascertainable, and therefore giving notice of the assignment to a debtor of a future receivable is impossible. A registration system would also enable the assignment of future receivables as well as floating charges, which include future receivables. It is useful in project financing where the debtor's future cash flow is important collateral.<sup>398</sup>

### 3-5-1-2. Facilitating Bulk Assignments of Receivables

A registration system for security interests in receivables facilitates bulk assignments of receivables. Many receivables financing transactions such as securitisation, factoring and block discounting consist of bulk assignments of receivables, which contain a great number of debtors of receivables and inevitably encounter

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<sup>398</sup> See Section 1-1

notification problems. A registration system could solve these notification problems. On the one hand, if there is a highly valued receivable, a potential assignee would not just check the registry and he would also directly contact the debtor of the receivable to enquire whether there is any prior security interest in or assignment of the receivable. For example, where company D owes bank X £10,000,000 and bank Y purchases the receivable from bank X, bank Y would give notice to company D to ensure the assignment of the receivable.

In the case where a bulk assignment of receivables consists of a number of small consumer receivables, a potential assignee of the receivables could not enquire after each debtor. Also, assignors usually would not want to give notice to the debtors of the receivables because assignors would not want to let the debtors know of the assignment. A registration system for the assignment of receivables allows a bulk assignment of receivables to be perfected without giving notice of the assignment to each of the consumer debtors.

### **3-5-2. Registration or No publicity**

In the jurisdictions of Groups RN, N and SR, there have been developments to resolve the problems of notification requirement towards two movements: either no-publicity or registration. Some states revised their civil codes or relevant laws to abolish the notification requirement, and some States enacted special laws for receivables financing adopting other methods to replace notice of the assignment to debtors. These

legislative efforts provide us references for establishing a unified international system in order to facilitate cross-border receivables financing.

For example, Belgium and the Netherlands revised their civil laws and abolished the notification requirement for the assignment of receivables and security interests in receivables. Belgium abolished the notification requirement in 1994,<sup>399</sup> and the Netherlands abolished it in 2004. Furthermore, the EU FCD disapplies any publicity requirement such as registration or notification for financial collateral arrangements of financial institutions.<sup>400</sup>

In comparison, France, Korea, Japan and China, where notice of the assignment to the debtor is required for priority, have enacted special laws for receivables financing and securitisations. Although the style of code and classification of rights were influenced by the German Civil Code (BGB), the Japanese Civil Code adopted the notification requirement from the French Civil Code for the assignment of receivables.<sup>401</sup> The Korean Civil Code follows the Japanese Civil Code. If the Japanese Civil Code had adopted the no-publicity approach for the assignment of receivables and followed the German ‘time of creation’ doctrine,<sup>402</sup> the registration system would not have been needed in Japan.

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<sup>399</sup> Still, in Belgium, priority is determined by the order of notification. See Appendix II. 9 Qs 3, 4, 5

<sup>400</sup> See Appendix II. 15-3

<sup>401</sup> According to French Civil Code, art 1690, either notification by an official letter (*signification* in French) delivered by a bailiff (*huissier*), or consent of the debtor by a notarised deed (*acte authentique*) with a certain fixed date, is required for an assignment to be effective against third parties. See Appendix II. 8 Q1-1. However, under the Japanese Civil Code, only a certified document with a fixed date stamp is required for notice of the assignment to a debtor or consent of a debtor. See Appendix II. 7 Q1,2,3,4-1

<sup>402</sup> Under the German Civil Code, the assignee prior in time of conclusion of the assignment contract has priority regardless of notification, and notice of the assignment to the debtor is not required for the assignment of receivables. See Appendix II. 12 Q1-1

There are three special methods that replace notice of the assignment to the debtor in particular legislation: (1) delivery of a transfer deed, (2) public notice on newspapers and (3) filing or registration. France adopted the method of delivering a transfer deed. By delivering such a transfer deed, which is called ‘*bordereau*’, an assignment of a receivable is perfected against third parties as well as the debtor of the receivable.<sup>403</sup> This solution under the French Monetary and Financial Code is in effect a no-publicity approach.<sup>404</sup>

Special legislative reformation tends to be influenced by the legal systems of neighbouring states. These influences are either towards the time-of-creation doctrine of Germany<sup>405</sup> or the registration system of the US. Japan is close to the US, and thus adopted a UCC Article 9-style registration system. In Japan, special legislative actions were initially taken to facilitate securitisation for the purpose of disposing of non-performing loans<sup>406</sup> and then later extended the scope of registration from securitisation assets to other receivables.<sup>407</sup> Korea established a registration system referring to UCC Article 9 and the Japanese system.<sup>408</sup> China adopted the method of public notice in

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<sup>403</sup> See Appendix II. 8 Q1-2

<sup>404</sup> See Section 3-2-2-4-2

<sup>405</sup> The method of a transfer deed in France is rather similar to the time-of-creation doctrine.

<sup>406</sup> Non-performing loans are loans on which debtors have failed to make contractual payments for a predetermined time. Usually, loans become non-performing after being in default for 3 months, but this can depend on the contract terms. Chae-Jin Lee, ‘Study on Development and Evolving Process of Securitisation Laws in Korea’, (2005.06) Vol.18, No.2, *Commercial Case Study (Sang Sa Pan Rye YeonGu)* 208-9

<sup>407</sup> See Section 2-4-4-3-2

<sup>408</sup> See Section 2-4-4-4

newspapers.<sup>409</sup> Public notice in newspapers is a kind of publicity. However, this publicity method is inconvenient for potential assignees to search.

This thesis argues that for a worldwide unified system, registration is more appropriate than no publicity. A no-publicity solution might be workable between tightly interconnected financial institutions such as under the EU Financial Collateral Arrangement Directive. However, for a global financial market, a registration system could provide certainty of transactions. In addition, there is a practical reason that it would be difficult for jurisdictions familiar with publicity such as registration or notice under their current laws to adopt the concept of no-publicity.

### **3-5-3. Problems with No Publicity of Assignments**

In the jurisdictions of Group C, there is no *ex ante* measure for a potential assignee to investigate whether a specific receivable belongs to an assignor except by asking such assignor. This begs the question as to the acceptability of a system where there is no publicity requirement for the assignment of receivables.

Nonetheless, the assignment system works very well in Germany without a notification requirement.<sup>410</sup> Companies do not want the assignment information revealed to debtors or the public at large. The system seems fine in a limited, inter-connected and stable society like Germany where financier communities develop methods of

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<sup>409</sup> See Appendix II. 4 Q1-2 .

<sup>410</sup> Interview with Ulrich Drobniig, Professor, Max Planck Institute for Comparative and International Private Law (Hamburg, Germany, 20 October 2010)

communication that reliably distribute financial information of its members, so that a fraudulent non-possessory security interests are difficult to hide.

Although neither notice to the debtor nor registration is required for the outright transfer of receivables, there is no public debate about clandestine assignments of receivables and no apparent lobbying or push for a change in this regard in Germany.<sup>411</sup> Rakob found that the German banking and factoring industry appears satisfied with the current situation and does not perceive the risks of fraudulent assignments or of mistaken double assignments as serious.<sup>412</sup>

However, it seems that there could be problems for two reasons. First, there is no way for a potential assignee to check whether there is a prior assignment of or security interest in the receivable that might be purchased or taken as collateral. A potential assignee's only option is to trust the assignor. There may be warranties or conditions in the assignment contract. Still, if there were a prior assignment, the subsequent assignee would not have any rights in the receivable, just a claim for damages. This is unsecure and dangerous on insolvency of the assignor. Furthermore, if a subsequent assignee gives notice to the debtor of the receivable, and the debtor pays the subsequent assignee, the prior assignee can theoretically claim against the subsequent assignee for unjust enrichment. However, it is a personal claim and therefore unsecured if the subsequent assignee became insolvent or otherwise unavailable.

Second, without any third party involvement, it is easy for the assignor and the assignee to falsify the date of the assignment contract and to hide such conspiracy.

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<sup>411</sup> Julia Klauer Rakob, Germany, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 112-113

<sup>412</sup> *ibid* 113

Where X assigned his receivable to Y1 and then Y2 (X is an assignor; Y1 and Y2 are assignees; and the assignment to Y1 is prior in time to the assignment to Y2). X might have incentive to backdate of the assignment contract with Y2 prior to the assignment contract with Y1 if X favours Y2 over Y1. If X actually did so, X will be charged with **fraud** if X signed the documents confirming there is no prior assignment when X assigns his receivable to Y1 and to Y2.

If X backdates the assignment contract with Y2 to a time prior to the date of the assignment contract with Y1, and as there is no third party involvement, the backdating is not revealed, it would appear that X assigned the receivable to Y2 before signing the document confirming to Y1 that there was no prior assignment, and therefore Y2 would have priority over Y1. This would constitute fraud against Y1.

If the backdating is revealed, Y1 has priority over Y2, and it would be fraud against Y2 because Y2 will lose his right to the receivable. In either case, the assignor would be guilty of fraud.

### **3-5-4. Is Registration Necessary?**

Registration informs the public of assignments of and security interests in receivables, and may be used as evidence in resolving disputes such as priority disputes. However, some legal practitioners argue that registration is not necessary for receivables financing. They argue that receivables transactions do not have to be publicised, and that additional evidence of receivables transactions besides the relevant contract is not needed.

Priority between competing assignees is only relevant if an assignor sells the same receivable twice, grants competing security interests in a receivable, or sells a receivable that has already been pledged as security. A judgment creditor of an assignor may be treated in the same way as an assignee. If an assignee has not completed the registration requirement before an attachment is perfected, the assignment is not perfected against the judgment creditor.

Practitioners argue that such concerns are out-of-date because accidental double assignments are not prevalent in highly sophisticated financial markets where trading is managed with computer accounting systems. If a financial institution erroneously sold the same receivable twice, or sold the receivable that had been pledged as security, it would be quickly discovered and few would do business with such a suspicious financial institution in the future. Once a financial institution loses its goodwill, it cannot continue business. If a financial institution commits a wrong, it will be sufficiently punished and burdened with severe repercussions.

The counter-argument is that registration is necessary because a company running into insolvency might sell the same receivable twice or secretly sell the receivable that

has been provided as security, or might grant a security interest in the receivable that has already been assigned, before filing for insolvency. A person or a company on the brink of insolvency, that has nothing to lose except possible criminal punishment, might conduct such fraudulent behaviour intentionally. Small trading companies might well make a mistake or engage in fraudulent behaviour when they assign their receivables to a bank or receivables financier, and then become bankrupt. As long as the assignor is solvent, the second assignee who does not have priority can recover the full amount of the receivable plus damages from the assignor although the second assignee cannot claim directly against the debtor. But if the assignor becomes insolvent, the second assignee cannot obtain proper restitution.

Still, legal practitioners argue that those who know the financial situation of a potential assignor would not buy receivables from that company if it were on the verge of insolvency. As such, the law does not have to require registration for the assignment of receivables, nor does it have to provide notice or registration for priority purposes. In such situations, an intending assignee or secured creditor should properly investigate the assignor's or security provider's financial situation to prevent double assignments. If there was no registration requirement, financiers would have to pay greater attention to the financial condition and creditability of the assignor or security provider.

Such duty of caution is already present in the insolvency laws of many jurisdictions. For the purpose of preventing fraudulent transactions relating to company assets, insolvency laws of many jurisdictions provide that the insolvency representative may apply to the court to revoke the insolvent assignor's transactions made within a certain period which is called the suspect period. The suspect period is calculated

retrospectively from the date of the assignor's insolvency,<sup>413</sup> or from the date of application for the insolvency proceedings.<sup>414</sup>

Accordingly, the insolvency representative may avoid the assignment of receivables made within the suspect period if the consideration received for the receivables assigned is unreasonable. If an assignee purchased some receivables with an unreasonably cheap price, the assignment might be revoked. There is a high probability that the second assignment could be avoided by the insolvency representative if within the suspect period. Such avoidance provisions would serve to protect creditors, or potential creditors, of the company that has assigned its receivables. For this reason, a potential assignee should have to pay greater attention to the probability for the assignor to become bankrupt. However, the difficulty and costs of enforcement by the insolvency representative may mean that in fact the possibility of avoidance is not a great disincentive.<sup>415</sup> Thus, registration is necessary to prevent fraudulent assignments.

Finally, since fraudulent double assignments rarely occur in sophisticated financial systems, the most important purpose of registration in practice is perfection against the insolvency representative or a judgment creditor of an assignor. It is necessary to establish a system verifying the date of the assignment that will be compared with the date of bankruptcy adjudication or attachment notice. Without such a system, where there

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<sup>413</sup> For example, UK Insolvency Act 1986, s 238; Chinese Insolvency Law, art 31(2)

<sup>414</sup> For example, German Insolvency Statute (*Insolvenzordnung*), s 131 Under the German Insolvency Statute, the suspect period is three months, but with some exceptions.

<sup>415</sup> Rebecca Parry and others, *Transaction Avoidance in Insolvencies* (2nd edn, OUP, 2011) Parry shows that the avoidance provision should not deter people from dealing with struggling companies and rescue efforts which would otherwise be viable.

is an assignment, the parties might be tempted to backdate another assignment contract to have priority.

### **3-6. CONCLUSION OF PART 3**

Today, legal systems around the world vary widely in how they deal with the assignment of receivables and security interests in receivables and choice of laws. This legal variety makes it difficult for financiers to conduct their international receivables financing business.

In this world where different laws on assignments of and security interests in receivables and private international laws in each jurisdiction are commingled, establishing an international registration system for assignments of and security interests in receivables is the best solution to facilitate international receivables financing.

Notification to the debtor is still required in many international assignments of receivables, which is a major obstacle to international receivables financing. Therefore the choice-of-laws approach proposed by the UN Receivables Convention could not solve the problem. A unified substantive rule for priority with an international registration system for the assignment of and security interest in receivables is required.

In receivable financing, it is impractical for financiers to ask the account debtors whether they received notice of any prior assignment or security interest before the assignment and to give notice of the assignment to account debtors after the assignment. One registration in the IRSAR can replace an unlimited number of notifications.

The IRSAR would pave the way of circumventing the notification requirement in some jurisdictions where notice of the assignment to the debtor is required for third party effectiveness. This function is essential to facilitate the assignment of future receivables and bulk assignments of receivables. In conclusion, registration is the best solution to facilitate international receivables financing.

## **PART 4. LIMITATION OF SCOPE OF THE IRSAR**

### **4-1. INTRODUCTION**

Let us first think about the most desirable international registration system to facilitate international receivables transactions. If there were one unified law which governs all assignments of receivables and all security interests in receivables in the world, enabling assignments or security interests to be secured, once they have been registered with a unified international registration system, receivables could be traded freely internationally without need for any further domestic perfection and without even paying heed to any domestic perfection rules.

In reality, each State has different national laws for the assignment of receivables and security interests in receivables. If the proposed IRSAR Convention would override those national laws with respect to priority and perfection requirements, and if every State would join the proposed IRSAR Convention, it would be the same as the most desirable status mentioned above.

However, the most desirable status is impracticable for the following reasons: First, practically speaking, it is expected that some States would not join the proposed IRSAR Convention due to various reasons. Thus the IRSAR would be applied to parties only in the Contracting States.

Second, the IRSAR has to solve the problem of language barriers. If the IRSAR were to override the perfection requirements of national law, every single assignment of receivables (both international and domestic) in the Contracting States would have to be registered with the IRSAR in order to secure its priority. If even purely domestic assignments and security interests would have to be registered in the IRSAR, the system should provide translation service since some people cannot read English. It would raise the cost and ultimately the registration fee. The more States would join the proposed IRSAR Convention, the higher is the cost for translation.

Third, the volume of IRSAR registration would become too large to manage at reasonable cost whilst keeping the registration fee at an affordable level.

This thesis does not reject a system overriding national requirements. However, this thesis emphasizes that if we would adopt a system overriding national requirements, the scope of application must be limited anyhow in order to solve these practical problems. Part 4 tries to find the best solution to limit the scope of application of the IRSAR while maintaining the merits of international receivables financing.

With respect to receivables, there are broadly two ways of using receivables for financing: one is an assignment of receivables and the other is creating security interests in receivables, which are exemplified by the following four types of receivables transactions: First, bank loans usually have particular terms or length of maturity. In contrast, depositors may withdraw their savings from a bank at any time. Thus, if all depositors suddenly withdraw their savings from a bank at once, the bank will run out of cash. To mitigate such liquidity risk, a bank may assign its loan receivables to other banks through inter-bank transactions and get influx of cash. In addition, in order to meet

the requirement of capital adequacy ratio under the Basel III, banks need to dispose of bad loans. Second, a company which does not have sufficient real estate or tangible assets to mortgage for a loan can create security interests in its account receivables and borrow money from banks. Third, a bank may borrow money from central banks with providing security interests in its loan receivables. Fourth, a company may assign its account receivables through factoring and a financial institution may assign its credit card receivables or lease receivables through securitisation in order to disperse the default risk. Part 4 tries to find the best solution to limit the scope of application of the IRSAR while facilitating these types of international receivables transactions. In Part 4, assignments of receivables and the granting of security interests in receivables are collectively referred to as assignments.

Chapter 4-2 compares three approaches to unify national laws on the assignment of and security interests in receivables around the world. Chapter 4-3 goes on to identify a workable model in terms of the relationship between the proposed IRSAR Convention and the different national laws, whether the former should prevail over the latter. The issue is whether IRSAR registration should be compulsory or optional.

Chapters 4-4 and 4-7 look at ways of restricting the scope of application of the proposed IRSAR Convention with the invention of the vehicle for the international convention. Chapter 4-8 proposes that the scope of registration should be limited to an assignment where both the assignor and the assignee (or the security provider and the secured creditor) are legal persons (companies). This is because of the identification issue. It also defines the interaction between the proposed IRSAR Convention and the Cape Town Convention.

## **4-2. THREE APPROACHES TO UNIFY THE LAWS**

A new regime to uniformly cover the world would be the next step to the continued development of international receivables financing. If so, the question becomes which system should be the model. There are three possible suggestions to achieve harmonisation of receivables financing regimes: (1) a compulsory registration system; (2) an optional registration system; and (3) a legislative guide encouraging each state to adopt a relatively unified registration system.

### **4-2-1. Compulsory Registration**

First, an example of a compulsory registration system is the International Registry of Mobile Assets,<sup>416</sup> established by the Cape Town Convention and its Aircraft Protocol. Once a state signs and ratifies the Cape Town Convention and the Aircraft Protocol, every security interest in the subject mobile equipment must be registered in order to have priority. Under this approach, a compulsory registration system prevails over domestic receivables financing regimes.

### **4-2-2. Optional Registration**

Second, an optional registration system is an alternative international registry that would be added to the existing domestic regimes and would allow parties to select it. It is

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<sup>416</sup> <<https://www.internationalregistry.aero/irWeb>> accessed 1 July 2011

similar to the proposed European security interest.<sup>417</sup> Realising that it is much more difficult to unify property laws and security laws than to unify contract laws in the EU, some scholars including Kieninger proposed a European security interest. A European security interest would be a new security interest perfected by registration in a European registry, which would be added onto the existing domestic security interests regimes. The idea is that a European security interest does not change the existing domestic security interests laws of the EU Member States for the time being. This approach is similar to the registration systems under the Korean Security Registration Act and under the Japanese Assignment Registration Act in that these special registration systems co-exist with the assignment of receivables regimes under civil laws.

#### **4-2-3. Providing Guides, Models**

Third, to make a legislative guide on receivables financing and encourage each state to establish a domestic registration system is also a recommendable way to harmonise receivables financing regimes around the world. The UNCITRAL Legislative Guide on Secured Transaction is a good example. There are other models such as ‘Publicity of Security Interests: Guiding Principles for the Development of a Charges Registry’ (2004) and ‘Publicity of Security Interests: Setting Standards’ (2005) of the

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<sup>417</sup> Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Tangibles* (Sellier 2007) 34. This suggestion was first made by Kreuzer, *Europäisches Mobiliarsicherungsrecht oder: Von den Grenzen des Internationalen Privatrechts*, in Stoffel/Volken (eds.), *Conflits et harmonisation: mélanges en l’honneur d’Alfred E. von Overbeck à l’occasion de son 65ème anniversaire* (1990) 613 et seq. Eva-Maria Kieninger, *Security interests in Movable Property* (CUP 2004) 665-672. The European Security interest could be introduced under a regulation issued pursuant to Article 308 of the EC Treaty, which stipulates, “If action by the Community should prove necessary to attain, in the course of the operation of the common market, one of the objectives of the Community, and this Treaty has not provided the necessary powers, the Council shall, acting unanimously on a proposal from the Commission and after consulting the European Parliament, take the appropriate measures.”

EBRD, ‘Guide to Movables Registries’ (2002) of the Asian Development Bank, Draft Common Frame of Reference (2010),<sup>418</sup> ‘Model Registry Regulations under the Model Inter-American Law on Secured Transactions’ (October 2009) of the Organization of American States and ‘Secured Transactions Systems and Collateral Registries’ (January 2010) of the International Finance Corporation (World Bank). These guides and model laws for registration systems are modelled on the financing statement filing under UCC Article 9 and registration under the PPSAs in Canada and New Zealand. They cover outright assignments of receivables, security assignments of receivables and security interests in receivables.

However, leaving countries to voluntarily revise national laws and establish national registration systems for receivables would take a long time to unify international registration systems to facilitate international receivables transactions.

### **4-3. RELATIONSHIP BETWEEN THE PROPOSED IRSAR CONVENTION AND NATIONAL LAWS**

#### **4-3-1. Compulsory or Optional**

Establishing an international registration system for the assignment and security interest of receivables is no easy task. Broadly speaking, two models of an international registration system for the assignment and security interest of receivables suggest

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<sup>418</sup> Section 3 of Chapter 3 (Effectiveness as Against Third Parties) (Registration) of Book IX (Proprietary Security in Movable Assets)

themselves. The first model is an international registration system which overrides the perfection requirements of national law, which would result in compulsory registration with the international system.<sup>419</sup> This model would involve issues of practicality that may inhibit its adoption by States around the world. An international registration system designed to override the perfection requirements of national law might probably result in states not adopting the international Convention.

The second model is an international registration system equivalent to the perfection requirements of national law, which would result in optional registration with the international system.<sup>420</sup> This model would, however, undermine the utility of the registration system. An international registration system that did not override, but was equivalent with the perfection requirements of national law would be less useful to registrants and searchers.

In its search for a solution, based on the first model, this thesis proposes to confine the sphere of application using the proposed ‘vehicle to the international registration system’.

#### **4-3-2. Problems with Optional Registration System**

Establishing an international registration system that does not override the perfection requirements of national law might be a solution. Examples of such a

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<sup>419</sup> This is the option set out in Section 4-2-1

<sup>420</sup> This is the option set out in Section 4-2-2

registration system are the Korean Security Registration Act and the Japanese Assignment Registration Act.

Under the Korean and the Japanese Civil Codes, an assignment of receivables is perfected against third parties only if the assignor gives notice to the debtor by means of a certified document with a fixed date stamp.<sup>421</sup> In Korea and Japan, to circumvent this notification requirement, registration systems have been developed such as under Article 9 of the American Uniform Commercial Code ('UCC Article 9'). When contemplating the establishment of registration systems, the Korean and Japanese legislators, rather than revising their respective civil codes, which would have entailed costs and caused confusion, adopted alternative optional registration systems to co-exist with existing laws. In Korea, priority is determined by the order of notification of pledges under the Korean Civil Code or registration of security interests under the Korean Security Registration Act.<sup>422</sup> In Japan, according to the Japanese Assignment Registration Act, where a legal person has assigned a receivable and the assignment has been registered, the assignment is perfected vis-à-vis third parties except the debtor of the receivable.<sup>423</sup>

This thesis reviews the possibility of establishing an international version of such an alternative optional registration system so as to provide a method of perfecting international assignments of receivables as an alternative to the requirements of national legal systems. In particular, it would dispense with the need to give notice of the assignment to the debtors of the receivables as a condition of priority against third parties.

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<sup>421</sup> Korean Civil Code, art 450(2); Japanese Civil Code, art 467(2)

<sup>422</sup> Korean Security Registration Act, art 35(3).

<sup>423</sup> Japanese Assignment Registration Act, art 4(1)

An optional registration model would provide the parties with optional ways to perfect the assignment of receivables, and enable the parties to an assignment contract to choose whichever of these methods - international registration or the perfection method under their domestic laws - is best suited them to achieve perfection against third parties.<sup>424</sup> Where there are large numbers of debtors of receivables, most assignors and assignees would choose international registration rather than be forced to notify all these debtors of receivables. For example, in a bulk receivables transaction, where notice to the debtor is required for perfection, the assignor would have to make sure that every single debtor received notice since even one omission could cause the entire transaction to fall apart. An optional registration system would enable the parties to opt for the most efficient way both of perfecting the assignment or the security interest and of searching the registration.

However, such an optional registration model could defeat the object of international registration. A prospective registrant would have to investigate applicable national laws to establish whether there had been perfection under that law, which would have to be treated as though it were a registration with the international registry. In a country possessing a registration system, this would involve searching the national register. In countries (such as Germany) without perfection requirements, where an assignment is effective against third parties upon being made, there is no visibility at all, so that someone intending to register an assignment in the international registry would

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<sup>424</sup> The U.S. system under UCC Article 9 may also in some ways be said to be optional between filing and non-filing in some aspects since there is no obligation to file or not to file. However, if a security interest in receivables is not filed, it is not perfected against third parties. Interview with Steven L. Schwarcz, Professor, Duke University School of Law (University of Oxford, 26 November 2010)

have absolutely no way of knowing whether there had been a prior assignment domestically.

In one country it might be practicable to check both the registry and enquire of account debtors. If all the parties were in one country - e.g., in Germany or in Korea or in Japan - it might be practical to check the IRSAR and the other perfection methods under the applicable national law i.e. national registry or account debtors. However, in an international level, it would be impracticable because the would-be assignee should check all of the national registries since a potential hidden competing assignee might be in any country. This could defeat the object of international registration.

Such an optional registration model could not meet the basic requirements for an effective registry system. In the jurisdictions, where an assignment or a security interest must be registered for perfection against third parties, the basic requirements for an effective registry system is that it should enable a searcher to rely with confidence on the absence of an entry in the register and a registrant to be confident that it will have priority over a later registrant or one who has not registered. Thus, an optional registration model co-existing with national perfection methods would not be desirable for an international registration model.

#### **4-4. COMPULSORY REGISTRATION SYSTEM WITH LIMITED SCOPE OF APPLICATION**

According to Goode,<sup>425</sup> in preparing private law conventions in international trade, three limitations on the scope of a project have been found helpful. These are to confine the convention to commercial dealings and cross-border transactions, and to concentrate on a specific type of commercial transaction, selected for its importance in terms of the unit value of the subject-matter or the continuity of dealings involving property transfers. The international registration system proposed in this thesis concentrates on receivables.

This thesis presents four approaches to confining the scope of application of the proposed IRSAR Convention. The first is to define internationality as between the parties: the assignor, the assignee and the debtor of the receivable. The second is to limit the types of receivable to be registered. The third is to limit the amount of receivables to be registered. The fourth is to limit the parties: the assignor, the assignee or the debtor of the receivable to be registered. These methods to limit the scope of application are analysed in the following subsections.

##### **4-4-1. To Confine Internationality of the Assignment of Receivables**

Confining the scope of a relevant Convention to purely international transactions would considerably reduce pressure on the system, provided the concept of internationality was adequately defined. This means finding ways of segregating

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<sup>425</sup> Roy Goode, 'The Protection of Interests in Movables in Transnational Commercial Law' [1998] *Uniform Law Review* 453, 459-60

international transactions to be registered with an international registration system from purely domestic transactions. However, distinguishing international from domestic assignments of receivables is impractical, since they are subject to change and are sometimes commingled.

The UN Receivables Convention applies to assignments of international receivables and to international assignments of receivables.<sup>426</sup> If, at the time of conclusion of the original contract, the assignor and the debtor are located in different States, it is an international receivable.<sup>427</sup> If, at the time of conclusion of the contract of assignment, the assignor and the assignee are located in different States, it is an international assignment.<sup>428</sup> However, this approach would not be workable for the assignment of receivables.

The following example may illustrate this. A and C are domestic companies, B is a foreign company, and the debtor of the receivable is a domestic company. A has assigned a domestic receivable to a foreign company B. The assignment from A to B is an international assignment and eligible to be registered in the IRSAR. Subsequently, A fraudulently or mistakenly once again assigns the same receivable to C. This is not an international assignment and cannot be registered in the IRSAR. C achieves perfection of the assignment under the domestic laws. However, if the IRSAR were designed to override the perfection requirements of national law, the domestic perfection would not be valid. As a result, a domestic company must always check the IRSAR before making an assignment, even with a domestic company. If the IRSAR were designed to override

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<sup>426</sup> UN Receivables Convention, art 1 (Scope of application) (1)(a)

<sup>427</sup> UN Receivables Convention, art 3 (Internationality)

<sup>428</sup> UN Receivables Convention, art 3 (Internationality)

the perfection requirements of national law, domestic assignees would have to check IRSAR each time the assignee registers an assignment in order to secure their priority, and furthermore purely domestic assignments would also have to be registered in the IRSAR in order to protect their priority.

The following example will illustrate this. A domestic company has assigned its receivables to a foreign company and registered the assignment in an IRSAR which overrides the perfection requirements of national law. A prospective domestic assignee would first have to check the IRSAR to see whether there was any prior assignment. Furthermore, domestic assignees would also have to register their domestic assignments in the IRSAR in order to protect their priority against any future international assignment. As a result, the existence of an IRSAR overriding the perfection requirements of national law means that any assignment, whether international or domestic, must be registered in the IRSAR, if the scope of application is limited by the concept of internationality as defined in the UN Receivables Convention. Thus, confining the scope by using the concept of internationality could give rise to complications.<sup>429</sup>

The concept of internationality as defined in the UN Receivables Convention is impractical and this seems to be one of the reasons why the UN Receivables Convention was not so successful. Confining the scope of application by using the concept of internationality as defined in the UN Receivables Convention could give rise to complications. Confining the scope of application by using the concept of internationality as defined in the UN Receivables Convention means all assignments of receivables either

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<sup>429</sup> Since, if an IRSAR were to provide a translation service, it would increase the registration fee. Thus, the IRSAR would be set up in English, and it could increase transaction costs for non-English speaking nationals.

international or domestic must be registered in the IRSAR to secure its priority and perfection since a competing assignee may be an international assignee.

#### **4-4-2. To Limit Types of Receivables**

Restricting the types of receivables is impractical because there are various types of receivables and the margins are not clear. For example, a convention could limit its scope to credit card receivables or account receivables for sales of goods. However, these types of receivables are often traded domestically. It is difficult to find certain types of receivables which are traded mainly internationally rather than domestically.

If the scope of registration were limited by the types of receivables, it is expected that disputes about the scope of registration would be inevitable because of the following reasons. In receivables financing there are many low-value receivables that are more susceptible to change over time. By contrast, ships and aircraft are high-value, tangible assets. An aircraft that is registered in the International Registry of Mobile Assets under the Cape Town Convention is highly identifiable. Its manufacturer's serial number, the name of the manufacturer and its model designation are necessary (and sufficient) to identify the aircraft object.<sup>430</sup> Registration in the International Registry of Mobile Assets requires the use of a drop-down menu, provided by the aircraft manufacturing companies, to identify the object of registration.<sup>431</sup> Registrants only need to select and click the appropriate item in the drop-down menu to identify the object. Nevertheless, there is still

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<sup>430</sup> Cape Town Convention Aircraft Protocol, art VII

<sup>431</sup> Reply to Frequently Asked Question No. 11 on the International Registry on Mobile Assets website <<https://www.internationalregistry.aero/irWeb/showFAQs.do>> accessed 17 September 2011. See also Regulations and Procedures for the International Registry, Regulations, s 5.1.

an argument as to whether an object should be registered in the International Registry or in a domestic registry with respect to the Cape Town Convention and its Aircraft Protocol. This is because there are limitations to the scope of application according to the weight and number of people an aircraft may carry under the Aircraft Protocol.<sup>432</sup> If there is disagreement even with respect to aircraft, it is to be expected that there might be even more disagreement with respect to receivables were the scope to be restricted to certain types of receivables.

#### **4-4-3. To Limit Amount of Receivables**

Restricting the scope of registration on the basis of the estimated value of the receivables transaction appears equally impractical. For the purpose of an international registry, the scale of transactions to be registered must be sufficiently large that the parties would be willing to pay additional registration fees. However, there is some difficulty in estimating the value of receivables, which fluctuates over time. The valuation of future receivables is even more challenging. If registration were limited to a certain value, disputes in relation to borderline receivables would be bound to result.

#### **4-4-4. To Limit the Parties to be Registered**

Restricting the parties - assignor, assignee or debtor of the receivable - to be registered in the IRSAR could be a solution for the purpose of limiting the sphere of

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<sup>432</sup> Cape Town Convention Aircraft Protocol, arts I(2)(e) and I(2)(l).

application. The UNIDROIT Convention on International Factoring (Ottawa, 28 May 1988) limits its sphere of application by defining a ‘factor’: the Convention applies to the assignment of receivables where the assignee is a factor stipulated in the Convention.<sup>433</sup>

There are basically two methods how to index a registry: an asset-indexed registration system and a security provider-indexed registration system. An asset-based registration system is only practical for certain types of assets such as land,<sup>434</sup> cars, ships and airplanes. Registration of these assets may be indexed by a description of the object asset because they have certain defined identity,<sup>435</sup> and therefore searching against a certain object asset shows all transfers of ownership of the asset and all security interests in the asset.

The first issue that arises when designing a new registration system is whether registration should be based on the assets themselves or on the person owning the assets. A registration system for assignments of and security interests in receivables should be an assignor-based registration system. If it were an asset-based registration system, the asset i.e. receivables would need to be indexed clearly. In order to pinpoint specific receivables, a searcher would input the name of the assignor, the debtors of the receivables, the cause of the receivables, the date of the contract that created the receivables, the date when the receivables would become due, etc. In many cases, the debtors of the receivables are too many to list all of them because receivables financing usually consists of bulk assignments of receivables or security interests in a group of receivables, and therefore

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<sup>433</sup> UNIDROIT Convention on International Factoring, arts 1(1), 1(2) and 2(1)

<sup>434</sup> See Section 2-3-1-5

<sup>435</sup> Lynn M. LoPucki and Elizabeth Warren, *Secured Credit: A Systems Approach* (6th ed, Aspen Publishers 2009) 296.

only a general description of the debtors of the receivables is registered in the IRSAR. It is technically difficult to identify and specify registered receivables by a general description of the debtors of the receivables.<sup>436</sup>

The most precise and definite information by which the IRSAR could be indexed is the name of the assignor (or the security provider). When a third party looks up the IRSAR, he could search against the name of the assignor that he is trading with. For these reasons, this thesis proposes to limit the sphere of application by restricting the assignor (or the security provider) to be registered. This restriction is discussed in Chapter 4-5.

## **4-5. RESTRICTION OF THE SCOPE OF APPLICATION OF THE PROPOSED IRSAR CONVENTION**

### **4-5-1. The ‘Vehicle for the International Registration System’ (VIRS)**

This thesis suggests restricting the assignors (or secured creditors) entitled to register assignments (or security rights) in the IRSAR. The proposed IRSAR Convention would apply only to the assignment of receivables where the assignor is a special purpose company registered with the IRSAR Registrar. That company will be referred to hereinafter as the ‘Vehicle for the International Registration System’ (‘VIRS’). This

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<sup>436</sup> In fact, it is difficult to identify and specify a receivable even in the filing system under UCC Article 9. In particular, a future receivable is much more difficult to specify and identify technically. Even the information on the financing statements only triggers further investigation of the assignment of receivables. The filed information does not actually specify and identify the receivable or group of receivables subject to a security interest. Rather, the filing focuses on identifying the assignor and the assignee, of whom a potential interested party may ask about the assignment.

thesis invented the idea of a VIRS. A VIRS is a legal person. Any legal person may register itself as a VIRS. Confining the scope of application by using the concept of a VIRS, it is much clear and definitive. If the assignor or security provider is a VIRS, a potential assignee or secured creditor does not have to check the domestic registers, since the IRSAR prevails over the domestic registers. The proposed IRSAR Convention would exclusively deal with receivables of a VIRS. In this thesis, a ‘receivable of a VIRS’ is referred to as a ‘VIRS receivable’.

This approach does not distinguish international from domestic assignments of receivables. Even domestic parties, if the assignor or security provider is a VIRS, would have to register their assignments or security interests in the IRSAR in order to secure their priority. Priority would be determined by the order of IRSAR registration.<sup>437</sup> Under the IRSAR Convention, a registered assignment of or security interest in a receivable prevails over an unregistered assignment of or security interest in the receivable.<sup>438</sup> An unregistered assignment of or security interest in a receivable is not protected against a subsequently registered assignment of or security interest in the receivable. This rule induces every assignment or security interest of a VIRS to be registered. Thus, the IRSAR is a compulsory registration system. If none of competing assignments are registered, priority is determined by the applicable national law.<sup>439</sup>

The scope of application of the proposed IRSAR Convention would be limited to assignments of receivables of a VIRS (that is the assignor) and security interests in receivables of a VIRS (that is the security provider). The proposed IRSAR Convention

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<sup>437</sup> See Section 5-3-1

<sup>438</sup> Draft IRSAR Convention, art 5(1). See 318

<sup>439</sup> See Section 5-1-1

would apply only to cases where the assignor or security provider is a VIRS. In order to be registered under the proposed IRSAR Convention, the assignor or the security provider must be a VIRS. Assignments of receivables by a VIRS would be governed by the proposed IRSAR Convention. Assignments of receivables to a VIRS would be governed by the applicable national laws. Security interests in receivables provided by a VIRS would be governed by the proposed IRSAR Convention. Security interests in receivables provided to a VIRS would be governed by the applicable national law.

#### **4-5-2. Assignor or Security Provider needs to be a VIRS**

The proposed IRSAR Convention applies where the assignor or security provider is a VIRS registered as such with the IRSAR Registrar at the time of the conclusion of the assignment or security interest agreement.<sup>440</sup> Assignments of or security interests in VIRS receivables must be registered in the IRSAR to be perfected against third parties. The IRSAR is indexed by assignor and by security provider.

It does not matter whether the assignee or secured creditor is a VIRS or not. The fact that the assignee or secured creditor is situated in a non-Contracting State would not affect the applicability of the proposed IRSAR Convention.<sup>441</sup> If the assignor or security provider is a VIRS, the proposed IRSAR Convention would apply not only where the assignee or secured creditor is a foreign party but also where it is a domestic party. All

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<sup>440</sup> The Cape Town Convention also takes this approach as to where the debtor is located, but does not have a system like the 'registered VIRS' system. Cape Town Convention, art 3

<sup>441</sup> The Cape Town Convention also takes this approach. Cape Town Convention, art 3(2)

assignments (both international and domestic) made by a VIRS must be registered in the IRSAR to be perfected against third parties.

The assignee or secured creditor need not be a legal person in a Contracting State. A legal person in either a Contracting State or a non-Contracting State would be able to be registered as an assignee or secured creditor. Thus, any company from any jurisdiction may achieve perfection against third parties by IRSAR registration. As a result, even a domestic party must be aware that when it purchases a receivable from, or is granted a security interest in a receivable by, a VIRS, perfection is not governed by the applicable national laws but by the proposed IRSAR Convention.

#### **4-5-3. VIRS-Indexed Registry**

The IRSAR would be indexed by VIRSs, which are assignors and security providers. Under the IRSAR Convention, assignors and security providers of receivables must be VIRSs. Therefore an assignor-indexed registration system for the IRSAR means a VIRS-indexed registration system. A third party, who would like to purchase a VIRS receivable or to provide a loan to a VIRS taking its receivable as security, would check the IRSAR against the VIRS to investigate whether there is any prior assignment of or security interest in the VIRS receivable. If the assignor or security provider is a VIRS, the counterparty would only have to investigate the IRSAR and would not have to investigate applicable national laws to see if there has been perfection under that law, thus avoiding choice of law difficulties.

## **4-6. REGISTRATION OF A VIRS**

### **4-6-1. Public Notification of the list of VIRS**

In order to make it absolutely clear that a company is a VIRS, a very important prerequisite for a VIRS is that it must be registered with the IRSAR Registrar. Registration of a VIRS provides public notification. The IRSAR Registrar must publish the list of registered VIRS, so that registrants may be aware they are dealing with a VIRS. If a company is a VIRS, even domestic parties (e.g. prospective assignees of the company's receivables) must be aware that the proposed IRSAR Convention could be applied and the application of national laws overridden.

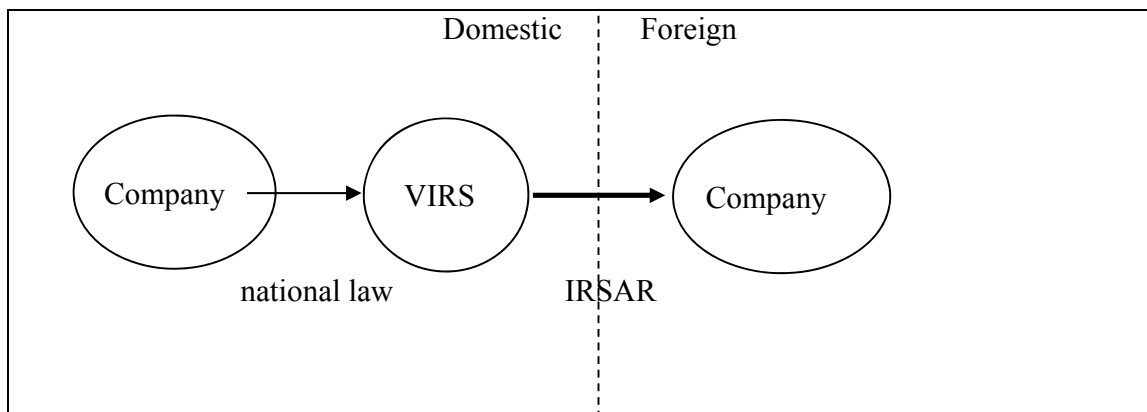
Anyone would be able to investigate whether a company is a VIRS in the list provided on the IRSAR website. If the State where a company is registered is a Contracting State of the proposed IRSAR Convention, the company may be a VIRS. If the State where a company is registered is not a Contracting State, the company cannot be a VIRS. In this thesis, 'registration of a company as a VIRS with the IRSAR Registrar' is referred to as 'VIRS registration'.

### **4-6-2. Two Methods to use the IRSAR**

Where a company (originator) in a Contracting State wishes to assign its receivables to a foreign investment company under the proposed IRSAR Convention, this thesis envisages two methods: (1) an ordinary company establishes a separate new VIRS

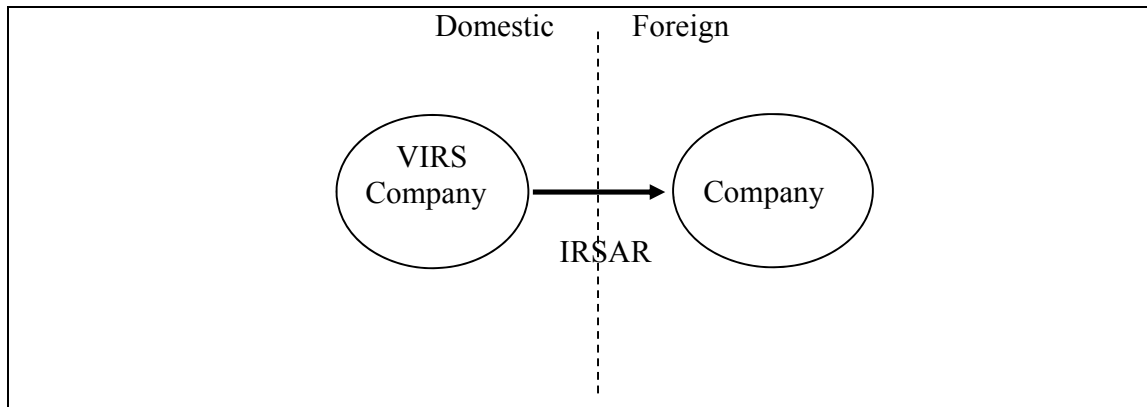
and transfer its receivables to the new VIRS; or (2) an existing ordinary company registers itself as a VIRS with the requisite authority.

#### 4-6-2-1. Establishing a Separate VIRS



A company may establish a separate new VIRS and register it with the IRSAR Registrar to assign its receivables to a foreign company under the proposed IRSAR Convention. Once a company have established a VIRS, the company may use the existing registered VIRS to assign its receivables under the proposed IRSAR Convention. Then, a company's pre-existing receivables vesting prior to the establishment of the VIRS will need to be assigned to the VIRS as it is a separate legal entity. That assignment to the VIRS will be outside the IRSAR system, and be governed by applicable national laws.

#### 4-6-2-2. Registering itself as a VIRS



An ordinary company can register itself as a VIRS with the IRSAR Registrar, which will change the status of the company into a VIRS. In this way, the VIRS is the same legal entity as the company holding the pre-existing interests. Then, the company, after having become a VIRS, would be able to assign its receivables to a foreign company by registering the assignment in the IRSAR. Assignments which took place after the VIRS registration of the company are governed by the IRSAR Convention, whereas assignments which had already taken place at the time of the VIRS registration are governed by applicable national laws.<sup>442</sup>

First, a company wishing to dispose of non-performing loans would register itself as a VIRS with the IRSAR Registrar. An asset management company would register itself as a VIRS with the IRSAR Registrar in order to assign non-performing loans to foreign investors under the proposed IRSAR Convention.

Second, a company seeking to borrow funds using its receivables as collateral would register itself as a VIRS with the IRSAR Registrar. To create a floating charge

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<sup>442</sup> See Section 4-6-4

over receivables, a company would register itself as a VIRS with the IRSAR Registrar in order to use the IRSAR.

Third, a bank which wishes to borrow money from central banks with providing security interests in its loan receivables, would register itself as a VIRS with the IRSAR Registrar.

Fourth, a company originating factoring or securitisation would register itself as a VIRS with the IRSAR Registrar to transfer its receivables to the factor or the securitisation SPV to raise finance in international financial markets.

Once a company is registered as a VIRS with the IRSAR Registrar, the proposed IRSAR Convention (instead of national laws) would apply where the company assigns its receivables or provides security interests in its receivables.

#### **4-6-3. Pre-existing Security Interests**

When a company registers itself as a VIRS with the IRSAR Registrar, the treatment of pre-existing security interests in (including security assignments of) the company's receivables is a problem. 'Pre-existing security interests' means in this thesis the security interests in (and the security assignment of) a company's receivables which are perfected under the applicable national laws prior to the date of the VIRS registration. If such pre-existing security interests would be continuously valid, a would-be assignee would have to check both the IRSAR and the national perfection methods forever. On the other hand, if pre-existing security interests becomes invalid all of a sudden upon VIRS registration, the pre-existing secured creditor's rights would be unfairly infringed.

Thus, the proposed IRSAR Convention provides the transitional period of one year from the date of the VIRS registration of a company.<sup>443</sup> It is to avoid a situation in which post-VIRS security interests are indefinitely subordinated to pre-existing security interests, and to allow pre-existing secured creditors a reasonable time within which to perfect or re-perfect their security interests by registering them in the IRSAR.<sup>444</sup>

If a pre-existing secured creditor registers his pre-existing security interests in the IRSAR within the one year transitional period, the pre-existing secured creditor can enjoy the priority of the date when the pre-existing security interests are perfected under the applicable national laws, and thus has priority over any post-VIRS security interests registered prior to the pre-existing security interests.

After the one year transitional period, without a pre-existing security interests being registered in the IRSAR, an assignee or secured creditor registered in the IRSAR has priority over any other secured creditor subsequently registered in the IRSAR and over any other secured creditor not registered in the IRSAR, even though those secured creditors have been perfected under the applicable national laws.

Let us suppose a case where an ordinary company perfected a security assignment (for the purpose of security) of its receivables under the applicable national law, and subsequently the company registers itself as a VIRS with the IRSAR Registrar, and registers an assignment of or security interest in the same receivables in the IRSAR. The assignment or security interest registered in the IRSAR is subject to the previous security

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<sup>443</sup> Draft IRSAR Convention, art 3(4). See 317

<sup>444</sup> This transitional period functions similarly with the transitional provisions under Cape Town Convention, art 60. Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008), 289 [4.348]-[4.349]

assignment perfected under the applicable national laws, if not registered in the IRSAR, but only during the one year transitional period.

#### **4-6-4. Pre-existing Assignments**

Let us suppose a case where an ordinary company absolutely assigned its receivable to a third party (not for the purpose of security), and perfected the absolute assignment of the receivable under the applicable national law, and subsequently registers itself as a VIRS with the IRSAR Registrar. If the company, after becoming a VIRS, registers another assignment of or security interest in the same receivable in the IRSAR, the registration in the IRSAR is a registration of an ineffective assignment. It is because the receivable has been already absolutely assigned to a third party under the applicable national law and does not belong to the assets of the company at the time of the IRSAR registration. IRSAR registration does not create a legal right.

As a result, perfection of an absolute assignment of a company's receivable under the applicable national law prior to the VIRS registration of the assignor company prevails over the IRSAR registration of an assignment or a security interest. However, perfection of an assignment under the applicable national law after the VIRS registration cannot prevail over the IRSAR registration of an assignment or a security interest.

This might harm the benefit of the IRSAR, that a would-be assignee only has to check the IRSAR if the assignor of a receivable is a VIRS in the following situations: First, where the assignor company has fairly recently registered itself as a VIRS with the IRSAR Registrar, potential assignees will have to keep checking national registers etc. to

check that there are no absolute assignments prior to the VIRS registration of the assignor company. Second, where the assignor VIRS is itself an assignee from an assignor which is not a VIRS, a would-be assignee would have to check to make sure that the receivables were properly and effectively assigned to the VIRS, i.e. that the assignment was perfected under the applicable national law (which might require notice to the debtors).

These problems result from the shortcoming of an assignor (or security provider)-indexed registry. The IRSAR is indexed based on the assignors or security providers (rather than the receivables), and thus it does not show an ownership transfer of a particular receivable. For creation of a receivable, registration is not required. Only assignments of or security interests in receivables can be registered in the IRSAR.<sup>445</sup> As a result, not all receivables of a VIRS have been registered in the IRSAR. Thus, searching the IRSAR does not guarantee to investigate whether the VIRS owns the specific receivable in question. A would-be assignee may also refer to the financial statement of the VIRS, but the financial statement provides only general information of receivables as items among various categories of assets of the VIRS.

This thesis does not suggest a transition period for absolute assignments. In a security assignment, the assignee takes care of the assigned receivables because the assignee should return back the receivables to the assignor when the assignor pays the assignee, and therefore, the assignee would not assign the receivables to a third party. However, in an absolute assignment, the assignee would assign the receivables to a third party, who might assign the receivables to another third party, and so on. After assigning

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<sup>445</sup> It may also record absolute rights where outright assignments of receivables are included. Still, it does not record all of the receivables created.

the receivables to a third party, the absolute assignee would not take care of the receivables any more. Thus, it is not expectable for the assignee to register the absolute assignment, which has already been lawfully perfected under the applicable national law, once again in the IRSAR within one year from the VIRS registration of the assignor company. For this reason, a transition period requiring registration of absolute assignments in the IRSAR within one year of the VIRS registration would not work.

The only way of dealing with this is a sanctions based approach. The best way to prevent a VIRS from assigning and creating a security interest in the receivable, which the VIRS has absolutely assigned to a third party or which is not properly and effectively assigned to the VIRS and thus the VIRS does not own, is sanctions for false registration. In the first case where a VIRS assigns or creates a security interest in the receivable which the VIRS has absolutely assigned to a third party, the VIRS is intentional or at least negligent. In the second case where a VIRS assigns or creates a security interest in the receivable which is not properly and effectively assigned to the VIRS, it is the VIRS's responsibility to make sure that the receivable has been properly and effectively assigned to the VIRS.

#### **4-6-5. Sanction for False Registration**

##### **4-6-5-1. Fine**

The proposed IRSAR Convention imposes severe fines upon the VIRS which commits false registration or consent. If a VIRS intentionally or negligently registers an assignment of or a security interest in the receivable that the VIRS does not own (e.g.

which have been already absolutely assigned to a third party) in the IRSAR, or consents to such false registration applied by an assignee or a secured creditor, the VIRS will be imposed with a fine no more than 10% of the amount of the receivables falsely registered. Until the VIRS pays the fine to the IRSAR Registrar, any registration with respect to the VIRS is suspended.<sup>446</sup>

#### 4-6-5-2. Disqualification of the VIRS

The proposed IRSAR Convention provides disqualification of the VIRS which commits false registration or consent. If a VIRS registers an assignment of or a security interest in the receivable that the VIRS does not own in the IRSAR, or consents to such false registration applied by an assignee or a secured creditor intentionally or negligently more than three times, the VIRS will be disqualified as a VIRS and cannot become a VIRS any more forever.<sup>447</sup>

#### 4-6-5-3. Compensatory Damages

In addition, a purported assignee or secured creditor who suffered loss due to such false registration or consent of a VIRS can sue the VIRS for compensatory damages under the applicable national laws.

On account of these sanctions for false registration or consent, it is expected that a VIRS would not assign or create a security interest in the receivable which the VIRS does not own. This would reduce the possibility of there being pre-existing assignments of the

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<sup>446</sup> Draft IRSAR Convention, art 18(1). See 326

<sup>447</sup> Draft IRSAR Convention, art 18(2). See 326

receivable and the need to investigate applicable national laws to see whether the receivable has already been assigned to a third party.

#### **4-7. DEREGISTRATION OF A VIRS**

For a VIRS to recover its ordinary company status and deregister from the list of VIRS, the consent of all assignees and secured creditors of the receivables of the VIRS, previously registered in the IRSAR, is required. Once a company has been deregistered from the list of VIRS, the status of the company being changed from a VIRS back to an ordinary company, any assignment or security interest registered in the IRSAR will lose its priority. Thus, assignees or secured creditors will again have to perfect their assignments or security interests under the applicable national law.

One year before the date of deregistration ('D-date'), prior notice must be registered in the IRSAR as follows: 'this company will be deregistered from the list of VIRS and the status of this company will be changed into an ordinary company from the D-date, and the proposed IRSAR Convention shall not apply to the assignment of or a security interest in the receivables of this company from the D-date.' This requirement is intended to protect potential assignees or security providers who relied on the list of VIRS before the VIRS was deregistered.

## **4-8. SPHERE OF APPLICATION OF THE PROPOSED IRSAR CONVENTION**

### **4-8-1. Connecting Factor**

The proposed IRSAR Convention would apply to assignments of and security interests in receivables in which the assignor or security provider is a VIRS.<sup>448</sup> The fact that the assignor or the security provider is a VIRS means that the assignor or security provider is incorporated and registered in a Contracting State.

Where the assignor or security provider is a VIRS, if the forum state is a Contracting State, according to Article 2(1) of the proposed IRSAR Convention, the proposed IRSAR Convention would be applied.

Where the assignor or security provider is a VIRS, if the forum state is not a Contracting State, but according to the private international law of the forum state, the law of the assignor's or security provider's state is the governing law, the court in the forum state would apply the proposed IRSAR Convention.

However, even though the assignor or security provider is a VIRS, if the forum state is not a Contracting State, and according to the private international law of the forum state, the law of the debtor's state is the governing law, and the debtor of the receivable is situated in a non-Contracting State, the court in the forum state might not apply the proposed IRSAR Convention.

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<sup>448</sup> Draft IRSAR Convention, art 2(1). See 316

## 4-8-2. Future Receivables

The proposed IRSAR Convention applies to both present and future receivables.<sup>449</sup> Article 2(1) of the proposed IRSAR Convention stipulates: ‘This Convention applies to an assignment of and a security interest in a receivable, present or future’. The ‘present or future’ part means that the IRSAR covers future receivables.

Currently, most registration systems around the world cover future receivables. UCC Article 9, the PPSAs of Canada, New Zealand and Australia, the UK Companies Act 2006 and the UNCITRAL Legislative Guide on Secured Transactions require only a general description of the encumbered asset.<sup>450</sup> Thus, it is easy to register an assignment of future receivables even though a debtor of the future receivable is not specified yet.

In Korea, the name and the address of the debtor of the receivable are required to be registered.<sup>451</sup> However, if the debtor of the receivable is not specified at the time of registration, it is not required to be registered. Therefore an assignment of future receivables may be also registered. The Korean Security Registration Act expressly stipulates that it covers future receivables<sup>452</sup> and movable assets which the security provider will get in the future.<sup>453</sup>

In Japan, under the Japanese Assignment Registration Act, it is possible to perfect the assignment of future receivables against unspecified debtors through registration. For future receivables, the debtor’s name and address cannot be registered because the debtor

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<sup>449</sup> Draft IRSAR Convention, art 2(1). See 316

<sup>450</sup> See Section 6-2-5-1

<sup>451</sup> See Section 6-2-5-1-6

<sup>452</sup> Korean Security Registration Act, art 34(2)

<sup>453</sup> Korean Security Registration Act, art 3(2)

of future receivables is not specified at the time of registration, whereas for existing receivables, the debtor's name and address must be registered. Instead, for future receivables, details of the contract upon which the future receivables will accrue must be registered to specify the contract.<sup>454</sup> This also very cumbersome, but Japanese lawmakers thought that this should be required to identify future receivables.<sup>455</sup>

### 4-8-3. Legal Person (Company)

The proposed IRSAR scheme limits the scope of registrants to an assignment of or a security interest in a receivable where both the assignor and the assignee, or both the security provider and the secured creditor, are legal persons that have company registration numbers in their states.<sup>456</sup> In the IRSAR, each user would be identified by the country code and the company registration number of its own state. As a result, a VIRS can assign its receivables to only a company registered and having registration number in its country, and must not assign its receivables directly to an individual. If a VIRS needs to assign its receivables to an individual, it has to first assign its receivables to a company and then the company may assign the receivables to an individual.

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<sup>454</sup> Assignment of Personal Property and Receivables Registration Regulation, art 9(1)(iii)

<sup>455</sup> During the legislation process, it was discussed whether the debtor's name and address may be additionally registered after a future receivable has actually accrued. However, this idea was not accepted. It was because there was worry about the situation where the debtor registered later might not be the person who the parties intended at first in the contract registered previously. Katsuhiko UEKAKI (植垣勝裕) and Hideki OGAWA (小川秀樹), *Q&A on the Japanese Assignment Registration Act (Ichi Mon Ichi Tou Dousan Saiken Jouto Tokurei Hou, 『一問一答・動産・債権譲渡特例法』)* (3rd edn, Shouji Houmu (商事法務) 2008) 96-97

<sup>456</sup> Draft IRSAR Convention, art 2(2). See 317

This thesis argues that the scope of assignors, assignees, security providers and secured creditors in the IRSAR should be limited to legal persons (companies), and the IRSAR cannot apply to individual natural persons because of the following reasons:

First is the language barrier (English capability). On account of cost effectiveness, an international registration is operated in one language, which would be English. Therefore users of an international registration need to understand English. However, many natural persons around the world cannot read English, and thus cannot use an international registration in English.

Second is the problem of identification. Since the IRSAR is an assignor (or security provider)-indexed system, identification of the assignor (or security provider) is important. Furthermore, because IRSAR registration is confirmed by mutual reciprocal confirmation of the assignor and the assignee, both the assignor and the assignee must be certified entities and identifiable. Identification of a legal person (company) is clear and convenient. In most countries, there is a registry for companies, and therefore each company has its registration number in its own country. Assignments of receivables from a company to another company may be registered using the company registration number in order to identify the assignor company and the assignee company.

However, for individuals in many countries it is very difficult to find a method to accurately identify a natural person and to guarantee the identification of an individual. A name is insufficient because there are many cases where different persons have the same name. For example, in the US where every individual may register his or her security interests, there are many problems related to accuracy of names of debtors

(security providers).<sup>457</sup> Furthermore, identifying foreigners in English or translation of a name into English is much more complicated and difficult.

Third, it is to prevent a VIRS from hiding its receivables by registering the assignment of the receivables to fictitious people using fake names in the situation of running into bankruptcy.

Fourth, a natural person does not usually use receivables for financing whereas the purpose of the IRSAR is to facilitate financing using receivables.

In comparison, in Korea, the Korean Security Registration Act applies to security interests where the security provider is a legal person or a natural person only if the natural person registered his trade name under the Korean Commercial Registration Act.<sup>458</sup> The security interest, which is created by a legal person or a natural person who registered his trade name, may be registered under the Korean Security Registration Act. Therefore the self-employed, farmers, fishermen and livestock raiser may also register their security interests, if they registered the trade name. The legal person registration number or the resident registration number of a security provider and a secured creditor must be registered. A foreign legal person can also register its security interest as a security provider in Korea.<sup>459</sup> For a foreign legal person, that does not have a legal person registration number, its business office or other office located in Korea or, if it does not

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<sup>457</sup> Lynn M. LoPucki and Elizabeth Warren, *Secured Credit: A Systems Approach* (6th ed, Aspen Publishers 2009) 284.

<sup>458</sup> Korean Security Registration Act, art 2(5)

<sup>459</sup> Korean Security Registration Act, art 2(5)

have any office in Korea, the representative of the foreign legal person and his or her address must be registered.<sup>460</sup>

In Japan, under the Japanese Assignment Registration Act, the assignor must be a legal person. If an assignor is a natural person, he cannot register his assignment. A legal person registration number or a resident registration number is not to be registered in Japan. A foreign legal person can also register its assignment as an assignor in Japan.<sup>461</sup> For a foreign legal person, the Japanese Assignment Registration Act stipulates, the business office or other office located in Japan must be registered.<sup>462</sup> Therefore it might be interpreted that a foreign legal person which does not have any office in Japan cannot register its assignment in Japan.

#### **4-8-4. Interaction with the Cape Town Convention**

##### **4-8-4-1. Scope of the Cape Town Convention and its Protocols**

There might be overlaps between the proposed IRSAR Convention and the Cape Town Convention because the latter also stipulates the effect, formal requirement and priority of assignments of so-called ‘associated rights’.<sup>463</sup> Associated rights include receivables secured by or associated with the object registrable under the Cape Town Convention.<sup>464</sup> These rules apply to aircraft equipment, railway rolling stock and space

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<sup>460</sup> Korean Security Registration Act, art 47(2)(iv); Korean Security Regulation Rule, art 34

<sup>461</sup> Japanese Assignment Registration Act, art 5(2)

<sup>462</sup> Japanese Assignment Registration Act, art 7(2)(iii)

<sup>463</sup> Cape Town Convention, arts 31-37.

<sup>464</sup> Cape Town Convention, art 1(c).

assets<sup>465</sup> in accordance with the Protocol to the Convention on International Interests in Mobile Equipment on Matters specific to Aircraft Equipment ('Aircraft Protocol'),<sup>466</sup> the Luxembourg Protocol to the Convention on International Interests in Mobile Equipment on Matters specific to Railway Rolling Stock ('Rail Protocol')<sup>467</sup> and the Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Space Assets ('Space Protocol').<sup>468</sup> Associated rights include receivables for the repayment of purchase-money loans and the payment of rentals under leases.<sup>469</sup>

#### 4-8-4-2. Assignment of Associated Receivables

Let us take the case of a VIRS that advances money to a Debtor for the Debtor's general purposes under a loan agreement providing for the grant of a security interest in an aircraft owned by the Debtor to secure the Debtor's repayment obligation under the loan agreement.<sup>470</sup> At the time of the conclusion of the agreement on the security interest in the aircraft, the Debtor was situated in a Contracting State of the Cape Town Convention.<sup>471</sup> The VIRS registered its security interest in the aircraft in the International Registry of Mobile Assets. Later, the VIRS assigns its receivables under the loan

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<sup>465</sup> Cape Town Convention, art 2(3).

<sup>466</sup> adopted in Cape Town on 16 November 2001

<sup>467</sup> adopted in Luxembourg on 23 February 2007

<sup>468</sup> adopted in Berlin on 9 March 2012

<sup>469</sup> Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008), 83 [2.143]

<sup>470</sup> *ibid* 252 [4.258] Illustration 37

<sup>471</sup> Cape Town Convention, art 3(1)

agreement together with the security interest in the aircraft, first, to A1 and, second, to A2.

In principle, perfection of the assignment of the receivables by IRSAR registration is independent from perfection of the security interest in the aircraft by registration in the International Registry of Mobile Assets under the Cape Town Convention. In order to secure priority of the assignment of the receivables, the assignment must be registered in the IRSAR. Furthermore, in order to secure priority of the assignment of the security interest in the aircraft, the assignment of the security interest in the aircraft must be registered in the International Registry of Mobile Assets.

#### 4-8-4-3. Extension of the Cape Town Convention to the Assignment of Receivables

Nevertheless, if the loan contract between the VIRS (creditor) and the debtor states that the receivables are secured by or associated with the aircraft,<sup>472</sup> and if the VIRS receivables under the loan agreement are related to the aircraft,<sup>473</sup> the Cape Town Convention extends its sphere of application to the assignment of receivables.<sup>474</sup>

Let us take the following example. A VIRS owns an aircraft and leases the aircraft to an airline company; the lease receivables are secured by the aircraft. At the time of the conclusion of the agreement on the security interest in the aircraft, the airline

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<sup>472</sup> Cape Town Convention, art 36(1)(a).

<sup>473</sup> Cape Town Convention, art 36(1)(b).

<sup>474</sup> Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008), 83 [2.143]

company (debtor) was situated in a Contracting State of the Cape Town Convention,<sup>475</sup> and the VIRS' security interest in the aircraft was registered in the International Registry of Mobile Assets. Later, the VIRS assigns the lease receivables together with the security interest in the aircraft first to one financial institution, F1, and then to another, F2. The priority of assignments of the lease receivables between F1 and F2 is determined by the order of registration in the International Registry of Mobile Assets according to Article 29 of the Cape Town Convention.

The rationale is that by looking at the contract between the VIRS (creditor) and the airline company (debtor), a would-be assignee can determine whether to search the International Registry of Mobile Assets.<sup>476</sup> In the case of reservation-of-title agreements or financial lease agreements, the receivables necessarily relates to the purchase or lease of the aircraft. Thus, a would-be assignee would be in a position to search the International Registry of Mobile Assets.<sup>477</sup>

The likelihood of the proposed IRSAR Convention overlapping with the Cape Town Convention is low. This is because the proposed IRSAR Convention only deals with priority and perfection of assignments of, and security interests in, the receivables of a VIRS, and the Cape Town Convention and its Protocols apply only to aircraft equipment, railway rolling stock or space assets.

In the case of overlap, the proposed IRSAR Convention would not prevail over the Cape Town Convention with respect to priority issues. However, an assignee or

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<sup>475</sup> Cape Town Convention, art 3(1)

<sup>476</sup> Steven L. Harris, 'The International Rail Registry' (2007) *Uniform Law Review* 531, 544

<sup>477</sup> Charles W. Mooney, Jr., 'Assignments of international interests in mobile equipment and related receivables under the UNIDROIT Convention: When should the tail wag the dog?' (1999) Vol. 20:3 *University of Pennsylvania Journal of International Economic Law* 443, 448

secured creditor registered under the proposed IRSAR Convention would be perfected against the insolvency representative of a VIRS from the time of registration in the IRSAR.

#### **4-8-5. Contractual Prohibition on the Assignment of Receivables**

A VIRS must not agree upon contractual prohibition on the assignment of receivables with its debtors. It is prohibited for a VIRS to agree to insert an anti-assignment clause in any contract generating receivables between the VIRS and account debtors. Contractual prohibition on the assignment of VIRS receivables is not effective.<sup>478</sup>

If a receivable is assigned to a VIRS properly and effectively, the assignment to the VIRS itself means that the receivable is transferable and there is not an anti-assignment clause in the contract generating the receivable between the assignor and the account debtor.

However, let us suppose a case in which there is an anti-assignment clause in the contract generating the receivable between the assignor and the account debtor, and a VIRS purchased the receivable without notice of the anti-assignment clause and subsequently assigned the receivable to a third party. Later, if the assignment of the receivable from the assignor to the VIRS is invalidated on account of the anti-assignment clause according to the applicable national law in the jurisdiction,<sup>479</sup> consequently the

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<sup>478</sup> Draft IRSAR Convention, art 20(1). See 327

<sup>479</sup> Under English Law and under the Dutch Civil Code and the German Civil Code, the assignment of receivables is invalid when there is an anti-assignment clause. In *Barbados Trust Co Ltd v Bank of*

assignment of the receivable from the VIRS to a third party also becomes invalid. As a result, the registration of the assignment from the VIRS to a third party becomes false registration. Then, a fine will be imposed upon the VIRS. When purchasing a receivable, a VIRS must investigate whether there is an anti-assignment clause in the contract generating the receivable. It is the duty of a VIRS, and therefore if a VIRS did not find an anti-assignment clause, the VIRS is deemed as negligent.

Let us suppose another case in which there is an anti-assignment clause in the contract generating a receivable between an ordinary company and its account debtor, and later the company registered itself as a VIRS with the IRSAR Registrar, and then the company, after having become a VIRS, assigns the receivable to a third party. Under the proposed IRSAR Convention, the anti-assignment clause made by a company and its account debtor becomes ineffective after the VIRS registration of the company.<sup>480</sup> Even if there is an anti-assignment clause made by a company and its account debtor before the VIRS registration of the company, the assignment of the receivable of the company after the VIRS registration of the company is valid, but the VIRS must compensate damages due to the assignment to the account debtor who relied upon the anti-assignment

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*Zambia*, however, the English Court of Appeal opened an effective way for a party in position of an assignee to circumvent the block of an anti-assignment clause and sue a debtor joining the creditor (purported assignor) as a defendant (the so-called *Vandepitte* procedure), if the creditor makes a declaration of trust in favour of the purported assignee. *Barbados Trust Co Ltd v Bank of Zambia* [2007] EWCA Civ 148, (2007) 9 ITELR 689 (CA); *Vandepitte v Preferred Accident Insurance Corp of New York* [1933] AC 70 (PC). Under the German Commercial Code (HGB), UCC Article 9, the Saskatchewan PPSA, the UN Receivables Convention and the UNIDROIT Convention on International Factoring (Ottawa, 28 May 1988) and according to the French case law, the assignment of receivables is valid in spite of an anti-assignment clause. Under the Korean Civil Code and the Japanese Civil Code, it depends on whether the assignee knew of the anti-assignment clause when the assignee concluded the assignment agreement. If he knew of the anti-assignment clause, the assignment of receivables is invalid. If he did not know of the anti-assignment clause, the assignment of receivables is valid. For more information, see Woo-Jung Jon, 'A Comparative Analysis of the Regulations on Anti-assignment Clauses' (University of Oxford, Faculty of Law, MSt dissertation 2008) 55-68.

<sup>480</sup> Draft IRSAR Convention, art 20(2). See 327

clause.<sup>481</sup> This is to protect the assignees' trust or expectation that a VIRS cannot have an anti-assignment clause. Thus, the assignment of VIRS receivables is valid and effective regardless of whether there is an anti-assignment clause made before the VIRS registration of the assignor company.

#### **4-9. CONCLUSION OF PART 4**

The registration system may be created as optional or compulsory. Optional registration brings about the situation where a potential assignee needs to check both the IRSAR and national laws and perfection methods e.g. registry or notice to the debtor. The Korean Security Registration Act and the Japanese Assignment Registration Act use optional registration between the registration and Civil Code perfection. In one country it might be practicable to check both the registry and enquire of account debtors. However, in an international level, it would be impracticable because the would-be assignee should check all of the national registries since a potential hidden competing assignee might be in any country. This could defeat the object of international registration.

For this reason, the IRSAR is designed as compulsory registration which prevails over national perfection. However, it requires limitation of the scope of application, because otherwise all assignments of and security interests in receivables, domestic or international, must be registered in the IRSAR, which would be too large to manage at reasonable cost whilst keeping the registration fee at an affordable level.

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<sup>481</sup> Draft IRSAR Convention, art 20(3). See 327

The proposed IRSAR Convention confines its scope of application by defining the assignor or the security provider and inventing the concept of 'VIRS'. The proposed IRSAR Convention applies where the assignor or security provider is a VIRS. The proposed IRSAR Convention applies to the assignment of receivables where the assignor is a VIRS and security interests in receivables where the security provider is a VIRS.

Under the proposed IRSAR Convention, an intending assignee would have to investigate first whether the assignor is a VIRS and second whether there is any prior registration against the VIRS in the IRSAR. A potential assignee or secured creditor of receivables would first have to investigate whether its counterparty is a VIRS or not. Anyone would be able to investigate whether a company is a VIRS in the list provided on the IRSAR website. If the State where a company is registered is a Contracting State of the proposed IRSAR Convention, the company may be a VIRS.

The IRSAR would accelerate international assignments of receivables from a VIRS or between VIRSs in different jurisdictions. Insofar as an assignee or a secured creditor is also a VIRS, the sequence of assignments or security interests would be automatically traced by the IRSAR system. If an assignee or a secured creditor is not a VIRS, the sequence of assignments or security interests cannot be recorded in the IRSAR any further. In that case, one should consult national registries or perfection methods under the applicable national laws. Within national boundaries, the applicable national laws would regulate receivables transactions. Even in that case, the IRSAR would function as a useful bridge to cross national borders.



## **PART 5. PRIORITY RULES UNDER THE PROPOSED IRSAR CONVENTION**

### **5-1. INTRODUCTION**

Part 5 analyses priority rules with respect to assignments of and security interests in receivables under the proposed IRSAR Convention. Chapter 5-2 examines perfection in the event of insolvency the assignor or the security provider. Chapter 5-3 analyses priority by the order of registration (Section 5-3-1). It also explains that knowledge of an unregistered assignment or security interest has nothing to do with priority and perfection under the proposed international convention (Section 5-3-2), and that registration has nothing to do with effectiveness against the debtor of the receivable and for the latter notice to the debtor is required (Section 5-3-3).

Priority rules under the proposed IRSAR Convention in the following four situations are examined. There are four possible combinations of multiple assignments and security interests: double assignments (Section 5-3-6); an assignment and subsequent security interest (Section 5-3-5); a security interest and subsequent assignment (Chapter 5-4); and double security interests (Section 5-3-7).

Furthermore, Part 5 solves problems with respect to the double debtor problem, floating charges, reservation of title, preferential creditors, proceeds, bonds and subordination agreements, and proposes recommendable rules for the proposed IRSAR Convention. Chapter 5-4 solves the double debtor problem. Chapter 5-5 explains floating security interests under the proposed IRSAR Convention. Chapter 5-6 explores reservation of title. Chapter 5-7 explain the ranking of preferential creditors under the

proposed international convention. Chapter 5-8 clarifies that a security interest registered in IRSAR covers separated and identifiable proceeds. Chapter 5-9 shows that the IRSAR could facilitate international bond transactions. Chapter 5-10 explains the effectiveness of subordination agreements under the proposed international convention.

## **5-2. PERFECTION**

An assignment of and security interest in VIRS receivables is perfected against third parties by IRSAR registration. In the event of a VIRS insolvency, an assignee or secured creditor registered in the IRSAR retains priority over the insolvency representative of the VIRS. Registration prior to the commencement of insolvency proceedings against a VIRS would perfect the assignment or security interest against the insolvency representatives and other creditors of the VIRS. Assignees would have a right in the assigned receivables regardless of the higher priority of preferential creditors such as tax claims and labour claims in accordance with the national insolvency law. This is because upon registration in the IRSAR, the receivables are assigned to the assignee and hence are no longer the property of the VIRS.

With respect to a security interest in VIRS receivables, in the event of the VIRS insolvency, secured creditors registered in the IRSAR would be treated as secured creditors under the applicable national laws.

An assignment of (or security interest in) VIRS receivables which is not registered in the IRSAR is valid between the VIRS and the assignee (or between the

VIRS and the secured creditor) since registration is a perfection requirement for an assignment and a security interest, but not perfected against third parties including the insolvency representative.

## **5-3. PRIORITY**

### **5-3-1. Priority by Order of Registration**

Where the assignor or security provider is a VIRS, priority between its assignments or security interests would be governed by the proposed IRSAR Convention and hence determined by order of IRSAR registration. Under the proposed IRSAR Convention, the assignment of (or security interest in) a receivable registered in the IRSAR has priority over any other assignment of (or security interest in) a receivable subsequently registered in the IRSAR and over any other assignment of (or security interest in) a receivable that is not registered in the IRSAR, even though the assignment (or security interest) has been perfected under the applicable national laws.

IRSAR registration would override perfection under the applicable national laws. Priority under the proposed IRSAR Convention is irrelevant to registration in a national registry. For example, the priority of a foreign investment company could be secured once the assignment is registered in the IRSAR regardless of domestic perfection. Domestic courts in the Contracting States should accept IRSAR registration as perfection for domestic purposes.

An intending assignee or secured creditor could register its assignment or security interest in the IRSAR in order to secure priority over any other assignments or security interests, subsequently registered or not registered in the IRSAR. The assignment of a VIRS receivable<sup>482</sup> or a security interest in a VIRS receivable must be registered in the IRSAR in order to protect its priority.

The sanction for failing to do registration is loss of priority against other security interest holders. Even if not registered in the IRSAR, an assignment of or security interest in a VIRS receivable is still valid under the applicable national laws. If either of the interests is registered in the IRSAR, it would have priority over the other, notwithstanding the order of perfection under the applicable national laws. The assignment of a VIRS receivable or a security interest in a VIRS receivable, registered in the IRSAR, would have priority over a prior assignment or security interest if the prior assignment or security interest was not registered in the IRSAR. Any assignment of or security interest in VIRS receivables that is not registered in the IRSAR may not be asserted against a registered assignee or secured creditor.

If there are two security interests not registered in the IRSAR, priority between them is determined by the applicable national laws.

### **5-3-2. Knowledge of an Unregistered Assignment or Security Interest**

Knowledge of an unregistered assignment or security interest is irrelevant with regard to priority. A registered assignment or security interest has priority over an earlier

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<sup>482</sup> In this thesis, a 'receivable of a VIRS' is referred to as a 'VIRS receivable'.

unregistered assignment or security interest even if this was known to the registered assignee or secured creditor at the time of registration. It is to encourage assignees and secured creditors to register their assignments of and security interests in receivables as soon as possible. In addition, it is to avoid factual disputes as to whether the later assignee or secured creditor did or did not know of the earlier unregistered assignment of or security interest in a receivable.<sup>483</sup>

### **5-3-3. Registration has Nothing to do with Effectiveness against the Debtor**

Even if an assignment of a VIRS receivable is registered in the IRSAR, before the debtor of the receivable receives notice of the assignment, the assignee cannot sue and collect the receivable from the debtor of the receivable and conversely the debtor may discharge the debt by paying the original creditor (VIRS) that is an assignor.

It is noticeable that IRSAR registration is only for perfection against third parties and not for effectiveness against the debtor of the receivable. To perfect an assignment of a receivable against the debtor of the receivable notice of the assignment to the debtor is required in all jurisdictions. Even in jurisdictions with a registration system for the assignment of receivables, registration of an assignment of a receivable or a security interest in a receivable in the IRSAR has nothing to do with effectiveness of the assignment or the security interest against the debtor of the receivable.

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<sup>483</sup> The Cape Town Convention takes the same approach. Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008) 224 [4.183].

For example, suppose that a VIRS ('V') assigned its receivables against D to E, and registered the assignment in the IRSAR. The relationship between E and other competing assignees is different from the relationship with D. Thus, even if V's assignment to E is registered in the IRSAR, if D does not receive notice of the assignment, D may still discharge the debt by paying V.

This is because a debtor does not have to continuously check the register. Registration does not allow an assignee to sue the debtor of the receivable directly. There is no duty for a debtor to check the IRSAR before paying a debt to a VIRS. If it is assumed that an assignee could accomplish perfection even against a debtor of a receivable by IRSAR registration, a debtor would always have to search the IRSAR before paying a debt to a VIRS to confirm who to pay. Checking the IRSAR takes time. If a debtor might delay paying the debt while checking the IRSAR, the debtor would be liable for damages of the VIRS for the delay in payment after a due date. As such, if the law might require a debtor to check the IRSAR to determine who should be paid each time a payment is due, it would be unduly harsh on debtors. Furthermore, consumer debtors of auto loans or credit card receivables are usually unaware of registrations in the IRSAR.

#### **5-3-4. Priority between Registration and Notice to the Debtor**

There is a problem with respect to the relationship between registration of an assignment of a receivable and giving notice of an assignment to the debtor of the receivable in the double assignments situation where the first assignment of a receivable

is registered in the IRSAR and the second assignment of the same receivable is subsequently registered in the IRSAR, but the debtor of the receivable is notified of the second assignment prior to the first assignment and pays the second assignee.

In case X assigned his receivable to Y1 and Y1 registered the assignment in the IRSAR (but Y1 did not give notice to the debtor of the receivable), and later X assigned the same receivable to Y2 for the second time and Y2 gave notice to the debtor of the receivable, the debtor of the receivable only have to pay Y2 (who gave notice first) and will be discharged of the receivable.

However, between Y1 and Y2, according to the rule that priority is determined by the order of registration, Y1 should have priority. Then, whether Y1 can claim against Y2 for unjust enrichment is the issue to be settled. Such a problem occurs because as for receivables, effectiveness against the debtor of the receivable is different from perfection against third parties, which determines priority.<sup>484</sup>

Between the two assignments, the first assignment has priority over the second assignee since priority is determined by the order of IRSAR registration. The second assignee cannot be a *bona fide* purchaser for value without notice because the second assignee should have checked the IRSAR before the assignment of the receivable if the assignor is a VIRS.

Under the proposed IRSAR Convention, a debtor of a VIRS need not pay any purported assignee of a VIRS receivable without presenting registration of the assignment of the VIRS receivable in the IRSAR. If the debtor of the receivable might

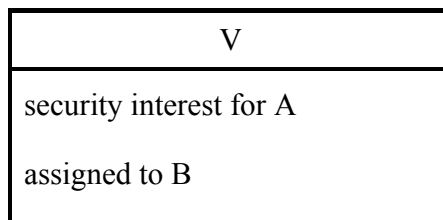
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<sup>484</sup> As for movable assets, effectiveness is only sole effectiveness against third parties, and there is not any equivalence of effectiveness against the debtor of the receivable.

mistakenly pay the second assignee even though the debtor has received notice of the second assignment without registration of the assignment in the IRSAR, the second assignee would have to yield the proceeds collected from the debtor to the first assignee. However, even though the assignee who first registered his assignment can claim for the proceeds that the subsequent assignee has received from the debtor of the receivable, this procedure would be burdensome. It is recommended that an assignee who has registered his assignment had better also give notice of the assignment to the debtor of the receivable as soon as available.

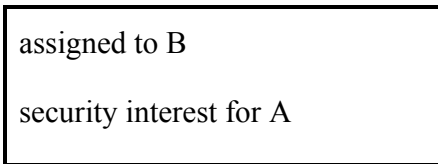
### **5-3-5. Priority between Assignments & Security Interests**

Under the IRSAR Convention, priority between assignments of and security interests in a VIRS receivable is determined by the order of registration in the IRSAR.

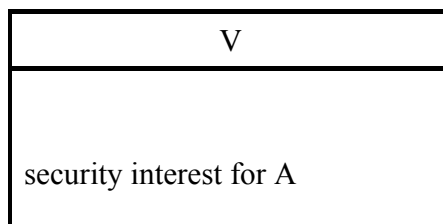


If in the IRSAR, a security interest is registered first and subsequently an assignment is registered, it causes the so-called 'double debtor problem' which will be analysed in detail in Chapter 5-4.





In reverse, if an assignment is registered first and subsequently a security interest is registered in the IRSAR, priority between B and A is determined by the order of registration, and thus B has priority over A. The assignment to B may be either absolute or by way of security. If the assignment to B is an absolute assignment, the VIRS no longer has a right to the assigned receivable and as a consequence cannot create a security interest in the receivable for A. On the other hand, if the assignment to B is by way of security for less than the full value of the assigned receivable, the VIRS may legitimately create a security interest for A.



If the absolute assignment to B, though first in time, is not registered in the IRSAR, then A has priority: this is an exception to the *nemo dat quod non habet* rule brought about by the rules of the IRSAR.

If a prior assignment is an equitable assignment in English law without giving notice to the debtor, since an equitable assignment is not perfected against third parties (even though it is perfected against the insolvency representative of the VIRS), a prior equitable assignment does not have priority over a subsequent assignment registered in the IRSAR.

Where a company registers itself as a VIRS in the IRSAR Registrar, if an absolute assignment of a receivable is not registered in the IRSAR but was perfected under the applicable national law prior to the VIRS registration of the company, the absolute assignment is valid<sup>485</sup> and any subsequent security interest in the receivable registered in the IRSAR is invalid, leading to the result that the IRSAR registration of such security interest is false registration and thus the VIRS will be sanctioned.<sup>486</sup>

If neither an assignment of nor a security interest in a VIRS receivable is registered in the IRSAR, applicable national laws will determine priority between the assignment and the security interest.

### **5-3-6. Double Assignments by a VIRS**

#### **5-3-6-1. Double Assignments by a VIRS**

If a VIRS assigns its receivables to an assignee and later to another assignee, priority between the two assignments would be determined by the order of IRSAR registration. The assignee first registered in the IRSAR would be the assignee of the receivable; any subsequent assignee registered in the IRSAR would not. The assignee first registered in the IRSAR would obtain 100% of the right in the receivable; any other assignee subsequently registered in the IRSAR would obtain none.

Before the assignment of a VIRS receivable, the potential assignee would check the IRSAR under the VIRS. If there is a prior assignment of the receivable registered in

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<sup>485</sup> See Section 4-6-4

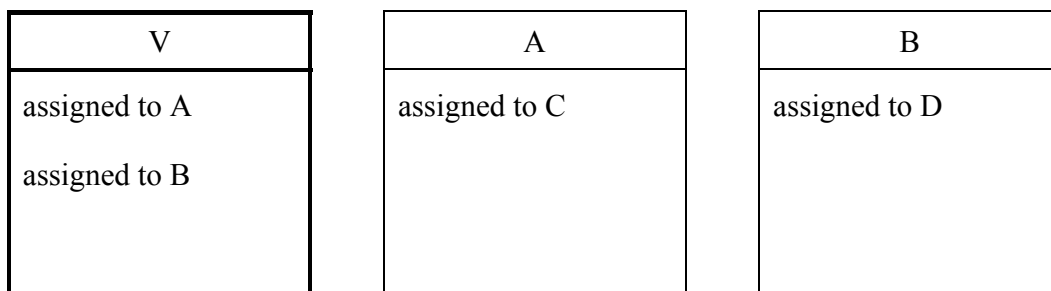
<sup>486</sup> See Section 4-6-5

the IRSAR under the VIRS, the potential assignee would not agree to the assignment of the receivable. As a result, if the assignment of a receivable or a group of receivables is registered in the IRSAR under a VIRS, no further assignment would be registered for the same receivable or for the same group of receivables under the same VIRS.

If more than one assignment of the receivable is mistakenly registered in the IRSAR under a VIRS, the assignment that is registered first in time is valid; the other assignments are invalid. Therefore, if the debtor of the receivable is notified of a subsequent assignment and pays the assignee of the subsequent assignment, the latter must give the proceeds received from the debtor of the receivable to the assignee of the first assignment.

### 5-3-6-2. Double Assignments by a VIRS and Subsequent Assignments by the Assignees

Assignments of a receivable may be continued. An assignee of a receivable may assign the assigned receivable to a third party. For example, a receivable may be assigned from V to A and then from A to C. Where V is a VIRS, A's priority is determined by the order of IRSAR registration. C retains the priority of A. C's priority is A's priority.



If two assignments are registered in the IRSAR over the same Receivable of V, the first in favour of A and the second in favour of B, and subsequently A assigns the receivable to C and B assigns the receivable to D, A has priority over B because A's registration is prior to B's registration in the IRSAR. As a result, A is the assignee of the receivable, but B is not the assignee of the receivable. A can assign the receivable to C, but B cannot. Thus, C is an assignee of the receivable, but D is not, whether or not the assignment from A to C was registered in the IRSAR.

Still, C should perfect the assignment under the applicable national law if A is not a VIRS<sup>487</sup> (or register the assignment of the receivable from A to C in the IRSAR if A is a VIRS), not to protect itself against other assignees or secured creditors of V but to secure protection against other assignees or secured creditors of A with respect to the receivable.

It is noticeable that priority between C and D is not determined by the order of perfection under applicable national laws even though A, B, C and D are not VIRSs. For example, under the English law, the assignment of the receivable from A to C and that from B to D can be perfected against third parties by giving notice of the assignment to the debtor of the receivable.<sup>488</sup> However, priority between C and D is not determined by the order of notice to the debtor of the receivable, but it is determined by the priority between A and B. It is because C and D are not the assignees from the same assignor. A and B are the competing assignees from the same assignor V.

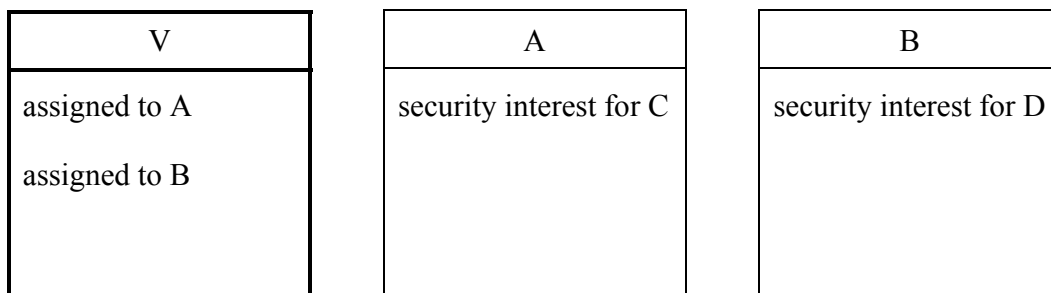
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<sup>487</sup> If A is not a VIRS, the assignment from A to C cannot be registered with the IRSAR.

<sup>488</sup> *Dearle v Hall* (1828) 3 Russ 1.

### 5-3-6-3. Double Assignments by a VIRS and Subsequent Security Interests by the Assignees

The same rule applies where a VIRS ('V') assigned its receivable to an assignee and subsequently the assignee creates a security interest in the assigned receivable for his creditor. For example, V assigned its Receivable to A and then A creates a security interest in the receivable securing a debt to C. Now C has a security interest in the receivable securing a debt to C. Now C has a security interest in the receivable. A's priority is determined by the order of registration in the IRSAR. C retains the priority of A. The priority of C is the priority of A.



If two assignments are registered in the IRSAR over the same Receivable of V, the first in favour of A and the second in favour of B, and later A created a security interest in the receivable for C and B created a security interest in the same Receivable for D, A has priority over B because A's registration is prior to B's registration in the IRSAR. As a result, A is the assignee of the receivable, but B is not the assignee of the receivable. A can create a security interest in the receivable securing his debt to C up to the value of the receivable, but B cannot create any interest in the receivable for D. Therefore C has a security interest in the receivable and D has not, regardless of whether C's security interest in the receivable of A as a security provider was registered or not.

Still, C should perfect his security interest under the applicable national law if A is not a VIRS<sup>489</sup> (or register his security interest in the receivable in the IRSAR if A is a VIRS), not to protect itself against other assignees or secured creditors of V but to secure protection against other assignees or secured creditors of A with respect to the receivable.

### **5-3-7. Double Security Interests created by a VIRS**

#### **5-3-7-1. Double Security Interests created by a VIRS**

If a VIRS creates first one, then another a security interest in the same receivable, priority between the two security interests is determined by the order of IRSAR registration. After satisfying the debt to the first-registered secured creditor from the proceeds of the receivable, the second-registered secured creditor may satisfy its debt from any remainder.

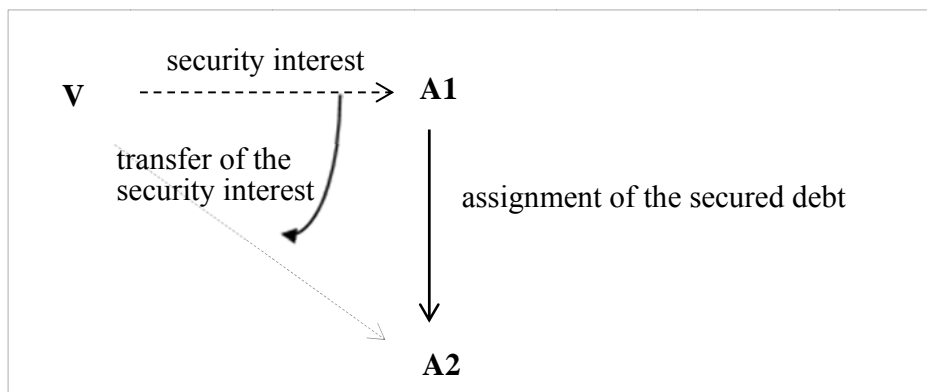
#### **5-3-7-2. Security Interests by a VIRS Following Assignments of Secured Creditors**

A security interest in a receivable cannot be transferred to a third party separately from the secured debt for which the security interest is intended. However, a security interest in a receivable may be transferred to an assignee, following the assignment of the right to the secured debt for which the security interest is intended, according to the

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<sup>489</sup> If A is not a VIRS, C's security interest in the receivable of A (A as the security provider and C as the secured creditor) cannot be registered with the IRSAR.

parties' agreement. Where a debt is secured by a debtor's receivable, if the creditor has assigned the right to the debt to an assignee, the assignee will have the right to the debt as well as the security interest in the receivable securing the debt according to the parties' agreement. That means there are two assignments: first, the assignment of the secured debt and second, the assignment of the security interest in the receivable.



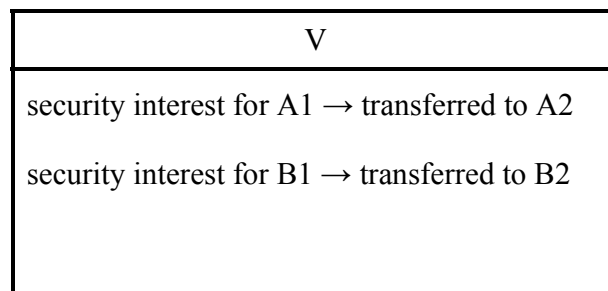
Let us take the following example. A VIRS ('V') has a receivable against its account debtor, and V owes a debt to A1. V provides a security interest in its receivable for A1, and registers A1's security interest in the receivable in the IRSAR. There are two receivables: the receivable and the secured debt. Subsequently, A1 assigns the secured debt to assignee A2 together with the security interest in the receivable securing the debt. The assignment of the secured debt from A1 to A2 cannot be registered in the IRSAR if A1 is not a VIRS. Nevertheless, the transfer of the security interest in the receivable can be registered in the IRSAR under V. Under the proposed IRSAR Convention, the transfer of a registered security interest can be registered in the IRSAR.<sup>490</sup> If more than one transferee claim that the security interest registered in the IRSAR was transferred to

<sup>490</sup> Draft IRSAR Convention, art 8(1). See 320

themselves, priority between the competing transferees is determined by order of registration of the transfer of the security interest in the IRSAR.<sup>491</sup>

With respect to V's other potential assignees or secured creditors, A2 can assert the priority of A1's security interest registered in the IRSAR if A2 can effectively prove the fact that A1 transferred the security interest to A2. Registration of the transfer of the security interest from A1 to A2 can evidence the fact.

### 5-3-7-3. Double Security Interests created by a VIRS Following Assignments of Secured Creditors



If two security interests are registered in the IRSAR over a VIRS receivable, in favour of A1 and B1, respectively, and A1 assigns the right to the secured debt (owed by V to A1) to A2 together with the security interest in the receivable, and B1 assigns the right to the secured debt (owed by V to B1) to B2 together with the security interest in the same receivable, A2's security interest in the receivable has priority over B2's security interest in the receivable, whether or not A2's security interest was registered in the IRSAR.

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<sup>491</sup> The Cape Town Convention follows the same logic. Cape Town Convention, art 35.

Under the proposed IRSAR Convention, the transferred security interest retains its original priority, i.e. the transferee of a security interest retains the transferor's priority.<sup>492</sup> The Cape Town Convention also stipulates that each assignee enjoys the same priority as its assignor.<sup>493</sup> Thus, the priority of A2's security interest is determined by the order of registration of A1's security interest in the IRSAR. A2 retains A1's priority, once A1's security interest has been registered in the IRSAR.

In the case above, A1's security interest in the receivable has priority over B1's security interest in it, since A1's interest was registered in the IRSAR prior to B1's, i.e., B1's security interest is subordinated to A1's. The transferred security interest retains its original priority. The transferee of a security interest retains the transferor's priority. As a result, A2's security interest in the receivable has priority over B2's. B2's security interest is subordinated to A2's.

Moreover, A2 should perfect the assignment of the secured debt from A1 to A2 in accordance with the applicable national laws if A1 is not a VIRS (or if A1 is a VIRS, A2 should register the assignment of the secured debt from A1 to A2 in the IRSAR.), in order to secure protection against any of A1's potential assignees, to whom A1 might assign the right to the secured debt owed by V together with the security interest in the receivable.

The same rule applies where a security interest in a receivable is transferred to a third party by legal or contractual subrogation. For example, the person who discharges

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<sup>492</sup> Draft IRSAR Convention, art 8(2). See 320

<sup>493</sup> Cape Town Convention, art 31(1)(b). Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008), 81 [2.141]

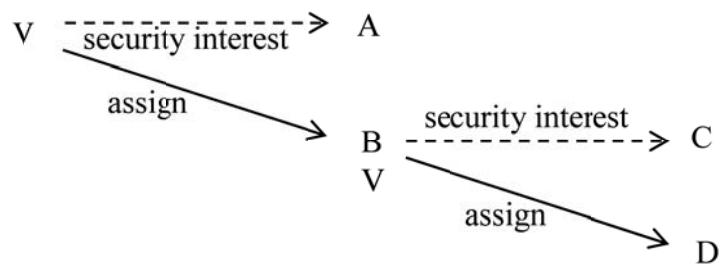
the debt owed by a debtor instead of the debtor itself takes over the security interest securing the debt held by the creditor.

#### 5-3-7-4. Security Interest created by a VIRS and Subsequent Security Interest by the Secured Creditor

Under the IRSAR Convention, it is not possible to create a security interest in a security interest in a receivable.

### 5-4. DOUBLE DEBTOR PROBLEM

#### 5-4-1. Security Interest & Subsequent Assignment

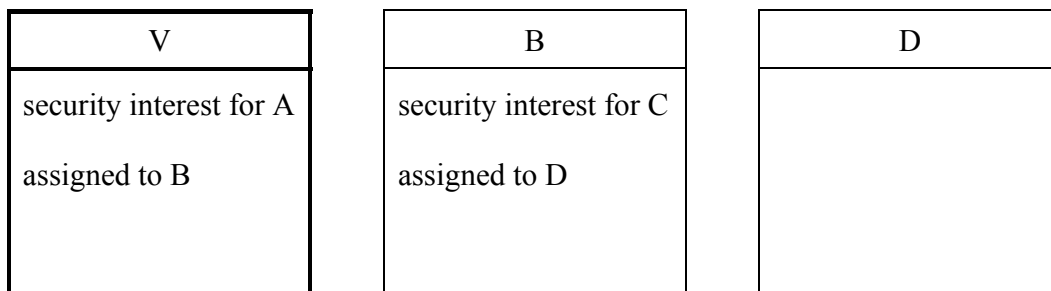


Let us take a VIRS ('V') that provides a security interest in its Receivable to A and registers the security interest in the IRSAR. V then assigns the receivable to B and registers the assignment in the IRSAR. A's security interest in the receivable has priority over B's right to the receivable since A's security interest was registered in the IRSAR prior to B's assignment. B should have checked the IRSAR because V is a VIRS, and registers the assignment in the IRSAR.

therefore B knew or should have known that A's security interest attached to the receivable. Thus, B's right to the receivable is subject to A's security interest.

Let us suppose that a VIRS created a security interest in its receivable and registered the security interest in the IRSAR and subsequently assigned the receivable and registered the assignment in the IRSAR. If the security interest in the receivable might continue to be perfected even after the receivable is assigned to a third party, the assignee of the receivable might take the receivable subject to the security interest of another creditor previously registered in the IRSAR.

If a security interest in a VIRS receivable registered in the IRSAR might become unperfected after the receivable is assigned to a third party, the validity of a security interest were to be invalidated and terminated by any subsequently registration of assignment of the receivable. Then, the security interest in the receivable could not be protected.



A problem arises where B assigns the receivable to D. According to the *nemo dat quod non habet* rule that a transferee cannot obtain more rights than the transferor had, D would obtain the receivable subject to A's security interest just as B did. If B is not a VIRS, the assignment from B to D is perfected under the applicable national laws, and therefore D would not need to check the IRSAR. If B provided a security interest in the

receivable for C, the priority between C and D would be determined by the applicable national law, hence C would be protected against D if C had completed the perfection of the security interest under the applicable national law. The question then arises, how can D know that the receivable is subject to A's security interest registered in the IRSAR? Such a problem is referred to as 'double debtor problem' since there are two debtors, an old debtor (V) and a new debtor (B) creating security interests in the same asset. Whether D or A should be protected is a problem.<sup>494</sup>

These problems have their origin in the assignor (or security provider)-based registration system. The IRSAR is indexed by the VIRS. In comparison, the International Registry of Mobile Assets under the Cape Town Convention and its Aircraft Protocol does not have such problems since it is an asset-based system in which each aircraft or other mobile asset is indexed separately.<sup>495</sup> Thus, a would-be buyer of an aircraft can see all records of security interests in a specific aircraft and check whether there is any prior security interest in the aircraft by searching the Registry against the aircraft.<sup>496</sup>

The question is how far the security interest in the receivable registered in the IRSAR should continue to be perfected after the receivable is assigned again and again to third parties away from the VIRS and the IRSAR? There are four options to solve the double debtor problem: the first option is that B and subsequently D take the receivable

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<sup>494</sup> This is the double debtor problem about which there is considerable literature in the US and in the PPSA jurisdictions. Jonathan C. Lipson (ed), *Forms Under Revised Article 9* (American Bar Association 2002) 37-39; Gerard McCormack, *Secured Credit Under English and American Law* (CUP, 2004) 159-61

<sup>495</sup> Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008) 50 [2.70]

<sup>496</sup> Ronald C.C. Cuming, *The International Registry for Interests in Aircraft: An Overview of its Structure* [2006] *Uniform Law Review* 45-46

free of A's security interest ('Solution I'). The second option is that B takes the receivable subject to A's security interest, but subsequently D takes the receivable free of A's security interest ('Solution II'). It requires a potential assignee to check the registry with respect to the assignor. The third option is that B and subsequently D takes the receivable subject to A's security interest ('Solution III'). The fourth option is that B takes the receivable free of A's security interest, but subsequently D takes the receivable subject to A's security interest ('Solution IV'). Solution III and Solution IV require a potential assignee to check the registry with respect to the assignor and the former assignor if the assignor purchased the receivable from the former assignor.

<Table 14> Double Debtor Problem

	A's security interest	C's security interest	D
Solution I	free of	free of	authority given by A, C
Solution II	free of	subject to	<i>bona fide</i> purchaser change of jurisdiction VIRS → Non-VIRS → Non-VIRS Non-VIRS → VIRS → VIRS
Solution III	subject to	subject to	<i>nemo dat quod non habet</i> rule VIRS → VIRS → Non-VIRS
Solution IV	subject to	free of	buyer in the ordinary course of seller's business

Sections 5-4-2 to 5-4-5 analyse how the English law, UCC Article 9 and the PPSAs, under which the registries are indexed by person and thus debtor (security provider)-based, solve this problem where a book debt over which a fixed charge is made is assigned to a third party. Then, Sections 5-4-6 to 5-4-8 present the solution of the proposed IRSAR Convention.

## 5-4-2. Actual or Apparent Authority

There are two exceptions for the validity of a security interest after the assignment of the receivable: (1) an authorised disposition and (2) a *bona fide* purchase in English law or a buyer in the ordinary course of business under the UCC Article 9 and the PPSAs.<sup>497</sup> First, if the assignor has either actual or apparent authorisation from the secured creditor having the security interest, the assignor may assign the receivable to the assignee free of the security interest. The second exception is examined in Sections 5-4-3-2 and 5-4-4-2.

If a secured creditor authorises disposition free of the security interest, the security interest does not continue in the receivable assigned to an assignee. In English law, apparent authorisation also counts. In the case of a floating charge, the chargor is held to be authorised to dispose of its assets.<sup>498</sup> Under UCC Article 9, if a secured creditor authorises the disposition, a buyer obtains the collateral free of the security interest.<sup>499</sup> However, the secured creditor's receiving the proceeds from the disposition does not in itself constitute an authorization of disposition, and whether it is an authorisation will be decided by the courts.<sup>500</sup> It takes the Solution I mentioned above.

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<sup>497</sup> It is similar but not identical to a *bona fide* purchaser because a buyer in the ordinary course of business takes free of a security interest even if the buyer knows of the existence of the security interest.

<sup>498</sup> Roy Goode and Louise Gullifer, *Goode on Legal Problems of Credit and Security* (4th edn, Sweet & Maxwell, 2008) 176 [5-05]

<sup>499</sup> UCC, s 9-315(a)(1)

<sup>500</sup> UCC, s 9-315 Official Comment [2]

### 5-4-3. English Law

#### 5-4-3-1. *Nemo Dat Quod Non Habet* Rule

Let us suppose that a company X creates a fixed charge over its receivable for its creditor A and registers the A's fixed charge in the Company Charges Register, and subsequently X assigns the receivable to a third party assignee B. Does B obtain the receivable with A's fixed charge attached? According to the *nemo dat quod non habet* rule that a transferee cannot obtain more rights than the transferor had, B should obtain the receivable subject to A's fixed charge just as X did.

In the UK, under the Companies Act 2006, *inter alia*, a charge over a receivable of a company must be registered in the Company Charges Register in order to secure validity against other secured creditors and against a liquidator or administrator.<sup>501</sup> However, in English law, priority between an assignment and a fixed charge is not determined by the order of registration in the Register of Company Charges.<sup>502</sup>

Priority is determined by *Dearle v Hall*,<sup>503</sup> according to which an assignee who is first to give notice of assignment to the debtor obtains priority over an earlier assignee or chargee that had not given notice of the earlier assignment or charge.<sup>504</sup> Thus, between A and B, whoever was first to give notice of the charge or assignment to the debtor of the

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<sup>501</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, ss 859A-G

<sup>502</sup> Registration of a fixed charge created by a company is meaningful for perfection against the insolvency representative of the company. If a fixed charge of a company is not registered in the Company Charges Register within 21 days (or such later time as is permitted by the court), it is not perfected against the insolvency representative of the company. Companies Act 2006 (Amendment of Part 25) Regulations 2013, ss 859H and 859F See Appendix II. 10 Q2

<sup>503</sup> (1828) 3 Russ 1

<sup>504</sup> Roy Goode and Louise Gullifer, *Goode on Legal Problems of Credit and Security* (4th edn, Sweet & Maxwell, 2008) 177 [5-08]

receivable has priority. Furthermore, according to the second limb of *Dearle v Hall*, if B knew of the prior fixed charge of A at the time of the assignment to B by any method, even if B gave notice of the assignment to the debtor of the receivable earlier than A gave notice of its charge to the debtor, B has no priority.

Registration of a fixed charge over a receivable in the Register of Company Charges constitutes notice to those who could reasonably be expected to search the registry except a buyer in the ordinary course of business.<sup>505</sup> Therefore the registration of fixed charges over receivables reduces the application of the *Dearle v Hall* rule in receivables financing because the second assignee will usually have notice of a prior fixed charge by virtue of the registration.<sup>506</sup> A potential assignee wishing to purchase a receivable from a company would search the Register of Company Charges against the company. Thus, B would be expected to search the Company Charges Register against company X before the receivable is assigned by X. Hence, B takes the receivable subject to A's fixed charge.

#### 5-4-3-2. *Bona Fide Purchaser*

Under English law, once a person, who does not have actual or constructive notice of a prior equitable interest, provides value and acquires a legal interest, takes

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<sup>505</sup> *ibid* 92 [2-29]

<sup>506</sup> *ibid* 177 [5-08]

priority over the holder of the prior equitable interest.<sup>507</sup> This doctrine is often called the ‘*bona fide* purchaser’ rule.<sup>508</sup>

If B assigns the receivable to D, according to the *nemo dat quod non habet* rule, D should take the receivable subject to A’s fixed charge just as B did. However, a chargee is postponed to a subsequent *bona fide* assignee who acquires the receivable in good faith without notice of the prior fixed charge.<sup>509</sup>

If D is a *bona fide* purchaser for value without notice, the assignee takes the receivable free of any charge. When B purchases the receivable from X, B has the obligation to check the registry before purchasing the asset. If B has not checked the registry, B would be regarded as negligent, meaning B cannot be a *bona fide* purchaser.<sup>510</sup>

Furthermore, if B assigns the receivable to another assignee D, D would be expected to search the Register of Company Charges with respect to B, but not against X. D could not find the record of A’s fixed charge by searching B’s registration record, since A’s fixed charge is registered against X. Therefore A’s fixed charge which is registered under X does not constitute notice to D. Thus, D takes the receivable free of A’s fixed charge, if D gave notice of the assignment to the debtor of the receivable before A gave

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<sup>507</sup> *Pilcher v Rawlins* (1872) LR 7 Ch App 259, 268-89; *Heath v Crealock* (1874) LR 10 Ch App 22, 29-30; *Joseph v Lyons* (1884) 15 QBD 280 (CA); *Hallas v Robinson* (1885) 15 QBD 288 (CA), 292-93; *Taylor v London and County Banking Company* [1901] 2 Ch 231 (CA), 256; *Re Diplock* [1948] Ch 465 (CA).

<sup>508</sup> Hugh Beale, Michael Bridge, Louise Gullifer and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) 434 [13.01].

<sup>509</sup> Roy Goode and Louise Gullifer, *Goode on Legal Problems of Credit and Security* (4th edn, Sweet & Maxwell, 2008) 193 [5-35]

<sup>510</sup> Notwithstanding, if Y is a purchaser in the ordinary course of business, Y does not have the duty to check the registry.

notice of its charge to the debtor. Then, A would lose his fixed charge and registration of A's fixed charge under X would become of no use. It takes the Solution II mentioned above.

#### **5-4-4. UCC Article 9, PPSAs**

##### **5-4-4-1. Taking Subject to Perfected Security Interest**

Under UCC Article 9, both security interests in receivables and assignments of receivables must be filed in the UCC Article 9 filing system in order to preserve priority. Priority of competing assignees and secured creditors is determined by the order of filing under UCC Article 9.<sup>511</sup> If collateral in which a secured creditor has a security interest perfected by filing under the law of the jurisdiction of the location of the debtor is transferred to a third party, the filing remains effective inside the same jurisdiction and the security interest continues in the collateral.<sup>512</sup> A security interest continues in collateral notwithstanding sale or other disposition thereof.<sup>513</sup>

If X sells an asset to B not in the ordinary course of business, under UCC Article 9, B acquires the asset subject to A's security interest, and C's security interest is subordinate to A's security interest. It is because C could have investigated the source of the asset and discovered A's filing before making an advance against the asset,<sup>514</sup>

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<sup>511</sup> UCC, s 9-322

<sup>512</sup> UCC, s 9-507(a) Jonathan C. Lipson (ed), *Forms Under Revised Article 9* (American Bar Association 2002) 37

<sup>513</sup> UCC, s 9-315(a)(1)

<sup>514</sup> Stephen L. Sepinuck (ed), *Practice Under Article 9 of the Uniform Commercial Code* (2d edn, ABA UCC Committee 2008) 438

whereas A could not search for filing against B since B's existence and identity at that stage was purely hypothetical.<sup>515</sup> Likewise, D takes the receivables subject to A's security interest. It takes the Solution III mentioned above.

In Canada, New Zealand and Australia, according to the *nemo dat quod non habet* rule, D takes the receivable subject to A's security interest.<sup>516</sup> It also takes the Solution III.

#### 5-4-4-2. Buyer in the Ordinary Course of Business

However, under UCC Article 9 and the PPSAs, there are two exceptions: (1) buyers in the ordinary course of business<sup>517</sup> and (2) interstate transactions changing the jurisdiction.<sup>518</sup> The second exception is examined in Section 5-5-5.

Under UCC Article 9 and the PPSAs, where the selling is in the ordinary course of the seller's business a buyer in the ordinary course of business takes free of a security interest created by the seller, even if the security interest is perfected and the buyer knows of its existence.<sup>519</sup> Under the PPSAs, only knowledge of the fact that the sale constitutes a breach of the security agreement under which the security interest was created stops the purchaser taking the goods free of a security interest.<sup>520</sup> Thus, a secured creditor who has

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<sup>515</sup> Gerard McCormack, *Secured Credit Under English and American Law* (CUP, 2004) 160

<sup>516</sup> The New Zealand PPSA expressly stipulates the *nemo dat quod non habet* rule in s 88.

<sup>517</sup> UCC, s 9-320

<sup>518</sup> UCC, s 9-316

<sup>519</sup> US UCC, s 9-320(a); Ontario PPSA s 28(1); Saskatchewan s 30(2); New Zealand PPSA s 53(1); Australian PPSA s 46(1)

<sup>520</sup> Ontario PPSA s 28(1); Saskatchewan s 30(2); New Zealand PPSA s 53(1); Australian PPSA s 46(1)

his security interest perfected could be subordinated to a buyer in the ordinary course of business from a seller in the business of selling goods of that kind.<sup>521</sup>

If B is a buyer in the ordinary course of X's business, B takes the receivable free of A's security interest. Furthermore, if D is a buyer in the ordinary course of B's business, D takes the receivable free of C's security interest. However, the ordinary course of business rule only applies to the security interest created by the seller. Thus, D takes the receivable free of C's security interest, but cannot take the receivable free of A's security interest. As a result, D takes the receivable subject to A's security interest. For this reason, if it is known that the receivable under sale has been assigned by another entity to the seller, searches should be made to see whether the entity has created a security interest in the receivable.<sup>522</sup> It takes the Solution IV mentioned above.

However, there is possibility that the ordinary course of business rule does not apply to the sale of receivables since UCC Article 9 and the PPSAs only stipulates that the rule applies to the sale of goods.

### **5-5-5. Change of Jurisdiction**

Under UCC Article 9 and the PPSAs, if a receivable is transferred to a different jurisdiction, the security interest in the receivable registered in the original jurisdiction becomes unperfected unless it is re-registered in the new jurisdiction. Thus, if the

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<sup>521</sup> Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Tangibles* (Sellier 2007) 38.

<sup>522</sup> Roger Fenton, *Garrow & Fenton's Law of Personal Property in New Zealand: Volume 2 Personal Property Securities* (7th edn, LexisNexis 2010) 534 [13.3]

collateral or the debtor is moved to a different jurisdiction from that where the security interest was filed, the security interest becomes unperfected after a grace period. It basically takes the Solution II mentioned above for the case of change of jurisdiction.

In addition, UCC Article 9 and the PPSAs provides grace periods during which a secured creditor may file its security interest in the new jurisdiction and obtain priority. If the secured creditor in the original jurisdiction re-perfects its security interest in the new jurisdiction within the grace period, the security interest trumps any security interest in the new jurisdiction. Hence, there remains uncertainty during the grace period, whether an unexpected security interest might trump a security interest registered in the new jurisdiction. After the lapse of the grace period, the security interest registered in the old jurisdiction loses its effectiveness unless it is re-perfected in the new jurisdiction.

Under UCC Article 9, the grace period is one year for interstate transfer of the collateral.<sup>523</sup> The 50 states that make up the US each have their own jurisdiction. The UCC Article 9 filing systems operate independently in each of the 50 states and are not connected with each other. A potential assignee is not expected to search the UCC Article 9 filing system of another state. So, in the case of an interstate assignment of a receivable, where the assignee is located in a jurisdiction different from that of the assignor, the secured creditor has a period of one year to perfect the security interest under the law of the assignee's jurisdiction.<sup>524</sup>

Under the PPSAs, perfection continues temporarily after the transfer of the collateral to a foreign jurisdiction. In Saskatchewan, Canada and New Zealand, the

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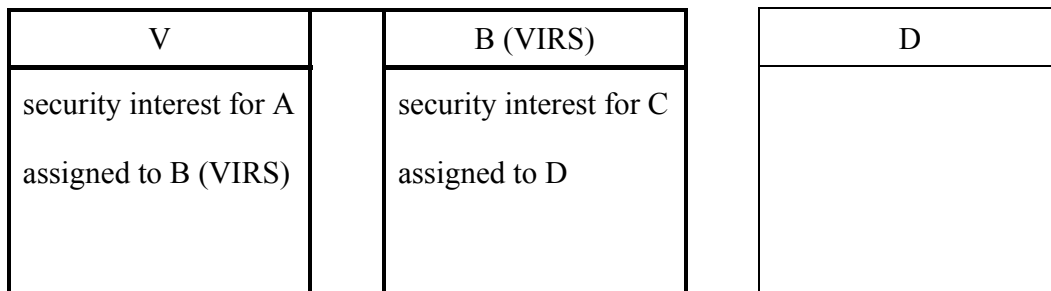
<sup>523</sup> UCC ss 9-316(a)(3) and (b)

<sup>524</sup> Jonathan C. Lipson (ed), *Forms Under Revised Article 9* (American Bar Association 2002) 37

temporary perfection period is the earlier of 60 days after the day on which the debtor transfers an interest in the collateral to a person located in the other jurisdiction or 15 days after the day on which the secured creditor has such knowledge.<sup>525</sup> In Australia, it is the earlier of 56 days after the day of the relocation or 5 business days after the day the secured creditor has actual knowledge of the relocation.<sup>526</sup>

### 5-4-6. IRSAR Jurisdiction

#### 5-4-6-1. VIRS → VIRS → non-VIRS



The proposed IRSAR Convention takes the Solution III mentioned above for the case where a VIRS assigns its receivable to another VIRS and the second VIRS assigns the receivable to a non-VIRS entity. The third option requires a potential assignee D to investigate the IRSAR against not only the assignor but also the assignor of the assignor.

If the assignor of the assignor is also a VIRS, it would not obstruct receivable transactions. If V is also a VIRS and thus the assignment from V to B is registered in the

<sup>525</sup> Saskatchewan, s 7(3); New Zealand PPSA, s 31

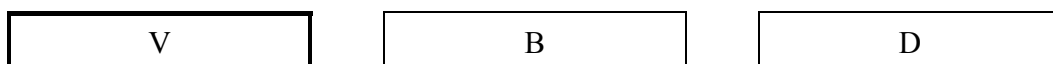
<sup>526</sup> Australian PPSA, s 40(3)(b)

IRSAR, it would be automatically linked to B's registration by the IRSAR system. Then, a potential assignee D could easily investigate any security interests created by V. If B is a VIRS, D would have to check the IRSAR under B and furthermore follow the link to V that would be automatically signposted by the IRSAR system. For this reason, D should have known or knew of the A's security interest. D would take the receivable subject to anything registered in the IRSAR under B and V.

The proposed IRSAR Convention creates a special world-wide jurisdiction where a VIRS assigns its receivables or provides a security interest in its receivables. A VIRS may trade receivables with other VIRSs, but if a VIRS assigns its receivables or provides a security interest in its receivables to a non-VIRS entity, the subsequent transactions of the non-VIRS entity are outside the jurisdiction of the proposed IRSAR Convention.

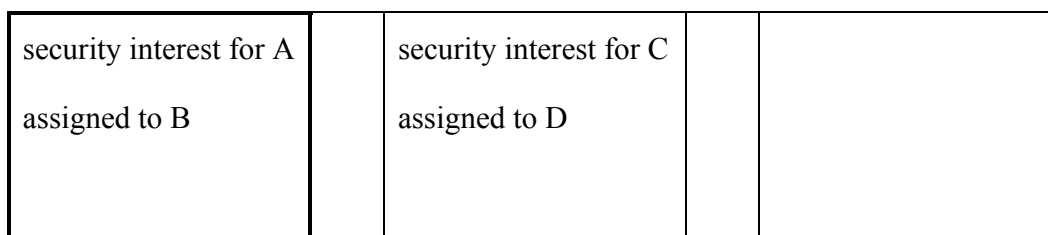
Under the proposed IRSAR Convention, if a security interest in a VIRS receivable created by a VIRS is registered in the IRSAR, the security interest continues to be perfected even after the receivable is assigned to another VIRS as far as it is continuously assigned to VIRSs and the sequence of assignments is automatically traced by the IRSAR system.<sup>527</sup> However, if the receivable is assigned to a non-VIRS entity, the security interest in the receivable registered in the IRSAR becomes unperfected unless it is re-perfected under the national law of the state where the non-VIRS entity is located.<sup>528</sup>

#### 5-4-6-2. VIRS → non-VIRS → non-VIRS



<sup>527</sup> Draft IRSAR Convention, art 16(1). See 325

<sup>528</sup> Draft IRSAR Convention, art 16(2). See 325



If a VIRS assigns its receivable to a non-VIRS entity and the non-VIRS entity assigns the receivable to a third party, the third party takes the receivable free of any security interests registered in the IRSAR. If the assignor is not a VIRS, a potential assignee or secured creditor only has to search the national registry against the direct counterparty VIRS or enquire of the account debtor, but does not have to check the IRSAR against the assignor of the assignor. If the assignor is not a VIRS, the assignee has no obligation to check the IRSAR. The purpose of the IRSAR is to facilitate international receivables financing. The proposed IRSAR Convention would eliminate any obligation to check the IRSAR which could slow down international transactions of receivables. As a result, IRSAR registration of a security interest might lose its effectiveness after two consecutive assignments of the receivable.

Let us suppose that neither B nor D is a VIRS. When B purchases the receivable from V, B must check the IRSAR. The proposed IRSAR Convention applies to V's assignment to B. However, the proposed IRSAR Convention does not require D to check the IRSAR because B is not a VIRS. The assignment from B to D is governed by the applicable national laws and therefore D must check the national registry or enquire of the account debtor. If D, purchasing the receivable from B, were required to check the IRSAR against V as well as the national registry or the account debtor, it would hamper receivable transactions. For this reason, under the proposed IRSAR Convention, D is not

required to check the IRSAR. Therefore, D should obtain the receivable free of A's security interest.

Where a receivable is assigned across national borders, the same problem occurs as in interstate assignments of receivables in the US. Let us take the case where secured creditor A registers its charge over a receivable in the Company Charge Register in the UK and subsequently the chargor assigns the receivable to a third party B, and B then assigns the receivable to an American Company D. Later, D assigns the receivable to an American Company E and registers the assignment under UCC Article 9. How can E know that the receivable is subject to A's charge?

The proposed IRSAR Convention for its part seeks to minimise that uncertainty and IRSAR registration does not provide such a grace period as under UCC Article 9 and the PPSAs.<sup>529</sup> As a result, IRSAR registration of a security interest would lose its effectiveness after two consecutive assignments of the receivable. It takes the Solution II mentioned above.

#### 5-4-6-3. non-VIRS → VIRS → non-VIRS

The same rule applies to the case where a non-VIRS entity assigns its receivable to a VIRS and the VIRS assigns the receivable to another non-VIRS entity. It is because if a potential assignee has to investigate national registry as well as the IRSAR, it would hamper receivable transactions.

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<sup>529</sup> See Section 5-5-5

V (non-VIRS)	B (VIRS)	D
security interest for A assigned to B	security interest for C assigned to D	

Let us suppose that V is a non-VIRS entity, and B is a VIRS. Under the proposed IRSAR Convention, if a potential assignee D is to purchase a VIRS receivable, it must check the IRSAR before making a transaction. Consequently D would purchase the receivable subject to the C's security interest. However, although D must check the IRSAR before purchasing the receivable from B, D has no such obligation to check the national registry where A's security interest is registered under V or enquire of the account debtor of V. Thus, D should obtain the receivable free of A's security interest. It takes the Solution II mentioned above.

If the state in which A's security interest is registered is a Contracting State and the law of the state provides the grace period, it might be declared as a non-consensual right under Article 10 of the proposed IRSAR Convention by the state.

#### **5-4-7. Secured Creditor's Right in Proceeds**

If D take the receivable free of A's security interest, A should seek the sale proceeds of the receivable that B obtains from D. A is a secured creditor of V. If V assigns the receivable to B, A retains the security interest in that receivable as well as in the sale proceeds which V obtained from B for consideration of the receivable. If B

assigns the receivable to D, A no longer owns the security interest in that receivable but only in the sale proceeds which B obtains from D for consideration of the receivable. If V assigns the receivable to B and then B assigns it to D, secured creditor A has two options: the security interest in the sale proceeds of the receivable that V obtains from B or the security interest in the sale proceeds of the receivable that B obtains from D, but only for one satisfaction of the debt which V owes A.<sup>530</sup>

In order to alert a secured creditor to the fact that its security interest might become ineffective after two consecutive assignments, the proposed IRSAR Convention requires the consent of previously registered secured creditors for the registration of the assignment of a receivable.

#### **5-4-8. Consent of Secured Creditors to Assignment to Non-VIRS**

Under the proposed IRSAR Convention, to register an assignment of a receivable to a non-VIRS entity, the assignor (VIRS) or the assignee must obtain the consent of all prior secured creditors registered in the IRSAR, who hold security interests (except floating security interests) in the receivable including the secured creditors of the former VIRS assignors, by whom the receivable is assigned to the assignor (VIRS).<sup>531</sup> Thus, if B is not a VIRS, to register the assignment of the receivable from V to B in the IRSAR, the consent of A is required.

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<sup>530</sup> See Section 5-8-3

<sup>531</sup> Draft IRSAR Convention, art 17. See 326

If B is a VIRS, to register the assignment of the receivable from B to D in the IRSAR, the consent of A and C is required. The IRSAR system would automatically indicate all prior secured creditors of the assignor (VIRS) and all secured creditors of the former VIRS assignors, by whom the receivable is assigned to the assignor (VIRS), registered in the IRSAR.

Such consent does not constitute authorisation for the VIRS to assign its receivables free of the security interest,<sup>532</sup> it is consent to assign the receivables subject to the security interest that is required for registration of an assignment in the IRSAR. When a VIRS or an assignee registers an assignment to a non-VIRS entity, the consent of all previously registered secured creditors is required.

As a result, the previously secured creditor would be notified of the assignment and accordingly know it needed to request the VIRS (i) to separate the sale proceeds from the other assets of the VIRS or (ii) to give notice of the prior security interest to the account debtor of the receivable. The security interest would extend to the sale proceeds and follow the assignment, so that the assignee obtained the receivable subject to the security interest. The secured creditor has a choice as to whether to enforce against the sale proceeds or the receivable assigned.

First, the secured creditor would have to request the VIRS to separate the sale proceeds from its other assets, for example, to open a blocked bank account into which the proceeds are deposited, since for a security interest to extend to the proceeds, the proceeds must be separated and identifiable. Under the proposed IRSAR Convention, if

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<sup>532</sup> To assign a receivable free of the security interest, the secured creditor's authorisation to waive its security interest is needed.

the proceeds are separated and identifiable, even if the VIRS obtains the sale proceeds from the assignee, the VIRS may not spend the proceeds but must retain them until the due date of the debt. If the VIRS becomes insolvent, the sale proceeds are separated from its insolvency assets so that the secured creditor can be satisfied before other creditors.<sup>533</sup>

Second, a previously secured creditor may give notice of its security interest to the account debtor of the receivable and, if the VIRS defaults, collect the receivable directly from the account debtor and satisfy the debt which the VIRS owes the secured creditor.<sup>534</sup>

## **5-5. FLOATING SECURITY INTEREST IN THE IRSAR**

### **5-5-1. Two Types of Security Interests over Receivables in the IRSAR**

#### **5-5-1-1. Characteristics of Receivables**

There is a problem with a security interest over receivables. In a company, receivables continually change into cash as account debtors pay up. Payment by the account debtors cancels the receivable and the total amount of receivables subject to the

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<sup>533</sup> See Section 5-8-4

<sup>534</sup> In English law, priority is determined by the order in which the debtor is notified of the assignment or the security interest under the *Dearle v Hall* rule. Thus, in England, a secured creditor should have given notice of its security interest to the account debtor of the receivable before the assignee did in order to collect the receivable directly from the account debtor at the default of the assignor (security provider). In the United State, under UCC Article 9, priority is determined by the order of filing of the assignment or the security interest, and even if the debtor of the receivable pays the assignee who gave notice first, the assignee should return the proceeds to the secured creditor who filed its security interest first since priority between the secured creditor and the assignee is determined by the order of filing.

security interest gradually decreases. For example, if a security interest over a receivable does not cover its proceeds, if the due date of the receivable is prior to the due date of the debt secured by the security interest over the receivable, and if the account debtor of the receivable pays the receivable before the due date of the debt secured by the security interest over the receivable, the security interest over the receivable becomes of no value. Thus, a security interest over a receivable without its proceeds is a very weak one.

#### 5-5-1-2. Practice of Financial Institutions

Broadly speaking, there are two different practices of receivables financing depending on the types of financial institution involved. On the one hand, receivables financiers, who advance against outright assignments or fixed charges, do require the proceeds as a means of repayment. They would use the normal ‘security interest’ in a receivable including its proceeds under the proposed IRSAR Convention.

On the other hand, most banks are interested in the outstanding receivables, and the security right is usually over a stream of receivables. They have little interest in the proceeds until enforcement, and are happy to let the borrower have access to them. They would use the ‘floating security interest’ over all present and future receivables under the proposed IRSAR Convention.

To reflect the practice of financial institutions, the proposed IRSAR Convention provides two types of security interest over VIRS receivables. First, a security interest in a receivable may extend to the proceeds of the receivable. Second, such decreasing amount of receivables subject to a security interest could be supplemented by future

receivables instead of or in addition to the proceeds. A VIRS could create a floating security interest over all its present and future receivables.

### 5-5-1-3. Security Interest

For the first type of security interest over a receivable, the proceeds must be separated and reasonably identifiable from any other property owned by the VIRS. Since the proceeds of a receivable are usually in cash (a receivable being a monetary claim) and since it is easy for cash to become commingled with the VIRS' other property, an assignee would be well-advised to require separation of the proceeds.

### 5-5-1-4. Floating Security Interest

Under the proposed IRSAR Convention, one way of solving the problem of dwindling amounts of receivables subject to a security interest is to create a floating security interest over all present and future receivables. A floating security interest over all present and future receivables is referred to as 'floating security interest' under the proposed IRSAR Convention<sup>535</sup> and this term will also be used in this thesis.

A floating security interest over all present and future receivables covers proceeds of receivables (both proceeds of collection and proceeds of sale, including cash or bank deposits) as far as they are held by the VIRS for the benefit of the secured creditor separately and are reasonably identifiable from the other assets of the VIRS. Although the floating charge covers the proceeds, this is not necessarily particularly valuable for

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<sup>535</sup> Draft IRSAR Convention, art 9. See 320

the chargee, since the chargor has the right to dispose of the proceeds freely. However, this will vary to some extent depending on what form the proceeds take.

## **5-5-2. Floating Security Interest v Subsequent Assignment**

### **5-5-2-1. English Floating Charge**

Under English law, once a charge has been perfected by registration, the charge has priority over subsequent charges. This applies to a fixed charge created by a company registered under the Companies Act 2006. However, a registered floating charge may still lose to a subsequent fixed charge in the race for priority.<sup>536</sup> A floating charge, by definition, allows the chargor to dispose of his assets in the course of business until some act or event occurs on the part of the chargor or the chargee causes the floating charge to crystallise into a fixed charge.<sup>537</sup> A company may continue business as usual, and the assets covered by a floating charge would change from time to time.<sup>538</sup> Thus, a fixed charge has priority over a prior floating charge. The reason why a subsequent fixed charge has priority over a prior floating charge is because the chargor has permission to create it. This applies to charges over receivables.

Since a chargor has the power to dispose of the receivables subject to a floating charge without the consent of the floating chargee,<sup>539</sup> a floating charge is subordinated to

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<sup>536</sup> Hugh Beale, Michael Bridge, Louise Gullifer and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) 330 [7.20].

<sup>537</sup> *Evans v Rival Granite Quarries Ltd* [1910] 2 KB 979 (CA), 999 per Buckley L.J.

<sup>538</sup> *Re Yorkshire Woolcombers Association Ltd* [1903] 2 Ch 284 (CA), 295 per Romer L.J.

<sup>539</sup> *Agnew v Commissioner of Inland Revenue* [2001] UKPC 28, [2001] AC 710 (PC), [32]; *Re Spectrum Plus* [2005] UKHL 41, [2005] 2 AC 680, [107]

a subsequent assignment of a specific receivable. The second limb of *Dearle v Hall*<sup>540</sup> does not apply to a floating charge. Even if a subsequent assignee had notice of the prior floating charge, the subsequent assignment trumps the prior floating charge and the subsequent assignee achieves priority over the prior floating chargee by giving notice of the assignment to the debtor of the receivable.<sup>541</sup>

#### 5-5-2-2. Security Interest in After-Acquired Property under UCC, PPSAs

The US, Canada, New Zealand and Australia have no floating charge, only security interests in after-acquired property which is subject to a *bona fide* purchaser in the ordinary course of business. Under UCC Article 9 and the PPSAs of Canada, New Zealand and Australia, a security agreement may create or provide for a security interest in all the security provider's present and after-acquired property (optionally excepting specified items or classes of personal property).<sup>542</sup> A security interest in after-acquired property makes it possible for the security interest to float on encumbered assets, the components of which are subject to change but which as a whole remains stable in identity and value.<sup>543</sup> Security interests in after-acquired property are most frequently used with regard to inventory and account receivable. A debtor continually sells some items and acquires others over time. A security interest in after-acquired property enables

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<sup>540</sup> (1828) 3 Russ 1

<sup>541</sup> *In re Hamilton's Windsor Ironworks, Ex parte Pitman & Edwards*, 187.9, 12 Ch.D. 707. Hugh Beale, Michael Bridge, Louise Gullifer and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) [14.11] fns 53, 54

<sup>542</sup> US UCC, s 9-204; Ontario PPSA s 12; Saskatchewan s 13; New Zealand PPSA ss 43 and 44; Australian PPSA ss 18(2) and (3), 20(2)(b) and 76(2)(b)

<sup>543</sup> *Stoumbos v Kilimnik*, 988 F.2d 949 (9th Cir.1993)

the parties to a long-term financing relationship to think of the collateral as the category rather than as the individual assets. A security interest in after-acquired property is also referred to as a floating lien in the United States.<sup>544</sup>

A security interest in after-acquired property is defeated by a purchaser for value in the ordinary course of the seller's business. The concept of ordinary course of seller's business was adopted to allow exceptions for a security interest in after-acquired property. If the selling is in the ordinary course of the seller's business, the purchaser takes the goods free of a security interest created by the seller.<sup>545</sup> Knowledge of the security interest does not stop the purchaser taking the goods free of a security interest. Under the PPSAs, only knowledge of the fact that the sale constitutes a breach of the security agreement under which the security interest was created stops the purchaser taking the goods free of a security interest.<sup>546</sup>

### 5-5-2-3. Floating Security Interest in the IRSAR

Under the proposed IRSAR Convention, a floating security interest over all present and future receivables of a VIRS is subordinated to the subsequent assignment of a specified receivable of the VIRS.<sup>547</sup> Let us suppose a floating security interest were not subordinated to a subsequent assignment of a specific receivable, in the case where a

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<sup>544</sup> Lynn M. LoPucki and Elizabeth Warren, *Secured Credit: A Systems Approach* (6th ed, Aspen Publishers 2009) 158.

<sup>545</sup> US UCC, s 9-320(a); Ontario PPSA s 28(1); Saskatchewan s 30(2); New Zealand PPSA s 53(1); Australian PPSA s 46(1)

<sup>546</sup> Ontario PPSA s 28(1); Saskatchewan s 30(2); New Zealand PPSA s 53(1); Australian PPSA s 46(1)

<sup>547</sup> Draft IRSAR Convention, art 9(1). See 320

floating security interest were registered and subsequently the assignment of a specific receivable were registered, the assignee of the specific receivable would take the receivable subject to the previously registered floating security interest. If so, once a floating security interest was registered, receivables transactions would be discouraged. Also, the parties in a floating security interest intend the security provider to be able to dispose of secured assets. For these reasons, the proposed IRSAR Convention provides that the assignment of a specified receivable prevails over a previously registered floating security interest.

### **5-5-3. Floating Security Interest v Subsequent Security Interest**

#### **5-5-3-1. Floating Security Interest v Subsequent Security Interest**

In English law, a floating charge is subordinated to a subsequent fixed charge.<sup>548</sup> In contrast, under UCC Article 9 and the PPSAs of Canada, New Zealand and Australia, a security interest in after-acquired property is not subordinated to a subsequently registered security interest.

With receivables often the financier wants a negative pledge clause vis-à-vis the receivables while is happy for the proceeds to be disposed of. In practice, a floating charge in English law usually comes equipped with a negative pledge clause or an

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<sup>548</sup> *Re Yorkshire Woolcombers Association Ltd* [1903] 2 Ch. 284, per Romer L.J. at 295; *Evans v Rival Granite Quarries Ltd* [1910] 2 K.B. 979, per Buckley L.J. at 999

automatic crystallisation clause<sup>549</sup> and functions as a security interest in after-acquired property under UCC Article 9 and the PPSAs.<sup>550</sup>

### 5-5-3-2. Floating Security Interest in the IRSAR

In principle, a floating security interest under the proposed IRSAR Convention follows English law on floating charges in that a floating security interest over all present and future receivables registered in the IRSAR is subordinated to a subsequent security interest in a specified receivable (which is similar to a fixed charge in English law).

In addition, in the case of a floating security interest, a negative pledge clause or an automatic crystallisation clause in the agreement on the floating security interest must be registered in the IRSAR to be effective vis-à-vis third parties.<sup>551</sup> If a floating security interest is registered with a negative pledge, it prevails over subsequent security interests but can be overcome by a subsequent assignment.

### 5-5-4. Crystallisation

If a floating security interest over all present and future receivables of a VIRS is registered in the IRSAR, upon the debtor's default, the floating security interest is crystallised into a security interest in all the receivables that the VIRS has outstanding at

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<sup>549</sup> An automatic crystallisation clause may provide that crystallisation occurs automatically upon any specified event, e.g., creating any subsequent fixed charge. The purpose of such an automatic clause is to crystallise a floating charge before the debtor grants a fixed charge to a competing creditor and thus to preserve the priority of the floating charge as against possible subsequent fixed charges. Law Commission, 'Registration of Security Interests: Company Charges and Property other than Land' (Law Com No 164, 2002) [2.44].

<sup>550</sup> Lynn M. LoPucki, Arvin I. Abraham and Bernd P. Delahaye, 'Optimizing English and American Security Interests' (2013) vol. 88 *Notre Dame Law Review* (forthcoming)

<sup>551</sup> Draft IRSAR Convention, art 9(2). See 321

the time of the crystallisation, which receivables would then be the object of liquidation, subject to any prior assignments of specified receivables or any prior security interests in specified receivables.

## 5-6. RESERVATION OF TITLE

### 5-6-1. Reservation of Title v Assignment

Retention of title is an acquisition financing method, sometimes referred as reservation of title. A reservation-of-title right is a non-possessory security interest.

V
receivable from the sale of the inventory to S debtor of the receivable : S
assigned to B security interest (extension of reservation-of-title) for R

R obtained a reservation-of-title right in company V's inventory. The reservation-of-title clause in the contract of sale in relation to the inventory stipulates that the reservation-of-title right extends to the proceeds of the inventory. Later, V sells the inventory to S and obtained a receivable for the price of the inventory against S. R claims the receivable as the proceeds of the inventory. However, V has assigned the receivable to a third party B and immediately registered the assignment of the receivable before R registers its reservation-of-title right.

### 5-6-1-1. English Law

If R had a reservation-of-title clause in the contract of sale in relation to the inventory, this would not automatically extend to the receivables under English law. If the contract purported to extend it to the receivables, the reservation-of-title right would be a charge and hence registrable.<sup>552</sup> If R's reservation-of-title right is registrable but not registered, it would not be enforceable against B. Priority between reservation-of-title sellers (R) and receivables financiers (B) is determined by the order of registration in the Company Charges Registry.

### 5-6-1-2. UCC Article 9, PPSAs

The UCC Article 9 has created a single, comprehensive security right in movable assets, unifying numerous and diverse possessory and non-possessory rights in tangible and intangible assets, including transfer-of-title and reservation-of-title arrangements, that existed under state statutes and common law.<sup>553</sup> For many years before the introduction of this UCC right, trade across state and provincial boundaries was hampered by the existence of diverse and highly particularised regimes for granting security.<sup>554</sup> The idea subsequently spread to Canada, New Zealand, Australia, etc.

Under UCC Article 9 and the PPSAs of Canada, New Zealand and Australia, basically a reservation-of-title agreement comes within the functional, integrated and comprehensive definition of security interests and thus filing is required for perfection.

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<sup>552</sup> *E. Pfeiffer Weinkellerei-Weineinkauf GmbH & Co v Arbuthnot Factors Ltd* [1987] BCLC 522 (QB), 533; [1988] 1 WLR 150; *Compaq Computer Ltd v Abercorn Group Ltd* [1993] BCLC 602 (Ch)

<sup>553</sup> UNCITRAL Legislative Guide on Secured Transactions (2007) 23 [62]

<sup>554</sup> UNCITRAL Legislative Guide on Secured Transactions (2007) 56 [103]

Thus, priority between reservation-of-title sellers (R) and receivables financiers (B) is determined by the order of UCC Article 9 filing or registration in the PPS registry.

Under UCC Article 9 and the PPSAs, a security interest in proceeds is automatically perfected if the security interest in the original collateral was perfected.<sup>555</sup> Under UCC Article 9, a security interest in proceeds becomes unperfected on the 21<sup>st</sup> day after the security interest attaches to the proceeds.<sup>556</sup> It is 10 days in Ontario, 15 days in Saskatchewan, Canada, 10 working days in New Zealand and 5 business days in Australia.<sup>557</sup> During these days, priority overlaps. Even if B registers the assignment of the receivable to B within the automatic perfection period, if R registers its reservation-of-title right over the inventory in the UCC Article 9 or PPS registry prior to B, R prevails over B. If R registers its security interest in the receivable within the automatic perfection period, R may prevail over B even if B registered it prior to R.

The same rule applies to security interests in receivables, and so priority between a reservation-of-title right and a security interest in the receivable is determined by the order of registration except for the automatic perfection period.

### 5-6-1-3. Purchase-Money Security Interests

The reservation-of-title right may well be a purchase-money security interest. A purchase-money security interest may trump a prior perfected security interest under

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<sup>555</sup> Stephen L. Sepinuck (ed), *Practice Under Article 9 of the Uniform Commercial Code* (2d edn, ABA UCC Committee 2008) 394

<sup>556</sup> UCC, s 9-315(d)

<sup>557</sup> Ontario PPSA, s 25(4); Saskatchewan, s 28(3); New Zealand PPSA, s 47; Australian PPSA, s 33(2)

UCC Article 9. Where C makes an advance to the debtor (D) on the security of D's future property, and later D subsequently acquires an asset (M) with the funds provided by P on the security of that asset (M),<sup>558</sup> C has a prior perfected security interest and P has a purchase-money security interest. Under UCC Article 9, the purchase-money lender has priority over any other security interests in the collateral because it has either supplied the collateral or made advances to enable the debtor to acquire the collateral.<sup>559</sup>

However, purchase money security interests under UCC Article 9 apply only to goods, inventory and livestock.<sup>560</sup> They do not apply to receivables unless they are inventory. Even though it is possible to purchase receivables (which are debts) with the cash borrowed from a bank, using the security of the receivables to obtain the difference between the interest rates, such receivables would not be inventory.

The PPSAs of Canada, New Zealand and Australia also provide priority of a purchase-money security interest over other security interest in the same collateral given by the same debtor.<sup>561</sup> However, they override this purchase-money security interest rule with a special first-to-file rule as regards receivables financiers with respect to a non-proceeds security interest or non-purchase money security interest in accounts receivable that is given for new value.<sup>562</sup>

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<sup>558</sup> Roy Goode and Louise Gullifer, *Goode on Legal Problems of Credit and Security* (4th edn, Sweet & Maxwell, 2008) 213 [5-62].

<sup>559</sup> UCC, s 9-324. Lynn M. LoPucki and Elizabeth Warren, *Secured Credit: A Systems Approach* (6th ed, Aspen Publishers 2009) 519.

<sup>560</sup> UCC, s 9-324.

<sup>561</sup> Ontario PPSA, s 33; Saskatchewan s 34; New Zealand PPSA ss 73-77; Australian PPSA ss 62-64

<sup>562</sup> Saskatchewan PPSA, s 34(6),(7); New Zealand PPSA, s 75A as inserted by PPS Amendment Act 2004, s 15; Australian PPSA, s 64(1)

English law has never recognised the priority of such purchase-money security interests,<sup>563</sup> although there are some cases concerning competing claims to an interest in land.<sup>564</sup> Similarly, the IRSAR would not acknowledge the exception for purchase money security interests to the rule that priority is determined by the order of registration. In the IRSAR, a purchase money security interest does not have priority over other prior assignments or security interests. In the IRSAR, priority is determined by the order of registration regardless of whether it is a purchase money security interest.<sup>565</sup>

#### 5-6-1-4. Proposed IRSAR Convention

Where the assignor or security provider is a VIRS, such extension to the proceeds would not be acknowledged unless registered in the IRSAR since priority of assignments of or security interests in a VIRS receivable is determined by the order of IRSAR registration. The problem is that a reservation-of-title right in a tangible movable asset cannot be registered in the IRSAR. As a result, a retention-of-title right would not automatically extend to receivables against S that are sale proceeds of the inventory subject to the reservation-of-title arrangement. A security interest in the receivables should be registered in the IRSAR separately. In conclusion, B would have priority over R with respect to the receivable against S if its assignment to B were registered in the IRSAR. Instead, R's reservation-of-title right would extend to the cash proceeds that B

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<sup>563</sup> Roy Goode and Louise Gullifer, *Goode on Legal Problems of Credit and Security* (4th edn, Sweet & Maxwell, 2008) 214 [5-62]

<sup>564</sup> *Re Connolly Bros Ltd (No. 2)* [1912] 2 Ch 25 (CA)

<sup>565</sup> See Draft IRSAR Convention, art 5. See 318

paid V for consideration of the receivable. If R registered its security interest, priority between B and R would be determined by the order of IRSAR registration.

The security interest in proceeds perfected automatically and continues for 5 to 20 days according to the UCC Article 9 and the PPSAs of Canada, New Zealand and Australia may be declared as a non-consensual right by the Contracting State according to Article 20 of the proposed IRSAR Convention. In the Contracting State where it is declared as a non-consensual right, if R registers its security interest in the receivable in the IRSAR within the automatic perfection period, R may prevail over B even if B registered it prior to R. Thus, when B purchases a receivable from a sale of an asset, B needs to check whether there is any security interest in the asset against V in the national registry e.g. the UCC Article 9 or PPS registry. After the lapse of the automatic perfection period, automatic perfection loses its effectiveness, and priority is determined by the order of VIRS registration.

### 5-6-2. Floating Security Interest v Reservation of Title

X
floating security interest over all present and future receivables for F
receivable from the sale of the inventory to S debtor of the receivable : S
security interest (extension of reservation-of-title) for R

Let us suppose that F is a bank holding a floating charge (or security interest) over all of company X's present and future receivables. F has registered the floating charge (or

security interest). Subsequently, R sold inventory to X and R obtains a reservation-of-title right in X's inventory. The reservation-of-title clause in the contract of sale with respect to the inventory stipulates that the reservation-of-title right extends to the proceeds of the inventory. Later, X sells the inventory to S and obtains a receivable for the price of the inventory against S. R claims the receivables as the proceeds of the inventory. Priority between the receivables financier and a reservation-of-title supplier claiming the receivables as proceeds in this situation under the English law, the US law and the IRSAR Convention will be analysed in the following sections.

#### 5-6-2-1. English Floating Charge

In English law, a reservation-of-title right is likely to constitute a registrable charge.<sup>566</sup> If R's reservation-of-title right is registrable but not registered, it is not perfected against a registered floating charge and therefore R's reservation-of-title right does not extend to the receivable as proceeds of the inventory.

On the other hand, if R registered its reservation-of-title right, it extends to the receivable as proceeds of the inventory according to the contract. A floating charge cannot bother this because a floating chargor has the power to dispose of its assets. The second limb of *Dearle v Hall*<sup>567</sup> does not apply to a floating charge. Even if R had notice of the prior floating charge, R's reservation-of-title right trumps the prior floating charge,

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<sup>566</sup> *E. Pfeiffer Weinkellerei-Weineinkauf GmbH & Co v Arbuthnot Factors Ltd* [1987] BCLC 522 (QB), 533; [1988] 1 WLR 150; *Compaq Computer Ltd v Abercorn Group Ltd* [1993] BCLC 602 (Ch)

<sup>567</sup> (1828) 3 Russ 1

and achieves priority over the prior floating chargee by registration in the Company Charges Registry.<sup>568</sup>

However, if F's floating charge is equipped with a negative pledge clause with respect to receivables, R's reservation-of-title right does not extend to the receivable as proceeds of the inventory. Negative pledge clauses in floating charges are the particulars that must be included in the register.<sup>569</sup> According to the position established in English case law,<sup>570</sup> parties have constructive notice of particulars which must be included in the register. Thus, there would be constructive notice of the pledge to subsequent chargees. If notice was given to R of the negative pledge clause, F can assert the negative pledge clause vis-à-vis R and prevent R's reservation-of-title arrangement with respect to the inventory.

#### 5-6-2-2. Security Interest in After-Acquired Property under UCC Article 9, PPSAs

Under UCC Article 9 and the PPSAs, a reservation-of-title right is just another security interest, and priority is determined by order of registration. F's security interest in after-acquired receivables prevails over R's reservation-of-title right because the

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<sup>568</sup> *In re Hamilton's Windsor Ironworks, Ex parte Pitman & Edwards*, 187.9, 12 Ch.D. 707. Hugh Beale, Michael Bridge, Louise Gullifer and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) [14.11] fns 53, 54

<sup>569</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, s 859D(2)(c)

<sup>570</sup> *English and Scottish Mercantile Investment Co v Brunton* [1892] 2 QB 700; *Standard Rotary Machine Co Ltd* (1906) 95 LT 829; *Wilson v Kelland* [1910] 2 Ch 306; *G & T Earle Ltd v Hemsworth* (1928) 44 TLR 605; *Siebe Gorman & Co Ltd v Barclays Bank Ltd* [1979] 2 Lloyd's Rep 142, 160

former is registered prior to the latter. As a result, R's reservation-of-title right does not extend to the receivable against S.

Once X collects the receivable from S, F's security interest in after-acquired receivables extends to the cash collected as proceeds of the receivable; likewise R's reservation-of-title right extends to the cash collected as proceeds of the inventory. Because F's security interest is registered prior to R's right, F has priority over R with respect to the cash collected. In any case, R's reservation-of-title right is not protected under UCC Article 9 or the PPSAs.

#### 5-6-2-3. Proposed IRSAR Convention

The proposed IRSAR Convention adopted the English law approach in that the VIRS providing a floating security interest to a creditor is entitled to dispose of its receivables in the ordinary course of business. Thus, any security interest (including reservation of title) subsequently registered in the IRSAR prevails over a floating security interest registered in the IRSAR unless a negative pledge clause is registered with the floating security interest.

### **5-7. PREFERENTIAL CREDITORS**

In terms of preferential creditors, the extent to which a floating security interest registered in the IRSAR should be subordinated to preferential creditors in the event of

the insolvency of a VIRS is a matter for the applicable national insolvency laws. Such a bankruptcy issue should be left up to national law. The IRSAR serves to determine priority among competing assignees or secured creditors with respect to receivables of a VIRS, not among preferential creditors which are regulated by the legislation of sovereign nations.

The proposed IRSAR Convention follows the solution provided by the Cape Town Convention<sup>571</sup> in that a Contracting State may declare those categories of non-consensual rights or interests which have priority over a security interest or a floating security interest registered with the IRSAR, whether in or outside insolvency proceedings. A non-consensual right or interest has priority over a security interest or a floating security interest registered with the IRSAR if the former is of a category covered by a declaration deposited prior to the registration of the security interest or the floating security interest.<sup>572</sup>

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<sup>571</sup> Cape Town Convention, art 39. Under Art 39(3) of the Cape Town Convention, any non-consensual right or interest e.g. State liens for unpaid taxes does not have priority over an international interest registered in the International Registry of Mobile Assets unless it is of a category covered by a declaration deposited prior to the registration of the international interest. Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008) 256-60 [4.264]-[4.276].

<sup>572</sup> Draft IRSAR Convention, art 10(3). See 321

## 5-8. PROCEEDS

### 5-8-1. Proceeds from Collection of Receivables & Sale of Receivables

There are two important kinds of proceeds in the context of a security interest in a receivable: (1) the proceeds of a receivable which the account debtor of a receivable pays a VIRS and (2) the proceeds from sale which an assignee of a receivable pays the VIRS that assigned the receivable to the assignee. Under the proposed IRSAR Convention, a security interest (except a floating security interest) in a VIRS receivable registered in the IRSAR extends to the proceeds from collection as well as the proceeds from sale.

In security assignments of receivables, even if the assignor (security provider) collects the proceeds from the account debtor of the receivable, it collects it as a trustee of the assignee (secured creditor) and thus the proceeds collected are separated from the assignor's (security provider's) other property. Under the proposed IRSAR Convention, even though proceeds are paid to the assignor (VIRS), insofar as the proceeds are separated upon the assignee's instruction and reasonably identifiable from the other assets of the VIRS, the assignee has priority over the paid proceeds.<sup>573</sup> This is intended to facilitate practices such as securitisation and undisclosed invoice discounting, where payments are usually channelled to a blocked bank account held by the assignor, separately from its other assets, on behalf of the assignee.<sup>574</sup>

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<sup>573</sup> Draft IRSAR Convention, art 7. See 319

<sup>574</sup> Explanatory note by the UNCITRAL secretariat on the United Nations Convention on the Assignment of Receivables in International Trade (UNCITRAL 2004), 42  
<<http://www.uncitral.org/pdf/english/texts/payments/receivables/ctc-assignment-convention-e.pdf>>  
accessed 1 March 2012.

### **5-8-2. Proceeds Separated and Reasonably Identifiable**

Registration of a security interest in a receivable in the IRSAR does not extend to proceeds of the receivable unless these proceeds are separated and reasonably identifiable from the other assets of the VIRS. In order for a security interest over a receivable to cover its proceeds, the proceeds must be identifiable. They are identifiable if the VIRS holds them separately under instructions from the secured creditor for the latter's benefit or in a blocked bank account containing only proceeds.

### **5-8-3. Dual Security Interests in Assigned Receivable and Proceeds from Sale**

Upon collection of the proceeds by the creditor from the debtor of the receivable, the receivable is satisfied and therefore cancelled.

Notwithstanding, where a VIRS assigns its receivable to which a security interest attaches to another VIRS, if the security interest in the receivable is registered in the IRSAR, the security interest continues to be perfected after the receivable is assigned to another VIRS and the assignee VIRS would take the receivable subject to the security interest. As a result, the secured creditor would have dual security interests: one in the receivable that has been assigned to the assignee as well as one in the sales proceeds that the assignor (debtor) obtained from the assignee for consideration of the receivable.<sup>575</sup>

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<sup>575</sup> See Section 5-4-7

#### **5-8-4. Proposed IRSAR Rules on Proceeds**

Under the proposed IRSAR Convention, the assignee has the same right as the secured creditor in the proceeds collected by the assignor.

With respect to the assignee's right over the proceeds and the security interest in the proceeds, the proposed IRSAR Convention, following the approach of the UN Receivables Convention,<sup>576</sup> stipulates that once proceeds are received by the VIRS, the right of the assignee in those proceeds has priority over the right of a competing claimant including the insolvency representative if the VIRS has received the proceeds under instructions from the assignee and if the proceeds are held by the VIRS for the benefit of the assignee separately and are reasonably identifiable from the assets of the VIRS.<sup>577</sup>

### **5-9. BOND**

#### **5-9-1. Bond**

The assignment of the right to a debt represented by a bond may not be registered in the IRSAR because the assignment of the right to a debt represented by a bond should be regulated by the applicable national law on bonds, under which whoever holds the bond has the right to the debt. So bonds are expressly excluded in the proposed IRSAR Convention.

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<sup>576</sup> UN Receivables Convention, art 24(2)

<sup>577</sup> Draft IRSAR Convention, art 7. See 319

However, a debt represented by a bond may be secured by the assets (e.g. receivables) of the bond issuer. Such security interests in the bond issuer's receivables can be registered in the IRSAR. It could function as a covered bond secured by the bond issuer's receivables.

Where a VIRS issues bonds, the VIRS is a debtor and the bond holder is a creditor. The security interest in VIRS receivables securing the debt represented by a bond can be registered in the IRSAR. Thus, the IRSAR could help to facilitate international trading of bonds secured by the bond issuer's receivables.

### **5-9-2. Covered Bond**

Sovereign bonds represent a large portion of international capital movements. However, since it is difficult to execute insolvency proceedings against a State, creditors of sovereign bonds often cannot collect even the principal.<sup>578</sup> For this reason, after the global financial crisis in 2008, covered bond markets have grown noticeably. A covered bond is a corporate bond with a security interest in a cover pool of assets of the covered bond issuer. In the event of the insolvency of the covered bond issuer, the covered bond holder may request the covered bond issuer to redeem the covered bond itself as well as execute the security interest in the cover pool of assets. The difference between a covered bond and an asset-backed securitisation is that in a covered bond, an originator itself issues cover bonds, whereas in an asset-backed securitisation, an originator

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<sup>578</sup> For example, in 2010, investors in Greek Sovereign bonds suffered huge losses.

transfers its assets to an SPV and the SPV issues securities. The main point is that in a covered bond there is redress against the cover pool of assets of the covered bond issuer.

Covered bonds are covered by specific regulation in specific countries. According to the EU Capital Requirement Directive,<sup>579</sup> classes of assets that are eligible as collateral for covered bonds are limited to mortgage loans (commercial and residential), senior MBS issued by securitization entities, loans secured by ships, etc. It seems that the reason why the scope of assets that are eligible as collateral for covered bonds is limited is that in the EU countries, there are not developed registration systems for collaterals of other types of assets. Mortgages are registered in the real estate registry. Ship mortgages are registered in the ship registry. If there were to be a registration system for the assignment of and security interest in receivables, it is expected that receivables could also be eligible as collateral for covered bonds.

### **5-9-3. Security Interest in the Bond Issuer's Receivables**

Where a VIRS issues a covered bond secured by its receivables, under the proposed IRSAR Convention, there could be three ways to protect the bond holder's security interest in the VIRS receivables.

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<sup>579</sup> Adopted by the European Council on 7 June 2006 and published in the Official Journal (OJ) of the European Union on 30 June 2006 (L177) under reference Directive 2006/48/EC and 2006/49/EC. For the UK covered bond market, the UK government introduced the Regulated Covered Bond Regulations 2008 in March 2008, and the FSA supervises Regulated Covered Bond programmes. <[http://www.fsa.gov.uk/fsaregister/use/other\\_registers/rcb\\_register/qanda](http://www.fsa.gov.uk/fsaregister/use/other_registers/rcb_register/qanda)> accessed 15 July 2012

First, if a bond issue is secured and the security is held by a trustee, the trustee may be registered as the secured creditor holding the security interest in the receivables of the VIRS in the IRSAR. This is usually the case.

Second, if a bond could be identified by the issuer and its serial number, the type of the bond, the terms of the bond, its interest rate, etc., ‘holder’ of the bond could be registered as an assignee of a VIRS receivable with the information identifying the bond itself, instead of identifying the bond holder, in the IRSAR.<sup>580</sup> ‘Holder’ of the bond could have priority from the date of registration. While the bond is traded in markets, whoever purchases the bond would be the ‘holder’ of the bond and could assert the priority of the bond with showing the bond.

Third, where a VIRS issues a bond and the bond is backed by a receivable of the VIRS, ‘holder’ of the bond could be registered as a secured creditor holding a security interest in the VIRS receivable in the IRSAR. If an initial bond holder is registered as a secured creditor holding the security interest in a VIRS receivable in the IRSAR with identification information of the bond, the subsequent purchaser of the bond that is secured by the security interest in the receivable may retain the priority of the initial bond holder by showing the bond. It is because a transferred security interest retains its original priority and the priority of the transferee is the priority of its transferor.

Where a VIRS issued a bond, once the security interest in the VIRS receivables securing the debt represented by a bond is registered in the IRSAR, a bond holder may request the VIRS to redeem the bond itself as well as execute the security interest in the VIRS receivables registered in the IRSAR in the event of the default of the VIRS.

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<sup>580</sup> Draft IRSAR Convention, art 13(b). See 323

## 5-10. SUBORDINATION AGREEMENTS

With respect to subordination agreements, the proposed IRSAR Convention would directly adopt the approach of the UN Receivables Convention and the Cape Town Convention. The priority of competing security interests under the proposed IRSAR Convention may be varied by subordination agreement between secured creditors.<sup>581</sup> Secured creditors may negotiate and relinquish priority in favour of a subordinate claimant where commercial considerations so warrant.<sup>582</sup> A registered secured creditor may agree to be subordinated to a subsequently registered secured creditor or a prior or subsequent unregistered secured creditor.<sup>583</sup> A secured creditor in whose favour a subordination has been made should register the subordination in the IRSAR, otherwise it would not bind an assignee of the subordinated security interest.<sup>584</sup> When subordinating priority in favour of future assignees, it can be effected unilaterally, for example, by means of an undertaking of the first ranking assignee to the assignor, empowering the assignor to make a second assignment ranking first in priority.<sup>585</sup>

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<sup>581</sup> See Cape Town Convention, art 29(5)

<sup>582</sup> Explanatory note by the UNCITRAL secretariat on the United Nations Convention on the Assignment of Receivables in International Trade (UNCITRAL 2004), 42  
<<http://www.uncitral.org/pdf/english/texts/payments/receivables/ctc-assignment-convention-e.pdf>>  
accessed 1 March 2012.

<sup>583</sup> Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008), 69 [2.111].

<sup>584</sup> *ibid* 69 [2.112].

<sup>585</sup> Explanatory note by the UNCITRAL secretariat on the United Nations Convention on the Assignment of Receivables in International Trade (UNCITRAL 2004), 43

## **5-11. CONCLUSION OF PART 5**

Under the proposed IRSAR Convention, priority of assignments of and security interests in VIRS receivables is determined by the order of IRSAR registration. With respect to the double debtor problem, under the proposed IRSAR Convention, if a VIRS assigns its receivable to a non-VIRS entity and the non-VIRS entity assigns the receivable to a third party, the third party takes the receivable free of any security interests registered in the IRSAR. Thus, a potential assignee or secured creditor only has to investigate the IRSAR against the direct counterparty VIRS and does not have to search against the assignor of the assignor. If the assignor is not a VIRS, the assignee has no obligation to check the IRSAR before purchasing the receivable. As a result, IRSAR registration of a security interest might lose its effectiveness after two consecutive assignments of the receivable.

For the protection of secured creditors registered in the IRSAR, to assign a VIRS receivable to a non-VIRS entity, the IRSAR requires the consent of all prior secured creditors registered in the IRSAR, who hold security interests in the receivable including the secured creditors of the former VIRS assignors. However, to assign a VIRS receivable to another VIRS, the consent of prior secured creditors is not required and the security interests registered in the IRSAR would be protected.

With respect to reservation of title, the automatic perfection period in some jurisdictions might produce uncertainty with respect to the priority rule of registration, but it is relatively short period. A Contracting State may declare this as a non-consensual right under Article 10 of the proposed IRSAR Convention. The categories of preferential

creditors who have super-priority may be determined and declared by the Contracting State.

A registered floating security interest equipped with a negative pledge clause prevails over subsequently registered security interests but not a subsequently registered assignment. A security interest (including a floating security interest) covers the proceeds of the receivables if they are separated and identifiable. The priority of competing security interests under the proposed IRSAR Convention may be varied by subordination agreement between secured creditors.

A bond holder may also be registered in the IRSAR as an assignee or secured creditor with identification information of the bond itself, so that whoever purchases the bond can assert the priority of the bond presenting the bond.

## **PART 6. OPERATION OF THE IRSAR**

### **6-1. INTRODUCTION**

Part 6 discusses the proposed operation of the IRSAR and the rules relating to this. The first issue is whether to adopt a notice-filing system or a document-filing system. Some jurisdictions have notice-filing systems and other jurisdictions have document-filing systems. Chapter 6-2 examines both of them to decide which is better and also deals with the advance registration issue. It reviews the English legal system as the origin of a general security rights registry. It examines UCC Article 9 as the originator of a notice-filing system, the UNCITRAL Legislative Guide on Secured Transactions which adopted such a system, and the Personal Property Security Acts of Canada, New Zealand and Australia, which follow the UCC Article 9 model. Taking this into account, it explains why the IRSAR should be a notice-filing system. Then, to decide what information is required to be noticed, it reviews information that a registrant should submit to the registry for registration of an assignment of or security interest in receivables in each jurisdiction, and defines required information for the IRSAR.

A serious concern with respect to a notice-filing system is the abuse of registration by secured creditors or assignees. Chapter 6-3 explores how to prevent the abuse of registration by secured creditors or assignees. It analyses whether the system should require the consent of an assignor or security provider upon the registration application of an assignee or secured creditor in order to increase the authenticity of the

contents of registration. It recommends parties' reciprocal confirmation on registration contents instead of registrar's review.

Chapter 6-4 explains email notification linked to IRSAR registration. Chapter 6-5 designs the IRSAR Registrar which operates the proposed IRSAR Convention and its supervisory authority, taking reference of the International Registry of Mobile Assets under the Cape Town Convention. Chapter 6-6 searches for how to search the IRSAR online. It analyses the online operation of the IRSAR in relation to registrant identification and search for registration.

## **6-2. NOTICE-FILING SYSTEM**

### **6-2-1. Comparison with Document-Filing System**

In a document-filing registration system, registrants must submit the document evidencing the transaction, such as a sale contract or a security contract, and the registry officials scrutinise those documents before permitting their registration.<sup>586</sup> Only those that have satisfied the registration procedures may register in the registry. Therefore registration can only be made after the contract, from which the security interest arises, is concluded. Through such process, the registry tries to prevent void registration. Consequently, in a document-filing system, 'the registration provides searchers with

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<sup>586</sup> For example, a land registry is a title registry, and the requirements and effect of the registration are strictly stipulated by law. The registration is the source of real rights. Harry C. Sigman, 'Security in movables in the United States - Uniform Commercial Code Article 9: a basis for comparison' in Eva-Maria Kieninger (ed), *Security interests in Movable Property in European Private Law* (CUP, 2004), 78.

actual or at least presumptive proof of the existence and scope of the security right referred to in the registration'.<sup>587</sup>

In some jurisdictions, original contract documents which are manually made with great formality are placed on the register. In the UK, only the registration form remains on the register once it had been checked against the charge document.<sup>588</sup> Under the Korean Security Registration Act, registrants must submit the document evidencing the cause of registration,<sup>589</sup> but such documents are reviewed only for verification of the registration application and are not searchable in the registry.

Jan-Hendrik Röver explains the function of a debtor-indexed notice registration of security interests with comparison to a traditional title registry as follows:<sup>590</sup>

Whereas traditional registers were understood as providing an accurate reflection of the facts registered, it is now being put forward that a security register for movables, at least, is not able to provide authenticity of the registered facts, i.e. good faith reliance on the registered information is not protected. A register for movables is seen as a tool of establishing priority between competing security holders and it provides a warning about existing security interests to potential creditors. Where registration is introduced it is also a creation requirement for the security interest (hence, if a security is not registered it cannot exist or at least not perfected). However, the registration of a security interest cannot be taken as showing that a security interest legally exists. This would, however, limit the usefulness of the register in practice. The rationale that a register is a source of verified and guaranteed information is a misconception, since

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<sup>587</sup> UNCITRAL Legislative Guide on Secured Transactions, 111 [33]

<sup>588</sup> There are proposals put forward by the Department for Business, Innovation and Skills (BIS), which would change this. Key elements of the revised scheme of August 2011 include the possibility of filing electronically. 'Registration of Charges Created By Companies and Limited Liability Partnerships - Proposals to amend the current scheme and relating to specialist registers' (BIS, 12 March 2010) 34, Proposal J(a)  
<[https://www.gov.uk/government/uploads/system/uploads/attachment\\_data/file/31493/10-697-registration-of-charges-created-by-companies-proposals.pdf](https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/31493/10-697-registration-of-charges-created-by-companies-proposals.pdf)> accessed 15 January 2013

<sup>589</sup> Korean Security Registration Act, art 43(1).

<sup>590</sup> Jan-Hendrik Röver, *Secured Lending in Eastern Europe: Comparative Law of Secured Transactions and the EBRD Model Law* (OUP 2007) 232 [16.83].

pledge registers should simply serve to publicize data as provided by the parties. The position of the pledge register is thus different from that of a land or companies register, which indeed has to establish a reliable record of the rights that exist in the land or the companies that have been created.

Because of the loophole in a debtor-indexed registry, there is no point in having a document-based registration system, where parties must submit a document evidencing their contract and the documents themselves are registered. Such efforts might be wasted since a debtor-indexed registry cannot ensure certainty with respect to registration.

### **6-2-2. Effect of Notice-Filing**

In a notice-filing system, ‘registration only provides notice that the secured creditor may have a security interest in the assets described in the notice.’<sup>591</sup> A notice-filing system ‘does not provide even presumptive evidence of the existence of the security interest’.<sup>592</sup> The UNCITRAL Legislative Guide on Secured Transactions also explains that ‘a notice-filing system is no guarantee of the actual existence of a security interest’,<sup>593</sup> and recommends that ‘the law should provide that registration of a notice does not create a security interest and is not necessary for the creation of a security interest’.<sup>594</sup> Lopucki demonstrates the essence of the notice-filing system under UCC Article 9 as follows:

The filing system is the principal means used to communicate the possible existence of a lien from a creditor who has one to a creditor who is thinking of acquiring one. ... The difficulty in transmitting notice from the

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<sup>591</sup> UNCITRAL Legislative Guide on Secured Transactions, 111 [33]

<sup>592</sup> *ibid* 112 [37]

<sup>593</sup> *ibid* 112 [37]

<sup>594</sup> *ibid* Recommendation 33

holder of a lien to the creditor who seeks to acquire one is that neither of these creditors has any way of knowing who the other is ... The solution to this problem is for each creditor who obtains a lien to leave a “to whom it may concern” message. For an Article 9 security interest, that message is in the form of a financing statement... Each year, the creditors who take security interests leave millions of these messages in the filing system. And before they take their liens, many of these filers search the records to see whether prior secured creditors left message for them.<sup>595</sup>

Filing a financing statement is one method of perfecting security interests under UCC Article 9. It is simply a form of publicity for actual or potential rights.<sup>596</sup> Filing a financing statement does not evidence the existence of a security interest.<sup>597</sup>

Lopucki explains that the filing system is a means for a secured creditor who takes a non-possessory security interest in property of a debtor to communicate the existence of that security interest to others who may later consider extending credit to that debtor.<sup>598</sup> Sigman also emphasizes that filing of a financing statement under UCC Article 9 is just a warning about the need for further investigation. It is a form of advertisement, which indicates that a security interest may then or thereafter exist in assets that fall within the description provided.<sup>599</sup> In New Zealand, the PPS Register is

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<sup>595</sup> Lynn M. LoPucki and Elizabeth Warren, *Secured Credit: A Systems Approach* (6th ed, Aspen Publishers 2009) 281.

<sup>596</sup> Harry C. Sigman, ‘Security in movables in the United States - Uniform Commercial Code Article 9: a basis for comparison’ in Eva-Maria Kieninger (ed), *Security interests in Movable Property in European Private Law* (CUP, 2004), 78.

<sup>597</sup> Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Tangibles* (Sellier 2007) 43.

<sup>598</sup> Lynn M. LoPucki and Elizabeth Warren, *Secured Credit: A Systems Approach* (6th ed, Aspen Publishers 2009) 404.

<sup>599</sup> Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Tangibles* (Sellier 2007) 43.

often described as an electronic notice board.<sup>600</sup> It is like a public bulletin board where anybody may put a notice of their security interests in a debtor's assets.

A notice-filing system is like putting in a footnote. It is a reader's responsibility to refer to the original materials. The text does not have to contain all of the original text that it quotes. The text only has to contain summarised contents and the exact citation by which readers can refer to the original materials. Notice-filing systems contain summarised core information of the registered right and how to search for further information.

### **6-2-3. Advance Registration**

Under UCC Article 9, the filed 'notice is independent from the security agreement'.<sup>601</sup> Filing a financing statement may occur before or after the security interest is created, before or after there is a security agreement, before or after the debtor has any rights in the collateral, or even before any collateral comes into existence.<sup>602</sup> Priority between competing secured creditors is determined by the order of filing regardless of the date of creation of security interests.<sup>603</sup>

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<sup>600</sup> Roger Fenton, *Garrow & Fenton's Law of Personal Property in New Zealand: Volume 2 Personal Property Securities* (7th edn, LexisNexis, 2010) 36 [2.2.2].

<sup>601</sup> UNCITRAL Legislative Guide on Secured Transactions, 174 [98]

<sup>602</sup> Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Tangibles* (Sellier 2007) 43.

<sup>603</sup> Harry C. Sigman, 'Security in movables in the United States - Uniform Commercial Code Article 9: a basis for comparison' in Eva-Maria Kieninger (ed), *Security interests in Movable Property in European Private Law* (CUP, 2004), 73.

The UNCITRAL Legislative Guide on Secured Transactions follows this first-to-register exception to the general principle of determining priority by reference to the date of perfection.<sup>604</sup> The UNCITRAL Legislative Guide on Secured Transactions recommends that ‘as between security interests that were made effective against third parties by registration of a notice, priority is determined by the order of registration, regardless of the order of creation of the security interests’.<sup>605</sup>

Under UCC Article 9, a single filed financing statement may support a number of assignments to the same party over an extended period of time.<sup>606</sup> This serves to reduce the cost of registration. Furthermore, the UNCITRAL Legislative Guide on Secured Transactions recommends that one notice should be sufficient for multiple security interests arising from multiple agreements between the same parties.<sup>607</sup> A notice-filing system removes any practical necessity for the existence of a one-to-one relationship between the registration and the security agreement.<sup>608</sup>

The UNCITRAL Legislative Guide on Secured Transactions explains the primary reasons for, and advantages of, this flexible approach. First, registration in advance of the creation of a security interest allows funds to be raised by using future assets. Advance registration accommodates efficient registration for security interests in future

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<sup>604</sup> UNCITRAL Legislative Guide on Secured Transactions, Recommendation 67. See also *ibid* 195 [48]

<sup>605</sup> *ibid* Recommendation 76(a)

<sup>606</sup> Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Tangibles* (Sellier 2007) 48.

<sup>607</sup> *ibid* Recommendation 68

<sup>608</sup> *ibid* 174 [98]

assets.<sup>609</sup> Advance registration facilitates the extension of credit secured by future assets by providing a single date for establishing priority.<sup>610</sup>

Second, advance registration facilitates a security provider's access to credit. Advance registration avoids the risk of registration being ineffective in cases where the underlying security agreement is technically deficient at the point of registration but is later revised.<sup>611</sup> Therefore it enables a secured creditor to establish its priority without having to worry about the timing of the execution of the security agreement.<sup>612</sup> It provides certainty by enabling secured creditors to determine the priority of their security interests before they extend credit.<sup>613</sup>

Third, advance registration encourages a secured creditor to register the notice as early as possible, which puts potential creditors on notice that a security interest might have already encumbered the asset in question.<sup>614</sup>

The IRSAR registrar would not have the resources to check or investigate the real time of conclusion of the contract. IRSAR registration would be electronic registration, and the IRSAR would only be able to record the time of registration when an assignment of or security interest in receivables is registered. For this reason, it is inevitable for the IRSAR to allow advance registration, which is in fact desirable. Since IRSAR registration does not require submitting the contract document, it is possible for parties to register even future assignments in advance, as far as it is not expressly prohibited by the draft

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<sup>609</sup> UNCITRAL Legislative Guide on Secured Transactions, 174 [100]

<sup>610</sup> *ibid* 195 [48]

<sup>611</sup> *ibid* 174 [99]

<sup>612</sup> *ibid* 174 [99]

<sup>613</sup> *ibid* 195 [48]

<sup>614</sup> *ibid* 195 [48]

IRSAR Convention. Thus, it would be possible for the parties to agree to register an assignment of or security interest in receivables before conclusion of the contract.

#### **6-2-4. Why the Proposed IRSAR should be a Notice-Filing System**

A notice-filing system is suitable for a security provider-based registration system. Since the proposed IRSAR is a security provider-based (assignor-based) registration system, a notice-filing system is suitable. Let us assume, though, that the IRSAR were a document-based registration system and required registration of the document of the transaction. The delivery of the application would be burdensome, and the number of documents submitted by registrants would be unmanageably large. Even if the documents could be sent electronically, the storage of such a large amount of data would require great facilities and cost a lot. Moreover, if the registrar had to review the documents and issue a certificate confirming that the registered matters met the registration requirements, it would take time and expense. As for the IRSAR, one Registrar would have to review transaction documents from all over the world, which would be impracticable because of language diversity. This would be inadvisable as it would delay transactions and add to their registration fees.

To reduce registration fees, the IRSAR must be a notice-filing system, because it is quick and saves database storage.<sup>615</sup> In addition, parties prefer a notice-filing system to a document-filing system because they do not like to reveal the details of their transactions. The registration must indicate the contact information of the relevant

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<sup>615</sup> UNCITRAL Legislative Guide on Secured Transactions, Recommendation 54(b)

parties, such as the security provider and the secured creditor or the assignor and the assignee,<sup>616</sup> so that a potential assignee may contact them and investigate further. The registration process in the IRSAR does not involve human intervention. The IRSAR would not require parties to submit the contract document for an assignment of receivables or a security interest in receivables.

### **6-2-5. Information Required for Effective Registration**

In a notice-filing system, only very basic information must be registered for the registered right to be identifiable. The information registered does not serve the function of verifying the right. This section considers what information should be included in registrations in the IRSAR. In order to canvass the possibilities, this section compares the registration requirements of a number of jurisdictions. Since the IRSAR only deals with receivables assigned by and to companies, this thesis limits the analysis of identification data to that pertaining to companies. As representative examples, it compares information to effect registration in the United States, New Zealand, Australia, the UK, Korea and Japan and under the UNCITRAL Legislative Guide on Secured Transactions.

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<sup>616</sup> Draft IRSAR Convention, art 13. See 323

## 6-2-5-1. Comparative Research

### **6-2-5-1-1. UCC Article 9**

UCC Article requires a financing statement to provide (1) the name of the security provider; (2) the name of the secured party or a representative of the secured party; and (3) to indicate the collateral covered by the financing statement.<sup>617</sup> A financing statement is only sufficient if it contains all three elements.

### **6-2-5-1-2. New Zealand PPSA**

The New Zealand PPSA stipulates that the following data must be contained in the financing statement to register it: (1) the name and address of the security provider and the name or job title, and contact details, of the person acting on behalf of security provider; (2) the unique number assigned to the security provider on its incorporation; (3) the name and address of the secured creditor; and the name or job title, and contact details, of the person acting on behalf of the secured creditor; and (4) a description of the collateral.<sup>618</sup>

### **6-2-5-1-3. Australian PPSA**

The Australian PPSA 2009 stipulates that a financing statement consists of the following data: (1) the details of the secured creditor or a person nominated by the

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<sup>617</sup> UCC, s 9-502(a)

<sup>618</sup> New Zealand PPSA, s 142(1)

secured creditor who has authority to act on behalf of the secured creditor; (2) the security provider's details; (3) an address (including an email address or fax number) for the giving of notices to the secured creditor relating to the registration and details of any identifier provided for the giving of notices to the secured creditor; (4) a collateral description and a description of proceeds; and (5) end time for registration.<sup>619</sup>

#### ***6-2-5-1-4. UNCITRAL Legislative Guide on Secured Transactions***

According to the recommendations of the UNCITRAL Legislative Guide on Secured Transactions, the following matters should be recorded on the registration filing: (1) identity of the security provider - the name that appears in the document constituting the legal person;<sup>620</sup> (2) identity of the secured creditor or its representative and its addresses;<sup>621</sup> (3) description of the encumbered asset in a manner that reasonably allows for its identification;<sup>622</sup> (4) duration of the registration;<sup>623</sup> (5) statement of the maximum monetary amount for which the security interest may be enforced, if applicable.<sup>624</sup>

#### ***6-2-5-1-5. UK Register of Company Charges***

The Companies Act 2006 stipulates that a company that creates charges must deliver the particulars of the charge, together with a certified copy of the instrument (if

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<sup>619</sup> Australian PPSA, s 153(1)

<sup>620</sup> UNCITRAL Legislative Guide on Secured Transactions, Recommendation 60

<sup>621</sup> *ibid* Recommendation 57(a)

<sup>622</sup> *ibid* Recommendations 63 and 14(d)

<sup>623</sup> *ibid* Recommendation 69

<sup>624</sup> *ibid* Recommendation 57(d)

any) by which the charge is created or evidenced, to the registrar for registration before the end of 21 days.<sup>625</sup> The registrar checks the application form against the certified copy of the instrument. It makes the registration consistent with the actual charge contract between the security provider and the secured creditor. Where the charge is created or evidenced by an instrument, a statement of particulars must include the following information: the registered name and number of the company; the date of creation of the charge; the name of each of the chargee; whether it is a floating charge; whether there is a negative pledge clause, etc.<sup>626</sup>

#### ***6-2-5-1-6. Korean Security Registration Act***

Under the Security Registration Act, the following matters will be recorded on the registration:<sup>627</sup> (1) the head office or principal office and company registration number of the security provider; (2) the trade name or other name and head office or principal office of the debtor; (3) the trade name or other name, head office or principal office and company registration number of the secured creditor; (4) if the security provider, the debtor or the secured creditor is a foreign legal person, its business office or other office located in Korea; (5) the cause of registration regarding the registration of security and the date thereof; (6) matters necessary for identifying the encumbered movables and receivables, which are specified by Korean Security Registration Rules made by the

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<sup>625</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, s 859A

<sup>626</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, s 859D(1) and (2)

<sup>627</sup> Korean Security Registration Act, art 47(2).

Supreme Court;<sup>628</sup> (7) the amount of secured claim or the maximum amount of credit; (8) special agreements in accordance with Article 10 or Article 12;<sup>629</sup> (9) the duration of the security interests (duration of effectiveness of registration); (10) the receipt number; and (11) the date of receipt.

#### ***6-2-5-1-7. Japanese Assignment Registration Act***

According to the Japanese Assignment Registration Act, the following matters are recorded on the registration of the assignment of movable assets or receivables:<sup>630</sup> (1) the trade name or other name of the assignor and its head office or principal office; (2) the name or other name and head office or principal office of the assignee; (3) the business office or other office located in Japan (if the head office or principal office of the assignor or the assignee is located in a foreign country); (4) the cause of registration regarding the registration of assignment of movable assets or receivables and the date thereof; (5) matters necessary for identifying the assigned movable assets or receivables, which are specified by the Japanese Assignment Registration Rule made by the Ministry of

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<sup>628</sup> In the case where the collateral is a receivable: (1) the type of the receivable; (2) the cause and the date of the accrual of the receivable, or the start date and the last date of the receivable; (3) the name and the address of the creditor of the receivable; and (4) the name and the address of the debtor of the receivable must be recorded. Assignments of future receivables (if the debtor of the receivable is not specified) and bulk assignments of receivables may be exempted from recording the fourth item. Korean Security Registration Rules, art 35(1)(ii)

<sup>629</sup> Under Korean Security Registration Act, art 10, the effect of a security interest in a movable asset will extend to all things that are attached to the encumbered movable asset, including its accessories, unless otherwise provided by law or a special agreement between the parties. If there is such a special agreement, it should be registered. In addition, according to Korean Security Registration Act, art 12, a security interest in a movable asset will secure the principal, interest, penalty, expense for enforcement of the security interest, expense for preservation of the encumbered movable asset, and the damages arising from the non-fulfilment of the obligation or from latent defects in the encumbered movable asset, unless otherwise provided by a special agreement between the parties. If there is such a special agreement, it should be registered.

<sup>630</sup> Japanese Assignment Registration Act, arts 7(2) (for movable assets) and 8(2) (for receivables).

Justice;<sup>631</sup> (6) the duration of the registration of assignment of movable assets or receivables; (7) the registration number; (8) the date of registration; (9) the total amount of the assigned receivables<sup>632</sup> (only for the assignment of receivables that have already been arisen, not for future receivables).

An agreement assigning a person's income for his whole life time is invalid. The valid term of registration for the assignment of existing receivables and the assignment of future receivables against a specified debtor may not exceed 50 years. It was taken into consideration that housing loans usually last for a long period.<sup>633</sup> With respect to future receivables against unspecified debtors, the valid term of registration must not be longer than ten years.<sup>634</sup> The valid term of registration may be extended if there is a special reason.<sup>635</sup>

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<sup>631</sup> In the case where the collateral is a receivable: (1) if there is more than one receivable, the serial numbers of the receivables; (2) if the debtor of the receivable is specified, the name and the address of the debtor and the creditor of the receivable; (3) if the debtor of the receivable is not specified, the cause of the accrual of the receivable and the name and the address of the creditor of the receivable; (4) the type of the receivable; (5) the date of the accrual of the receivable; and (6) the amount of the receivable (only if the receivable has already accrued) must be recorded. Japanese Assignment Registration Rule, art 9(1).

<sup>632</sup> Japanese Assignment Registration Act, art 8(2)(iii).

<sup>633</sup> Japanese Assignment Registration Act, art 8(3)(i).

<sup>634</sup> Japanese Assignment Registration Act, art 8(3)(ii).

<sup>635</sup> Japanese Assignment Registration Act, art 8(3).

<Table 15> Contents of Registration (in the case where the security provider is a company)

<b>UCC Article 9</b>	<b>New Zealand PPSA</b>	<b>Australian PPSA</b>	<b>UNCITRAL Legislative Guide</b>
notice-filing system	notice-filing system	notice-filing system	notice-filing system
name of the security provider	name and address of the security provider and the name or job title, and contact details of the person acting on behalf of security provider	security provider's details	identifier of the security provider
	unique number assigned to the security provider on its incorporation		
name of the secured party or a representative of the secured party	name and address of the secured creditor and the name or job title, and contact details of the person acting on behalf of the secured creditor	details of the secured creditor or a person nominated by the secured creditor who has authority to act on behalf of the secured creditor	identifier of the secured creditor
		address (including an email address or fax number) for the giving of notices to the secured creditor relating to the registration and details of any identifier provided for the giving of notices to the secured creditor	
the collateral covered by the financing statement	description of the collateral	collateral description description of proceeds	description of the encumbered asset
			maximum monetary amount for which the security interest may be enforced (optional)
		end time for registration	five years or as chosen by the parties

<b>UK</b>	<b>Korean registration</b>	<b>Japanese registration</b>
combination of document-filing system and notice-filing system	combination of document-filing system and notice-filing system	notice-filing system
registered name and number of the company	name, head office or principal office, company registration number of the security provider	name, head office or principal office of the assignor
name of each of the persons in whose favour the charge has been created	name, head office or principal office, company registration number of the secured creditor	name, head office or principal office of the assignee
short description of the property	type of the receivable cause and date of the accrual of the receivable, or start date and last date of the receivable name and address of the creditor of the receivable name and address of the debtor of the receivable (may be exempted)	serial numbers of the receivables (if there are more than one receivables) name and address of the creditor of the receivable name and address of the debtor of the receivable (if it is not specified, cause of the accrual of the receivable) type of the receivable date of the accrual of the receivable
date of creation of the charge	the cause of registration regarding the registration of security date of the cause	the cause of registration regarding the registration of assignment of movables or receivables date of the cause
obligations secured by the charge	the amount of secured claim or the maximum secured amount	the total amount of the assigned receivables (only for the assignment of receivables that have already been arisen, not for future receivables)
	duration of the security interests (no longer than five years, renewal possible)	duration of the registration of assignment of movables or receivables (no longer than ten years, renewal possible)
	receipt number	registration number
	date of receipt	date of registration

## 6-2-5-2. IRSAR Registration Information

Having compared the legal systems above, the conclusion is that most require the name of the debtor, identification of the assignor or the security provider, identification of the assignee or the secured creditor, a list or general description of the debtor of the receivable and general description of the assigned or encumbered asset. In the IRSAR, it must also be registered whether the registration is for an assignment or a security interest.

In Korea and Japan, the cause of registration and the date of the cause must be registered. However, registering the date of the cause would not be necessary for the IRSAR because advance registration is available and priority is determined by the date of registration regardless of the date of the cause.

Under the proposed IRSAR Convention, the following would be required to effect a registration: (1) information identifying the assignor or the security provider; (2) information identifying the assignee or the secured creditor (or, if a holder of a bond is the assignee or secured creditor, information identifying the bond); (3) a list or general description of the debtor of the receivable assigned or encumbered; and (4) a general description of the receivable assigned or encumbered, present or future, including the amount of monetary obligation and the due date.<sup>636</sup>

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<sup>636</sup> Draft IRSAR Convention, art 13 See 323

## **6-3. PARTIES' RECIPROCAL CONFIRMATION INSTEAD OF REGISTRAR'S**

### **REVIEW**

#### **6-3-1. Safeguard against Improper Registration under a Notice-filing System**

Chapter 6-2 concluded that an international registry should be a notice-filing system rather than a document-filing system. It is because, first of all, it would be impractical to store and manage documents from around the world. Second, reviewing documents in various languages for registration would be costly and take time. However, a notice-filing system has a shortcoming.

A serious concern with respect to a notice-filing system is the abuse of registration by secured creditors (or assignees). Because a notice-filing system does not require submitting the contract document, anyone could file a notice of intention to assign in relation to a person when there is actually no such proposal. They might do this maliciously to damage a person's credit record or they might be acting negligently. As such, on the one hand, a secured creditor (or an assignee) would maximise the scope of registration of security interests or assignments to ensure the protection of his rights.

On the other hand, a security provider (or an assignor) would wish to minimise the scope and amount of registration of security interests (or assignments). It is because, if a security interest is registered in the registry with respect to the security provider, it gives the impression that the security provider has such debts. A security provider-based registration system is a negative registry or a warning registry. Thus, if there are several assets registered under a security provider in a security provider-based registration

system, it is not good for the person. It means that those registered assets are pledged for debts. The assets registered in a security provider-based registry can no longer be used for security except the value of the assets exceeds the amount secured.

Analysing these two aspects, a security provider's (or assignor's) cross-check on the registration contents submitted by a secured creditor (or assignee) would help to prevent a secured creditor's abuse of registration.

Chapter 6-3 explores legal systems of each jurisdiction with respect to the various possible remedies for this problem and the requirement of the parties' cooperation for registration. The issue considered is whether to require the parties' reciprocal confirmation in the IRSAR. The conclusion is that an email request for consent from the assignor (or the security provider) is the best method.

In Chapter 6-3, a 'secured creditor' includes an assignee, a 'security provider' includes an assignor, and a 'security interest' in receivables includes an assignment of receivables except in the explanation regarding the Companies Act 2006 and the Korean Security Registration Act.

### **6-3-2. Comparative Research**

Based on a comparative analysis, it appears that there are three general approaches. First, under the Canadian, New Zealand and Australian PPSAs, the law does not require consent of the security provider for registration of a security interest in a movable asset or a receivable owned by the security provider. Therefore, a secured creditor by himself can apply for registration of a security interest. In these jurisdictions,

a secured creditor who registers his security interest must give notice of its filing to the security provider (or assignor) within a certain period of time.

Second, under UCC Article 9 and the UNCITRAL Legislative Guide on Secured Transactions and in English law, authorisation of a security provider is required but may be given either before or after registration. Furthermore, under UCC Article 9, authorisation of a security provider is implied from the authentication of the security agreement. Thus, a secured creditor may file any financing statement unilaterally. However, a security provider may at any time cancel an incorrect registration through a summary administrative or judicial procedure.<sup>637</sup> The focus is how efficiently the security provider could cancel an incorrect registration affecting him once an incorrect registration has been registered.

Third, in Korea, and Japan and under the DCFR and the Cape Town Convention, the law requires the parties' reciprocal consent before the registration is actually registered. This may be achieved by requiring both a security provider and a secured creditor (or both an assignor and an assignee) to visit the registration office to apply for a registration. Or it is achieved by an internet-based online registration system requiring the consent of the security provider (or assignor) to be transmitted to the system in order for the registration application to actually appear on the website.

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<sup>637</sup> UNCITRAL Legislative Guide on Secured Transactions, 176 [108]

## 6-3-2-1. Notice to the Security Provider Compulsory

### ***6-3-2-1-1. Verification Statement***

Under the PPSAs of Canada, New Zealand and Australia, a secured creditor may himself apply for the registration with respect to the security interest. Then, the secured creditor must send a ‘verification statement’ of a registration, issued by the registrar, to a security provider, so that the security provider may have an opportunity to apply for a change to the registration if the registration is incorrect. If a secured creditor does not send a verification statement to a security provider within a certain period,<sup>638</sup> he will be fined. There are sanctions for failing to send a verification statement.<sup>639</sup> However, even though a secured creditor does not send a verification statement to a security provider, the registration is still effective until the security provider files a ‘financing change statement’.

### ***6-3-2-1-2. Financing Change Statement***

After a security provider (or assignor) receives a verification statement of a registration, if the security provider believes that a certain financing statement is inaccurate or wrongfully filed, it may demand the secured creditor (or assignee) to file a ‘financing change statement’ to amend or discharge the registration. ‘Financing change statement’ means a form that requires data authorized by the regulations to be entered in

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<sup>638</sup> 30 days under Saskatchewan PPSA, s 43(12); 30 days under Ontario PPSA, s 46(6); 15 working days under New Zealand PPSA, s 148; ‘as soon as reasonably practicable after the time of the registration’ in Australia, Australian PPSA, s 157(1)(b).

<sup>639</sup> \$500 to the security provider under Ontario PPSA, s 46(7); punishment under the Australian Privacy Act 1988 (s 13) under Australian PPSA, s 157(4)

the register to renew, discharge, or amend a financing statement.<sup>640</sup> Upon filing the financing change statement, the financing statement in question will disappear from the registry.

Under the PPSAs of Saskatchewan and New Zealand, the security provider may give the secured creditor a written demand<sup>641</sup> to register a financing change statement within 15 days after the demand is given.<sup>642</sup> If it does not, the security provider may register the financing change statement himself upon providing the registrar with satisfactory proof that the demand has been given to the secured creditor.<sup>643</sup> Upon application to the court by a secured creditor, the court may order that the registration be maintained or be discharged or amended.<sup>644</sup>

Under the PPSAs of Ontario and Australia, a person registered as a security provider may give an amendment demand to the person registered as a secured creditor for a financing change statement to be registered to amend the registration.<sup>645</sup> In addition, the person registered as a security provider may also apply to the court for an order in relation to an amendment demand. Upon application, if the court considers the amendment demanded to be authorised, the court may order the Registrar to register a financing change statement amending or removing the registration.<sup>646</sup>

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<sup>640</sup> Saskatchewan PPSA, s 2(1)(q); Ontario PPSA, s 49; New Zealand PPSA, s 135; Australian PPSA, s 150(2)

<sup>641</sup> Saskatchewan PPSA, s 50(3); New Zealand PPSA, s 162

<sup>642</sup> Saskatchewan PPSA, s 50(4); New Zealand PPSA, s 163

<sup>643</sup> Saskatchewan PPSA, s 50(5); New Zealand PPSA, s 165(1)(a)

<sup>644</sup> Saskatchewan PPSA, s 50(7); New Zealand PPSA, s 167(1)

<sup>645</sup> Ontario PPSA, s 56(2.1); Australian PPSA, s 178(1)

<sup>646</sup> Ontario PPSA, s 56(5)(b)(i); Australian PPSA, ss 182(1), 182(4)(a)

### 6-3-2-2. Authorization of Security Provider Before or After Registration

Under UCC Article 9 and the UNCITRAL Legislative Guide on Secured Transactions, the secured creditor is not obligated to send notice of the registration to the security provider as under the PPSAs of Canada, New Zealand and Australia.

#### **6-3-2-2-1. UCC Article 9**

Prior to the revision, UCC Article 9 required a financing statement to be signed by the debtor (security provider).<sup>647</sup> Later, in order to facilitate electronic filing of financing statements, the security provider's signature on a financing statement was no longer required.<sup>648</sup> It was because the UCC filing offices were not up to that technological challenge.<sup>649</sup>

As a security provider's signature is not required, a person may only file a financing statement if the security provider authorises the filing in an authenticated record.<sup>650</sup> Before filing a financing statement, the secured creditor must obtain authorisation from the security provider in an authenticated record. If the security provider has not authorised the filing, the financing statement is ineffective.<sup>651</sup>

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<sup>647</sup> Even when the debtor's signature was required, the filing of unauthorised financing statements was a serious problem.

<sup>648</sup> Lynn M. LoPucki and Elizabeth Warren, *Secured Credit: A Systems Approach* (6th ed, Aspen Publishers 2009) 322.

<sup>649</sup> *ibid.*

<sup>650</sup> UCC, s 9-509(a)(1).

<sup>651</sup> UCC, s 9-510(a)

To make it easier for the secured creditor to obtain such authorisation, UCC Article 9 provides that by authenticating a security agreement, a debtor (security provider) authorises the filing of financing statement covering the collateral described in the security agreement.<sup>652</sup> Under UCC Article 9, if a security provider consents to the security agreement in writing, it authorises the registration of the security agreement. As a result, a secured creditor only needs to get the security provider to authenticate a security agreement in order to obtain the right to file a financing statement.

However, a third party has no way to check whether the security provider did not authorise the filing and therefore the filing is ineffective. If there is a dispute about the validity of a filing, one could challenge the validity by proving that the security provider did not authorise the filing.<sup>653</sup> If the filing is in advance to a security agreement, the filing is ineffective before the security agreement and becomes effective after the security agreement.<sup>654</sup>

UCC Article 9 does not require a secured creditor to send a notice of the registration of a security interest to a security provider. If there is any prior registration of security interest in the registry with respect to a security provider, a potential secured creditor would ask the security provider about the registration and thus letting the security provider know about any such registrations. Furthermore, the potential secured creditor would use the fact that there is a prior registration, if any, as a point of

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<sup>652</sup> UCC, s 9-509(b).

<sup>653</sup> Lynn M. LoPucki and Elizabeth Warren, *Secured Credit: A Systems Approach* (6th ed, Aspen Publishers 2009) 322.

<sup>654</sup> *ibid.*

negotiation.<sup>655</sup> Thus, anyhow a security provider would get to know any registration affecting him.

Under UCC Article 9, a security provider may file a correction statement with respect to a record indexed using the security provider's name if it is believed that the record is inaccurate or was wrongfully filed.<sup>656</sup> However, an initial financing statement or other filed record is not affected by the filing of a correction statement.<sup>657</sup> Thus, both the filing of the financing statement and the filing of the correction statement will be shown on the registry.<sup>658</sup>

#### **6-3-2-2-2. UNCITRAL Legislative Guide on Secured Transactions**

The UNCITRAL Legislative Guide on Secured Transactions, Recommendation 71 stipulates as follows:

The law should provide that registration of a notice is ineffective unless authorized by the security provider in writing. The authorization may be given before or after registration. A written security agreement is sufficient to constitute authorization for the registration. The effectiveness of registration does not depend on the identity of the registrant.

For this Recommendation, the UNCITRAL Legislative Guide on Secured Transactions explains that 'there is no need to obtain the separate written consent of the

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<sup>655</sup> 'For example, a prospective buyer or secured creditor can refuse to go ahead with a financing transaction unless a pre-existing registration is cancelled or unless the secured creditor identified in the registered notice undertakes to subordinate its right to that of the prospective buyer or secured creditor.' UNCITRAL Legislative Guide on Secured Transactions, 153 [18]

<sup>656</sup> UCC, s 9-518(a)

<sup>657</sup> UCC, s 9-518(c)

<sup>658</sup> Lynn M. LoPucki and Elizabeth Warren, *Secured Credit: A Systems Approach* (6th ed, Aspen Publishers 2009) 322.

security provider, as authorization will be treated as given implicitly by the fact that the parties entered into the security agreement'.<sup>659</sup> Recommendation 71 provides that the authorization may be given before or after registration. Thus, a registration in advance of a security agreement may be authorised afterwards. The UNCITRAL Legislative Guide on Secured Transactions further elaborates stating that 'the practical result is much the same as in States that do not explicitly require formal written authorization from the security provider (on the assumption that the security agreement constitutes consent)'.<sup>660</sup> It is because if a registration is not true, 'modern regimes enable the security provider to request cancellation of the registration through summary judicial or administrative proceedings and other law may provide penalties for fraudulent registrations'.<sup>661</sup>

#### **6-3-2-2-3. UK**

In the UK, under the Companies Act 2006, the company or any person interested in the charge may deliver to the registrar a statement of particulars.<sup>662</sup> In practice, the security provider usually signs the security contract, a secured creditor usually registers his security interest by himself, and the registrar sees the security contract on which the security provider signed (although in theory these need not be in a written agreement).

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<sup>659</sup> UNCITRAL Legislative Guide on Secured Transactions, 176 [8]

<sup>660</sup> *ibid* 176 [8]

<sup>661</sup> UNCITRAL Legislative Guide on Secured Transactions, 176 [8]

<sup>662</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, s 859A

### 6-3-2-3. Consent of Security Provider Required Before Registration

In Korea and Japan and under the Cape Town Convention and the DCFR, the consent of the security provider (or assignor) is required before registration. In Korea and Japan, both a security provider and a secured creditor (or both an assignor and an assignee) must apply together for registration. Under the Cape Town Convention and the DCFR, both parties must consent to the registration before the registration is complete.

#### ***6-3-2-3-1. Korean Security Registration Act***

Under the Korean Security Registration Act, the security provider and the secured creditor must apply together for registration.<sup>663</sup> This is to increase the authenticity of the registration contents. Both of the parties or their agents must visit the registry office and submit the application form in writing,<sup>664</sup> or may apply for the registration online according to the Supreme Court Regulations.<sup>665</sup>

#### ***6-3-2-3-2. Japanese Assignment Registration Act***

Under the Japanese Assignment Registration Act, an assignor and an assignee of a receivable (and in the case of a pledge of a receivable, a pledgor and a pledgee) must apply together for the registration. The parties may apply for the registration of an

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<sup>663</sup> Korean Security Registration Act, art 41(1).

<sup>664</sup> Korean Security Registration Act, art 42(i)

<sup>665</sup> Korean Security Registration Act, art 42(ii)

assignment (or pledge) of receivables either in person by visiting the Registry Office, by post<sup>666</sup> or online.

Since 2001, the Japanese Ministry of Justice has provided an online application system for registration of the assignment of movable assets and receivables. Thus, an assignor and an assignee may register their assignment of receivables on the official website administrated by the Ministry of Justice (<http://shinsei.moj.go.jp>). The registrants should register with their user ID and password and establish an electronic signature. An application that does not satisfy the legal requirements would be rejected. Once it is registered, even if there is a mistake in the online registration application, the parties cannot simply modify the mistake.

Yet, online application has not been commonly used. For example, during December 2005, only 34 (0.9%) out of 3,808 registration applications were submitted by online.<sup>667</sup> The rest were submitted in person or by post. The reason is that the applicants cannot modify mistakes but can only delete the previous registration and reapply for the registration after fixing the mistake unless the error or defect is due to the registry office's mistake.<sup>668</sup> Thus, applicants want to confirm with the registry officer in person that all items to be registered are correct on the application form, so that, if there is a

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<sup>666</sup> Japanese Assignment Registration Order, art 9.

<sup>667</sup> Toshiyuki DOTE, 'Current Utilization and Future Trends of Registration of Assignments of Movable Assets and Receivables', NBL, No. 831 (2006.4.15) 26.

<sup>668</sup> If the registry officer finds an error or defect in the registration of receivables assignment, and the error or defect is due to the registry officer's mistake, the registry officer must modify the error or defect with the permission of the Legal Affairs Bureau, and notify the applicant of the registration of the fact. Japanese Assignment Registration Order, art 12(1). In this case, the registry officer must also notify the Legal Affairs Bureau where the head office of the assignor is located. Japanese Assignment Registration Order, art 12(2).

defect, they can revise the form or add necessary documents immediately.<sup>669</sup> For this reason, applicants actually appear in person at the registration office in Tokyo, Japan.<sup>670</sup>

A system that can allow corrections or modifications in its online application must be designed to build a successful international receivables registration system since registrants from all over the world cannot come to the IRSAR Office each time to register. This problem could be solved, if parties could check and confirm a registration application or a registration amendment application submitted by the other party as the operation of the International Registry of Mobile Assets under the Cape Town Convention and its Aircraft Protocol.

#### ***6-3-2-3-3. Draft Common Framework of Reference (DCFR)***

Under the DCFR, only a secured creditor may apply for registration unilaterally and subsequently a security provider must consent to the application for registration completed by the secured creditor.<sup>671</sup> The DCFR stipulates that ‘an entry in the register can be made only if the security provider has consented to it by declaration to the register.’<sup>672</sup> The DCFR sees that the need for a requirement of the security provider’s consent could be replaced as in UCC Article 9 ‘only if it is sufficiently certain that the

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<sup>669</sup> Interview with Hiroto Dogauchi, Professor, Tokyo University, Faculty of Law (Tokyo University, Tokyo, Japan, 30 May 2008).

<sup>670</sup> There is only one registration office for the assignment of movable assets and receivables under the Japanese Assignment Registration Act in Japan, which is located at Nakano in Tokyo.

<sup>671</sup> *Draft Common Frame of Reference* Outline Edition (Sellier 2009) 466, art IX.-3:306(1)(d); 467, art IX.-3:309.

<sup>672</sup> *ibid* 467, art IX.-3:309(1).

security provider can reply on an efficient enforcement of its position before the court'.<sup>673</sup> However, the DCFR explains that because court proceedings are not yet satisfactorily quick and cost effective in all EU Member States, the DCFR requires the consent of the security provider for the registration.<sup>674</sup>

However, because the consent of a security provider is separated from the registration, the security provider does not always consent to a specific registration that has already been registered. Therefore a discrepancy could occur between the scope of the consent of the security provider and the scope of the registration that has actually been registered.

If the security provider gives its consent before the registration is actually registered or separately from the application procedure for the registration, there could be a discrepancy between the security provider's consent and the registration in terms of scope.

There are two ways to give consent to a specific registration. Either the consent of the security provider is given in the registration application or the consent to a specific registration is made after it is registered. Otherwise, there could be discrepancy between the registration and the consent for the registration.

For this reason, the DCFR creates three possible types of consent declarations: (1) unlimited consent in favour of a specified secured creditor; (2) consent to an entry with a specified content; and (3) partially limited consent.<sup>675</sup> However, because an online

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<sup>673</sup> *Draft Common Frame of Reference Full Edition Vol 6, Book IX (Sellier 2009) 5508, Comments to art IX.-3:309.*

<sup>674</sup> *ibid*

<sup>675</sup> *ibid* 5509-10, Comments to art IX.-3:309

system of registration cannot evaluate whether the content of the entry inputted by a secured creditor is the same as that provided by the security provider, the second type is not able to be used in an online system with automatic registration.<sup>676</sup>

#### **6-3-2-3-4. Cape Town Convention**

In the International Registry of Mobile Assets under the Cape Town Convention and the Aircraft Protocol, there is no authority review or human intervention in the process of registration.<sup>677</sup> Thus, it requires reciprocal consents of the parties without the registrar's review to increase the authenticity of the contents of registration. It requires consents from both the security provider and the secured creditor before the registration appears on the website of the International Registry of Mobile Assets. The IRSAR would also follow this reciprocal consents system.

Under the Cape Town Convention, either a security provider or a secured creditor applies for registration and the other party gives consent to the application through email. Each named party, other than the registering party, is required to consent in order for a registration to become effective.<sup>678</sup> If a party to a security agreement registers the security interest on the official website of the International Registry of Mobile Assets ([www.internationalregistry.aero](http://www.internationalregistry.aero)), the other party to the security agreement must log on

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<sup>676</sup> *ibid* 5510, Comments to art IX.-3:309

<sup>677</sup> See Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008) 201 [4.132].

<sup>678</sup> Cape Town Convention, art 20(1).

the website, check the information and transmit his consent electronically.<sup>679</sup> Either an assignor or an assignee may apply for the registration and then the other party will have to give consent to the application.<sup>680</sup> Once a registering party has entered the information on the website and has electronically signed it, each party identified in the registration will be notified by email sent by the system automatically and will be given 36 hours to consent on the website.<sup>681</sup> Upon receipt of the final consent, the registration becomes searchable.<sup>682</sup> If the other party fails to give its consent within the 36-hour period, the registration application will be automatically cancelled.<sup>683</sup> Registrations, amendments or discharges that are initiated but not completed, will not appear on any search results on the website.<sup>684</sup>

### **6-3-3. IRSAR Registration Procedure**

As Goode has said, the parties' reciprocal confirmation of the registration information is 'an important safeguard against improper registration'<sup>685</sup> particularly for an online registration system where no human intervention is involved to review the

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<sup>679</sup> Cape Town Convention, art 18(1)(a).

<sup>680</sup> Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008) 207 [4.146].

<sup>681</sup> Regulations and Procedures for the International Registry, Procedures, ss 12.2(a) and (b)

<sup>682</sup> In practice, usually, all relevant parties gather together in an office bringing laptop computers and right after one party registers online, the other parties immediately transmit their consent online. In this way, it can be a real-time registration.

<sup>683</sup> Regulations and Procedures for the International Registry, Procedures, s 12.2

<sup>684</sup> Regulations and Procedures for the International Registry, Procedures, s 12.7

<sup>685</sup> Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008) 207 [4.146].

information registered. In the IRSAR, there would be no authority to review or human intervention. Thus, the IRSAR would need to ensure the authenticity of the registration contents. If the law would require the consent of the VIRS, that is the security provider (or assignor), in advance of registration, it could prevent the VIRS from going through the difficult procedures to cancel an incorrect registration done by a secured creditor (or assignee) afterwards where there is some errors with the registration. For this reason, the proposed IRSAR Convention requires consent of the VIRS for registration of a security interest (or assignment) submitted by the secured creditor (or assignee).

Under the proposed IRSAR Convention, a security interest in (or assignment of) receivables may be registered in the IRSAR either by the VIRS or the secured creditor (or assignee). If the security interest (or assignment) is registered by the VIRS, the IRSAR system will request the secured creditor (or assignee) to confirm the registration information entered by the VIRS. Conversely, if the security interest in (or assignment of) receivables is registered by the secured creditor (or assignee), the IRSAR system will request the VIRS to confirm the registration information entered by the secured creditor (or assignee).<sup>686</sup>

Once one party, either the VIRS or the secured creditor (or assignee), logs on the website of the IRSAR, completes the electronic forms contained on the website, and inserts registration information about the security interest in (or assignment of) receivables, the other party would be notified by email.<sup>687</sup> The other party will be given

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<sup>686</sup> Draft IRSAR Convention, art 14(2). See 324

<sup>687</sup> Draft IRSAR Convention, art 14(2)(a). The IRSAR would be operated under the same principle as the International Registry of Mobile Assets under the Cape Town Convention and its Aircraft Protocol. Each company would be able to sign in to the online IRSAR website and post their receivables assignment records voluntarily.

the opportunity, logging onto the website, to consent to the registration made by one party unilaterally before the registration becomes searchable on the website. If the other party logs on the website and confirms the registration, the specific assignment of receivables would be registered immediately. Initiated, but not completed, registrations will not appear on any search results on the website.<sup>688</sup>

Email addresses are very important because every notice regarding the registration would be sent by email. The consent of the other party would also be initiated by the email automatically sent by the operation system.<sup>689</sup> Each user should provide three email addresses for receiving notices and the registration system should send the notice simultaneously to all three to be sure notice is received.

The process of amendment or discharge of a registration is the same as the application for registration, which requires the parties' reciprocal consents.<sup>690</sup> If there is a mistake in the registration information, the parties may revise the registration in the same manner with both of parties' consent but the date of registration will be recorded as of the revised date and time. As a result, though the parties might lose priority, it is their responsibility. As such, making the parties accountable for any mistakes without official review of the registrar, the system can eliminate the time gap between application and registration and finally accomplish real time registration.<sup>691</sup>

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<sup>688</sup> Draft IRSAR Convention, art 14(4). See 325

<sup>689</sup> Draft IRSAR Convention, art 14(2). See 324

<sup>690</sup> Draft IRSAR Convention, art 14. See 324

<sup>691</sup> The English Law Commission Report also recommended that the 21-day time gap between the assignment and registration should be abolished, and that removing the 21-day period of invisibility can be achieved by the combination of a notice-filing system and an online operation system. Law Commission, 'Company Security Interests' (Law Com No 296 Cm 6654, 2005) 4 [1.9], 52 [3.82]

## **6-4. METHOD OF GIVING NOTICE OF THE ASSIGNMENT TO THE DEBTOR**

### **6-4-1. Notice to the Debtor**

Notice of the assignment to the debtor of the receivable entitles the assignee to sue the debtor of the receivable. If the debtor of the receivable has received notice of the assignment, the assignee can sue and collect the receivable from the debtor. Thus, the debtor needs to be notified of the assignment.<sup>692</sup> In both the assignment of a receivable and the security interest in a receivable notice of the assignment or the security interest to the debtor of the receivable is required to sue the debtor of the receivable.

Where an assignee, who is unfamiliar to the debtor of the receivable, gives notice of the assignment to the debtor, the assignee must present the debtor with evidence of the assignment. IRSAR registration can be a good evidence of the assignment (or security interest) since the IRSAR requires reciprocal confirmation of registered information by both the assignor and the assignee.

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<sup>692</sup> Naturally, a creditor would first ask the debtor to pay the debt before bringing the case to the court. If an assignee sues a debtor without giving notice of the assignment, a court would deny the assignee's claim on the fact that the assignee does not have a proper cause of action.

## **6-4-2. Comparative Analysis**

### **6-4-2-1. Assignees Not entitled to Give Notice to the Debtor**

In some jurisdictions, only an assignor can give notice of the assignment to the debtor of the receivable.

Under the Korean and the Japanese Civil Codes, only an assignor can give valid notice of the assignment to the debtor.<sup>693</sup> An assignee is not entitled to give notice of the assignment to the debtor. Notice of the assignment by an assignee is invalid. It is because an assignee is unfamiliar to the debtor of the receivable. Thus, an assignee needs the cooperation of an assignor to give notice of the assignment to the debtor.

In receivables financing, assignors do not want to notify debtors of the assignment of receivables because it might damage the assignor's financial health or credit reputation. Therefore, in practice, the assignor and the assignee do not usually send notice of the assignment to debtors, and the assignor reserves the right to collect debts from debtors even after the assignment of receivables.

Under the Korean and the Japanese Civil Codes, if the assignor becomes bankrupt before the assignor gives notice of the assignment to the debtor, the assignee himself cannot give notice of the assignment to the debtor. As a result, the assignee cannot claim the debt directly against the debtor, and can only participate in the distribution proceedings of the insolvency assets as an unsecured creditor. This is a serious problem.

For this reason, in Korea and Japan, assignees need to ensure that the assignor gives notice of the assignment to the debtor before the assignor becomes bankrupt. Such

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<sup>693</sup> Section 6-4-2-1

notice of the assignment to the debtor must be done by means of a certified document with a fixed date stamp.<sup>694</sup> In receivables financing where too many account debtors are involved, it is very expensive to send notice to all of the debtors.

#### 6-4-2-2. Assignees Entitled to Give Notice to the Debtor

In some jurisdictions, both an assignor and an assignee may give notice of the assignment to the debtor. In these jurisdictions, when an assignee gives notice of the assignment to the debtor of the receivable, the assignee needs evidence to prove to the debtor that he or she is a lawful assignee.

In the US, France and Germany, both an assignor and an assignee may give notice of the assignment to the debtor. Under UCC Article 9, both the assignor and the assignee may give notice of the assignment to the debtor.<sup>695</sup> Where an assignee gives notice of the assignment to the debtor of the receivable, the assignee ‘shall seasonably furnish reasonable proof that the assignment has been made’ if requested by the debtor.<sup>696</sup>

Under the French Civil Code, both the assignor and the assignee may give notice of the assignment to the debtor.<sup>697</sup> However, such notification to the debtor must be done by an official letter (*signification*) delivered by a court bailiff (*huissier*).<sup>698</sup>

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<sup>694</sup> Korean Civil Code, art 450(1); Japanese Civil Code, art 467(1)

<sup>695</sup> UCC, s 9-404(a)(2). It stipulates that the rights of an assignee are subject to any defence or claim of the account debtor against the assignor, which accrue before the account debtor receives a notification of the assignment authenticated *by the assignor or the assignee*. (emphasis added)

<sup>696</sup> UCC, s 9-406(c).

<sup>697</sup> French Civil Code, art 1691. It stipulates that a debtor of a receivable may be discharged of the debt by paying the assignor before the debtor has been given notice *by the assignor or the assignee*. (emphasis added)

Under German law, notice of the assignment to the debtor is not required for the assignment of receivables.<sup>699</sup> Still, an assignee needs to give notice of the assignment to the debtor in order to sue on the debt.<sup>700</sup> Where an assignee gives notice of the assignment to a debtor of a receivable, the assignee should deliver the document relating to the assignment issued by the assignor to the debtor. If an assignor has issued a document that relates to the assignment to an assignee named in the document, the assignee's presentation of the document to the debtor is equivalent to notice of the assignment.<sup>701</sup> The debtor's obligation to the assignee is to perform only in exchange for the delivery of the document relating to the assignment, issued by the assignor.<sup>702</sup>

Under the Korean and the Japanese Civil Codes, an assignee cannot give notice of the assignment to the debtor. However, under the Korean Security Registration Act,<sup>703</sup> the Korean ABS Act, the Korean MBS Company Act<sup>704</sup> and the Japanese Assignment Registration Act,<sup>705</sup> a secured creditor or an assignee is also entitled to give notice of the security interest or the assignment to the debtor of the receivable by delivering a certificate of registration.<sup>706</sup> It is because a certificate of registration can evidence the

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<sup>698</sup> French Civil Code, art 1690.

<sup>699</sup> Appendix II. 12 Q1-1

<sup>700</sup> Even though notice of the assignment to the debtor is not required by law, it is typical to notify the debtor that the receivable is assigned to the assignee before filing a lawsuit against the debt. No one would file such a lawsuit without first asking the debtor to pay the debt.

<sup>701</sup> German Civil Code, s 409(1)

<sup>702</sup> German Civil Code, s 410(1)

<sup>703</sup> Act No. 10366, enacted on 10 June 2010, entered into force on 11 June 2012.

<sup>704</sup> Korean ABS Act, art 7(1); Korean MBS Company Act, art 6(1). Both an assignee and an assignor are entitled to give effective notice of the assignment to the debtor of the receivable if the securitisation plan, according to which the receivables are assigned, is filed at the Financial Services Commission of Korea.

<sup>705</sup> Act No. 87 of 2005, amended on 26 July 2005 and entered into force on 3 October 2005.

<sup>706</sup> Korean Security Registration Act, art 35(2); Japanese Assignment Registration Act, art 4(2)

security interest or the assignment. Under the Korean Security Registration Act, both a security provider and a secured creditor must together apply for registration.<sup>707</sup> Under the Japanese Assignment Registration Act, an assignor and an assignee must apply together for registration.<sup>708</sup> As a result, once a security interest or an assignment is registered, it means that a security provider or an assignor has agreed on the registration unless its consent is fraudulent in some way.

### **6-4-3. Email Notification linked to IRSAR Registration**

The proposed IRSAR Convention adopts a similar approach as the Korean Security Registration Act and the Japanese Assignment Registration Act. Under these acts, a secured creditor or an assignee may give notice of the security interest or the assignment to the debtor of the receivable by presenting a certificate of registration to the debtor of the receivable, even though under the Korean and the Japanese Civil Codes, a secured creditor and an assignee cannot give notice of the security interest or the assignment to the debtor of the receivable.<sup>709</sup> The rationale is that those Registration Acts require both the security provider and the secured creditor<sup>710</sup> or both the assignor and the assignee<sup>711</sup> together apply for registration, which verifies the contents of registration.

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<sup>707</sup> Korean Security Registration Act, art 41(1).

<sup>708</sup> Japanese Assignment Registration Act, art 8(2).

<sup>709</sup> See Section 6-4-2-1

<sup>710</sup> Korean Security Registration Act, art 41(1)

<sup>711</sup> Japanese Assignment Registration Act, art 8(2)

Under the proposed IRSAR Convention, an assignee (or secured creditor) may also give notice of the assignment (or security interest) to the debtor of the receivable providing the web address of the relevant IRSAR registration, which can evidence the assignment (or security interest).<sup>712</sup> This provision prevails over national laws. Thus, even if under national laws, an assignee (or secured creditor) is not entitled to give notice of the assignment (or security interest) to the debtor of the receivable, in a Contracting State an assignee (or secured creditor) is entitled to do so under the proposed IRSAR Convention.

The web address of the relevant IRSAR registration can be conveniently provided to the debtor, e.g. through email. For this, the assignee or secured creditor needs to ask the assignor or the security provider for the email addresses of the debtors of receivables. The IRSAR can be designed to support email notification where an assignor or an assignee gives notice of assignments of or security interests in receivables to the debtor of the receivable. Once the parties register an assignment of or a security interest in receivables on the IRSAR website, an assignee or secured creditor would be able to give notice of the assignment or security interest to the debtor of the receivable through an email containing the link to the relevant registration webpage on the IRSAR website. Then, clicking the linked web address would lead to the webpage containing the relevant registration. By just clicking the link in the email, the debtor of the receivable would be referred to the relevant registration webpage on the IRSAR website.

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<sup>712</sup> Draft IRSAR Convention, art 15. See 325

## 6-5. SUPERVISORY AUTHORITY & REGISTRY

Under the proposed IRSAR Convention, the IRSAR Registrar would have to be based somewhere. The International Registry of Mobile Assets under the Cape Town Convention and the Aircraft Protocol is the only international registry operating today and is a good example for the supervisory authority and the registrar for the IRSAR. The supervisory authority of the International Registry of Mobile Assets for aircraft objects is the Council of the International Civil Aviation Organisation ('ICAO'), which is a specialised agency of the United Nations.<sup>713</sup> The ICAO is advised by a Commission of Experts of the Supervisory Authority of the Aircraft Registry ('CESAIR').<sup>714</sup> The International Registry of Mobile Assets is located in Dublin, Ireland and the online registration system is operated completely by IT facilities. The International Registry of Mobile Assets was set up by Aviareto, a joint venture company of SITA SC<sup>715</sup> and the Irish government.<sup>716</sup> SITA SC owns 80 % of the shares while the Irish Government owns 20%. The International Registry of Mobile Assets is run by Aviareto pursuant to a five-year contract with ICAO.<sup>717</sup> Aviareto is assisted by the International Registry Advisory Board ('IRAB').<sup>718</sup>

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<sup>713</sup> Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008) 49 [2.67].

<sup>714</sup> *ibid.*

<sup>715</sup> SITA SC is an air transport telecommunications company owned by the world's airlines.

<sup>716</sup> Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008) 117 [3.30].

<sup>717</sup> *ibid.*

<sup>718</sup> IRAB is set up by Aviareto as Registrar to provide advice to the Registrar on matters relating to the operations of the Registry. *ibid.*

The supervisory authority and the IRSAR Registrar would be established as outlined in the proposed IRSAR Convention. It would be desirable if a specialised agency of the United Nations could be the supervisory authority. The IRSAR Registrar would be operated by online notice-filing system to reduce registration fees and to make registration real time 24 hours a day, 365 days a year. The IRSAR Registrar would not require applicants to submit transaction documents. Registration would be operated mainly in English and, if possible, simple legal terminology could be translated into several languages.

The International Registry of Mobile Assets under the Cape Town Convention distinguishes registry user entities and searching persons.<sup>719</sup> Registration is searchable by any member of the public but access for the purpose of amending or discharging registrations is tightly controlled. It is restricted to a registry user entity or an administrator of that entity,<sup>720</sup> approved, ‘when the Registrar reasonably concludes: (a) that such entity and administrator are who they claim to be; and (b) on the basis of information submitted, and without undertaking specific legal analysis, that the latter is entitled to act as administrator of the former’.<sup>721</sup> It is the Registrar’s job to investigate the identity of registry user entities or administrators of those entities.

Following the practice of the International Registry of Mobile Assets, the IRSAR Registrar would also have to investigate the identity of registry users. Registrars at the IRSAR would not review or conduct further scrutiny on the contents of registration

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<sup>719</sup> Roy Goode, *Official Commentary on the Convention on International Interests in Mobile Equipment and the Protocol thereto on Matters Specific to Aircraft Equipment* (Revised edition 2008) 119 [3.36].

<sup>720</sup> *ibid*

<sup>721</sup> Regulations and Procedures for the International Registry, Regulations, s 4.1

applications,<sup>722</sup> but would only check and confirm the identity of registry users. To log in to the IRSAR website, a legal person should have membership which would require an identification check by the IRSAR Registrar using phone calls, etc.

## **6-6. SEARCH FOR REGISTRATION**

This section explores the possibilities relating to search for registration in the UK, the US and Japan and under the Cape Town Convention as meaningful examples of differing approaches.

### **6-6-1. UK Register of Company Charges**

Any person may inspect the register under the Companies Act 2006.<sup>723</sup> A party searching the registry and obtaining details of a registered charge may further inspect a copy of the charge document at the company's registered office.<sup>724</sup> The documents and a company's register of charges must be made available for inspection at the company's registered office.<sup>725</sup> Where the company and a person wishing to carry out an inspection agree, the inspection may be carried out by electronic means.<sup>726</sup> Extracts of each of the

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<sup>722</sup> Cf. UNCITRAL Legislative Guide on Secured Transactions, Recommendation 54(d)

<sup>723</sup> Companies Act 2006, s 1085(1)

<sup>724</sup> The documents and register shall be open to the inspection of any creditor or member of the company without charge, and of any other person on payment of the fee. Companies Act 2006 (Amendment of Part 25) Regulations 2013, s 859Q(4)

<sup>725</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, s 859Q(2) and (3)

<sup>726</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, s 859Q(8)

charges registered against a company are searchable online on the website of the Companies House ([www.companieshouse.gov.uk](http://www.companieshouse.gov.uk)).

### **6-6-2. UCC Article 9**

On the official websites of some states of the US, it is possible to conduct a free unofficial search.<sup>727</sup> On some official websites, log-in is required for searching the registry but in others, log-in is not required. On some official websites, searching the registry is free and in others it is not free.

### **6-6-3. Japanese Assignment Registration Act**

In Japan, there are three types of certificate with regard to the registration of movable assets and receivables. They are (1) the Certificate of Registered Matters, (2) the Certificate of Summary of Registered Matters, and (3) the Certificate of Matters Recorded in Summary. They differ in terms of what information is included on the certificate, who can apply for the issuance of the certificate, and which office issues the certificate.

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<sup>727</sup> For example, Utah: <http://www.utah.gov/uccsearch>  
Florida: <http://www.floridaucc.com/UCCWEB/search.aspx>  
Tennessee: [http://www.tn.gov/sos/bus\\_svc/iets3/ieuc/PgUCCSearch.jsp](http://www.tn.gov/sos/bus_svc/iets3/ieuc/PgUCCSearch.jsp)  
Wisconsin: <http://www.wdfr.org/ucc/search>  
Iowa: <http://www.sos.state.ia.us/Search/UCC/search.aspx>.

<Table 16> Three Types of Registration Certificates in Japan

	Certificate of Registered Matters <sup>728</sup>	Certificate of Summary of Registered Matters <sup>729</sup>	Certificate of Matters Recorded in Summary <sup>730</sup>
Applicant	1. Assignor 2. Assignee 3. Debtor 4. Interested party specified by the government ordinance 5. Employer of the assignor	Anybody	Anybody
Certified Items	1. Assignor's name and address 2. Assignee's name and address 3. Debtor's name and address 4. Registration number 5. Registration date 6. Type of the contract upon which the receivables accrue and the contract date 7. Total amount of the receivables assigned at the time of the assignment 8. Valid term of the registration 9. Purpose of registration 10. Reason of extension registration 11. number of assignors and number of assignees	1. Assignor's name and address 2. Assignee's name and address  3. Registration number 4. Registration date 5. Type of the contract upon which the receivables accrue and the contract date 6. Total amount of the receivables assigned at the time of the assignment 7. Valid term of the registration	1. Assignor's name and address 2. Assignee's name and address  3. Registration number 4. Registration date  5. Recorded date
Issuing Office	Registry Office for the Assignment of Movable Assets and Receivables (Receivables Registration Department, Civil Administration Division of the Tokyo Legal Affairs Bureau in Nakano ward, Tokyo)		District Registry Offices of Commercial Registry covering the assignor's domicile

<sup>728</sup> Japanese Assignment Registration Act, art 11(2); Japanese Assignment Registration Order, art 15

<sup>729</sup> Japanese Assignment Registration Act, art 11(1).

<sup>730</sup> Japanese Assignment Registration Act, art 13.

#### **6-6-4. Cape Town Convention**

The general public is permitted to search the International Registry of Mobile Assets under the Cape Town Convention and its Aircraft Protocol to determine the priority of interest in particular assets on the official International Registry of Mobile Assets website ([www.internationalregistry.aero](http://www.internationalregistry.aero)). The search is not free.<sup>731</sup>

#### **6-6-5. IRSAR Online Search**

Having compared the legal systems above, this thesis proposes that the search systems in the US and under the Cape Town Convention are more appropriate for the IRSAR, while the search systems in the UK and Japan are rather problematic. In the UK, the problem is the 21-day gap between the creation of security interests and registration. In Japan, the problem is because a potential assignee is unable to search the registry directly. Instead, he must apply for issuance of a registration certificate of sorts and then has to wait a couple of days. In Japan, a potential assignee can apply for the issuance of a registration certificate online but cannot search the registry online. This system would not work for an international registry.

In the IRSAR, any person should be able to search registration online on the IRSAR website.<sup>732</sup> Applications for registration must be restricted to the legal person whose identification is strictly checked and confirmed. After the identification scrutiny, a legal person should pay fees for an ID and password to use the IRSAR but access to the

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<sup>731</sup> Regulations and Procedures for the International Registry, Appendix, Fee Schedule, s 1.8.

<sup>732</sup> Draft IRSAR Convention, art 19. See 326

registered information should be free. On this basis, notification of the assignment through email with the link to the webpage of the relevant registration would be available.<sup>733</sup>

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<sup>733</sup> See Section 6-4-3

## **6-7. CONCLUSION OF PART 6**

With respect to the contents and effect of IRSAR registration, the IRSAR would be in the shape of a notice-filing system along the lines of that adopted in UCC Article 9 and the PPSAs. This is because in the IRSAR, there would not be a registrar to review the documents submitted and it would be operated automatically online in order to realise a real time registration. No human intervention is involved in the process of IRSAR registration. For this reason, to increase the authenticity of the registration information, reciprocal confirmation of an assignor and an assignee (or a security provider and a secured creditor) regarding the registration information would be required for registration. Contents of IRSAR registration should be double checked by the parties' reciprocal confirmation.

Providing registration web address could be a good evidence of proving an assignment of or security interest in VIRS receivables, with which an assignee may give notice of the assignment to the debtor of the receivable. It would facilitate email notification linked to IRSAR registration to the debtor of the receivable. A party could send notice of the assignment to debtors of receivables through emails containing the link to the relevant international registration. So, debtors could refer to the relevant international registration by just clicking the link in the email.

In the IRSAR, an intending assignee could access the registry online in order to check whether a certain receivable has been assigned. Anybody should be able to search the IRSAR online.

## **PART 7. CONCLUSION**

This thesis first analysed the need for an international registration system for the assignment and security interest of receivables, and compared the registration system for the assignment of receivables of each jurisdiction, and then proposed establishing an international registration system for the assignment and security interest of receivables. Furthermore, this thesis presented a proper model for an international registration system for the assignment and security interest of receivables. The Cape Town Convention has established the first example of an international registration system for mobile equipment such as airplanes and railway rolling stock. This demonstrates that an international registration system for the assignment and security interest of receivables is also possible. The UN Receivables Convention is a move towards establishing international registration systems. It sets forth in its Annex alternative priority rules based on registration for states to choose.

Establishing an international registration system is desirable for several reasons. A registration system for security interests has many benefits. It enables companies to obtain more funding by using their movable assets and receivables as security. For investors, a registration system for security interests provides financial information about companies and the basis for further *ex ante* investigation before entering into transactions. After closing a transaction, it provides an *ex post* mechanism for secured creditors to prove, as an evidentiary matter, the existence of their security interests and the time when they were registered by the order of which priority is determined. Priority is determined by the order of registration in the IRSAR.

The key point of a general security rights registry is to meet the economic demand for non-possessory security interests in tangible movable assets. For tangible movable assets, non-possessory security interests are needed for a company to use its equipment and inventory as security. These advantages of a general security rights registry also apply to an international registration system for the assignment and security interest of receivables.

In an international level, establishing a general security rights registry which covers all movable assets and receivables might not be recommendable due to over-leverage and credit expansion problems, and would be impractical because of translation and identification problems. For these reasons, this thesis focuses on the registration system for assignments of and security interests in receivables.

The IRSAR has the following merits. The IRSAR would definitely facilitate international trades of receivables. It could also facilitate international receivables financing using future receivables and bulk receivables. The IRSAR would pave the way for the cross-border assignment of receivables. The IRSAR could help receivables financing to cross national borders, so that entrepreneurs can raise funds from a greater range of investors in global capital markets. It would ultimately result in efficient distribution of capital at a global level. International receivables financing is very important especially during a financial crisis. Since every company and every financial institution is influenced by a financial crisis and cash-flow is frozen, an influx of foreign capital is necessary. The IRSAR would also facilitate international project financing.

However, legal systems around the world vary widely in how they deal with priority and perfection of assignments of and security interests in receivables and choice

of law rules in private international laws. This legal variety makes it difficult for financiers to conduct their international receivables financing business. Under such circumstance, in order to facilitate international receivables financing this thesis proposes the IRSAR. Under the proposed IRSAR Convention, the international assignment of receivables would be regulated by a unified legal system with respect to priority and perfection. The proposed IRSAR Convention could help financiers to overcome the obstacles they currently encounter. The IRSAR would enable companies to raise finance from greater ranges of investors around the world through international receivables financing and to dispose of non-performing loans more easily.

In receivable financing, it is impractical for financiers to ask the account debtors whether they received notice of a prior assignment or security interest before the assignment and to give notice of the assignment to account debtors after the assignment. One registration in the IRSAR can replace an unlimited number of notifications.

The IRSAR would pave the way of circumventing the notification requirement in some jurisdictions where notice of the assignment to the debtor is required for third party effectiveness. This function is essential to facilitate the assignment of future receivables and bulk assignments of receivables. Giving notice of the assignment to all account debtors is impossible in the assignment of future receivables, and impractical in bulk assignments of receivables. It is time-consuming and costly.

The registration system may be created as optional or compulsory. Optional registration brings about the situation where a potential assignee needs to check both the IRSAR and national laws and perfection methods e.g. registry or notice to the debtor. In one country it might be practicable to check both the registry and enquire of account

debtors. However, in an international level, it would be impracticable because the would-be assignee should check all of the national registries since a potential hidden competing assignee might be in any country. This could defeat the object of international registration.

For this reason, the IRSAR is designed as compulsory registration which prevails over national perfection. However, it requires limitation of the scope of application, because otherwise all assignments of and security interests in receivables, domestic or international, must be registered in the IRSAR, which would be too large to manage at reasonable cost whilst keeping the registration fee at an affordable level. The proposed IRSAR Convention confines its scope of application by defining the assignor or the security provider and inventing the concept of 'VIRS'. The proposed IRSAR Convention applies where the assignor or security provider is a VIRS.

Under the proposed IRSAR Convention, priority of assignments of and security interests in VIRS receivables is determined by the order of IRSAR registration. With respect to the double debtor problem, under the proposed IRSAR Convention, if a VIRS assigns its receivable to a non-VIRS entity and the non-VIRS entity assigns the receivable to a third party, the third party takes the receivable free of any security interests registered in the IRSAR. Thus, a potential assignee or secured creditor only has to investigate the IRSAR against the direct counterparty VIRS and does not have to search against the assignor of the assignor. If the assignor is not a VIRS, the assignee has no obligation to check the IRSAR before purchasing the receivable. As a result, IRSAR registration of a security interest might lose its effectiveness after two consecutive assignments of the receivable.

For the protection of secured creditors registered in the IRSAR, to assign a VIRS receivable to a non-VIRS entity, the IRSAR requires the consent of all prior secured creditors registered in the IRSAR, who hold security interests in the receivable including the secured creditors of the former VIRS assignors. However, to assign a VIRS receivable to another VIRS, the consent of prior secured creditors is not required and the security interests registered in the IRSAR would be protected.

With respect to reservation of title, the automatic perfection period in some jurisdictions might produce uncertainty with respect to the priority rule of registration, but it is relatively short period. A Contracting State may declare this as a non-consensual right under Article 10 of the proposed IRSAR Convention. The categories of preferential creditors who have super-priority may be determined and declared by the Contracting State.

A registered floating security interest equipped with a negative pledge clause prevails over subsequently registered security interests but not a subsequently registered assignment. A security interest (including a floating security interest) covers the proceeds of the receivables if they are separated and identifiable. The priority of competing security interests under the proposed IRSAR Convention may be varied by subordination agreement between secured creditors.

With respect to the contents and effect of IRSAR registration, the IRSAR would be in the shape of a notice-filing system along the lines of that adopted in UCC Article 9 and the PPSAs. This is because in the IRSAR there would not be a registrar to review the documents submitted and it would be operated automatically online in order to realise a real time registration. Furthermore, since there would not be any human intervention in

the process of IRSAR registration, to increase the authenticity of the registration information, reciprocal confirmation of an assignor and an assignee (or a security provider and a secured creditor) regarding the registration information would be required for registration as under the Cape Town Convention.

Under the proposed IRSAR Convention, a party could send notice of the assignment to debtors of receivables through emails containing the link to the relevant international registration of the assignment of receivables on the IRSAR website. Debtors could refer to the relevant international registration by just clicking the link in the email. This system is safe from email fraud because the contents of the website of the IRSAR cannot be changed.

The proposed IRSAR Convention would be a receivables version of the Cape Town Convention. Priority would be determined by the order of IRSAR registration. With respect to the contents and effect of IRSAR registration, it would be in the shape of a notice-filing system along the lines of that adopted in UCC Article 9 and the PPSAs. Operationally, it would be an automatic online registration system operating 24 hours a day, 365 days a year like the International Registry of Mobile Assets under the Cape Town Convention. It is expected and hoped that the proposed IRSAR Convention could be signed and ratified by more states than the UN Receivables Convention.

**APPENDIX I. DRAFT CONVENTION ON PRIORITY OF ASSIGNMENTS OF AND  
SECURITY INTERESTS IN RECEIVABLES (‘DRAFT IRSAR CONVENTION’)**

Article 1 (Definitions)

In this Convention, except where the context requires otherwise, the following terms have the meanings set out below:

(a) “Assignment” means the transfer by agreement from one person (assignor) to another person (assignee) of an interest in the assignor’s contractual right to payment of a monetary sum (receivable) from a third person (the debtor of the receivable);<sup>734</sup>

(b) “Consenting party” is a party whose consent is required in accordance with Article 8(2) of this Convention in order for a registration, amendment or discharge to become effective (in an assignment of a receivable, if a VIRS is a registering party, a consenting party is an assignee, and if an assignee is a registering party, a consenting party is a VIRS; in a security interest in a receivable, if a VIRS is a registering party, a consenting party is a secured creditor, and if a secured creditor is a registering party, a consenting party is a VIRS);<sup>735</sup>

(c) “Floating security interest” is a security interest over all present and future receivables subject to change in quantity and value while the VIRS is allowed to dispose of its receivables, and becomes crystallised into a security interest in all the receivables that the VIRS has outstanding at the time of the crystallisation.

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<sup>734</sup> Cf. UN Receivables Convention, art 2

<sup>735</sup> Cf. Regulations and Procedures for the International Registry, Regulations, s 2.1.7

(d) “Insolvency representative” means a person or body, including one appointed on an interim basis, authorized in insolvency proceedings to administer the reorganization or the liquidation of the insolvency estate;<sup>736</sup>

(e) “International Registration System” means the international registration system for the assignment of and security interest in receivables established for the purposes of this Convention;<sup>737</sup> “IRSAR” is the abbreviation for “International Registration System”;

(f) “Judgment creditor” means a creditor, under the national laws of a Contracting State, who has obtained a judgement or provisional court order against the assignor or the security provider;<sup>738</sup>

(g) “Receivable” means an intangible monetary claim, excluding a right to payment evidenced by a negotiable instrument, a right to receive the proceeds under an independent undertaking and a right to payment of funds credited to a bank account;<sup>739</sup>

(h) “Registering party” is a party who completes the electronic forms with the relevant information required for registration in accordance with Article 8(1) of this Convention (in an assignment of a receivable, either a VIRS or an assignee is a registering party, in a security interest in a receivable, either a VIRS or a secured creditor is a registering party);<sup>740</sup>

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<sup>736</sup> Cf. UNCITRAL Legislative Guide on Secured Transactions, Terminology

<sup>737</sup> Cf. Cape Town Convention, art 1(p)

<sup>738</sup> Cf. UNCITRAL Legislative Guide on Secured Transactions, Recommendation 84

<sup>739</sup> Cf. UNCITRAL Legislative Guide on Secured Transactions, Terminology

<sup>740</sup> Cf. Regulations and Procedures for the International Registry, Regulations, s 2.1.9

(i) “Security provider” means a person that creates a security interest in a receivable to secure either its own obligation or that of another person;<sup>741</sup> and

(j) “Security interest” means a property right in a receivable that is created by agreement and secures payment, regardless of whether the parties have denominated it as a security interest. The term does not include a personal right against a guarantor or other person liable for the payment of the secured obligation.<sup>742</sup>

(k) “Vehicle for the International Registration System” is a special purpose company registered with the IRSAR Registrar in order to use the International Registration System. “VIRS” is the abbreviation for “Vehicle for the International Registration System”.

(l) A “VIRS receivable” is a receivable of a VIRS.

(m) “IRSAR registration” is registration of an assignment of, or a security interest in, a VIRS receivable in the IRSAR.

(n) “VIRS registration” is registration of a company as a VIRS with the IRSAR Registrar.

## Article 2 (Sphere of Application)

(1) This Convention applies to assignments of and security interests in receivables, present or future, in which the assignor or security provider is a VIRS.

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<sup>741</sup> Cf. UNCITRAL Legislative Guide on Secured Transactions, Terminology

<sup>742</sup> Cf. UNCITRAL Legislative Guide on Secured Transactions, Terminology

(2) A VIRS may assign its receivables or provide security interests in its receivables to legal persons that have company registration numbers in their States.

### Article 3 (Registration of Vehicle for the International Registration System)

(1) A company may be created as a VIRS by the registration with the IRSAR Registrar.

(2) An existing company may register itself as a VIRS with the IRSAR Registrar and become a VIRS from the time of the registration.

(3) The IRSAR Registrar must publish the list of registered VIRS.

(4) This Convention does not apply to a pre-existing security interest, which retains the priority it enjoyed under the applicable national law prior to the date of the VIRS registration of a company for one year from the date of the VIRS registration. After the one year, this Convention will become applicable, for the purpose of determining priority, including the protection of any existing priority, to pre-existing security interests.<sup>743</sup>

### Article 4 (Deregistration of Vehicle for the International Registration System)

(1) A VIRS may recover its ordinary company status by deregistering itself from the IRSAR Registrar.

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<sup>743</sup> Cf. Cape Town Convention, art 60

(2) In order to deregister a VIRS, the consent of all assignees and secured creditors of the receivables of the VIRS, previously registered with the IRSAR, is required.

(3) One year before the date of deregistration ('D-date'), prior notice must be registered with the IRSAR as follows: 'this company will be deregistered from the list of VIRS and the status of this company will be changed into an ordinary company from the D-date, and this Convention shall not apply to assignments of or security interests in the receivables of this company from the D-date.'

#### Article 5 (Priority)

(1) A registered assignment of or security interest in a receivable has priority over any other assignment of or security interest in the receivable subsequently registered and over an unregistered assignment of or security interest in the receivable, even if the registered assignee or secured creditor has notice of the prior assignment or security interest.

(2) Priority between competing assignments or security interests is determined by the order of registration of the assignment or security interest in the IRSAR (as defined in Article 11).

## Article 6 (Perfection)

(1) Upon registration of an assignment of a receivable or a security interest in a receivable in the IRSAR, the assignment or the security interest is perfected against the insolvency representative of the assignor or the security provider, if the registration information becomes searchable in accordance with Article 9 of this Convention prior to the time when the court adjudicates insolvency of the assignor or the security provider.

(2) Upon registration of an assignment of a receivable or a security interest in a receivable in the IRSAR, the assignment or the security interest is perfected against a judgment creditor of the assignor or the security provider, if the registration information becomes searchable in accordance with Article 9 of this Convention prior to time when the judgment creditor takes the steps necessary to acquire rights in the receivable by reason of a judgment or provisional court order.

(3) If an assignment of or security interest in a receivable of a VIRS is not registered in the IRSAR, the assignment or security interest cannot be asserted in the insolvency of the VIRS.

## Article 7 (Proceeds)

If proceeds are received by the VIRS, the right of the assignee or the secured creditor in those proceeds has priority over the right of a competing claimant including the insolvency representative in those proceeds to the same extent as the assignee's right or the secured creditor's security interest had priority over the right in the assigned or encumbered receivable of that claimant if:

(a) The VIRS has received the proceeds under instructions from the assignee or the secured creditor to hold the proceeds for the benefit of the assignee or the secured creditor; and

(b) The proceeds are held by the VIRS for the benefit of the assignee or the secured creditor separately and are reasonably identifiable from the assets of the VIRS, such as in the case of a blocked bank account containing only proceeds.

#### Article 8 (Transfer of Security Interest)

(1) A transferee of a security interest that has been registered in the IRSAR can register the transfer of the security interest in the IRSAR.

(2) The transferred security interest retains its original priority.

(3) Priority between competing transferees of a security interest that has been registered in the IRSAR is determined by the order of registration of the transfer of the security interest in the IRSAR.

#### Article 9 (Floating Security Interest)

(1) A floating security interest over all present and future receivables is subordinated to a subsequent assignment of or security interest in a specific receivable. It includes proceeds of receivables that are held by the VIRS for the benefit of the secured creditor separately and are reasonably identifiable from the other assets of the VIRS.

(2) In the case of a floating security interest, the following items must be registered in the IRSAR:

(i) Whether there is a negative pledge clause in the agreement of the floating security interest;

(ii) Whether there is an automatic crystallisation clause in the agreement of the floating security interest.

#### Article 10 (Rights having Priority without Registration)

(1) A Contracting State may declare those categories of non-consensual right or interest which have priority over a security interest or a floating security interest registered in the IRSAR, whether in or outside insolvency proceedings.

(2) A declaration made under the preceding paragraph may be expressed to cover categories that are created after the deposit of that declaration.

(3) A non-consensual right or interest has priority over a security interest or a floating security interest registered in the IRSAR if and only if the former is of a category covered by a declaration deposited prior to the registration of the security interest or the floating security interest.

(4) Notwithstanding the preceding paragraph, a Contracting State may, at the time of ratification, acceptance, approval of, or accession to the Protocol, declare that a right or interest of a category covered by a declaration made under paragraph 1 shall have

priority over a security interest or a floating security interest registered prior to the date of such ratification, acceptance, approval or accession.

## Article 11 (International Registration System)

An IRSAR shall be established for registrations of assignments of receivables and security interests in receivables.<sup>744</sup>

## Article 12 (The Supervisory Authority and the Registrar)<sup>745</sup>

- (1) There shall be a Supervisory Authority.
- (2) The Supervisory Authority shall:
  - (a) establish or provide for the establishment of the IRSAR;
  - (b) appoint and dismiss the Registrar;
  - (c) supervise the Registrar and the operation of the IRSAR;
  - (d) after consultation with the Contracting States, make or approve the regulation for the operation of the IRSAR;
  - (e) establish administrative procedures through which complaints concerning the operation of the IRSAR can be made to the Supervisory Authority;

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<sup>744</sup> Cf. Cape Town Convention, art 16(1)

<sup>745</sup> Cf. Cape Town Convention, art 17

(3) The Supervisory Authority shall own all proprietary rights in the data bases and archives of the IRSAR.

(4) The Registrar shall ensure the efficient operation of the IRSAR and perform the functions assigned to it by this Convention and the regulation.

### Article 13 (Information Required to Effect Registration)<sup>746</sup>

The information required to effect the registration of an assignment of a receivable or a security interest in a receivable is:

(a) the name, the location, the email address, the telephone number, the fax number, the contact person and the company registration number registered in the State of the assignor or the security provider;

(b) the name, the location, the email address, the telephone number, the fax number, the contact person and the company registration number in its State of the assignee or the secured creditor (or, if a holder of a bond is the assignee or secured creditor, the issuer of the bond, the type of the bond, its serial number, the terms of the bond and its interest rate);

(c) a list or general description of the debtor of the receivable assigned or encumbered; and

(d) general description of the receivable assigned or encumbered, present or future, including the amount of monetary obligation and the due date.

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<sup>746</sup> Cf. New Zealand PPSA, s 142(1)

## Article 14 (Registration, Amendment and Discharge)

(1) To effect, amend or discharge a registration, a registering party shall complete the electronic forms contained on the website with the relevant information required by Article 13 of this Convention.<sup>747</sup>

(2) A consenting party shall be electronically requested to consent thereto prior to that registration, amendment or discharge becoming searchable. Once a registering party has entered registration, amendment or discharge information on the website and has digitally signed it, a consenting party:

(a) will be notified thereof by electronic mail; and

(b) shall be given the opportunity to consent thereto, through the website, for a period of 36 hours.

In the event that a consenting party fails to give its consent within the 36-hour period, the registration, amendment or discharge will be automatically aborted.<sup>748</sup>

(3) Upon receipt of the consent of a consenting party, the Registrar shall automatically issue a confirmation thereof by email to the registering party and the consenting party, provided that the email addresses of the parties have previously been provided.<sup>749</sup>

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<sup>747</sup> Cf. Regulations and Procedures for the International Registry, Procedures, s 12.1

<sup>748</sup> Cf. Regulations and Procedures for the International Registry, Procedures, s 12.2

<sup>749</sup> Cf. Regulations and Procedures for the International Registry, Procedures, s 12.3

(4) Initiated, but not completed, registrations, amendments or discharges shall not appear on any search results.<sup>750</sup>

(5) Rectification of any error or inaccuracy in a registration, once searchable, may only be effected through an amended registration.<sup>751</sup>

### Article 15 (Assignees Entitled to Give Notice to the Debtor)

An assignee or secured creditor is entitled to give notice of the assignment or security interest registered in the IRSAR to the debtor of the receivable with providing the web address of the relevant registration in the IRSAR.

### Article 16 (IRSAR Jurisdiction)

(1) If a security interest in a VIRS receivable created by a VIRS is registered in the IRSAR, the security interest continues to be perfected after the receivable is assigned to another VIRS as far as it is continuously assigned to VIRSs and the sequence of assignments is automatically traced by the IRSAR system.

(2) If a receivable of a VIRS is assigned to a non-VIRS entity, the security interest in the receivable registered in the IRSAR becomes unperfected unless it is re-perfected under the national law of the state where the assignee is located.

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<sup>750</sup> Cf. Regulations and Procedures for the International Registry, Procedures, s 12.7

<sup>751</sup> Cf. Regulations and Procedures for the International Registry, Procedures, s 12.6

## Article 17 (Consent of Secured Creditors to Assignment to Non-VIRS)

To register an assignment of a receivable to a non-VIRS entity in the IRSAR under a VIRS, the assignor (VIRS) or an assignee must obtain the consent of all prior secured creditors registered in the IRSAR, who hold security interests (except floating security interests) in the receivable including the secured creditors of the former VIRS assignors, by whom the receivable is assigned to the assignor (VIRS).

## Article 18 (Sanction for False Registration)

(1) If a VIRS intentionally or negligently registers an assignment of the receivable which the VIRS does not own or a security interest in the receivable which the VIRS does not own in the IRSAR, or consents to such false registration applied by an assignee or a secured creditor, the VIRS will be imposed with a fine no more than 10% of the amount of the receivables falsely registered. Until the VIRS pays the fine to the IRSAR Registrar, registration with respect to the VIRS is suspended.

(2) If a VIRS commits false registration or consent described in the preceding paragraph intentionally or negligently more than three times, the VIRS will be disqualified as a VIRS and cannot become a VIRS any more forever.

## Article 19 (Search)

Upon the consent of a consenting party to the information inputted by a registering party in accordance with Article 14 of this Convention, the registration

information becomes searchable by any person on the website of the IRSAR. Searches of the IRSAR may be performed against an assignor of a receivable or a security provider of a receivable.

## Article 20 (Contractual Prohibition on Assignments of Receivables)

(1) Contractual prohibition on the assignment of receivables of a VIRS is not effective.

(2) Contractual prohibition on the assignment of receivables agreed upon between a company and its account debtor becomes ineffective after the company registers itself as a VIRS with the IRSAR Registrar.

(3) Even if there is an anti-assignment clause made by a company and its account debtor before the VIRS registration of the company, the assignment of the receivable of the company after the VIRS registration of the company is valid, but the VIRS must compensate damages due to the assignment to the account debtor who relied upon the anti-assignment clause.

## **APPENDIX II. ANSWERS TO THE SIX COMMON QUESTIONS**

### **1. Six Common Questions**

Q1. What should E do to be perfected against the insolvency representative of the assignor C in the case of C's insolvency?

Q2. What should the secured creditor S do to be perfected against the insolvency representative of C in the case of C's insolvency?

Q3. How is priority between E and E2 determined?

Q4. How is priority between S and S2 determined?

Q5. How is priority between E and S determined?

Q6. What should a potential assignee P check before executing the assignment contract or the security interest contract in order to secure priority over any prior assignment of or security interest in the receivable?

## 2. United States

### Qs 1, 2. Perfection

UCC Article 9 applies both to a transaction that creates a security interest in personal property<sup>752</sup> and a sale of accounts. Thus, the priority and perfection rules under UCC Article 9 apply to both a security interest in receivables and an assignment of receivables.<sup>753</sup>

Security interests in receivables and assignments of receivables must be filed before the insolvency of an assignor in order to be perfected against the insolvency representative. UCC Article 9 stipulates that a financing statement must be filed to perfect all security interests including the assignment of a payment intangible.<sup>754</sup> ‘Payment intangible’ refers to only those general intangibles under which the debtor’s main obligation is a monetary obligation.<sup>755</sup>

### Qs 3, 4, 5. Priority

In the US, priority of assignments of and security interests in receivables is determined by the order of filing the financing statement under UCC Article 9. A filed assignment or security interest has priority over a conflicting assignment or security

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<sup>752</sup> UCC, s 9-109(a)(1).

<sup>753</sup> In the US, there is no need for a security assignment of receivables, because both an outright transfer of receivables and a charge over receivables should be filed under UCC Article 9. For a security assignment of receivables, see Chapter 1-4

<sup>754</sup> UCC, s 9-310(a)

<sup>755</sup> UCC, s 9-102(a)(61)

interest that is not filed.<sup>756</sup> Conflicting filed assignments or security interests are ranked according to priority in time of filing.<sup>757</sup> A financing statement may be filed before a security agreement is finalized or a security interest otherwise attaches, i.e. advance filing.<sup>758</sup> Priority dates from the time of filing.<sup>759</sup>

A security agreement may provide that collateral secures future advances, regardless of whether the advances are made.<sup>760</sup> If they are made, the priority established by the original filing applies to all future advances so long as the perfection is continuous.

## Q6. Potential Assignee's Check Points

A potential assignee only has to check the UCC Article 9 filing registry to confirm whether there is a prior assignment of or security interest in the receivable.

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<sup>756</sup> UCC, s 9-322(b) The first assignment or security interest to become effective has priority if conflicting assignments or security interests are not filed. UCC, s 9-322(c).

<sup>757</sup> UCC, s 9-322(a)

<sup>758</sup> UCC, s 9-502(d)

<sup>759</sup> UCC, s 9-322(a)

<sup>760</sup> UCC, s 9-204(c)

### 3. Canada

The Canadian provinces are governed by their respective provincial laws, which are similar in many respects but not identical. For present purposes, the laws of Ontario and Saskatchewan will be examined.

#### Qs 1, 2. Perfection

In Canada, the registration system covers charges over personal property including receivables and outright sales of receivables. Under the Ontario PPSA, ‘security interest’ includes ‘the interest of a transferee of an account’ regardless of whether the interest secures payment or performance of an obligation.<sup>761</sup> Under the Saskatchewan PPSA, ‘security interest’ includes ‘the interest of a transferee pursuant to a transfer of an account’ that does not secure payment or performance of an obligation.<sup>762</sup> Thus, the priority and perfection rules under the Saskatchewan and Ontario PPSAs apply to both a security interest in receivables and an assignment of receivables.

In order to be perfected against the insolvency representative, security interests in receivables and assignments of receivables have to be registered before the insolvency of an assignor.<sup>763</sup> Registration is filed electronically at the PPS Register established under

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<sup>761</sup> Ontario PPSA, s 1(1).

<sup>762</sup> Saskatchewan PPSA, s 2(1)(qq)(ii)(A).

<sup>763</sup> Ontario PPSA, s 20(1)(b); Saskatchewan PPSA, ss 20(1)(c) and (2)

their respective PPSAs, and does not require a signed authorization from the debtor (security provider).<sup>764</sup>

### Qs 3, 4, 5. Priority

Under the Ontario and Saskatchewan PPSAs, in relation to outright assignments of and security interests in receivables, priority is determined by the order of financing statement registration.<sup>765</sup> If an assignment or security interest is perfected by registration and another assignment or security interest is not, the registered assignment or security interest has priority over the unregistered assignment or security interest. If no assignments or security interests are registered, priority is determined by order of attachment.<sup>766</sup> Under the Ontario and Saskatchewan PPSAs, the financing statement may be registered before or after the security agreement is executed by the debtor (security provider).<sup>767</sup> In fact, it is industry practice in Ontario to pre-register against a debtor (security provider), so that searches confirming no prior registrations may be obtained prior to funding.<sup>768</sup>

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<sup>764</sup> Simon Finch, Canada (Ch 6) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 81 [6.13].

<sup>765</sup> Ontario PPSA, s 30(1)1; Saskatchewan PPSA, s 35(2)

<sup>766</sup> Ontario PPSA, s 30(1)4

<sup>767</sup> Ontario PPSA, s 45(3); Saskatchewan PPSA, s 43(4)

<sup>768</sup> Simon Finch, Canada (Ch 6) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 81 [6.13].

## Q6. Potential Assignee's Check Points

A potential assignee only has to check the PPS Register of the assignor's province<sup>769</sup> to confirm whether there is a prior assignment of or security interest in the receivable.

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<sup>769</sup> In Canada, each province has an independent PPS Register as in the United States.

## 4. New Zealand

### Qs 1, 2. Perfection

Under the New Zealand PPSA, a security interest includes ‘an interest created or provided for by a transfer of an account receivable’ whether or not the transfer secures payment or performance of an obligation.<sup>770</sup> The priority and perfection rules under the New Zealand PPSA apply to both a security interest in receivables and an assignment of receivables with a few exceptions. Section 23 of the New Zealand PPSA lists the types of receivables to which it does not apply.<sup>771</sup>

A security interest is perfected if the security interest has attached and the financing statement registered.<sup>772</sup> New Zealand does not have provisions that declare unregistered interests to be void against the insolvency representative or a company liquidator.<sup>773</sup> As such, an unperfected security interest is still effective against the security provider and its insolvency representative as an equitable security interest.<sup>774</sup> However, given that competing secured creditors may easily perfect their security

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<sup>770</sup> New Zealand PPSA, s 17(1)(b). The New Zealand PPSA is designed as a code for all transactions giving rise to security over personal property.

<sup>771</sup> Rights of such exceptions will be determined in accordance with existing common law and equitable principles. In order to achieve priority of these types of assignments, an assignee must give notice to the debtor in accordance with the rule in *Dearle v. Hall*.

<sup>772</sup> New Zealand PPSA, s 41(1)

<sup>773</sup> Roger Fenton, *Garrow & Fenton's Law of Personal Property in New Zealand: Volume 2 Personal Property Securities* (7th edn, LexisNexis 2010) 49 [2.2.18].

<sup>774</sup> See Australian Attorney-General's Department, *Discussion Paper 2 (Extinguishment, Priorities, Conflict of Laws, Enforcement, Insolvency), Review of the law on Personal Property Securities* (March 2007) 85 [342], <[http://www.ag.gov.au/www/agd/agd.nsf/Page/PersonalPropertySecurityReform\\_PPSDownloads#papers](http://www.ag.gov.au/www/agd/agd.nsf/Page/PersonalPropertySecurityReform_PPSDownloads#papers)> accessed on 10 January 2011.

interests, an unperfected security interest might be of little commercial value.<sup>775</sup> An assignment of or security interest in receivables is not perfected against a judgment creditor if the assignment or security interest is not registered at the time of execution of a judgment.<sup>776</sup>

### Qs 3, 4, 5. Priority

The rule in *Dearle v Hall*<sup>777</sup> continues to apply to interests that do not come within the PPSA priority system. However, where the PPSA applies,<sup>778</sup> an assignee should ensure that the assignment is perfected by registration so as to preserve priority.<sup>779</sup>

A registered assignment of or security interest in receivables has priority over an unregistered assignment or security interest.<sup>780</sup> Priority between registered assignments or security interests in the same receivables is determined according to the order of the registration of a financing statement.<sup>781</sup> The assignee or secured creditor that was first to

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<sup>775</sup> Matt Yarnell and Richard May, New Zealand (Ch 27) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 403.

<sup>776</sup> New Zealand PPSA, s 103(1). 'Time of execution' means (a) if the collateral is seized by an execution creditor or on an execution creditor's behalf, the time of seizure; or (b) in any other case, the time when a charging order or a garnishee order is made. New Zealand PPSA s 103(1A).

<sup>777</sup> (1828) 3 Russ 1

<sup>778</sup> The New Zealand PPSA applies to account receivables. Under the New Zealand PPSA, 'account receivables' means a monetary obligation that is not evidenced by chattel paper, an investment security, or by a negotiable instrument, whether or not that obligation has been earned by performance. New Zealand PPSA, s 16

<sup>779</sup> Roger Fenton, *Garrow & Fenton's Law of Personal Property in New Zealand: Volume 2 Personal Property Securities* (7th edn, LexisNexis 2010) 390 [9.14].

<sup>780</sup> New Zealand PPSA, s 66(a). Priority between unregistered assignments or security interests in the same receivables is determined by the order of attachment of the assignment or security interest. New Zealand PPSA, s 66(c)

<sup>781</sup> New Zealand PPSA, s 66(b)(i)

register the assignment or security interest has priority regardless of whether attachment occurred at the time of registration.

A financing statement may be registered before or after a security agreement is made, or a security interest has attached.<sup>782</sup> For this reason, it is common for a party that intends to take a security interest in a particular receivable to register a financing statement relating to that security interest in advance of the transaction being consummated.<sup>783</sup> If the security agreement extends to future advances, the priority established by the original registration applies to all future advances so long as the perfection is continuous.<sup>784</sup>

## Q6. Intending Assignee's Check Points

A potential assignee only has to check the PPS Register to confirm whether there is a prior assignment of or security interest in the receivable.

## 5. Australia

### Qs 1, 2. Perfection

With respect to perfection and priority, the Australian PPSA unified the laws of each state. The Australian PPSA was passed in December 2009, and entered into force in

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<sup>782</sup> New Zealand PPSA, s 146

<sup>783</sup> Matt Yarnell and Richard May, New Zealand (Ch 27) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 394 [27.14].

<sup>784</sup> New Zealand PPSA, s 72

May 2011. Under the Australian PPSA, a security interest includes ‘the interest of a transferee under a transfer of an account’ regardless of whether transaction concerned, in substance, secures payment or performance of an obligation.<sup>785</sup> A security interest in receivables includes a transfer of receivables. Therefore the priority and perfection rules under the Australian PPSA apply to both a security interest in receivables and an outright assignment of receivables.

Perfection is done by registration. If not registered prior to a winding up or insolvency, an assignment of receivables or a security interest in receivables is not perfected upon such winding up or insolvency of the assignor or security provider.<sup>786</sup>

### Qs 3, 4, 5. Priority

A registered assignment of or security interest in certain receivables has priority over an unregistered assignment of or security interest in the same receivables.<sup>787</sup> Priority between two or more assignments of or security interests in receivables that are currently perfected is to be determined by the order in which the registration for the assignment or security interest occurs.<sup>788</sup> An assignment or security interest may be registered before or after it is made or attached.<sup>789</sup>

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<sup>785</sup> Australian PPSA, s 12(3)(a).

<sup>786</sup> Australian PPSA, ss 267 and 267A.

<sup>787</sup> Australian PPSA, s 55(3). Priority between unregistered assignments of or security interests in the same receivables is to be determined by the order of attachment of the assignment or security interests. Australian PPSA, s 55(2).

<sup>788</sup> Australian PPSA, ss 55(4) and 55(5)(a).

<sup>789</sup> Australian PPSA, s 16.

## Q6. Potential Assignee's Check Points

A potential assignee only has to check the PPS Register to confirm whether there is a prior assignment of or security interest in the receivable.

## 6. Korea

### Qs 1, 3. Assignments

In Korea, the insolvency representative of the assignor is treated as a third party, and therefore perfection against third parties includes perfection against the insolvency representative. Thus, perfection against the insolvency representative is the same as the perfection against third parties by which priority is determined. So, the answers to Questions 1 and 3 are the same. Perfection and priority are determined by notification of assignments under the Korean Civil Code or filing of securitisations under the ABS Act or the MBS Company Act.

#### *Qs 1, 3 -I. Assignment under Korean Civil Code*

Under the Korean Civil Code, the assignment of a receivable is not perfected against third parties, including the insolvency representative, unless the assignor gives notice of the assignment to the debtor of the receivable or the debtor consents to the assignment.<sup>790</sup> Such notice or consent must be by means of a certified document with a fixed date stamp in order for the assignment of the receivable to be perfected against third parties.<sup>791</sup> This regime intends to designate a debtor as an information centre, so that a potentially interested party may inquire of the debtor of the receivable regarding notice of an assignment. Priority among competing assignees is determined by the order in which the debtor receives notice of the assignment. There are exceptions to the Civil Code: the ABS Act and the MBS Company Act.

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<sup>790</sup> Korean Civil Code, art 450(1).

<sup>791</sup> Korean Civil Code, art 450(2).

***Qs 1, 3 -2. ABS Act***

Under the ABS Act, a SPV can perfect an assignment of receivables against third parties by filing the securitisation plan and the assignment of receivables in accordance with the plan at the Financial Services Commission.<sup>792</sup> Upon filing the assignment of receivables in accordance with the securitisation plan at the Financial Services Commission, the perfection requirement under Article 450(2) of the Korean Civil Code will be deemed satisfied. Thus, the assignment of the securitised receivables is perfected against third parties, even if no notice is given to the debtor. Upon the filing, the receivables assigned to the SPV will not belong to the insolvency estate of the assignor, and creditors of the assignor may not attach the receivable assigned to the SPV.<sup>793</sup>

***Qs 1, 3 -3. MBS Company Act***

If the mortgage-backed securitisation plan and the assignment of receivables in accordance with the plan are filed at the Financial Services Commission, the perfection requirement under Article 450(2) of the Korean Civil Code will be deemed satisfied. Thus, the assignment of receivables is perfected against third parties on the date of the filing.<sup>794</sup> If the receivables assigned in accordance with a mortgage-backed securitisation plan are secured by a pledge or a mortgage, the assignee of the receivables (the SPV) will acquire the pledge or the mortgage upon filing the assignment of receivables in

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<sup>792</sup> Korean ABS Act, art 7(2).

<sup>793</sup> Mee-Hyon Lee, 'Securitisation in Korea', (2002) Vol.2, No.1 *Journal of Korean Law* 116.

<sup>794</sup> Korean MBS Company Act, arts 6(2) and 5(1). cf. Korean ABS Act, arts 7(2) and 6(1).

accordance with the mortgage-backed securitisation plan at the Financial Services Commission.<sup>795</sup>

## Qs 2, 4. Security Interests

As discussed, in Korea, perfection against the insolvency representative is the same as the perfection against third parties by which priority is determined. Thus, the answer to Question 2 is the same as the answer to Question 4.

### *Qs 2, 4 -1. Pledge under Korean Civil Code*

Under the Korean Civil Code, the method of creating a pledge of a receivable is to transfer the receivable.<sup>796</sup> A pledge of a receivable becomes effective by the method of the assignment of a receivable. In order to perfect a pledge of a receivable against third parties, a pledgor is required to give notice of the pledge to, or receive consent from, the debtor of the receivable regarding the creation of the pledge. The notice must be by means of a certified document with a fixed date stamp.<sup>797</sup>

### *Qs 2, 4 -2. Korean Security Registration Act*

Korea enacted the Korean Security Registration Act in order to provide a registration system for security rights in movable assets and receivables. This Act entered into force on 11 June 2012. The Korean Security Registration Act covers

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<sup>795</sup> Korean MBS Company Act, art 7. cf. Korean ABS Act, art 8(1).

<sup>796</sup> Korean Civil Code, art 346.

<sup>797</sup> Korean Civil Code, arts 349 and 450(2).

security rights in and security assignments of receivables,<sup>798</sup> but does not cover outright assignments of receivables.

The Korean Security Registration Act creates a new form of security interest guaranteed by registration in addition to the pledge under the Korean Civil Code. It does not replace the notification requirement for a pledge of receivables under the Korean Civil Code. Pledges coexist with security interests under the Korean Security Registration Act. Priority is determined by the order of notification of pledges under the Korean Civil Code or registration of security interests under the Korean Security Registration Act.<sup>799</sup>

As a result, parties may choose to use either a pledge of receivables under the Korean Civil Code or a security interest in receivables under the Korean Security Registration Act. If parties choose to use a pledge of receivables under the Civil Code, notice of the pledge to the debtor by means of a certified document with a fixed date stamp is required for perfecting the pledge against third parties. If parties choose to use the security interest under the Korean Security Registration Act, they may perfect the security interest against third parties by simply registering it.

## Q5. Priority between Assignments & Security Interests

With respect to receivables, there could be assignments or pledges under the Korean Civil Code, security interests under the Korean Security Registration Act, or

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<sup>798</sup> Korean Security Registration Act, arts 34(1) and 2(1).

<sup>799</sup> Korean Security Registration Act, art 35(3).

securitisations under the ABS Act or the MBS Company Act. The person who completes any one of perfection methods first will have priority.

Priority between competing assignments of, pledges of or security interests in receivables is determined by the order of notice of assignments or pledges to (or consent of) the debtor of the receivable under the Korean Civil Code or registration of the security interest under the Korean Security Registration Act.<sup>800</sup> In addition, for the assignment of receivables in accordance with a securitisation plan, upon filing the assignment of receivables at the Financial Services Commission of Korea, the perfection requirement under the Korean Civil Code will be satisfied.<sup>801</sup>

As a result, priority is determined by the order of notice to the debtor, filing at the Financial Services Commission or registration under the Korean Security Registration Act.

## Q6. Potential Assignee's Check Points

In Korean law, to make sure there is not any prior assignee or any prior secured creditor of the receivable, a potential assignee of a receivable should (1) ask the debtor of the receivables whether he received notice of a prior assignment or security interest; (2) check the securitisation filing registry at the Financial Services Commission of Korea; and (3) check the security registry for receivables under the Korean Security Registration Act.

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<sup>800</sup> Korean Security Registration Act, art 35(3).

<sup>801</sup> Korean ABS Act, arts 7(2) and 6(1); Korean MBS Company Act, arts 6(2) and 5(1)

## 7. Japan

### Qs 1, 2, 3, 4. Perfection & Priority

In Japan, the perfection against the insolvency representative is the same as the perfection against third parties by which priority is determined. Furthermore, the notification requirement for the assignment of receivables under the Japanese Civil Code also applies to pledges of receivables. The registration system under the Japanese Assignment Registration Act applies to both assignments of receivables and pledges of receivables.<sup>802</sup> As a result, the answers to Questions 1, 2, 3 and 4 are all the same.

#### *Qs 1, 2, 3, 4 -1. Japanese Civil Code*

Under the Japanese Civil Code, both perfection and priority of assignments as well as pledges of receivables are all determined by notification to the debtor of the receivable.

An assignment of a receivable is perfected against third parties including the insolvency representative, if the assignor gives notice of the assignment to the debtor of the receivable by means of a certified document with a fixed date stamp or the debtor has consented to the assignment by means of a certified document with a fixed date stamp.<sup>803</sup> Therefore priority among competing assignees is determined by the order in which the debtor receives notice of the assignment (or the pledge) of the receivable.

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<sup>802</sup> Japanese Assignment Registration Act, art 14.

<sup>803</sup> Japanese Civil Code, art 467(2). Notice or consent of the assignment of receivables must be done by a certified document with a fixed date stamp.

Under the Japanese Civil Code, the method of creating a pledge of a right is to transfer the right.<sup>804</sup> The pledge of a right becomes effective by the assignment of the right. To perfect a pledge of a receivable against the debtor of the receivable and third parties, the pledger is required to give notice of the pledge to, or receive consent from, the debtor of the receivable regarding the creation of the pledge.<sup>805</sup>

***Qs 1, 2, 3, 4 -2. Japanese Assignment Registration Act***

Under the Japanese Assignment Registration Act, both perfection and priority of assignments as well as pledges of receivables are all determined by registration. Provisions of the Japanese Assignment Registration Act may apply *mutatis mutandis* to pledges of receivables.<sup>806</sup>

Japan has adopted registration systems without revising the Japanese Civil Code. Registration is optional and co-exists with notification of the assignment to the debtor under the Japanese Civil Code. The Japanese Assignment Registration Act does not replace the notification requirement for the assignment of receivables under the Japanese Civil Code,<sup>807</sup> but it provides registration as an alternative to perfecting an assignment of receivables against third parties.

Where a legal person has assigned a receivable and when an assignment of a receivable has been registered, notice shall be deemed given to third parties by means of a certified document with a fixed date stamp under Article 467 of the Japanese Civil

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<sup>804</sup> Japanese Civil Code, art 364.

<sup>805</sup> Japanese Civil Code, art 466(1).

<sup>806</sup> Japanese Assignment Registration Act, art 14.

<sup>807</sup> Japanese Civil Code, art 467

Code.<sup>808</sup> Here, the date of the registration is dealt as the fixed date. Thus, registration is a method of perfection. If an assignment of receivables is registered, it is perfected against third parties including the insolvency representative.

Priority among competing assignees is determined by the order of registration. Therefore the debtor of a receivable needs to know the exact time of the registration to determine the proper payee. For this reason, notice should be given to the debtor with the certificate of registration. If an assignor gives notice of the assignment to the debtor in accordance with the Japanese Civil Code, he should provide it by means of a certified document with a fixed date stamp.<sup>809</sup>

If an assignor fraudulently assigns the same receivable to two assignees, both assignment contracts are valid,<sup>810</sup> but the second assignee may rescind the second assignment contract by the reason of the assignor's fraud.

## Q5. Priority between Assignments & Security Interests

Under the Japanese Assignment Registration Act, if an assignment is registered, it is perfected against third parties without giving notice of the assignment to the debtor. In addition, even if an assignment is not registered, the assignor may perfect it against third parties by giving notice to the debtor according to the Japanese Civil Code. The same rule applies to a pledge of receivables.

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<sup>808</sup> Japanese Assignment Registration Act, art 4(1)

<sup>809</sup> Japanese Civil Code, art 467(2).

<sup>810</sup> The assignment contract between an assignor and an assignee is always valid in law between the assignor and the assignee. Thus, the assignor bears obligation to the assignee. The question of priority is different from that of validity.

Assignments or pledges of the same receivable may be perfected by either notice to (or consent of) the debtor of the receivable under the Japanese Civil Code or registration under the Japanese Assignment Registration Act. If both perfection methods exist with respect to a receivable, the assignment or pledge that is perfected first will prevail.<sup>811</sup> Priority is determined by the order of registration or notice to the debtor. The assignee, that first gives notice to the debtor, will have priority over the assignee that registers the assignment at a later time, and vice versa.

#### Q6. Potential Assignee's Check Points

A potential assignee should both check the registry under the Japanese Assignment Registration Act and ask the debtor of the receivable whether it received notice of a prior assignment or security interest in the receivable.

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<sup>811</sup> Takashi UCHIDA, *Civil Code III Credit General and Security Interest* (3<sup>rd</sup> edn, University of Tokyo Press 2006) 223.

## 8. France

### Q1. Perfection of Assignments

#### *Q1-1. Assignment of Receivables (Cession de créances)*

Under the French Civil Code, notification to or an acceptance of a debtor of a receivable is required for the assignment of a receivable to be perfected against third parties including the insolvency representative.<sup>812</sup> Notification to a debtor requires formality. Notification to a debtor must be done by an official letter (*signification*) delivered by a court bailiff (*huissier*).<sup>813</sup> Alternatively, a debtor may give acceptance of the assignment in a notarised deed (*acte authentique*).<sup>814</sup> Because of this stiff formality, an outright assignment of receivables is rarely used as a financing device in France. If an assignment of receivables is used for the purpose of security, it would be characterised as a pledge of receivables.<sup>815</sup>

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<sup>812</sup> French Civil Code, art 1690.

<sup>813</sup> French Civil Code, art 1690. See Eva-Maria Kieninger (ed), *Security Rights in Movable Property in European Private Law* (CUP, 2004) 538; Philip Wood, *Principles of International Insolvency* (Sweet & Maxwell 2007) 297. If a notification is served by bailiff (*huissier*), it costs approximately €250 per debtor. See Olivier Hubert, France (Ch 13) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 179.

<sup>814</sup> French Civil Code, art 1690.

<sup>815</sup> James Leavy, France, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 136. See also Olivier Hubert, France (Ch 13) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 179.

### ***Q1-2. Assignment under the French Monetary and Financial Code***

In 1981, France enacted the *Dailly Act (Loi Dailly)*<sup>816</sup> in order to circumvent the notification requirement under the French Civil Code. In 2000, the *Dailly Act* was incorporated into the Monetary and Financial Code (*Le Code Monétaire et Financier*)<sup>817</sup> as Articles L313-23 to L313-34. The French Monetary and Financial Code applies to both assignments of receivables and pledges of receivables in which: (1) the assignee is a credit institution (*établissement de crédit*);<sup>818</sup> (2) the assignor is a private-law or public-law corporation or a natural person; (3) the assignor assigns a bulk of claims, present or future, that he has over one or several debtors, provided as the assignment is relates to his business activities;<sup>819</sup> and (4) the debtor of the receivable is a third party private-law or public-law corporation, or natural person. This largely applies to receivables financing transaction.

Under the French Monetary and Financial Code, an assignment of receivables may be perfected against third parties by simple delivery of a transfer deed (*bordereau*) signed by the assignor and dated by the assignee, where the assignee is a credit institution (*établissement de crédit*), and the assignor is a corporation or a natural person conducting

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<sup>816</sup> *loi n° 81-2 du 2 janvier 1981. Dailly is the surname of the senator who initiated this Act.*

<sup>817</sup> *loi n° 2006-64 du 23 janvier 2006.*

<sup>818</sup> French Monetary and Financial Code, art L313-26

<sup>819</sup> French Monetary and Financial Code, art L313-23

business activity.<sup>820</sup> The transfer deed (*bordereau*) must include the signature of an assignor and must be dated by an assignee to be perfected against third parties.<sup>821</sup>

Where the assignor becomes bankrupt and even if no notice is given to the debtor of the receivable, the assignee credit institution with the transfer deed (*bordereau*) can declare his claim to the insolvency representative of the assignor and claim payment directly from the debtor of the receivable.<sup>822</sup> However, if the debtor of the receivable has already paid the assignor by cash or by bank transfer<sup>823</sup> before receiving notice of the assignment, the assignee only has the option of joining in the insolvency proceedings,<sup>824</sup> since the cash payment would have been commingled with other cash in the assignor's account.

### ***Q1-3. Securitisation under the French Monetary and Financial Code***

In securitisation, an assignment of receivables is perfected against third parties simply upon delivery of a transfer deed (*bordereau*) to the assignee from the date indicated on the transfer deed (*bordereau*) when it is handed over.<sup>825</sup> The terms of a transfer deed (*bordereau*) are determined by decree.<sup>826</sup> A transfer deed (*bordereau*) must be named an act of assignment of receivables. It must indicate that it is subject to the

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<sup>820</sup> French Monetary and Financial Code, art L313-23 to L313-34

<sup>821</sup> French Monetary and Financial Code, art L313-25. See Arthur F. Salomons, 'Deformalisation of Assignment Law and the Position of the Debtor in European Property Law', *European Review of Private Law* (The Netherlands 2007) 644.

<sup>822</sup> Eva-Maria Kieninger (ed), *Security interests in Movable Property in European Private Law* (CUP, 2004), 541.

<sup>823</sup> Cass. Com 4 July 1995, Bull civ IV, No 203; D 1996, Som, 208, obs. Piedelièvre; JCP 1995, II, 22553, note Legeais; RTDC 1996, 192, obs. Gauthier.

<sup>824</sup> Eva-Maria Kieninger (ed), *Security interests in Movable Property in European Private Law* (CUP, 2004) 541-542.

<sup>825</sup> French Monetary and Financial Code, art L214-43

<sup>826</sup> French Monetary and Financial Code, art L214-43

provisions of the Monetary and Financial Code addressing asset securitisation. The name of the assignee must be included. The assigned receivables must be indicated and identified.<sup>827</sup>

An assignment of receivables, which comes into existence after the date of the assignment contract, is not affected by the commencement of insolvency proceedings against the assignor.<sup>828</sup> Therefore an assignment of future receivables is possible. According to a decision of the Commercial Chamber of the *Cour de Cassation* in December 2004, the assignment of future receivables is perfected against third parties and future cash flows arising from the collection of the assigned receivables is not affected by the insolvency of the assignor.<sup>829</sup> This decision applies to *Dailly* assignments as well as to securitisations under the French Monetary and Financial Code.

## Q2. Perfection of Security Interests

### ***Q2-1. Pledge under the Revised French Civil Code of 2006***

Under the revised French Civil Code of 2006,<sup>830</sup> for a pledge of a receivable (*Nantissement de créance*), an executed pledge contract document (*l'acte*) is sufficient

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<sup>827</sup> Décret n°2004-1255 du 24 novembre 2004 pris en application des articles L. 214-5 et L. 214-43 à L. 214-49 du code monétaire et financier et relatif aux fonds communs de créances, art 18.

<sup>828</sup> Fabrice Grillo, Hervé Touraine, *France* (chapter 19), *The International Comparative Legal Guide to: Securitisation 2007* (Global Legal Group, 2007) 139 [4.10].

<sup>829</sup> Sharon Lewis, Philip Boys, Ch. 15 France, *The International Comparative Legal Guide to: Securitisation 2005* (Global Legal Group) 95 [4.2].  
<<http://www.iclg.co.uk/khadmin/Publications/pdf/355.pdf>> accessed 12 August 2011.

<sup>830</sup> *loi* n°2006-399 du 4 avril 2006 renforçant la prévention et la répression des violences au sein du couple ou commises contre les mineurs (1).

for the pledge to be perfected against third parties.<sup>831</sup> Neither notification to the account debtor nor registration is required for a pledge of a receivable to be perfected against third parties. This is an exception to the new general rule that pledges of tangible movable assets must be registered under Article 2337 of the French Civil Code. The pledge of a receivable (*créance*), including a future receivable, is perfected against third parties as of the date of concluding the pledge contract document (*l'acte*).<sup>832</sup> In France, a security assignment of receivables is treated as a security interest in receivables, and therefore notice to the debtor is not required.

#### ***Q2-2. Pledge under the French Monetary and Financial Code***

A pledge as well as an assignment is perfected against third parties from the date indicated on the transfer deed (*bordereau*) when it is handed over, regardless of the origination date, maturity date or due date of the receivables.<sup>833</sup> It provides a simple method to pledge or transfer commercial receivables to a bank as security for financing.<sup>834</sup>

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<sup>831</sup> French Civil Code, art 2361.

<sup>832</sup> French Civil Code, art 2361.

<sup>833</sup> French Monetary and Financial Code, art L313-27.

<sup>834</sup> James Leavy, France, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 123.

### Q3. Priority of Assignments

Under the French Civil Code, priority of assignments of receivables (*Cession de créances*) is determined by the order of notification. The assignee who first gives notice to the debtor has priority.<sup>835</sup>

Under the French Monetary and Financial Code, priority is determined by the date indicated on the transfer deed (*bordereau*) when it is handed over, if either both of the *Dailly* assignee<sup>836</sup> gives notice to the debtor of the receivable,<sup>837</sup> or no *Dailly* assignee gives notice to the debtor of the receivable.<sup>838</sup> However, if one *Dailly* assignee gives notice to the debtor of the receivable and the others did not, the *Dailly* assignee who gives notice has priority over any other *Dailly* assignee or an assignee or a pledgee under the French Civil Code, regardless of the date of the respective assignment or pledges.<sup>839</sup> If more than one *Dailly* assignee give notice to the debtor of the receivable, priority is determined by the date indicated on the transfer deed (*bordereau*) when it is handed over.

For this reason, even though a prior *Dailly* assignee does not have to give notice to the debtor of the receivable immediately, in order to secure priority, he must give notice to the debtor of the receivable before payment would be made to any other competing assignee. The French priority regime encourages a *Dailly* assignee to give notice of the assignment to the debtor of the receivable.

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<sup>835</sup> *Draft Common Frame of Reference* Full Edition Vol 2, Book III (Sellier 2009) 1051.

<sup>836</sup> In this thesis, a *Dailly* assignee means an assignee who has assigned a receivable by a transfer deed (*bordereau*) under the French Monetary and Financial Code.

<sup>837</sup> Cass. Com. 12 January 1999, D. Aff. 1999, 336; RTD com. 1999, 479, obs. *Cabrillac*.

<sup>838</sup> Cass. Com. 5 July 1994, RTD com. 1995, 172, obs. *Cabrillac*.

<sup>839</sup> James Leavy, France, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 134.

#### Q4. Priority of Security Interests

Under the revised French Civil Code of 2006, priority of pledges or security assignments of receivables (*Nantissement de créances*) is determined by the order of the date of the relevant pledge or security assignment contract documents. All pledges or security assignments of receivables must be evidenced in writing.<sup>840</sup> Such writing is sufficient to perfect a pledge or security assignment against third parties.<sup>841</sup>

Under the French Monetary and Financial Code, priority of competing pledges is determined by the date indicated on the transfer deed (*bordereau*) when it is handed over, if either both of the pledgees or no pledgee gave notice to the debtor of the receivable. If one *Dailly* pledgee gives notice to the debtor of the receivable, the *Dailly* pledgee who gives notice has priority.

#### Q5. Priority between Assignments & Security Interests

With respect to assignments under the French Civil Code, priority is determined by the order in which the debtor receives notice of the assignment with formality. With respect to *Dailly* assignments and pledges, priority is determined by the order of the date of the relevant documents, i.e. pledge contracts or transfer deeds (*bordereau*), if neither a

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<sup>840</sup> France Civil Code, arts 1326 and 1341.

<sup>841</sup> James Leavy, France, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 134.

*Dailly* assignee nor a pledgee gives notice to the debtor of the receivable.<sup>842</sup> However, giving notice to the debtor of the receivable may trump the date of the relevant documents. If one assignee under the French Civil Code, *Dailly* assignee or pledgee gives notice to the debtor of the receivable and the others did not give notice to the debtor of the receivable, the assignee or pledgee who gives notice to the debtor of the receivable has priority over the others.

## Q6. Potential Assignee's Check Points

If a potential assignee is a financial institution, it may use a *Dailly* assignment under the French Monetary and Financial Code. In France, it is possible that there might be a prior assignment or pledge under the French Civil Code or a prior *Dailly* assignment. A potential assignee should first ask the debtor of the receivable whether it received notice of a prior assignment, pledge or *Dailly* assignment. A potential assignee should give notice to the debtor of the receivable as soon as possible. However, this still does not guarantee the assignee's priority. If another pledgee or *Dailly* assignee subsequently gives notice to the debtor of the receivable, and the date of pledge contract document or the date on the transfer deed (*bordereau*) is prior to the assignment date of the potential assignee, the pledgee or *Dailly* assignee will have priority.

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<sup>842</sup> Cass. Com. 13 February 1996, Banque 1996, No. 569, 91, obs. *Guillot*.

## 9. Belgium

### Q1. Perfection of Assignments

Under Article 1690 of the Belgian Civil Code, as altered by the Law of 6 July 1994, an assignment of a receivable is effective between an assignor and an assignee and is perfected against third parties including the insolvency representative upon the conclusion of an assignment agreement. Belgium has abolished the notification requirement for the assignment of receivables. Compared with the French *Dailly Act* 1981, which abolished the notification requirement for the limited scope of assignments of credit institutions, the Belgium reform has uniformly abolished the notification requirement for the assignment of receivables and the pledge of receivables. The primary aim of this abolition is to facilitate securitisation.<sup>843</sup>

### Q2. Perfection of Security Interests

A pledge of receivables is perfected against third parties from the moment a valid pledge agreement is entered. Article 2075 of the Belgian Civil Code abolished the transfer of possession requirement for the pledge of receivables. Previously, this had been required by Article 2076 of the Belgian Civil Code, under which the pledgee was to take possession of the receivable at the conclusion of the pledge agreement.

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<sup>843</sup> Jan Peeters and Wouter Ghijsels, *Increasing activity in the Belgian market*, (Stibbe 2005) <[http://www.stibbe.be/assets/publications/articles/peeters\\_ghijsels-increasing\\_activity\\_in\\_the\\_belgian\\_market.pdf](http://www.stibbe.be/assets/publications/articles/peeters_ghijsels-increasing_activity_in_the_belgian_market.pdf)> accessed 15 August 2010.

### Qs 3, 4, 5. Priority

Even though Belgium abolished the notification requirement for perfection against third parties including the insolvency representative, priority of competing assignees is still determined by the order in which the debtor receives notice of the assignment or the pledge.<sup>844</sup> Priority between competing assignees and/or pledgees of the same receivable is determined by the order in which the debtor of the receivable receives notice of the assignment or the pledge.<sup>845</sup>

### Q6. Potential Assignee's Check Points

To secure priority, a potential assignee has to ask the debtor of the receivable whether it received notice of a prior assignment or pledge.

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<sup>844</sup> Belgian Civil Code, art 1690(1)

<sup>845</sup> Marc Vermylen, Belgium (Ch 4) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 54 [4.32].

## 10. England

### Q1. Perfection of Assignments

#### *Q1-1. Assignment of Receivables*

An assignment without notice to the debtor is still valid as an equitable assignment.<sup>846</sup> Moreover, the receivables equitably assigned are separated from the assignor's insolvency estate. As a result, an equitable assignee, like a statutory assignee, prevails against the insolvency representative of the assignor.<sup>847</sup> Equitable assignments in English law are close to the assignment in German law in that they do not require notice of the assignment to the debtor for an equitable assignment which is perfected against the insolvency representative and judgment creditors.<sup>848</sup>

#### *Q1-2. Individual Person's General Assignment of Book Debts*

If a natural person makes a general assignment of existing or future book debts, the assignment must be registered under the Bills of Sale Act 1878 to be perfected against the insolvency representative of the assignor.<sup>849</sup> A 'general assignment' does not include an assignment of book debts due at the date of the assignment from specified debtors or

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<sup>846</sup> *Gorringe v Irwell India Rubber and Gutta Percha Works* (1886) LR 34 Ch D 128 (CA).

<sup>847</sup> For this reason, in England, at first notice will not normally be given to the debtors because an equitable assignment is effective even without notice to a debtor and the assignor generally wishes to maintain its relationship with its customers (debtors of receivables) and continue to collect on the debt. Since an assignee may give notice of the assignment to the debtor at any time, once the other requirements of a statutory assignment are satisfied, an equitable assignee is always able to change an equitable assignment into a statutory assignment without an assignor's cooperation. Thus, an assignee factor will usually send notice to debtors only if and when it needs to collect the debt itself, unless the arrangement is notification financing. For example, in the case of an assignor's insolvency or refusal to pay the debt, the assignee will give notice to the debtor.

<sup>848</sup> See Section 3-2-3-2

<sup>849</sup> Insolvency Act 1986, s 344

an assignment of debts becoming due under specified contracts.<sup>850</sup> In this context, an ‘assignment’ includes both a security assignment of and a charge on book debts.<sup>851</sup>

## Q2. Perfection of Security Interests

Under the Companies Act 2006 (Amendment of Part 25) Regulations 2013, all charges (including charges over receivables) created by a company can be registered in the Registrar of Companies at Companies House. If a charge created by a company is not registered within 21 days (or such later time as is permitted by the court) beginning with the day after the date of creation of the charge,<sup>852</sup> it is not perfected against a liquidator, administrator and creditor of the company.<sup>853</sup>

## Q3. Priority of Assignments

Under English law, priority is not related to perfection. In *Dearle v Hall*, priority between competing assignees is determined by the order in which the debtor receives notice of the assignment unless the subsequent assignee knew of the prior assignment at the time of his assignment.<sup>854</sup>

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<sup>850</sup> Insolvency Act 1986, s 344(3)(b)(i).

<sup>851</sup> Insolvency Act 1986, s 344(3)(a).

<sup>852</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, s 859A(4)

<sup>853</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, ss 859H and 859F

<sup>854</sup> *Dearle v Hall* (1828) 3 Russ 1. See Section 3-2-2-2

### ***Q3-1. Priority of Equitable Assignments***

#### Q3-1-1. First View of Transferring Receivables

There are two views on how the doctrine of *Dearle v Hall* was framed and how it operates. According to the first view, the prior equitable assignment to A1 is valid between the assignor and the assignee even though no notice is given to the debtor, and consequently the assigned receivable no longer belongs to the assignor's estate in bankruptcy or insolvency. Since under the *nemo dat quod non habet* rule a transferor cannot transfer what he does not have, it might seem odd that the assignor can make a similar assignment to A2 which can have priority over the assignment to A1.<sup>855</sup>

Nevertheless, A2 could be a *bona fide* purchaser if A2 purchased the receivable without notice of the prior equitable assignment to A1 even though A2 gave notice of his assignment to the debtor of the receivable. It is likely that A2 would give notice to the debtor of the receivable as A2 is likely to have made enquiries as to whether there was any prior assignment. In order for A2 to be a *bona fide* purchaser, A2 should have enquired of the debtor and in the process of the enquiry A2 could naturally give notice of his assignment to the debtor. In this view, the *Dearle v Hall* rule is framed in terms of the *bona fide* purchase without notice rule. This view explains why A2 prevails over A1.

However, the shortcoming of this view is that it does not explain why A2 must give notice to the debtor. A2 would have to give notice of his assignment to the debtor to protect his position against a potential third assignee since a potential third assignee

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<sup>855</sup> Michael Bridge, Louise Gullifer, Gerard McMeel and Sarah Worthington, *The Law of Personal Property* (Sweet & Maxwell, 2013) [36-012]

cannot be a *bona fide* purchaser without notice once A2 has given notice. Still, it does not really explain why notice is necessary for A2 to have priority over A1.

### Q3-1-2. Second View of Creating Equivalent Equitable Interests Engrafted Upon Legal Interests

According to the second view, it is explained as a particular case of conflict between mere equities. Because each assignment in equity just creates a new claim against the assignor, the assignor can create multiple claims. An equitable assignment merely creates and vests in the assignee an equitable interest. Equitable interests are ‘engrafted’ or ‘impressed’ upon legal interests rather than ‘carved out of’ them.<sup>856</sup> Equitable interests are not drawn out of legal interests.<sup>857</sup> The underlying equitable nature of assignment is an engraftment of an equitable personal chose in action with a power of control onto the personal debt claim. Thus, an equitable assignment does not involve a disposition.<sup>858</sup> It is possible for the same assignor to create equally valid claims against himself by multiple intentional assignments of the same debt.<sup>859</sup> Priority between them is determined by the *Dearle v Hall* rule.

If there are two equitable assignments and neither assignee gives notice to the debtor, priority is determined by the order of conclusion of the assignment agreement.<sup>860</sup>

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<sup>856</sup> Gregory Tolhurst, *The Assignment of Contractual Rights* (Hart Publishing 2006) [3.11] 40

<sup>857</sup> *ibid* [3.12] 43

<sup>858</sup> *ibid* [3.11] 40

<sup>859</sup> David Fox, ‘Relativity of Title at Law and in Equity’ (2006) 65 CLJ 330, 354

<sup>860</sup> Hugh Beale, Michael Bridge, Louise Gullifer and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) 438 [13.09].

<Table 17> Application of *Dearle v Hall*

		Prior Assignment to A1	Subsequent Assignment to A2	
Equitable assignment	First view transferring receivables without notice	Valid	Void <i>nemo dat quod non habet</i>	Exception: <i>bona fide</i> purchaser for value without notice (or <i>Dearle v Hall</i> )
Statutory assignment	Substantive view			
Equitable assignment	Second view creating equivalent equitable interests engrafted upon legal interests	Valid	Valid	<i>Dearle v Hall</i>
Statutory assignment	Procedural view			

### Q3-2. Priority of Statutory Assignments

#### Q3-2-1. Substantive View of Statutory Assignments

The two views of equitable assignments could similarly apply to statutory assignments under Section 136(1) of the Law of Property Act 1925. The substantive view of statutory assignments follows the logic of the first view of equitable assignments. The primary argument for the substantive view flows from the words of Section 136(1) of Law of Property Act 1925, which stipulates ‘Any absolute assignment ... is effectual in

law ... to pass and transfer ... the legal right to such debt or thing in action'.<sup>861</sup> The substantive view is that the assignment actually takes effect as a transfer at law for all purposes.

In English law, the original common law rule was that a chose in action was not assignable, with only a few permitted exceptions.<sup>862</sup> However, equity took the view that a chose in action is property which ought to be transferable in the interest of commercial convenience, e.g. to provide security for a loan.<sup>863</sup> Even when equity gave effect to an assignment of a legal right, equity did not enforce the assignee's claim, which was enforced in the common law courts and in the assignor's name.<sup>864</sup> An equitable assignee must join the assignor in any proceedings against the debtor to enforce the thing in action,<sup>865</sup> as either co-claimant or as co-defendant.<sup>866</sup>

Section 25(6) of the Judicature Act 1873 introduced a form of statutory assignment effect at law, which is a variant of the equitable system. Under Section 136(1) of the Law of Property Act 1925, the benefit of a contract may be transferred to a third party by a process called 'statutory assignment'. If the requirements of Section 136(1) of

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<sup>861</sup> Gregory Tolhurst, *The Assignment of Contractual Rights* (Hart Publishing 2006) [5.06] 107

<sup>862</sup> There were two main reasons for non-assignability. The first reason was that the personal relationship between the debtor and the creditor forbids the substitution of any other party for the original creditor. The second reason was that the assignment of a chose in action would multiply contentions and suits and bring about great oppression of the people including terre-tenants. (e.g. *Lampet's Case* (1612) 10 Co Rep 46b) Oshley Roy Marshall, *Assignment of Choses in Action* (London: Pitman, 1950) 35-36

<sup>863</sup> Guenter Treitel, *The Law of Contract* (London: Sweet & Maxwell, 2003) 674

<sup>864</sup> Gregory Tolhurst, *The Assignment of Contractual Rights* (Hart Publishing 2006) [8.83] 452-53

<sup>865</sup> *Three Rivers District Council v Governor and Company of the Bank of England* [1996] QB 292, 298, 308-09, CA

<sup>866</sup> *Holt v Heatherfield Trust Ltd* [1942] 2 KB 1

the Law of Property Act have been met, the assignee may proceed directly against the debtor without joining the assignor.

### Q3-2-2. Set-off

In the assignment of claims, the debtor may preserve rights of set-off even after the assignment of claims. It is because the rights of the assignee against the debtor could be no more than the rights enjoyed by the assignor.<sup>867</sup> Set-off is excluded in some receivables which are likely to be assigned, such as certain bank loans.

There are two types of non-contractual set-off: equitable (substantive or transaction) set-off and independent (procedural or statutory) set-off. For equitable set-off, the debtor's cross-claim must be closely or inseparably connected with the assignor's claim.<sup>868</sup> An equitable set-off will arise when a claim and cross-claim are so closely connected that it would be inequitable for the assigned claim to proceed without giving credit for the debtor's cross-claim<sup>869</sup> and that it would be unconscionable for an assignee to deny the debtor's cross-claim.<sup>870</sup> Close connection will exist only when the debtor's cross-claim impeaches the title of the assignor's claim.<sup>871</sup> The assignee takes subject to equitable set-off because it results in an impeachment of the title taken by the assignee.<sup>872</sup>

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<sup>867</sup> *Mangles v Dixon* (1852) 3 HLC 702, 10 ER 278, PC; James LJ in *Phillips v Lovegrove* (1873) LR 16 Eq 80, 88

<sup>868</sup> *Bim Kemi AB v Blackburn Chemicals Ltd (No 1)* [2001] EWCA Civ 457; [2001] 2 Lloyd's Rep 93

<sup>869</sup> R Derham, 'Recent Issues in Relation to Set-Off' (1994) 68 ALJ 331, 332

<sup>870</sup> Gregory Tolhurst, *The Assignment of Contractual Rights* (Hart Publishing 2006) [8.64]-[8.65] 435-37

<sup>871</sup> *ibid* [8.64] 436

<sup>872</sup> *ibid* [8.65] 437

Thus, equitable set-off will be permitted, even if the debtor's cross-claim accrues after the debtor receives notice of the assignment.<sup>873</sup>

For independent set-off, the debtor's cross-claim does not have to be connected with the assignor's claim.<sup>874</sup> Independent set-off is related with the notice of the assignment of the claim. A debtor may rely on the cross-claims, which the debtor could enforce against the assignor until notified of the assignment, against an assignee. A debtor may set-off against an assignee the cross-claims that the debtor had against the assignor until notified of the assignment.<sup>875</sup> Notice of the assignment to the debtor of the receivable prevents the debtor from setting-off any cross-claims that the debtor had against the assignor that arise after notice. Once the debtor receives notice of the assignment, the debtor cannot reduce his liability to the assignee by the independent set-off arising after receiving notice of the assignment. The law should not protect the debtor's right of set-off where the debtor has voluntarily obtained his cross-claim against the assignor after knowing that the assignor already assigned the claim to the assignee.<sup>876</sup>

At the time when the debtor receives notice of the assignment of the claim, the cross-claim does not have to be fallen due for payment or be payable,<sup>877</sup> but the debtor's

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<sup>873</sup> *Banco Central SA v Lingos & Falce Ltd (The Raven)* [1980] 2 Lloyd's Rep 266

<sup>874</sup> Roy Goode and Louise Gullifer, *Goode on Legal Problems of Credit and Security* (4th edn, Sweet & Maxwell, 2008) 298-99 [7-36]

<sup>875</sup> It is not a mandatory rule, and thus a debtor may voluntarily waive any defences or rights of set-off before or even after notified of the assignment. The Cape Town Convention, art 31(4) and its Space Protocol, art X(3) stipulate the obligor's waiver of defences and rights of set-off by agreement in writing.

<sup>876</sup> Roy Goode and Louise Gullifer, *Goode on Legal Problems of Credit and Security* (4th edn, Sweet & Maxwell, 2008) 320 [7-67]

<sup>877</sup> *Roxburghe v Cox* (1881) 17 Ch D 520, CA; *In Re Pinto Leite and Nephews* [1929] 1 Ch 221

cross-claim against the assignor must have arisen and accrued due before the debtor receives notice of the assignment.

Under English law, set-offs can arise in relation to receivables subject to a floating charge until both the floating charge has crystallised and the debtor of the receivable receives notice of the crystallisation.

### Q3-2-3. Procedural View of Statutory Assignments

On the other hand, the procedural view of statutory assignments follows the logic of the second view of equitable assignments. The procedural view focuses on the part of Section 136(1) of the Law of Property Act 1925 that a statutory assignment is ‘subject to equities having priority over the right of the assignee’.<sup>878</sup> The procedural view is that it only enables the assignor to sue in its own name as a matter of procedure, but otherwise it does not change the position at all, so that the interest of the assignee is equitable for other purposes, such as priority. As a result, the *Dearle v Hall* rule still applies.<sup>879</sup>

However, since notice to the debtor is a requirement for a statutory assignment, there will rarely be a situation where the application of the substantive view will lead to a different result from that which would follow from the application of the procedural view. Where there are two assignments which comply with the statutory requirements, priority is determined by the order in which the debtor receives notice of the assignment in writing.

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<sup>878</sup> *Compaq Computers Ltd. v Abercorn Group Ltd.* [1991] B.C.C. 484, 501, Michael Bridge, Louise Gullifer, Gerard McMeel and Sarah Worthington, *The Law of Personal Property* (Sweet & Maxwell 2013) [36-013]

<sup>879</sup> Michael Bridge, Louise Gullifer, Gerard McMeel and Sarah Worthington, *The Law of Personal Property* (Sweet & Maxwell, 2013) [27-006]

### ***Q3-3. Priority of Equitable Assignment and Statutory Assignment***

In the case where there are a statutory assignment and an equitable assignment of the same receivable, if the procedural view of statutory assignments is taken, the *Dearle v Hall* rule applies. If the substantive view of statutory assignments is taken, a statutory assignee usually has priority over an equitable assignee. If an equitable assignment is first and if the debtor received notice of the equitable assignment earlier than the notice of the statutory assignment, the statutory assignee is to take subject to the equitable assignment.<sup>880</sup> If a statutory assignment is first, *ex hypothesi* the statutory assignee is the first to give notice to the debtor.

### **Q4. Priority of Security Interests**

Priority of competing charges over receivables is governed by the *Dearle v Hall* rule,<sup>881</sup> once the charges are registered within 21 days of creation.<sup>882</sup> Registration of a charge (including a charge over receivables) in the Registrar of Companies constitutes a constructive notice to someone taking a security interest.<sup>883</sup> As a result, a subsequent

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<sup>880</sup> Law of Property Act 1925, s 136(1) stipulates that a statutory assignment is '(subject to equities having priority over the right of the assignee)'. *E. Pfeiffer Weinkellerei-Weineinkauf GmbH & Co v Arbuthnot Factors Ltd* [1987] BCLC 522 (QB), 533; [1988] 1 WLR 150, 162; *Compaq Computer Ltd v Abercorn Group Ltd* [1993] BCLC 602 (Ch), 621-22.

<sup>881</sup> (1828) 3 Russ 1.

<sup>882</sup> Companies Act 2006 (Amendment of Part 25) Regulations 2013, s 859A

<sup>883</sup> To whom registration of a charge over company book debts in the Registrar of Companies constitutes a constructive notice is not firmly settled. But, many scholars agree that registration is constructive notice to subsequent chargees of the registered company book debt. Some scholars argue that a bank taking commercial security would be expected to search. They also argue that in practice most assignees will search the registry because it is safer to scour the registry than to remain

chargee cannot later give notice of the charge to the debtor of the receivable and obtain priority over the prior charge that is registered.<sup>884</sup> Thus, the chargee who registered its charge first has priority over any subsequent chargee. Consequently, priority between competing charges is determined by the order of registration. If neither of the chargees gives notice of their charges to the debtor of the receivable, priority is determined by the order of creation of the charge according to the first in time rule.

## Q5. Priority between Assignments & Security Interests

### ***Q5-1. Prior Charge - Subsequent Assignment***

If a charge over a receivable is perfected and the same receivable is later assigned to a third party, priority is determined by the order in which the debtor of the receivable receives notice of the charge or the assignment.<sup>885</sup> For a charge over receivables that is to be registered in the Registrar of Companies under the Companies Act 2006, if such registration constitutes a constructive notice, the subsequent assignee cannot have priority over the prior chargee by giving notice of the assignment to the debtor of the receivable. Most financiers of receivables would check the register in the ordinary course of business. Thus, registration might constitute a constructive notice.

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uncertain. Hugh Beale, Michael Bridge, Louise Gullifer and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) 441-42 [13.13].

<sup>884</sup> The second limb of *Dearle v Hall* (1828) 3 Russ 1. *Ellerman Lines Ltd v Lancaster Maritime Co Ltd* [1980] 2 Lloyd's Rep 497 (QB), 503. Until it has been registered, the subsequent chargee will not be on constructive notice of the earlier charge.

<sup>885</sup> *Dearle v Hall* (1828) 3 Russ 1.

### ***Q5-2. Prior Assignment - Subsequent Charge***

If a receivable is assigned to an assignee and a charge is subsequently created over the same receivable, the subsequent chargee would have no way to have actual or constructive notice of the prior assignment since an assignment is not registered.<sup>886</sup> Priority is determined by the order in which the debtor of the receivable receives notice of the charge or the assignment.<sup>887</sup> Therefore a subsequent chargee may give notice of his charge to the debtor of the receivable first (while the debtor of the receivable is not notified of the prior assignment) and obtain priority over the prior assignment.

### **Q6. Potential Assignee's Check Points**

Under English law, a potential assignee should both check the Registrar of Companies and ask the debtor of the receivable whether it received notice of a prior assignment or security interest in the receivable.

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<sup>886</sup> Hugh Beale, Michael Bridge, Louise Gullifer and Eva Lomnicka, *The Law of Personal Property Security* (OUP 2007) 442 [13.14]. But, in practice many receivable financiers also take a charge over all the assets of a financial company.

<sup>887</sup> *Dearle v Hall* (1828) 3 Russ 1.

## 11. China

### Q1. Perfection of Assignments

#### *Q1-1. Assignment of Receivables under the Contract Law*

Owing to Article 80 of the Chinese Contract Law, it is not clear whether an assignment is perfected against the insolvency representative of the assignor if a debtor has not been notified of the assignment. This is because the Chinese Contract Law does not stipulate perfection of an assignment of a receivable against third parties.

Some scholars argue that notice of the assignment to the debtor is required for priority.<sup>888</sup> Other scholars argue that, even though a debtor has not been notified, an assignment can be perfected against the insolvency representative of the assignor once the assignee has paid proper consideration to the assignor for the receivable.<sup>889</sup> They cite Article 31(2) of the Chinese Insolvency Law as support.<sup>890</sup> However, an avoidance provision such as Article 31(2) of the Chinese Insolvency Law exists in many

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<sup>888</sup> See Xuezhong ZHANG, 'Notification: Effectiveness Requirement of the Assignment of Rights', *Legal Science Monthly* 7 (2005); Jianping SHEN, *Research on the Assignment of Rights - Focused on Assignment Notice* (Law Press China, 2008) 167-71.

<sup>889</sup> See Jianyuan CUI, *Contract Law* (3rd edn Law Press China, 2004) 178; Shiyuan HAN, *Contract Law General Principles* (Law Press China, 2004) 568-570.

<sup>890</sup> Chinese Insolvency Law, art 31(2) stipulates that, within one year before the court accepts an application for bankruptcy, the insolvency representative has the right to plead to the court to revoke the following transactions of the debtor's assets: (1) transferring the assets free of charge; (2) transaction at an obviously unreasonable price; (3) providing asset guaranty to those debts without any asset guaranty; (4) paying off the undue debts in advance; or (5) giving up the creditor's right. Nonetheless, this method has the time limitation and sometimes it might be difficult to prove whether that consideration is obviously unreasonable.

jurisdictions regardless of the approach for perfection against the insolvency representative.<sup>891</sup>

In fact, it is controversial whether an assignment of a receivable is perfected against the insolvency representative upon conclusion of the assignment contract without notice of the assignment to the debtor, unless the assignment is denied by the insolvency representative as a transaction at an obviously unreasonable price under the Chinese Insolvency Law.<sup>892</sup>

If an assignment of a receivable is perfected against the insolvency representative without notice to the debtor, the practice of the assignment of receivables in China would be similar with that under the English equitable assignment, although China does not have the concept of equity.

### ***Q1-2. Disposal of Non-Performing Loans***

In April 2001, the Supreme People's Court of China issued 'The Supreme People's Court Provisions Regarding Several Issues on Examining Applicable Laws Concerning Financial Asset Management Company's Acquisition, Management and Disposal of Non-Performing Loan Asset of State-Owned Bank Cases' ('SPC Provisions on Disposal of NPLs').<sup>893</sup> The SPC Provisions on Disposal of NPLs stipulates that if,

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<sup>891</sup> The avoidance of the insolvency representative is for the protection of creditors of the insolvent assignor. For the purpose of preventing unfair fraudulent trade of company assets, insolvency laws of many jurisdictions provide that an insolvency representative may avoid the assignment if the consideration for the assignment of receivables was an unreasonable price and the assignment was made within a certain period of time before the insolvency date.

<sup>892</sup> Chinese Insolvency Law, art 31(2).

<sup>893</sup> Supreme People's Court Judicial Interpretation [2001] No. 12

after a state-owned bank assigns its receivables to an asset management company,<sup>894</sup> the state-owned bank publishes a notice about the assignment of receivables in an influential newspaper distributed nationally or provincially, the court may acknowledge that the state-owned bank has completed the duty of notice under Article 80 of the Chinese Contract Law.<sup>895</sup> Such an assignment is perfected by publication on an influential newspaper distributed national or provincial wide. This provision exempts the difficulties of notification to debtors from the assignment of receivables by a state-owned bank to an asset management company in China.

### ***Q1-3. Securitisation***

For securitisation, China adopted the method of public notice in newspapers for perfection against the insolvency representative of the assignor (originator). It was adopted by Article 6 of the SPC Provisions on Disposal of NPLs and Article 12 of the

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<sup>894</sup> In China, there are the ‘big four’ state-owned commercial banks: the Bank of China, the China Construction Bank, the Industrial and Commercial Bank of China (‘ICBC’), and the Agricultural Bank of China. These banks have historically formed the bulk of the lending to state-owned companies or state-controlled companies and each is focused on particular industries and sectors. Years of government-directed lending resulted in the big four state-owned banks being left with many non-performing loans. According to a People’s Bank of China report, non-performing loans (NPLs’) accounted for 21.4% to 26.1% of the total lending of China’s four big banks in 2002. Furthermore, it was said that the real ratio of bad loans is much higher. In 2003, the Chinese government estimated the amount of such NPLs at around \$240 billion and independent estimates ranged from \$410 to \$815 billion. In 1999, the Chinese government established four asset management companies (资产管理公司) to deal with NPLs. They are Orient (东方), Cinda (信达), Huarong (华融) and Great Wall (长城) asset management companies. About RMB 1,400 billion NPLs were transferred from the big four state-owned banks to the four asset management companies. Each of the four asset management companies mirror one of the big four state-owned banks. Baozhong Gao, *Institutional Analysis of Asset Securitisation in China* (2005) 155; Weitseng Chen, *Legal Implications of a Rising China: WTO: Time’s Up for Chinese Banks—China’s Banking Reform and Non-Performing Loan Disposal*, 7 CHI. J. INT’L L. 239 (2006) 240-43; Yanrong Hong, *Studies of Legal Issues Concerning Asset-Backed Securitisation* (2004) 223; Johnny P. Chen, “*Non-Performing Loan Securitisation in the People’s Republic of China*” (Stanford University Department of Economics, May 2004) 22.

<sup>895</sup> SPC Provisions on Disposal of NPLs, art 6.

Administrative Measures for the Securitisation of Credit Assets ('AMSCA').<sup>896</sup> The AMSCA regulates the pilot work of credit asset securitisation.<sup>897</sup> After the success of these securitisations, there have been several securitisation practices in China.<sup>898</sup>

Perfection against the insolvency representative is achieved by establishing a special purpose trustee ('SPT') and public notice in accordance with the AMSCA. The AMSCA stipulates that an originator must publish a notice about the originator establishing a SPT and that the credit assets are transferred to the SPT on a nationwide medium.<sup>899</sup> The AMSCA provide that an assignment of credit assets may be perfected by making a public announcement rather than giving individual notice to each debtor. The Administrative Measures also stipulates that in the event of originator's insolvency, the trust property is not included in the insolvency asset.<sup>900</sup> It provides that the assets transferred from the originator to the SPT is separated from the originator and will not be affected by the bankruptcy of the originator.

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<sup>896</sup> Announcement of the People's Bank of China and China Banking Regulatory Commission No. 7 [2005]. Enacted on 20 April 2005

<sup>897</sup> AMSCA, art 1. The AMSCA was designed to parallel the pilot asset-backed securitisation ('ABS') scheme of the China Development Bank's (国家开发银行) and the pilot residential mortgage-backed securitisation ('RMBS') scheme of China Construction Bank (建设银行). China Development Bank issued asset-backed securitisations, and China Construction Bank issued residential mortgage-backed securitisations on the same day, 15 December 2005.

<sup>898</sup> For example, China Development Bank (国家开发银行) issued the first ABS amounting RMB 4.178 billion on 15 December 2005, the second ABS on 25 April 2006, and the third ABSs amounting RMB 7.8 billion on 22 June 2007. Shanghai Pudong Development Bank (浦东发展银行) issued ABS amounting RMB 4.383 billion on 14 September 2007. Industrial and Commercial Bank of China (中国工商银行) issued the first ABS amounting RMB 4 billion on 10 October 2007, and the second ABS amounting RMB 8 billion on 27 March 2008. Industrial Bank (兴业银行) issued ABS amounting RMB 5.3 billion in 2007. As for MBS, China Construction Bank (建设银行) issued the first RMBS amounting RMB 3 billion, backed by mortgage receivables, whose average value is RMB 245,430 and average repayment period is 32 months, on 15 December 2005; and the second RMBS amounting RMB 4 billion on 14 December 2007.

<sup>899</sup> AMSCA, art 12

<sup>900</sup> AMSCA, art 6.

## Q2. Perfection of Security Interests

The Chinese Property Law, which is enacted in 2007, stipulates that account receivables (*YingShouZhangKuan*) may be used as pledges.<sup>901</sup> A pledge of a receivable becomes effective upon its registration in the Credit Reference Centre.<sup>902</sup> Registration is required for a pledge of a receivable to be perfected against third parties, but notice of the pledge to the debtor of the receivable is not required for creation of the pledge.<sup>903</sup>

In 2008, to provide a registration system for pledges of receivables under the Chinese Property Law, the People's Bank of China<sup>904</sup> formulated the Measures for Registration of the Pledge of Receivables ('MRPR'),<sup>905</sup> and established a registration system for pledges of receivables in the Credit Reference Centre.<sup>906</sup> However, the registration system is only for pledges of receivables and not for outright assignment of receivables. Therefore outright assignments do not have to be registered. It is similar to

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<sup>901</sup> Chinese Property Law, art 223(6).

<sup>902</sup> Chinese Property Law, art 228.

<sup>903</sup> William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 644.

<sup>904</sup> The People's Bank of China is China's central bank. The People's Bank of China generally formulates and implements monetary policy and performs the functions of regulating inter-bank lending market and inter-bank bond market, maintaining normal operation of the payment and settlement system, etc.

<sup>905</sup> Adopted at the 21st governor's meeting on September 26th, 2007, were promulgated by Order No.4 [2007] of the People's Bank of China, and came into force as of October 1st, 2007.

<sup>906</sup> MRPR, art 2 provides for a centralized registration system for security interests in account receivables, that is the Credit Reference Centre of the People's Bank of China. It is welcomed especially by small and mid-sized enterprises and other enterprises engaged in manufacturing with high levels of account receivables and inventory. Now, lenders or other parties will be able to access a single centralized system in order to obtain information about a borrower or other registered security interests. Joshua T. Klein, "Recent Legal Changes That Affect Secured Financing In The People's Republic Of China", 27-JAN Am. Bankr. Inst. J. 38 (2009) 72-73. The official website of the Chinese Credit Reference Centre is <[http://www.pbccrc.org.cn/chanpinfuwu\\_305.html](http://www.pbccrc.org.cn/chanpinfuwu_305.html)> accessed 10 January 2011.

English law where only charges over company book debts must be registered and an outright assignment of a receivable cannot be registered.

### Q3. Priority of Assignments

Under Chinese law, it is not clear whether notice of assignment to the debtor is required for priority. This is because the Chinese Contract Law<sup>907</sup> stipulates that notice of the assignment to the debtor is required for effectiveness against the debtor of the receivable but does not stipulate priority.

Although it is debatable, it seems that at least priority among competing assignees is determined by the order in which the debtor receives notice of the assignment. For example, suppose there are two assignees: E1 and E2. Even though the date of conclusion of the assignment contract to E1 is prior to the assignment contract to E2, if the debtor received notice of the assignment to E2 but has not received notice of the assignment to E1, E2 have priority over E1 under Chinese law. Thus, it could be said that notice to the debtor is required for priority.

### Q4. Priority of Security Interests

Priority of pledges of receivables is determined by the order of registration of the pledge in the Credit Reference Centre.

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<sup>907</sup> Chinese Contract Law, art 80. The title of this article is 'Duty to Notify When Assigning Rights; Revocation of Assignment Subject to Assignee's Consent'.

## Q5. Priority between Assignments & Security Interests

Priority between assignments or security interests is determined by the order of notification of the assignment to the debtor or registration of the pledge in the Credit Reference Centre.

## Q6. Potential Assignee's Check Points

A potential assignee should check both the receivables pledges registry in the Credit Reference Centre and ask the debtor of the receivable whether it received notice of a prior assignment of the receivable.

## **12. Germany**

### **Q1. Perfection of Assignments**

#### ***Q1-1. Assignment of Receivables***

In German law, with respect to an assignment of receivables, there is no difference between the perfection of an assignment and the creation of an assignment. An assignment of receivables is perfected against third parties (including the insolvency representative of the assignor) upon conclusion of the assignment agreement of the parties.

For the creation of an assignment of receivables, only an agreement between an assignor and an assignee is required, and the participation of a debtor of a receivable is not required. A failure to give notice of the assignment to the debtor of the receivable does not void the assignment.

In German law, any third party involvement or confirmation is not required for the assignment of receivables to be perfected against third parties. The transfer of a receivable does not have to be published, whereas the ownership transfer of land must be published by registration and the ownership transfer of tangible movable assets must be published by delivery of possession. The German Civil Code does not require publicity for the assignment of receivables. Instead, an assignor functions as the information centre. Thus, a potential assignee needs to enquire of the assignor about the status of a receivable. This is sensible because an assignor is the person in the best position to know the status of a receivable that belongs to him.

The German Civil Code stipulates that when the assignment contract is entered into, ‘the new creditor (assignee) steps into the shoes of the previous creditor (assignor)’.<sup>908</sup> Therefore an assignee acquires all the same rights over the receivables that the assignor possessed. An assignee is entitled to receive payments and may take any required actions without joining the assignor. If a debtor is not notified of the assignment, he is free to pay the assignor (original creditor). Still, an assignee is entitled to get such payments from the assignor.<sup>909</sup>

### ***Q1-2. Global Assignment (Globalzession)***

German provisions on the assignment of receivables permit a global assignment (*Globalzession*).<sup>910</sup> Global assignment is a contract pursuant to which an assignor assigns all its current and future receivables originated from certain legal acts or from certain designated debtors. However, for the global assignment agreement to be effective, it must be possible to identify the future receivables.<sup>911</sup>

### ***Q1-3. Securitisation***

Such liberal regulation as the German regime on the assignment of receivables allows more flexibility in structuring asset securitisation transactions that best suit the interests of the particular company. The assignment of receivables under the German Civil Code could be the best method of transferring receivables for asset securitisation.

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<sup>908</sup> German Civil Code, s 398

<sup>909</sup> Lina Aleknaitė, ‘Why The Fruits Of Capital Markets Are Less Accessible In Civil Law Jurisdictions Or How France And Germany Try To Benefit From Asset Securitisation’ (Winter 2007) 5 *DePaul Business & Commercial Law Journal* 191, 219, n 187

<sup>910</sup> *ibid* 221

<sup>911</sup> Hendrik Haag and Oliver Peglow, Germany (Ch 14) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 196

Jurisdictions following German law such as Austria and Switzerland are in a good position to facilitate receivables financing. Nonetheless, statistics show that there have not been as many securitisation practices in these states as in the US.<sup>912</sup> This could be because their banks might not prefer securitisation.

## Q2. Perfection of Security Interests

### ***Q2-1. Pledge of Receivables (Forderungsverpfändung)***

The creation of a pledge of a receivable requires notice of the pledge to the debtor of the receivable.<sup>913</sup> Notice of the pledge must be given by the pledgor. Alternatively, if notice is given by the pledgee, it must be authorised by the pledgor.<sup>914</sup> Notification need not be in writing.<sup>915</sup>

### ***Q2-2. Security Assignment of Receivables (Sicherungsabtretung)***

Compared to a pledge of receivables, the security assignment of receivables does not require notice to the debtor of the receivable. The security assignment of receivables is only valid if the assignor (security provider) and the assignee (secured creditor) agree

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<sup>912</sup> Interestingly, the statistics show that securitisation is issued and used incomparably more in the United States than in Germany. ESF (European Securitisation Forum) Securitisation Data Report Q2:2009 (SIFMA (Securities Industry and Financial Markets Association), 2009) 3 <<http://www.afme.eu/document.aspx?id=2788>> accessed 5 April 2011.

<sup>913</sup> German Civil Code, s 1280 stipulates that the pledging of a receivable, for whose transfer a contract of assignment suffices, is effective only if the creditor gives notice thereof to the debtor ('Die Verpfändung einer Forderung, zu deren Übertragung der Abtretungsvertrag genügt, ist nur wirksam, wenn der Gläubiger sie dem Schuldner anzeigt.').

<sup>914</sup> Julia Klauer Rakob, Germany, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 118.

<sup>915</sup> *ibid.*

on the assignment.<sup>916</sup> The assignee may collect the receivable without joining the assignor, as if the assignee were the creditor of the receivable.<sup>917</sup> Because a security assignment of receivables does not require giving notice to the debtors of the receivable, in Germany, security assignments have replaced pledges under the Civil Code as the common form of security interests in receivables.<sup>918</sup>

### Q3. Priority of Assignments

Under the German Civil Code, notice to a debtor is not required for the assignment of a receivable. The assignee prior in time of the assignment agreement has priority regardless of notification. Under German law, priority between an assignee, the insolvency representative, and a judgment creditor is determined according to the order of conclusion of the assignment contract,<sup>919</sup> bankruptcy adjudication and attachment notice.

If an assignee asks an assignor for a publicly certified copy of the assignment contract, the assignor must provide it but the assignee should pay the cost.<sup>920</sup> The date of

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<sup>916</sup> Hansjörg Weber, *Kreditsicherungsrecht* (8<sup>th</sup> den, München 2006) 302.

<sup>917</sup> Hendrik Haag and Oliver Peglow, Germany (Ch 14) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 200 [14.16].

<sup>918</sup> Julia Klauer Rakob, Germany, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 93.

<sup>919</sup> German Civil Code, s 403

<sup>920</sup> German Civil Code, s 403

the assignment is verified by a publicly certified document evidencing the assignment (if it is issued). However, in practice, it is not often issued because of the time and costs.<sup>921</sup>

The debtor who had no notice of the first assignment may discharge the debt by paying the second assignee.<sup>922</sup> However, if the second assignee has collected the debt from the debtor, he must surrender the money to the first assignee even though he gave value and knew nothing of the first assignment.<sup>923</sup> If a second assignee gives notice to a debtor first, a debtor may discharge the debt by paying the second assignee until such time as the first assignee gives notice to the debtor. The second assignee must surrender any payments he received from the debtor to the first assignee. If a debtor of a receivable is truly uncertain as to who has priority, the debtor may deposit the payment with the court, which will ultimately determine which assignee has priority.

If an assignor fraudulently or mistakenly assigns the same receivable to different assignees, the assignor will have to compensate the assignees for damages and be criminally charged with fraud. Usually, the assignor signs a document confirming that there is no prior assignment of or security interest in the receivable before the assignment agreement. The assignor will be punished for fraud against the assignee.<sup>924</sup> It can also give rise to civil liability.

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<sup>921</sup> Interview with Ulrich Drobniig, Professor, Max Planck Institute for Comparative and International Private Law (Hamburg, Germany, 20 October 2010)

<sup>922</sup> German Civil Code, ss 407 and 408

<sup>923</sup> See Section 3-2-2-4-1

<sup>924</sup> With respect to forgery, even though the assignor signed a document that confirms there is no prior assignment of or security interest in the receivable, and before or after signing such a document, the assignor assigned or assigns the receivable to another assignee, it does not constitute a forgery (*Urkundenfälschung*) under German Criminal Code, s 267. The assignor is a rightful composer of the document assuming he did not use another person's name or title. This only creates an erroneous private document, which is not subject to criminal punishment except in the case of health certificates under German Criminal Code, s 278.

#### Q4. Priority of Security Interests

Priority of pledges of a receivable is determined by the order in which the debtor of the receivable receives notice of the pledge. In the case of two pledges of one receivable, the pledge of which the debtor received notice earlier takes priority over the later one.<sup>925</sup> The right to enforce the pledge rests with the holder of the priority pledge.<sup>926</sup>

#### Q5. Priority between Assignments & Security Interests

Priority of assignments or pledges of a receivable is determined by the order of conclusion of the assignment agreement or notification of the pledge to the debtor of the receivable.

#### Q6. Potential Assignee's Check Points

A potential assignee should ask the debtor of the receivable whether it received notice of a prior pledge. However, it does not guarantee the assignee's priority. If there is another assignment with a contractual effective date that is prior to that of the potential assignee, then the potential assignee does not have priority. A potential assignee may, of course, also ask the assignor whether there was a prior assignment.

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<sup>925</sup> Hendrik Haag and Oliver Peglow, Germany (Ch 14) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 196 [14.07].

<sup>926</sup> German Civil Code, s 1290

## 13. Austria

### Qs 1, 3. Assignments

An outright assignment of receivables does not require notification to a debtor. The assignment of receivables is done only by the agreement of the parties.<sup>927</sup> Neither notice to the debtor of the receivable nor consent of the debtor of the receivable is required for the assignment to be perfected against third parties including the insolvency representative of the assignor.<sup>928</sup> It is the same under German law. Where the first assignee does not give notice to the debtor of the receivable and the second assignee gives notice of the assignment to the debtor of the receivable, if the debtor of the receivable pays the second assignee then the first assignee may claim against the second assignee for unjust enrichment (*Bereicherungsanspruch*). Furthermore, if the second assignee knew of the first assignment, or was negligent, the first assignee can claim against the second assignee under tort law (*Schadenersatzanspruch*) as in German law. Priority is determined by the order of conclusion of the assignment contract.

### Qs 2, 4. Security Interests

The pledge of receivables requires an explicit act (*Zeichen*) which allows its existence to be ascertained by third parties.<sup>929</sup> Notification to a debtor qualifies as an explicit act (*Zeichen*). In addition, a pledgor company may have records in their book

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<sup>927</sup> Austrian Civil Code, art 1392.

<sup>928</sup> Austrian Civil Code, art 1394. See Rudolf Welser, *Koziol-Welser Bürgerliches Recht Band II* (Manz, 2007) 120.

<sup>929</sup> Austrian Civil Code, arts 452 and 427.

(*Buchvermerk*), which evidence each receivable, the pledge, its date and the assignee, for the explicit act (*Zeichen*) requirement to be satisfied.<sup>930</sup> Thus, for the pledge of a receivable, either notice of the pledge to the debtor of the receivable or a written record in the book of the pledgor company is required in order to perfect a pledge of a receivable against third parties including the insolvency representative of the assignor. These records are not available for potential assignee or pledgee to check. The record is solely intended to prevent backdating by immediately recording an exact date. A potential assignee or pledgee may ask the debtor of the receivables whether he received notice of a prior pledge. However, it is not definitive because there is the possibility of future assignments or hidden pledges made without full disclosure to the debtor of the receivable.

Priority is determined by the order of notification of the pledge to the debtor of the receivable or the recordation of the pledge in the book (*Buchvermerk*) of the assignor, comparing the date of the notice of the pledge to the debtor and the date of the recordation of the pledge in the book (*Buchvermerk*) of the assignor.

## Q5. Priority between Assignments & Security Interests

Priority is determined by the order of conclusion of the assignment contract, notice of the pledge to the debtor of the receivable or recordation of the pledge in the book (*Buchvermerk*) of the assignor. Comparing the date of the conclusion of the assignment contract with the time of notice of the pledge to the debtor or the time of

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<sup>930</sup> Rudolf Welsler, *Koziol-Welsler Bürgerliches Recht Band II* (Manz, 2007) 120.

recording of the pledge in the book (*Buchvermerk*) of the assignor, the first in time has priority.

#### Q6. Potential Assignee's Check Points

A potential assignee should ask the debtor of the receivable whether it received notice of a prior pledge. The book (*Buchvermerk*) of an assignor company is not available for a potential assignee to check.

## 14. The Netherlands

<Table 18> Perfection Methods of Assignment & Pledge in Dutch Law

	Assignment	Pledge	
notice to the debtor of the receivable	O	disclosed pledge ( <i>openbaar pand</i> )	O
notarisation of a transfer deed	O	undisclosed pledge ( <i>stil pand</i> )	O
registration of a transfer deed with TRD	O		O

### Q1. Perfection of Assignments

#### *Q1-1. Outright Assignment*

The Netherlands abolished the notification requirement for the outright assignment of receivables in 2004.<sup>931</sup> The Dutch Civil Code allows the following three methods of perfection against the insolvency representative: (1) notice of the assignment to the debtor of the receivable, (2) notarisation of a transfer deed (*akte*), or (3) registration of a transfer deed with the Tax Registration Department (*Belastingdienst/Registratie en successie*) ('TRD').<sup>932</sup> Parties may choose one of the three perfection methods.

The last two methods of (2) and (3) mean that an assignment of receivables can be perfected by the mere execution of a written transfer deed,<sup>933</sup> which must be signed by both an assignor and an assignee. They are available only for receivables that already

<sup>931</sup> Dutch Civil Code, art 3:94. Originally, Dutch law had not required notice of the assignment to the debtor; but in 1994 it was decided that the notification requirement was necessary; and finally on 1 October 2004 the notification obligation was revoked. Philip Wood, *Principles of International Insolvency* (Sweet & Maxwell 2007) 297.

<sup>932</sup> Dutch Civil Code, art 3:94(3).

<sup>933</sup> Angélique Thiele, 'Dutch securitisations: a step forward', *The In-House Lawyer* (February 2005) 30 <[http://www.legal500.com/assets/images/devs/nether/fi/nlfi\\_014.pdf](http://www.legal500.com/assets/images/devs/nether/fi/nlfi_014.pdf)> accessed 7 January 2009.

exist at the time of the assignment and future receivables that arise directly from a legal relationship that already exists at the time.<sup>934</sup> However, neither notarisation of a transfer deed or registration with the TRD is publicity, since they are not available to the public or any other interested parties. They are only to certify the assignment of receivables. Registration is a substitute for notarisation, but notarisation is costly.

### ***Q1-2. Security Assignment***

Under the Dutch Civil Code, transfer of title to a receivable for security purposes is, in principle, not permitted.<sup>935</sup> In the Netherlands, a security assignment of receivables was disallowed by a Dutch Supreme Court decision<sup>936</sup> referring to Article 3:84(3) of the Dutch Civil Code, which stipulates that a judicial act intended to transfer property for the purpose of security or which does not have the purpose of vesting title in the transferee after the transfer, does not constitute a valid title transfer of that property.<sup>937</sup>

## **Q2. Perfection of Security Interests**

Under Dutch law, there are two ways to use receivables as collateral: a pledge with notification (disclosed pledge, *openbaar pand*) and a pledge without notification (undisclosed pledge, *stil pand*).

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<sup>934</sup> Dutch Civil Code, art 3:94(3). See Sander Timmerman and Michael Veder, Netherlands, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 183.

<sup>935</sup> Dutch Civil Code, art 3:84(3).

<sup>936</sup> Sogelease case, HR 19 May 1995, NJ 1996, 119.

<sup>937</sup> Sander Timmerman and Michael Veder, Netherlands, in Harry C. Sigman and Eva-Maria Kieninger (eds), *Cross-Border Security over Receivables* (Sellier 2009) 185.

A disclosed pledge (*openbaar pand*) is created through the perfection method of (1). Notification is not subject to any specific form requirement. Notification may be oral or in writing.<sup>938</sup>

An undisclosed pledge (*stil pand*) may be created by the perfection methods of (2) and (3). In the case of an undisclosed pledge, the pledgee is authorised to give notice of the pledge to the debtor of the receivable if the pledgor is in default or if the pledgee has good reason to believe that such a default will occur.<sup>939</sup>

### Qs 3, 4, 5. Priority

Priority is determined by the order of perfection of the assignment or the pledge by one of the following three perfection methods: (1) notice of the assignment to the debtor of the receivable, (2) notarisation of a transfer deed or (3) registration of a transfer deed with the TRD.<sup>940</sup> Once one of these three methods has been achieved, the assignment or the pledge of receivables is perfected against third parties. The assignee or pledgee completing any one of the three perfection methods first has priority over any subsequent assignee or pledgor. The rule for priority is that the earlier pledge prevails, *i.e.* first in time, first in right. Therefore any subsequently disclosed right of pledge will not

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<sup>938</sup> Notification is not subject to any specific form requirement. Notification may be oral or in writing. *ibid* 212.

<sup>939</sup> *ibid*.

<sup>940</sup> Dutch Civil Code, art 3:94(3).

have priority over earlier undisclosed rights of pledge, even if the second pledgee acted in good faith.<sup>941</sup>

## Q6. Potential Assignee's Check Points

A potential assignee should ask the debtor of the receivable whether it has received notice of a prior assignment or a prior pledge of the receivable. The best approach for a potential assignee would be to register the assignment of a receivable with the TRD as soon as possible. However, even so, it does not guarantee the assignee's priority. If another assignee or pledgee notarises an assignment or pledge prior to the potential assignee's registration with the TRD, that assignee or pledgee would have priority.

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<sup>941</sup> William Rank, Netherlands (Ch 25) in William Johnston (ed), *Security Over Receivables - An International Handbook* (OUP 2008) 360 [25.29].

## 15. EU Directive on Financial Collateral Arrangements

### 15-1. The Parties - Financial Institution

Directive 2002/47/EC on financial collateral arrangements as amended by Directive 2009/44/EC is referred to as 'EU FCD' in Appendix II. 15. The EU FCD generally does not cover receivables except those owed to financial institution.

Directive 2002/47/EC on financial collateral arrangements<sup>942</sup> limits its scope of application to the cases where none of the parties (the security provider or the secured creditor) is a natural person,<sup>943</sup> and at least one or both of the parties belong to one of the following categories: (a) a public authority;<sup>944</sup> (b) a central bank, the European Central Bank, the Bank for International Settlements, a multilateral development bank, the International Monetary Fund and the European Investment Bank;<sup>945</sup> (c) a financial institution subject to prudential supervision,<sup>946</sup> or (d) a central counterparty, settlement agent or clearing house.<sup>947</sup> If one party belongs to one of these four categories, the counterparty on the other side may be any legal person including unincorporated firms

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<sup>942</sup> Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements [2002] OJ L168/43 For the information about national implementation of Directive 2002/47/EC on financial collateral arrangements, refer to EUR-Lex, Bibliographic notice 72002L0047  
<<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:72002L0047:EN:NOT>>  
accessed 15 January 2013

<sup>943</sup> EU FCD, art 1(2)(e).

<sup>944</sup> EU FCD, art 1(2)(a).

<sup>945</sup> Directive 2002/47/EC on financial collateral arrangements, art 1(2)(b) as amended by Directive 2009/44/EC, art 2(4)(a).

<sup>946</sup> Directive 2002/47/EC on financial collateral arrangements, art 1(2)(c) as amended by Directive 2009/44/EC, art 2(4)(b).

<sup>947</sup> EU FCD, art 1(2)(d).

and partnerships outside of the banking industry.<sup>948</sup> It extends the scope of application beyond collateral arrangements between central banks and financial institutions.

## 15-2. Financial Collateral

### *15-2-1. Cash, Financial Instruments*

Directive 2002/47/EC on financial collateral arrangements has removed any publicity requirements such as registration or notification<sup>949</sup> for the arrangement of financial collateral consisting of cash or financial instruments.<sup>950</sup>

Directive 2002/47/EC on financial collateral arrangements also recognises the assignment of credit claims for security purposes.<sup>951</sup>

### *15-2-2. Credit Claims*

In 2007, the European Central Bank introduced credit claims as an eligible type of collateral for Eurosystem credit operations.<sup>952</sup> In line with the change, Directive 2009/44/EC<sup>953</sup> amended Directive 2002/47/EC on financial collateral arrangements, and has expanded the scope of the Directive to include the financial collateral consisting of

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<sup>948</sup> EU FCD, art 1(2)(e). However, States may opt out this provision. EU FCD, art 1(3)

<sup>949</sup> EU FCD, recital 10 and art 3(1)

<sup>950</sup> EU FCD, art 1(4)(a).

<sup>951</sup> EU FCD, arts 2(1)(b) and 6

<sup>952</sup> European Central Bank (ECB) press release of 15 September 2006  
<[http://www.ecb.eu/press/pr/date/2006/html/pr060915\\_1.en.html](http://www.ecb.eu/press/pr/date/2006/html/pr060915_1.en.html)> accessed 15 January 2013

<sup>953</sup> Directive 2009/44/EC of the European Parliament and of the Council of 6 May 2009 amending Directive 98/26/EC on settlement finality in payment and securities settlement systems and Directive 2002/47/EC on financial collateral arrangements [2009] OJ L146/37 For the information about national implementation of Directive 2009/44/EC, refer to EUR-Lex, Bibliographic notice 72009L0044  
<<http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:72009L0044:EN:NOT>> accessed 15 January 2013

‘credit claims’,<sup>954</sup> i.e. receivables arising out of an agreement whereby a credit institution grants credit in the form of a loan.<sup>955</sup> Such credit claims are basically bank loans used as collateral for advances from the European Central Bank and other central banks.<sup>956</sup> It facilitates an assignment or pledge of bank loans to the central banks for security purposes.

### 15-3. Perfection

A financial collateral arrangement may not be declared invalid or void if the financial collateral arrangement has come into existence or the financial collateral has been provided prior to the order or decree making the commencement of insolvency proceedings or reorganisation measures.<sup>957</sup> It does not require any publicity for perfection against the insolvency representative. As a result, credit claims can be pledged or assigned for security purposes in the same way as financial instruments or cash. In the insolvency of the security provider, the secured creditor can realise the credit claim as financial collateral even though the secured creditor did not give notice to the debtor of the credit claim prior to the insolvency adjudication. If an EU jurisdiction requires registration of security interests in or security assignments of such credit claims under its national law for perfection against insolvency representatives,<sup>958</sup> it must repeal the

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<sup>954</sup> Directive 2009/44/EC, art 2(4)(c).

<sup>955</sup> Directive 2009/44/EC, art 2(5)(a)(ii).

<sup>956</sup> Louise Gullifer, ‘What Should We Do about Financial Collateral?’ (2012) 65 *Current Legal Problems* 377, 404

<sup>957</sup> EU FCD, art 8(1)(a).

<sup>958</sup> EU FCD, arts 8(1) and (2)

legislation to the extent it applies to interests over financial collateral. The EU FCD contributes to harmonising legal standards with respect to credit claims, used among credit institutions in EU Member States.

#### 15-4. Priority

Where credit claims are provided as financial collateral, priority is determined by the order of execution of financial collateral agreements. However, it is allowed for Member States to require publicity such as registration or notification for priority vis-à-vis third parties.<sup>959</sup>

#### 15-5. Implementation

<Table 19> Implementation of the EU Directive on Financial Collateral Arrangements

	Directive 2002/47/EC on financial collateral arrangements	Directive 2009/44/EC amending Directive 2002/47/EC
France	Articles L211-36 to L211-40 of the French Monetary and Financial Code <sup>960</sup>	
Belgium	Financial Collateral Act of 15 December 2004	Act of 26 September 2011
UK	Financial Collateral Arrangements (No 2) Regulations 2003 <sup>961</sup>	Financial Collateral Arrangements (No 2) Regulations 2003 (Amendment) Regulations 2009 <sup>962</sup>

<sup>959</sup> Directive 2009/44/EC, art 2(6)(a).

<sup>960</sup> inserted by Order No. 2009-15 of 8 January 2009 Art. 1 Official Journal of 9 January 2009

<sup>961</sup> SI 2003/3226. Its scope of application with respect to parties is wider than that of the EU FCD in that the UK Regulations 2003 applies to financial collateral arrangements where the collateral-provider and the collateral-taker are both non-natural persons. Financial Collateral Arrangements (No 2)

		Financial Markets and Insolvency (Settlement Finality and Financial Collateral Arrangements) (Amendment) Regulations 2010 <sup>963</sup>
Germany	Law of the 5th of April 2004 implementing the Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements <sup>964</sup>	Law implementing the amended Banking Directive and the Capital Adequacy Directive amended <sup>965</sup>
Austria	Federal Law implementing the Federal Law governing safety on financial markets (Financial Markets Safety Act – FinSG) and modifying the Private International Law Act <sup>966</sup>	Financial Collateral Act ( <i>Finanzsicherheiten-Gesetz</i> ) <sup>967</sup>
The Netherlands	Law of 22 December 2005 to implement Directive 2002/47/EC of the	Law of 21 April 2011 amending the Civil Code and the Bankruptcy Act to implement Directive 2009/44/EC amending Directive

Regulations 2003, reg 3. It does not require one of the parties to be a financial institution. There was an argument that it is ultra vires section 2(2) of the European Communities Act 1972, but such argument is unlikely to succeed. *R (on the application of Cukurova Finance International Limited) v. Her Majesty's Treasury* [2008] EWHC 2567 (Admin)

<sup>962</sup> SI 2009/2462

<sup>963</sup> SI 2010/2993. The amended Regulations cover receivables on loans made by credit institutions. The Financial Collateral Arrangements (No.2) Regulations 2003, reg 3 was amended by the Financial Markets and Insolvency (Settlement Finality and Financial Collateral Arrangements) (Amendment) Regulations 2010, regs 4(2)(b)(i) and (ii). Accordingly, for financial collateral arrangements with respect to receivables on loans made by credit institutions, no publicity (neither registration nor notice to the debtor) is required.

<sup>964</sup> Gesetz vom 5/4/2004 zur Umsetzung der Richtlinie 2002/47/EG vom 6/6/2002 über Finanzsicherheiten und zur Änderung des Hypothekbankgesetzes und anderer Gesetze, Bundesgesetzblatt, (2004) part I, No 15, p 502  
<[http://ec.europa.eu/internal\\_market/finances/actionplan/transposition/germany/f\\_d7\\_de\\_en.htm](http://ec.europa.eu/internal_market/finances/actionplan/transposition/germany/f_d7_de_en.htm)> accessed 15 January 2013

<sup>965</sup> Gesetz zur Umsetzung der geänderten Bankenrichtlinie und der geänderten Kapitaladäquanzrichtlinie, Bundesgesetzblatt (2010) part I, No 58, pp 1592-1613

<sup>966</sup> Bundesgesetz, mit dem ein Bundesgesetz über Sicherheiten auf den Finanzmärkten (FINSG) erlassen wird und das Bundesgesetz über das internationale Privatrecht geändert wird, Bundesgesetzblatt für die Republik Österreich (BGBl) n° 117 vom 16/12/2003 p. 1645  
<[http://ec.europa.eu/internal\\_market/finances/actionplan/transposition/austria/f\\_d7\\_at\\_en.htm](http://ec.europa.eu/internal_market/finances/actionplan/transposition/austria/f_d7_at_en.htm)> accessed 15 January 2013

<sup>967</sup> Bundesgesetzblatt für die Republik Österreich (BGBl), I Nr. 90/2010

	European Parliament and European Council of 6 June 2002 concerning financial collateral arrangements <sup>968</sup>	98/26/EC on settlement finality in the settlement of payments and securities transactions in payment and securities settlement systems and Directive 2002/47/EC on financial collateral arrangements as regards linked systems and credit claims <sup>969</sup>
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<sup>968</sup> Wet van 22 december 2005 tot uitvoering van Richtlijn nr. 2002/47/EG van het Europees Parlement en de Raad van de Europese Unie van 6 juni 2002 betreffende financiële zekerheidsvereenkomsten, Staatsblad 2006, 15

<[http://ec.europa.eu/internal\\_market/finances/actionplan/transposition/netherlands/f\\_d7\\_nl\\_en.htm](http://ec.europa.eu/internal_market/finances/actionplan/transposition/netherlands/f_d7_nl_en.htm)> accessed 15 January 2013

<sup>969</sup> Wet van 21 april 2011 tot wijziging van het Burgerlijk Wetboek en de Faillissementswet ter implementatie van Richtlijn 2009/44/EG van het Europees Parlement en de Europese Raad van 6 mei 2009 tot wijziging van Richtlijn 98/26/EG betreffende het definitieve karakter van de afwikkeling van betalingen en effectentransacties in betalings- en afwikkelingssystemen en Richtlijn 2002/47/EG betreffende financiële zekerheidsvereenkomsten wat gekoppelde systemen en kredietvorderingen betreft (PbEU L 146/37) Staatsblad 2011, 210

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