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Should Clauses Prohibiting Assignment Be Overridden by Statute?

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A. Introduction

Many contracts for the supply of goods or services include a clause prohibiting assignment by the supplier of its rights under the contract. The existence of such clauses, both in particular contracts and more generally, can have a chilling effect on the use of receivables as collateral to obtain financing. Thus, in many jurisdictions, there is a legislative override for such clauses, so that they are not enforceable against third parties. There is an ongoing debate as to whether English law should follow suit and, if so, what form the override should take, which has now led to a power to make reforms being included in sections 1 and 2 of the Small Business, Enterprise and Employment Act 2015.[1] This chapter examines the arguments for and against an override in English law, informed by two small-scale surveys undertaken by the author and others over the last four years.[2]

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[1] The need for statutory reform is not universally accepted. The Financial Law Committee of the City of London Law Society argue that any practical problems in financing transactions relating to anti-assignment clauses can be dealt with by consensual means, see R Calnan, 'Ban the Ban: Prohibiting Restrictions on the Assignment of Receivables' [2015] *Journal of International Banking and Financial Law* 136.

[2] One was carried out by Hugh Beale and Louise Gullifer in 2011 ('the 2011 study'), with the assistance of Anna Kloeden. It was funded by the Asset Based Finance Association (ABFA), who stressed from the outset that it wanted a completely independent view to be taken. The second was carried out in 2014 as part of the work of the Secured Transactions Law Reform Project ('the 2014 study') by Sarah Paterson. I am grateful to both Hugh Beale and Sarah Paterson for permitting me to use this material in this chapter, and for many useful discussions. For further discussion of the results of the surveys, see H Beale, L Gullifer and S Paterson, 'Ban on Assignment Clauses: Views from the Coalface' (2015) 30 Butterworths Journal of International Banking and Financial Law 463 and H Beale, L Gullifer and S Paterson, 'A Case for Interfering with Freedom of Contract? An Empirically Informed Study of Bans on Assignment' [2016] Journal of Business Law 203.

The form of an override is not discussed in detail, for reasons of space. One model is that found in Personal Property Securities Acts (PPSAs) such as the Saskatchewan Personal Property Securities Act,[3] which provides that an anti-assignment clause is binding on the assignor, but only to the extent of making it liable for damages for breach of contract, and is unenforceable against third parties. Another model is that found in the Uniform Commercial Code (UCC) Article 9, which provides that an anti-assignment clause is ineffective to the extent that it prohibits or restricts assignment, or the creation of a security interest, and also to the extent that it provides that an assignment is a breach of contract. The draft Regulations circulated by the UK Department for Business, Innovation and Skills[4] followed the UCC model.

In this chapter, the arguments for and against an override are examined in section B. Sections C to F discuss the reasons why an override has not been a policy imperative in England and Wales until recently. Section G considers whether there should be a statutory override and section H concludes that, on balance, such an override would be beneficial.

B. The Arguments

If the availability of finance and credit in the economy is to be maximised, it is important that as many sources of wealth as possible can be used as collateral. To do this, the source of wealth (the asset) must be able to be alienated to the secured creditor. In the past, the obvious assets which could be alienated were tangible assets: goods and land. However, sources of wealth also included intangible assets, most importantly rights to be paid by another. Thus, many centuries ago, it became possible to use obligations owed to a borrower as collateral for

[3] Section 41.

[4] Available at www.gov.uk/government/uploads/system/uploads/attachment_data/file/383538/draft-statutory-instrument-business-contract-terms-restrictions-on-assignment-of-receivables-regulations-2015.pdf.

a loan, first by pledging a document which represented that obligation (a documentary intangible) and then by enabling the benefit of obligations to be assigned, either absolutely or by way of security. A major difference between the use of tangible property (goods and land) as collateral and the use of such obligations, known in English law as choses or things in action,[5] is that in the latter case there is another person to consider, namely the obligor. There is no real problem when the obligor undertakes an obligation which is designed to be transferred, for example a negotiable instrument. But where the obligation can be transferred without the agreement, or even the knowledge, of the obligor, a policy imperative arises in competition to that of maximising available collateral by permitting alienability: that of protection, where necessary, of the obligor. This latter policy is demonstrated in English law, for example, by the rule that only an assignee who has taken a statutory assignment can sue the debtor[6] (if an equitable assignment is taken, the assignor must be joined in any action). The main criteria for a statutory assignment, namely that the assignment is in writing, that it does not relate to part of a debt or a future debt and that notice of the assignment has been given to the debtor, all serve some function in protecting the debtor. The policy is also shown by the rule that the benefit of a contract for personal services cannot be assigned,[7] and, more widely, by permitting the obligor to protect himself by restricting the ability of the obligee to assign the benefit of the obligation to another. This permission is also justified by another, even wider policy: that of freedom of contract.

Thus, whether there should be a statutory override of anti-assignment clauses can be seen as a matter of balancing competing policy imperatives: alienability of assets, which maximises available collateral, and freedom of contract, which allows obligors to protect

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[5] Also known as intangibles, but the category of intangibles is potentially wider than just choses in action, including, for example, intellectual property, carbon trading units etc.

[6] Law of Property Act 1925 s 136.

[7] *Tolhurst v Associated Portland Cement Manufacturers (1900) Ltd* [1903] AC 414.

themselves against adverse effects of assignment of the right to which their obligation correlates. In assessing that balance, many jurisdictions and transnational instruments have come down in favour of alienability.[8] Gilmore described the view in favour of the unrestricted and unrestrictable alienability of contract rights as 'so fundamental an order [that] belief is instinctive and irrational, not logical and reasoned'.[9] This argument has been used to justify a statutory provision making an anti-assignment clause unenforceable against third parties.

It is suggested here that the policy position is not so simple. At least from the English law perspective, there is a view that the policy imperatives can be satisfied without any statutory interference.[10] It is also thought that legislative change has to be justified by economic arguments based on the effects of uncertainty of outcome and on evidence that the availability and the cost of borrowing is actually affected by the existence, or potential existence, of anti-assignment clauses in contracts giving rise to receivables. These views are held for various interconnected reasons:[11] first, that the current law, to a large extent, accommodates the protection of the obligor and the validity of a proprietary interest of the assignee; second, that receivables financiers in England and Wales have managed reasonably well up to now by adopting 'workarounds' enabling them to function within the current system; third, that the main concern about anti-assignment clauses relates to borrowers who

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[8] See, in relation to the Australian Personal Property Securities Act 2009, A Duggan and D Brown, *Australian Personal Property Securities Law* (Sydney, LexisNexis, 2nd edn, 2016) 42; UNCITRAL Legislative Guide on Secured Transactions, II.107; See also, in relation to the UNCITRAL Convention on Assignment of Receivables in International Trade, UNCITRAL A/CN.9/397 (report of Secretary-General) para 23, A/CN.9/489 (analytical commentary on the draft Convention) para 100).

[9] G Gilmore, *Security Interests in Personal Property* (Boston, Little, Brown & Co, 1965) 7.6 p 212.

[10] See Calnan (n 1) 136. See, however M Bridge, 'The nature of assignment and non-assignment clauses' (2016) 132 Law Quarterly Review 47, who argues that the current law is uncertain and accepts that a statutory override will restore marketability.

[11] Another reason, which is not examined here in detail, is a fundamental belief in freedom of contract. The question whether such freedom should be statutorily interfered with is examined throughout this chapter.

are small businesses, and is part of a wider problem of inequality of bargaining power; and fourth, that anti-assignment clauses play an important and justifiable role in loan agreements, in derivative contracts and in other financial transactions, and there is real concern over defining the scope of statutory controls so that these benefits are not lost.

Each of these reasons will now be considered.

C. The Accommodation of the Current Law

In discussing the law in this area, terminology can be confusing. In this analysis, terms are adopted which relate to receivables arising from supply contracts, since this is the context in which anti-assignment clauses are said to cause most problems.[12] The parties to the contract giving rise to the receivable are called the 'supplier' (the obligee) and the 'customer' (the obligor). The supplier is the client of the 'financier' to whom it assigns, or attempts to assign, the receivable.

A financier is concerned about three things in relation to the receivables it takes as collateral. The first is that it has a proprietary interest in the receivables and their proceeds which will survive the insolvency of the supplier. The second is that it has priority over any subsequent assignee, or other person claiming an interest in the receivables. The third is that, if the customer does not pay, the financier can ensure that the debt is enforced, and that it has a proprietary claim to the proceeds of that enforcement. The following paragraphs examine the extent to which these are achievable under English law.

(i) Statutory Assignment

[12] Another context, that of receivables under loan agreements, is considered in Section F.

Under English law there are two types of assignments. A statutory assignment under section 136 of the Law of Property Act 1925 takes place when certain conditions are satisfied.[13] The most important, for current purposes, is that there must be notification to the obligor (the customer). Once this has occurred, the customer will, and indeed must, pay the financier rather than the supplier.[14] If the customer fails to pay, the financier is able to sue the customer direct. In effect, the supplier drops out of the picture. A statutory assignment will also give the financier a proprietary interest in the receivable in the event of the insolvency of the supplier, or of a competing interest.[15] There is clear authority that a receivable which contains an anti-assignment clause cannot be the subject of a statutory assignment,[16] so that the customer can continue to pay the supplier, and cannot be sued (at law) by the financier.

(ii) Equitable Assignment: No Anti-assignment Clause

The other type of assignment is an equitable assignment. An assignment will be equitable when one of the conditions for a statutory assignment is not fulfilled; for example, a valid equitable assignment can take place without notification of the customer. A financier who takes an equitable assignment has a proprietary interest in the receivable which survives the insolvency of the supplier, and will also have priority over a competing interest, subject to the rules on priority. Until the customer is notified, if it pays it will, of course, pay the supplier, and will obtain a good discharge by so doing. The supplier, though, will hold those proceeds

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[13] See Section B.

[14] If the customer pays the supplier, it will have to pay the financier as well and try to recover the payment made to the supplier.

[15] The priority rules, which depend on those set out in the nineteenth-century case of *Dearle v Hall* (1828) 38 ER 475, are somewhat complex.

[16] *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd* [1994] 1 AC 85, 106–09. Of course, the true effect of a clause will always depend on its exact wording, and the case of *Linden Gardens*, though laying down certain principles, was considering a particular form of words.

on trust for the financier.[17] Moreover, valid set-offs can continue to arise between the supplier and the customer until the customer receives notification of the assignment;[18] after this, only set-offs arising from the contract itself or closely connected claims can arise.[19] If the customer does not pay, the financier cannot (at least in theory) sue the customer for non-payment without joining the supplier to the action, although this rule is less restrictive than it sounds. It is easy to join a party to an action (no consent is needed if they are joined as a defendant) and the court will not require joinder if there is no good reason.[20] Also, if the financier wishes to enforce, it will give notice of the assignment to the customer, which will not only require the customer to pay it rather than the supplier,[21] but will also, in most cases, convert the equitable assignment into a statutory assignment,[22] thus enabling the financier to sue the customer direct. Of course, where the financing is on a non-notification basis, such as invoice discounting,[23] the financier will normally expect the supplier to enforce against the non-paying customer, and, if the financing is with recourse, will have contractual rights

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[17] This trust is often expressly declared, but would arise in any event: *GE Crane Sales Pty Ltd v Commissioner of Taxation* (1971) 126 CLR 177, 213–14; *Barclays Bank Ltd v Willowbrock International Ltd* [1987] 1 FTLR 386.

[18] *Roxburghe v Cox* (1881) 17 Ch D 520..

[19] *Government of Newfoundland v Newfoundland Rly Co* (1888) LR 13 App Cas 199 ; *Business Computers Ltd v Anglo-African Leasing Ltd* [1977] 1 WLR 578, 585.

[20] *William Brandt's Sons & Co v Dunlop Rubber Co Ltd* [1905] 2 AC 454; *Sim Swee Joo Shipping Sdn Bhd v Shirlstar Container Transport Ltd* (unreported) 17 February 1994; *Raiffeisen Zentralbank Österreich AG v Five Star General Trading LLC* [2001] EWCA Civ 68 at [60]. Good reasons would include the possibility that the supplier might contest the assignment, or that the assignment is only of part of the debt, so that, unless the supplier is before the court, the customer might face more than one action.

[21] *Jones v Farrell* (1857) 1 De G & J 208; *Brice v Bannister* (1878) 3 QBD 569; *William Brandt's Sons & Co v Dunlop Rubber Co Ltd* [1905] 2 AC 454.

[22] This would not be the case if the conditions for a statutory assignment were not fulfilled, for example if the assignment was for part of a debt.

[23] See Section D(i).

against the supplier so that the risk of non-payment is on the supplier.[24] It is only where the supplier either refuses to sue or is insolvent that the financier will be concerned to have the right to sue the customer itself. Even then, the financier might not need to enforce directly, if there is an efficient means of enforcing against the customer through the insolvency process of the supplier.[25]

(iii) Purported Equitable Assignment: Anti-assignment Clause Present

If the receivable contains an anti-assignment clause, some, but not all, of the above analysis changes. The customer, who is discharged by paying the supplier before notification of the assignment, is also similarly discharged by paying the supplier after notification: it is entitled to ignore the notification. Once the debt is paid, though, the supplier will hold the proceeds on trust for the financier despite the anti-assignment clause: there is little *direct* authority on this point in English law, but there are a number of dicta supporting this view,[26] and much academic support.[27] In fact, it is extremely common for invoice discounting agreements to include an express provision that the proceeds are held on trust for the financier, and an anti-

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[24] See H Beale, M Bridge, L Gullifer and E Lomnicka, *The Law of Security and Title-Based Financing*, 2nd edn (Oxford, Oxford University Press, 2012) para 7.127.

[25] See Section D.

[26] *Re Turcan* (1888) 40 Ch D 5, 10–11, supported by Lord Browne-Wilkinson in *Linden Gardens Trust Ltd v Lenesta Sludge Disposal Ltd* [1994] 1 AC 85, 106 and Waller LJ and Rix LJ in *Barbados Trust Co Ltd v Bank of Zambia* [2007] EWCA Civ 148 at [28], [77]. See also *Devefi Pty Ltd V Mateffy Perl Nagy Pty Ltd* (1993) 113 ALR 225, 236 and *Don King Productions Inc v Warren* [2000] Ch 291, 312, 321–22, 332.

[27] B Allcock, 'Restrictions on the Assignment of Contractual Rights' [1983] *Cambridge Law Journal* 328, 335–36; G Tolhurst, 'Prohibitions on Assignment and Declaration of Trust' [2007] *Lloyd's Maritime and Commercial Law Quarterly* 278; G McMeel, 'The Modern Law of Assignment: Public Policy and Contractual Restrictions on Transferability' [2004] *Lloyd's Maritime and Commercial Law Quarterly* 483, 507–08; M Smith, *The Law of Assignment* (Oxford, Oxford University Press, 2007) 347. P Zonneveld, 'The Effectiveness of Contractual Restrictions on the Assignment of Contractual Debts' (2007) 22 Journal of International *Business and Financial Law* 313; C Tham, 'Notice of Assignment and Discharge by Performance' [2010] *Lloyd's Maritime and Commercial Law Quarterly* 38, 77; L Gullifer (ed), *Goode on Legal Problems of Credit and Security*, 5th edn (London, Sweet & Maxwell, 2013) para 3-39.

assignment clause will not prevent this being effective.[28] It is thought that even if the clause purported to prohibit such a declaration, this would be ineffective to prevent such a trust arising, since the customer has no interest in preventing the alienation of the proceeds and such a clause would be against public policy.[29] However, this point has never been litigated, so the position is not entirely clear.

If the customer does not pay, it is clear that the financier cannot sue it directly, as there can be no statutory assignment. Provided, however, that the agreement between the supplier and the financier can be said to give rise to a trust of the unpaid receivable (either expressly or impliedly),[30] it is likely that the financier can sue the customer, joining the supplier as defendant to the action, under a procedure known as the *Vandepitte* procedure. A beneficiary under a trust of a right can bring an action to force the trustee to bring an action to enforce that right for its benefit; the *Vandepitte* procedure merely short-circuits this process by enabling the beneficiary to instigate an action which brings all parties before the court.[31] In a case dealing with the purported assignment of a syndicated loan containing a restriction on assignment, a majority of the Court of Appeal decided that the *Vandepitte* procedure was

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[28] *Don King Productions Inc v Warren* [2000] Ch 291, 321; M Smith and N Leslie, *The Law of Assignment* (Oxford, Oxford University Press, 2013) paras 25.33–25.36.

[29] R Goode, 'Inalienable Rights?' (1979) 42 *Modern Law Review* 553; *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd* [1994] 1 AC 85, per Lord Browne-Wilkinson at 108. The supplier would be in breach of contract by declaring the trust, but it is hard to see what the damages would be.

[30] Whether this is the case depends on the interpretation both of the anti-assignment clause and the purported assignment. Two recent cases show that this is fact specific, and therefore subject to considerable uncertainty: *Co-operative Group Limited v Birse Developments Limited* [2014] EWHC 530 (TCC); *Stopjoin Projects Ltd v Balfour Beatty Engineering Services (HY) Ltd* [2014] EWHC 589 (TCC).

[31] It is named after the case of *Vandepitte v Preferred Accident Insurance Corp of New York* [1933] AC 70 in which it was first used.

available to the 'assignee',[32] but doubt as to its appropriateness in this context has been expressed by other judges.[33]

Further, if there is an effective trust of the receivable, the financier will have a proprietary interest which survives the supplier's insolvency, and against competing interests in the receivable. What is not entirely clear, however, is whether it is possible for a carefully drafted anti-assignment clause to prevent a trust of the receivable from arising. The judges in the *Barbados Trust* case were divided on this issue,[34] and although a strong case can be made for an analysis whereby the trust is invalid to the extent that it affects the customer, but arises validly between the financier and the supplier,[35] there is still considerable uncertainty.[36]

From the point of view of the customer, the anti-assignment clause protects its position by enabling it at all times to get a good discharge by paying the supplier: it will never be required to pay anyone else. Even if it is sued by the financier under the *Vandepitte* procedure,[37] the order will be that the customer must pay the supplier (the trustee), who will then hold the proceeds on trust for the financier. Further, a notice of assignment received by

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[32] *Barbados Trust Co Ltd v Bank of Zambia* [2007] EWCA Civ 148.

[33] *Don King Productions Inc v Warren* [2000] Ch 291, 321 per Lightman J and *Barbados Trust Co Ltd v Bank of Zambia* [2007] EWCA Civ 148 at [139] per Hooper LJ.

[34] *Barbados Trust Co Ltd v Bank of Zambia* [2007] EWCA Civ 148 at [44]–[47], [88], [129]–[139].

[35] Gullifer (ed) (n 27) para 3-42. See also Bridge (n 10).

[36] A contrary view, namely that the clause renders the receivable inalienable, so that a valid trust cannot be declared of it, is expressed in A McKnight, 'Contractual Restrictions on a Creditor's Right to Alienate Debts' [2003] *Journal of International Banking Law and Regulation* 43; G McMeel, 'The Modern Law of Assignment: Public Policy and Contractual Restrictions on Transferability' [2004] *Lloyd's Maritime and Commercial Law Quarterly* 483; P Turner, 'Charges of Unassignable Rights' (2004) 20 *Journal of Contract Law* 97; GJ Tolhurst and JW Carter, 'Prohibitions on Assignment: A Choice to be Made' (2014) 73 *Cambridge Law Journal* 405.

[37] This would only occur if, despite the clause, a valid trust of the receivable existed.

the customer is probably ineffective to prevent set-offs arising between the supplier and the customer.[38]

(iv) The Current Level of Protection for Financier and Customer Under Current English Law

The legal position, therefore, is that, on the whole, the interests of the financier and the customer can both have a certain degree of protection if an anti-assignment clause is used. This is subject to several caveats. First, the law is complex, and, in some areas, quite uncertain. There are few cases precisely on the relevant points, and even those that there are have not arisen in the context of receivables financing.[39] Second, the legal position will depend on the precise wording of the anti-assignment clause, and of the purported assignment or declaration of trust.[40] Third, even if in theory a financier is protected by the rule that the proceeds are held on trust, this will not help if the supplier has not kept the proceeds in an identifiable state so that they can be traced on its insolvency. A financier might be better off with a proprietary right to a debt owed by a solvent customer, than to proceeds which may or may not be held by an insolvent supplier.

It should be pointed out that the fact that there is a reasonable degree of protection in the current law does not necessarily rule out statutory intervention. For example, UCC former

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[38] If, despite the clause, there is a valid declaration of trust, this will break the mutuality required for set-off. If the clause renders a trust invalid to the extent that it affects the customer, then the notification of the trust could be said to be ineffective for all purposes, including preventing set-offs, see J Marshall, 'Declaring a Trust over Rights to an "Unassignable" Contract' (1999) 12 *Insolvency Intelligence* 1; A Tomson and A Rose, 'No Assignment Clauses and Bank Insolvency' [2014] *Corporate Rescue and Insolvency* 228. The position is not, however, completely certain.

[39] The one exception is *Stopjoin Projects Ltd v Balfour Beatty Engineering Services (HY) Ltd* [2014] EWHC (TCC) 589, which did concern receivables financing.

[40] *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd* [1994] 1 AC 85; *Don King Productions Inc v Warren* [2000] Ch 291; *Barbados Trust Co Ltd v Bank of Zambia* [2007] EWCA Civ 148; *Co-operative Group Limited v Birse Developments Limited* [2014] EWHC 530 (TCC); *Stopjoin Projects Ltd v Balfour Beatty Engineering Services (HY) Ltd* [2014] EWHC 589 (TCC).

Article 9-318(4) (which contained an override of anti-assignment clauses)[41] was included in the original UCC to reflect the existing US law rather than to change it.[42] This was, however, in the context of a codification of commercial law, and the introduction of a whole new system for secured financing. To make a case for free-standing legislation there has to be a policy imperative.

D. Industry Workarounds

(i) Financing Structures

Until recently, there were two types of receivables financing: factoring, which is on a notification basis, and invoice discounting, which is non-notification.[43] Factoring tends to be used for smaller suppliers, where a financier has concerns about the ability of the supplier to run its ledger properly and to operate a trust account, and also where the financier has concerns about the supplier's financial position.[44] Since it involves a statutory assignment, factoring gives the financier much more control over the collection of the debts. Factoring is more expensive for the supplier than invoice discounting, and a supplier can pay even more for extra services, such as the taking on by the financier of the credit risk of the customer.[45]

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[41] This provision is the forerunner of revised Art 9-406(d), which is currently in force.

[42] This is made clear by the official comment to the old Article 9, which says: 'It can be regarded as a revolutionary departure only by those who still cherish the hope that we may yet return to the view entertained some two hundred years ago by the Court of the King's Bench'. Even this, however, is an overstatement. There were contrary cases which were overruled by the legislation, such as *Alhusen v Caristo Construction Corp* 303 NY 446, 103 NE 2d 831 (1952).

[43] Much of the information in this section comes from the 2011 study, updated to take into account recent developments.

[44] Sometimes a financier will shift a client from an invoice-discounting basis to a factoring basis if the client gets into financial difficulties.

[45] Most receivables financing is on a recourse basis, whereby the supplier either guarantees payment of the receivables or agrees to repurchase unpaid receivables.

In invoice discounting, the collection of the receivables is carried out by the supplier, who holds the proceeds in a trust account for the financier.

Recently, two variations on these structures have become more popular, although the details vary in each case. One is discounting of individual invoices over an online platform: this takes place on a non-notification basis, with the platform merely acting as an intermediary. Another is supply chain financing, whereby a customer arranges with a financier that the latter purchase receivables owed by the customer to its suppliers at the point when the receivables arise, once the invoice has been confirmed by the customer. This has the advantage that there are less likely to be disputes about the invoice, and also that the financing can be based on the credit rating of the customer rather than the (smaller) supplier.[46] Having said that, this kind of financing is usually only offered to established suppliers whose invoices reach a certain, reasonably high, level and is also only offered by large customers.[47] There is also a concern that supply chain financing encourages large customers to extend the credit period they require, forcing small businesses to pay for a longer period of financing, albeit at a lower rate.[48]

(ii) Checking for Anti-assignment Clauses

Although some of the workarounds discussed below are adopted regardless of whether particular receivables arise from contracts containing an anti-assignment clause, English financiers very frequently check for the presence of anti-assignment clauses (and for other

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[46] The UK government launched a scheme in 2012 to encourage businesses and government agencies to offer supply chain financing, see www.gov.uk/government/news/prime-minister-announces-supply-chain-finance-scheme.

[47] 2011 study.

[48] See www.telegraph.co.uk/finance/yourbusiness/9634184/Payment-concerns-over-supply-chain-finance-move.html; http://realbusiness.co.uk/article/15791-the-supply-chain-finance-scheme-hit-or-miss; www.selectfactoring.co.uk/supply-chain-finance-scheme.

problematic clauses) in the invoices they finance.[49] Thus, one of the major arguments for a statutory override made in other jurisdictions (that it is not feasible for a receivables financier to discover about anti-assignment clauses,[50] so the whole cost of financing rises as a result) is not really made out in England and Wales. However, checking contracts is burdensome and takes time, particularly if it is necessary to consult lawyers about the effect of a particular clause.[51] The need to do so clearly increases costs, although it is probably the case that some checking would still take place even if there were to be a statutory override of anti-assignment clauses. It is also the case that most supply contracts are on a customer's standard terms, and financiers get to know the terms of large customers and whether they contain an anti-assignment clause, so checking involves merely looking at who the customers are rather than reading individual contracts.

(iii) Workarounds Used by Financiers: Non-notification Financing

If the financing is on a non-notification basis, the presence of an anti-assignment clause does not create problems for the financier on a day-to-day basis, since the customer does not know of the assignment, and continues to pay the supplier.[52] Of course, the supplier would be in breach of contract: this could be of concern, for example, if it enabled the customer to terminate the supply agreement.[53] The financier might worry about two situations: if the

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[49] Those interviewed for the 2011 study all said that they checked, while the picture was more mixed in relation to the 2014 study, although most said that they checked, at least in many cases.

[50] Australian Personal Property Securities Act 2009; Duggan and Brown (n 8) 42.

[51] 2011 study.

[52] In the 2011 study we were told that anti-assignment clauses created great problems for online auctions. However, the 2014 study revealed that since then this part of the industry has developed workarounds similar to those in regular invoice discounting, and so what is said in relation to that applies also to online auctions.

[53] Although such a breach is unlikely to be repudiatory, it could fall within a clause entitling the customer to terminate for 'any material breach' (which is quite common) or could trigger a cross-default clause. The absence of a general duty of good faith in English law could mean that a customer could rely on such a termination

supplier becomes insolvent, and if the customer does not pay and the supplier refuses to enforce.[54]

In relation to the first situation, financiers almost universally protect themselves by taking a security interest over all the assets of the supplier.[55] This has the effect, under English law, of enabling the financier to appoint an administrator of the supplier were it to become insolvent.[56] The financier is then in a good position to direct the administrator to collect in the receivables, and to pass the proceeds to it. There seems to be little concern among financiers about the collecting in of debts if an administrator is appointed (even if he is not appointed by that particular financier), although the costs are sometimes a problem if the supplier is a very small business.[57] Financiers also see an 'all-assets' security interest as having an additional benefit, namely that it will cover receivables which are not assigned to the financier because of an anti-assignment clause: sometimes they will specify that such 'non-vesting debts' fall within a fixed charge, while much of the all-assets security interest will be a floating charge. This ignores the fact that, depending on the wording of the clause, an anti-assignment clause may prevent the creation of a valid security interest to the same extent that it prevents a valid assignment.[58]

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clause even if its real motivation for termination was something entirely different. In theory, a breach could entitle a customer to obtain an injunction to prevent further breaches (although this is unlikely) or to sue for damages. However, it is hard, usually, to see what loss is suffered by the customer.

[54] The 2014 study indicated that the latter concern is at least as important, and, for invoice discounters, more important than the former, although the sample for this particular question was small.

[55] 2011 study and 2014 study.

[56] Paragraph 14 of sch B1 to the Insolvency Act 1986 provides that a qualifying floating charge holder can appoint an administrator out of court.

[57] Discussion at seminar for receivables financiers hosted by the Secured Transactions Law Reform Project on 8 May 2014, and 2014 study.

[58] Although a charge is not, in theory, an assignment, many charges are drafted as equitable mortgages, which are. A fixed charge has been treated as an assignment in a number of cases, *Biggerstaff v Rowatt's Wharf Ltd* [1896] 2 Ch 93; *NW Robbie & Co v Witney Warehouse Co* [1963] 1 WLR 1324, CA; *Foamcrete (UK) Ltd v*

Another mode of protection often coupled with the all-assets security interest is for financiers to take a personal guarantee from the directors of the supplier company.[59] To be effective this of course depends on the creditworthiness of the directors, and also might entail costs in enforcing the claims under the guarantees, to which there could be arguable defences.

Yet another possibility is for the financier to take a power of attorney enabling it to sue the customer in the name of the supplier.[60] This protection tends to be more useful in the second situation: when the supplier is solvent but refuses to sue. For the power of attorney to be irrevocable on the insolvency of the supplier, the financier would need to have some sort of proprietary right in the receivables or would need to be owed the receivables directly.[61] Where there is an anti-assignment clause, the latter is clearly not the case, and it is unclear whether a right under a trust is a sufficient proprietary interest to render the power irrevocable. The legal position is uncertain and untested.[62]

(iv) Workarounds Used by Financiers: Notification Financing

An anti-assignment clause causes much greater problems for financiers who operate on a notification basis. Here, there is a likelihood that the customer will refuse to pay the financier when notified, and will, instead, pay the supplier. The financier is then at risk of the proceeds being dissipated by the supplier, leaving the financier at the credit risk of the supplier. As a result, such financiers often refuse to finance receivables arising from contracts containing

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Thrust Engineering Ltd [2000] EWCA Civ 351, [2002] BCC 221. See also *Re Turner Corporation Ltd (In Liq)* (1995) 17 ACSR 761 where the Federal Court of Australia took the view that a clause prohibiting assignment also prohibited a charge.

[59] 2011 study and 2014 study.

[60] 2014 study.

[61] Powers of Attorney Act 1971 s 4.

[62] See discussion in M Bridge, L Gullifer, G McMeel and S Worthington, *The Law of Personal Property* (London, Sweet & Maxwell, 2013) para 29-043.

such clauses, or demand that the customer agrees to a waiver.[63] The evidence from the 2014 study is that financiers only sometimes pursue a waiver. There was considerable agreement[64] that the time and effort involved in obtaining a waiver was substantial or significant, and that by no means all customers were willing to agree to a waiver. Some customers would only agree to a waiver on terms which were disadvantageous to the supplier: this depended on the bargaining power between them and also on whether the financing was being sought at the beginning of the supplier/customer relationship.

(v) Supply Chain Financing

In one sense, the increasing availability of supply chain financing is a workaround. It is customer driven: the customer waives the anti-assignment clause to enable supply chain financing with its nominated financier, but relies on it to prevent the supplier obtaining financing elsewhere. This means that the supplier is locked into the supply chain financing deal, which could be seen as anti-competitive. The discount rate for such financing is usually reasonably low, since it is based on the credit rating of the (large) customer, but the period for which financing is required may be increased.[65] However, supply chain financing does achieve protection for the customer; only invoices approved by the customer are financed, which reduces disputes, and the customer does not have to deal with a financier with whom it has no relationship.

(vi) Effect of Workarounds

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[63] 2011 study. It should be pointed out that invoice discounters also sometimes refuse to finance receivables if they contain an anti-assignment clause, or will only finance them on a factoring basis, or demand a waiver. This is particularly true if, for some reason, a security interest over the supplier's assets is not taken.

[64] 12 out of the 18 respondents.

[65] See Section D(i).

It can be seen that the industry has developed a number of workarounds which mean that, with the exception of factoring where the financier cannot or does not try to obtain a waiver, receivables containing anti-assignment clauses are usually financed. However, the workarounds are costly in terms of time and effort, and also create more uncertainty, which can lead to costly disputes. In fact, one concern of the industry is that the existence of an enforceable anti-assignment clause may give a customer traction in disputes which it would not otherwise have, or will enable the customer to negotiate benefits for itself which would otherwise not exist. Although it is hard to prove, it seems likely that the existence of enforceable anti-assignment clauses increases the cost of financing.[66]

E. Inequality of Bargaining Power

(i) Reasons for the Inclusion of Anti-assignment Clauses

At this point it is necessary to consider the reasons why a customer might want to include an anti-assignment clause in a supply contract. The reasons usually given in the literature are that the customer wishes to avoid paying the wrong party, that it wishes to make sure that set-offs can continue to arise between it and the supplier, and that it wishes to continue to deal with the supplier rather than the financier, who is an unknown quantity.[67] The information

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[66] In the 2014 study, 11 out of 18 answered 'always' or 'sometimes' to the question: *Do you consider that (a) receivables are purchased at a greater discount to face value, or (b) the advance rate applied to the purchase of receivables will be reduced, as a result of the possibility that the contract governing the receivable may contain a valid prohibition on assignment, than would apply if such prohibitions on assignment were not binding as against an assignee?* However, only a small minority answered 'yes' to the question *Do you consider that the cost of finance is increased as a result of the inclusion of a prohibition on assignment within funded ledgers?* This discrepancy may be explained by the latter question being interpreted as relating only to where receivables with anti-assignment clauses were actually included in the funded ledger, which is seldom the case in factoring arrangements.

[67] See eg O Akseli, 'Contractual Prohibitions on Assignment of Receivables: An English and UN Perspective' [2009] *Journal of Business Law* 650, 656; L Gullifer and J Payne, *Corporate Finance Law: Principles and*

gathered from the two surveys (which came from all three constituencies: customers, suppliers and financiers) shows that the motivations are more mixed. There appeared to be little concern about paying the wrong party per se,[68] but there did appear to be genuine concern about incorrect invoicing and the sorting out of disputes.[69] It was thought that financiers would be more concerned that the invoice was paid, and would wish disputes to be sorted out afterwards between the customer and the supplier. The problem of incorrect invoicing was being tackled both by self-invoicing and by electronic invoice platforms.[70] However, the desire to retain the relationship with the supplier in order to sort out disputes is ongoing.[71] Opinions, not surprisingly, varied as to how helpful the financiers were in sorting out disputes and how aggressively they sought payment.

Perhaps also surprisingly, the issue of set-off did not seem to be of great importance.[72] This may reflect the fact that transaction set-off, that is, set-off of cross-claims arising out of the same contract or closely related to the claim, is not affected by assignment of the receivable. The desire to lock the supplier into a supply chain finance agreement was mentioned by one respondent to the 2014 study, and one respondent to the 2011 study mentioned one customer who wanted total confidentiality, so did not want its identity revealed to a financier. However, there seemed to be considerable consensus that in many cases customers did not really include anti-assignment clauses to prevent receivables financing at all, but to prevent 'assignment' (or subcontracting) of suppliers' obligations

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Policy (Oxford: Hart Publishing, 2011) 378–79; R Goode, 'Contractual Prohibitions against Assignment' [2009] *Lloyd's Maritime and Commercial Law Quarterly* 300, 302.

[68] This was mentioned by the financiers in the 2011 study but by no one else.

[69] 2011 study, especially evidence from customers.

[70] Such as www.tungsten-network.com/uk/en/expertise/e-invoicing/.

[71] It was mentioned by a number of respondents to the 2014 study.

[72] This was the view of the customers in the 2011 study, though one supplier thought that it was critical.

under the contract. Of course, under English law an obligation cannot be assigned, and so such a clause would be unnecessary, but it might be included out of ignorance or in order to make the subcontracting of obligations a repudiatory breach which would entitle the customer to terminate the relationship. In any event, many financiers felt that the clauses, in the form where they precluded receivables financing, were included without a great deal of thought: out of 'habit' or 'fear of the unknown', or out of an over-abundance of caution by lawyers who drafted the boilerplate contract.[73]

(ii) Balance of Bargaining Power

It is certainly the case that anti-assignment clauses are generally found in standard-form contracts used by large companies for their small and medium-sized suppliers.[74] The suppliers cannot negotiate the terms of the contracts and, as previously discussed, may find it difficult to obtain a waiver. Where the balance of bargaining power is reversed, so that the supplier is a large company and the customer is a small company or a consumer, the latter are not able to bargain for the protection of an anti-assignment clause. Control of anti-assignment clauses therefore raises a wider question of protection of small businesses against potentially unfair terms. Under English law, unreasonable exclusion and limitation clauses included in standard-form contracts are unenforceable against businesses (of all sizes),[75] and penalty clauses are, in some circumstances, unenforceable,[76] but otherwise any control of unfair

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[73] 2014 study.

[74] All the respondents to the 2014 study selected either large companies or government agencies (or both) as likely to include anti-assignment clauses in their contracts, although four also selected 'small companies'.

[75] Under ss 3, 6(3) and 7(3) of the Unfair Contract Terms Act 1977.

[76] G Treitel, The Law of Contract (E Peel, ed. , 14th edn 2015, London, Sweet & Maxwell) paras 20-129–20-145.

terms relates to consumer contracts. The Law Commission suggested in 2005[77] that some control should be extended to contracts with micro businesses,[78] but this suggestion has not been implemented. Some of the suppliers who responded to the 2011 study suggested that there was a problem with unfair terms in supply contracts[79] which was wider than just with anti-assignment clauses, and that either legislation, or maybe wider codes of practice,[80] were needed.

If it is right that inequality of bargaining power enables large customers to impose potentially unfair terms on small suppliers, then statutory control of anti-assignment clauses could have the effect that, deprived of this protection, the customers just imposed more swingeing terms in other areas.[81] This is a reason for reform to be approached with care, but not a clinching reason against statutory reform.

F. The Role of Anti-assignment Clauses in Financial Transactions

In many financial transactions, there are specific reasons for the inclusion of anti-assignment clauses which are important for the proper functioning of the market. In some cases, the clause does not ban assignment, but permits it to certain entities and requires consent for assignment to others. Thus, for example, in syndicated loan agreements, it is very common for a clause to permit assignment to certain financial institutions, but to require consent for

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[77] Law Commission Report 292, *Unfair Terms in Contracts* (2005).

[78] Businesses with nine or fewer employees.

[79] One example is a term making large sums payable on termination of the contract by the supplier.

[80] For example, the Groceries Supply Code of Practice, see www.gov.uk/government/publications/groceries-supply-code-of-practice.

[81] Such as a term that an invoice for goods or services is not payable until the invoice has been approved by the customer. This possibility was discussed with the respondents to the 2011 study, but is, of course, speculation: there can be no hard evidence.

assignment to others. This stems from a concern that were the loan to be assigned to, for example, a hedge fund specialising in distressed debt, it would be enforced in a much more aggressive way than it would be by a bank,[82] and also from a concern that a loan might be sold to one of the competitors of the borrower.[83] In derivatives contracts, which depend on close-out netting to protect against credit risk and for enforcement, it is critical that mutuality of parties is maintained, and so restrictions on assignment are very important.

The existence of these good reasons for anti-assignment (or restrictions on assignment) clauses to be enforceable means that any statutory override of anti-assignment clauses should be limited in scope to the context in which such clauses cause most problems, namely receivables financing. This, of course, raises definitional issues: for example, how do you exclude contracts for financial products without also excluding contracts for the provision of services relating to finance (such as computing services and financial advice)? The difficulties that such definitional issues pose, and the concern about the effects on the financial industry for getting the limitation of scope wrong, have led to considerable opposition to the statutory control of anti-assignment clauses from City lawyers and bankers.

G. Should There be a Statutory Override?

As indicated, the debate in England and Wales has largely moved from a clash of policies to a discussion based on pragmatism and cost-benefit analysis. In most situations, the presence of anti-assignment clauses does not prevent suppliers financing their receivables. This is because the law has developed in such a way that generally a financier will have an equitable interest in, at least, the proceeds of the receivables and probably in the receivables

[82] The market has therefore developed ways of transferring the risk and benefit of the loan without actually assigning it, such as loan participation and, more commonly now, credit default swaps.

[83] Law Commission, *Company Security Interests*, Law Com No 296 (2005) 5.33.

themselves. Further, the industry has developed a number of workarounds, which means that the receivables will be collected for the ultimate benefit of the financier both where the customer does not pay and when the supplier is insolvent. None of this is surprising. In the absence of any statutory control of anti-assignment clauses it is to be expected that both the law and the industry will accommodate the interests of all parties, to the extent that they can.

This, however, is not the end of the story. If the current position imposes costs on the industry, and thus on financing, which are not outweighed by the benefit of such clauses to the customers, then this would be a good reason for legislation. A further reason could be if certain suppliers were unable to obtain financing. Moreover, if it were felt that legislation could do no or little harm, but would have the beneficial effect of clarifying the existing law and making the balance of protection between all parties clear, this could also justify legislative change. All three of these arguments pertain in England and Wales today.

It is reasonably clear from both surveys[84] that some small suppliers, whom financiers will not finance on the basis of invoice discounting because of concerns about their ability to collect in the receivables and hold them on trust for the financier, are unable to have certain invoices financed because they contain anti-assignment clauses. The only way round this problem is for the customer to waive the clause, and this is not possible on some occasions, either because the costs of doing so outweigh the benefits to both the supplier and the financier, or because the supplier has so little bargaining power compared with the customer. The UK government is very concerned about the funding of small businesses at the moment: they are seen critical to economic recovery.[85] This, then, is a good reason for a statutory override of anti-assignment clauses.

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[84] The 2011 study and the 2014 study. It should be borne in mind that both surveys were fairly small scale.

[85] www.gov.uk/government/news/small-business-big-support-confirmed-by-prime-minister.

It is also clear that the presence of such clauses leads to costs for the financing industry. There is the cost of discovering such clauses, although it should not be overemphasised.[86] Waivers can be costly, as is the development and execution of the workarounds discussed above. Moreover, the existence of the workarounds themselves increases *ex ante* uncertainty, both in terms of the law[87] and also in that it increases the possibility of disputes. Finally, the law itself is complex and uncertain. A financier cannot be sure that it has a valid interest in a receivable containing an anti-assignment clause. It is clearer that it has an equitable interest in the proceeds, but this is not any good if the proceeds are not traceable.

Are these costs outweighed by the benefits of the clauses? It is clear that such clauses are of value in the context of financial contracts. However, some of the reasons why customers seem to include them in their contracts are of little merit[88] and the results from the (small-scale) surveys suggest that some do not seem of concern in the real world.[89] The concern about preserving a relationship with the supplier in the event of dispute or incorrect invoices is a real one, but the latter point can be overcome with modern invoicing techniques, and the former argument is undermined by the fact that customers are prepared to permit assignment to a financier of their choice under a supply chain finance scheme. The argument that a financier might be more aggressive in enforcing invoices than a supplier is also flawed, since the risk of a third party influencing enforcement is an ever present one: the supplier could be taken over by a more aggressive management. The customer's concern to remain in

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[86] This is because the financiers are familiar with the standard terms of the big customers, and also because they would read the contracts anyway for other adverse clauses.

[87] For example, whether a power of attorney will be enforceable on insolvency of the supplier, or whether an anti-assignment clause renders a charge void.

[88] The prevention of subcontracting does not require an anti-assignment clause, and the 'habit' or 'fear of the unknown' reasons seem unmeritorious.

[89] There seems to be little concern about set-off, or about the danger of paying the wrong party.

a relationship with the supplier may have more to do with the fact that the supplier is a small business compared with it, the customer, and therefore the customer is likely to have more of an upper hand in negotiations than it would have with a financier. The use of an anti-assignment clause to lock a supplier into supply chain financing also seems unmeritorious. If the supply chain financing was sufficiently attractive to the supplier, it would choose it anyway in preference to other sources of financing.

This brings us to the argument that a statutory override would do little harm, and could do some good in clarifying the law. One possibility of harm is that the override is not sufficiently limited, and causes problems in the financial markets. This is a serious risk, but could be overcome by careful drafting, even if this were at the expense of not including some borderline cases within the override.[90] Another possibility is that an override leads to harsher terms being imposed by large customers on small suppliers in other areas. This again would be serious, but could be controlled by a code of practice.[91] It therefore seems that the benefit in clarifying the law would outweigh any possible detriment.

H. Conclusion

This chapter has sought to elucidate the arguments both for and against a statutory override of anti-assignment clauses in English law. It is suggested that the arguments are not ones of principle, or even policy, but are more pragmatic. Since such clauses have not ever been the subject of statutory intervention, the common law has developed in such a way as to give all parties limited protection, and the industry has worked around the law to enable receivables

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[90] The power included in the Small Business, Enterprise and Employment Act 2015 s 1 excludes financial services contracts.

[91] See, for example, the UK Groceries Supply Code of Practice (4 August 2009) available at www.gov.uk/government/publications/groceries-supply-code-of-practice/groceries-supply-code-of-practice.

financing to take place. However, on the basis of two recent surveys, the pragmatic arguments are assessed, and, on balance, it appears that a statutory override would be beneficial.