

# Non-assignment clauses as obstacles to true sale securitisations

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### ABSTRACT

The new European rules on securitisation entered into force in 2019 with a view to revitalising the securitisation market. By introducing public law rules, the regulation intends to avoid the re-creation of the risks that played a role in the 2008–2009 financial crisis. The regulation, however, does not contain private law rules. Consequently, the substantive rules pertaining to securitisation will remain to be formed by the national laws of the Member States of the European Union. This paper argues that the ways in which non-assignment clauses are regulated in Member States will have a significant impact on the availability of securitisation.

### KEYWORDS

assignment, non-assignment clause, securitisation, transferability

## 1. INTRODUCTION

The new harmonised European securitisation rules, which apply as of 1 January 2019 were adopted to serve as ‘an important building block of the Capital Markets Union. They will help provide additional funding sources for companies, strengthen banks’ ability to support the

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economy and spread risks across market participants, while avoiding the excesses that led to the financial crisis.<sup>1</sup> Based on the calculation of the European Commission, '[i]f EU securitisations could be revived – safely – to pre-crisis average issuance levels, banks would be able to provide an additional amount of credit to the private sector of more than EUR 100 billion.'<sup>2</sup> The goal of the legislator is, therefore, to '[r]evitalise simple, transparent and standardised European securitisations to free up capacity on banks' balance sheets and provide access to investment opportunities for long term investors.'<sup>3</sup>

It is often argued that '[t]he securitization of subprime mortgages into mortgage-backed securities (MBS) and collateralized debt obligations (CDOs) was a major contributing factor in the subprime mortgage crisis.'<sup>4</sup> As e.g. the U.S. Financial Crisis Inquiry Commission Report concluded, 'major financial institutions facilitated the growth in subprime mortgage-lending companies with [...] securitization.'<sup>5</sup> An analysis of the European Parliamentary Research Service found that '[s]ecuritisation amplified the crisis by contributing to lengthening the intermediation chain, by creating conditions for incentives and interests between participants in the securitisation chain to be misaligned, by increasing the reliance on mathematical models and on external risk assessments and, finally, by increasing both individual and systemic bank risks.'<sup>6</sup>

The role of securitisation in the financial crisis, and how the EU legislator intends to revive the European securitisation market without re-creating the risks that led to the above-referred problems in 2008 are not within the scope of this paper. This paper assumes that by introducing well balanced public law rules, the new EU regulations on securitisation<sup>7</sup> will avoid the above-mentioned structural problems. This paper will, instead, focus on a question that falls outside the sphere of public law, namely the effect of non-assignment clauses, i.e. clauses included in the contract between the assignor (originator) and its debtor that exclude or limit the creditor's right to transfer the receivables arising from the contract.

Depending on the consequence of non-assignment clauses, securitisation could become impracticable if the underlying contracts contain prohibitions on assignment. '[N]on-assignment clauses set two primary values at odds with each other, namely freedom of contract and the free alienation of items of property.'<sup>8</sup> It is, therefore, crucial for the functioning of a securitisation market that a fine balance is drawn between the creditor's interests relating to the free transferability of the receivables it has against the debtor and the debtor's interest in protecting its power to decide with whom it wishes to be in a contractual relationship. The ultimate question, which the

<sup>1</sup>Link 1.

<sup>2</sup>Action plan 4.

<sup>3</sup>Action plan 6.

<sup>4</sup>Link 2.

<sup>5</sup>Final Report 101.

<sup>6</sup>Delivorias (2015) 14.

<sup>7</sup>Regulation (EU) 2017/2401 of the European Parliament and of the Council of 12 December 2017 amending Regulation (EU) No 575/2013 on prudential requirements for credit institutions and investment firms and Regulation (EU) 2017/2402 of the European Parliament and of the Council of 12 December 2017 laying down a general framework for securitisation and creating a specific framework for simple, transparent and standardised securitisation, and amending Directives 2009/65/EC, 2009/138/EC and 2011/61/EU and Regulations (EC) No 1060/2009 and (EU) No 648/2012.

<sup>8</sup>Bridge (2016) 47.



national legislator needs to answer is whether non-assignment clauses render the transfer of the receivables impossible (this will be referred to as third-party effect) and if such transfer is possible even in case of non-assignment clauses, what effect the breach of such clause has.

The focal point of the paper is, therefore, on the balance between the functioning of securitisation and the protection of the justified expectations of the debtors.

The next Section of this paper provides a brief introduction to securitisation and explains why the transferability of receivables is only relevant in the case of true sale securitisations. It does not provide a detailed overview of securitisation, rather, its purpose is to show how true sale securitisations are affected by non-assignment clauses and to explain why synthetic securitisations may work even if the underlying contracts contain non-assignment clauses. Given the beneficial treatment of true sale securitisation in EU law, this paper focuses on true sale securitisations.

Section 3 explains how various legal systems accepted the right of creditors to transfer their receivables to third parties without the involvement of the debtor. The section starts with Roman law and shows through the examples of German and English law that, surprisingly, the evolution of both civil law jurisdictions and English law followed very similar logic. Although we take the free transferability of receivables for granted, that was not the case until the 19th century. These legal systems originally refused to accept the free transferability of receivables and only provided procedural solutions enabling enforcement by the assignee. It happened only in the last two centuries that legal systems accepted that the creditor may be substituted in a legal relationship, without the need of the debtor's participation. This paper does not analyse the differences between the various methods of how receivables may be transferred in various European countries. It does not address, either, the question of whether the transfer is structured according to the consensual or the traditional approach, as it is not relevant for the analysis of non-assignment clauses. To avoid confusion regarding terminology arising from the differences among countries, when possible, this paper uses the most neutral terms. E.g. it refers to the 'transfer' of receivables to avoid distinguishing the *causa* and the transfer.<sup>9</sup> Furthermore, this paper does not deal with the question of whether, in the legal systems analysed below, receivables qualify as items of property.<sup>10</sup> Finally, also the intriguing question of whether it is possible to limit the free transferability of receivables by way of contract is beyond the scope of our discussion.<sup>11</sup>

Section 4 shows how non-assignment clauses were handled by the German, the Austrian, the Hungarian and the English legal system prior to legal reforms introduced towards the beginning of this century. Although these were slightly different regarding their methods of regulation, they generally accepted that non-assignment clauses have third party effects, and therefore an

<sup>9</sup>See e.g. Schütze (2005). It is controversial whether an equitable assignment qualifies as transfer. (See e.g. Tolhurst arguing it does (Tolhurst (2006) 3), and Edelman-Elliott arguing that 'when equitable assignment is involved, an alternative formulation to the transfer conception is needed'; Edelman-Elliott (2015) 229.

<sup>10</sup>See e.g. Bridge (2016).

<sup>11</sup>To hint at the relevance of this question, we refer to two English cases. Whereas Darling J seemed to have accepted that the free transferability of receivables cannot be restricted by contract, arguing that non-assignment clauses 'could no more operate to invalidate the assignment than it could to interfere with the laws of gravitation' (Tom Shaw & Co. v Moss Emires Ltd (1890) 25 T.L.R. 190.), a century later, Lord Browne-Wilkinson stated in Linden Gardens Trust Ltd Respondent v Lenesta Sludge Disposals Ltd and Others Appellants ([1994] 1 AC 85, 107.) that 'the restraints doctrine was limited to land because it is a finite resource. He thought there was no public policy reason overriding a prohibition on the alienation of tangible property and no public need for a market in choses in action.' Tolhurst (2006) 252.



assignment in breach of a non-assignment clause was ineffective and the receivables would not transfer to the assignee. This section will also provide some examples of the market effects of these rules based on primarily German research.

Section 5 shows, in chronological order, how problems arising from the original regulations were handled by the legislators of these jurisdictions. The analysis starts with the German reform in 1994, then turn to the solutions proposed by the otherwise unsuccessful [United Nations Convention](#) on the Assignment of Receivables in International Trade (hereinafter: ‘UNCITRAL Convention’) in 2001 and the UNIDROIT Principles on International Commercial Contracts (hereinafter: ‘UNIDROIT Principles’). After these international instruments, the Austrian, the Hungarian and the English approach will be introduced. As it will be seen, although the solutions differ in many details, the common point in these rules is that the third-party effect of non-assignment clauses is limited. In certain cases, these clauses are ineffective against third parties, and therefore the receivables will transfer to the assignee. However, these rules also accept that in case of a non-assignment clause, the transfer of receivables qualifies as a breach of contract, and therefore the consequences of the breach of contract apply.

Section 6 looks at the policy reasons behind the treatment of non-assignment clauses. Although various authors provide different grounds for why debtors may wish to include a non-assignment clause in their contracts, the main arguments are very similar: to avoid the risk of double payment, to maintain the right to set-off, to avoid a hard-nosed creditor and, in general, because of the importance of the identity of the creditor. It is argued that these reasons should not lead to the acceptance of third-party effects of non-assignment clauses. The benefits of the transferability of receivables outweigh the detriment of the debtor, and these risks should be more efficiently handled by way of regulation.

The final section summarises the findings of this paper, showing how the changes in the legal systems discussed have led to the result that non-assignment clauses no longer have third-party effects. This development is important for true sale securitisations. However, the existing differences in the regulation of non-assignment clauses among EU member states still make true sale securitisation difficult.

## 2. THE RELEVANCE OF NON-ASSIGNMENT CLAUSES FOR SECURITISATION

Wood provides a simple explanation to securitisation: ‘The basic classical transaction is as follows: an owner of receivables (the originator or seller) sells receivables to a third party (the purchaser or special purpose company or SPV). The purchaser borrows money to finance the purchase price and repays the borrowing out of the proceeds of the receivables bought by it.’<sup>12</sup> Two basic types of securitisation may be distinguished: true sale and synthetic securitisation. The most significant difference between these types is that while true sale securitisation involves the transfer of the underlying receivables, in case of synthetic securitisation only the credit risk of these assets is transferred by way of derivatives.<sup>13</sup>

<sup>12</sup>Wood (2008) 450.

<sup>13</sup>Wood (2008) 458–59.



It follows from the difference between the two basic types of securitisation that non-assignment clauses do not play a significant role in synthetic securitisations, as these do not involve the actual transfer of the receivables, and therefore the effects of prohibitions of, and restrictions on transferability are not relevant. Non-assignment clauses are, however, crucial for true sale securitisation. If the effect of the non-assignment clause is that the receivable will not transfer to the assignee or the transfer requires consent from the debtor, true sale securitisation will not be available, and markets, where non-assignment clauses are widely used, may find it more difficult to obtain financing. One of the important reasons for this is that debtors' consent is difficult to obtain, and the due diligence required for the analysis of the receivables may make the transaction too expensive.

One might argue that as synthetic securitisation does not involve the transfer of the receivables, non-assignment clauses have no effect on these transactions, and therefore securitisation is available even on markets and in jurisdictions where third-party effects of non-assignment clauses are recognised. From a purely legal point of view, this argument is valid. However, as EU law provides significant benefits from a capital requirement perspective to simple, transparent and standardised securitisations,<sup>14</sup> and since synthetic securitisation, by definition, cannot qualify as simple, transparent and standardised securitisation,<sup>15</sup> the regulation of non-assignment clauses is relevant for achieving an effective securitisation regime.

### 3. HISTORY OF ACCEPTING THE TRANSFERABILITY OF RECEIVABLES

Although transferability of receivables is taken today for granted, transferability of receivables in a true sense was only acknowledged around the 19th century. Roman law did not accept the transferability of receivables, as receivables were seen to be bound to the creditor and the debtor.<sup>16</sup> In order to mobilise contractual positions, several procedural solutions were developed in Roman law, such as *novatio*<sup>17</sup> and *delegatio*.<sup>18</sup> The most important solution developed by classical Roman law was the *mandatum agendi*, which made it possible for the assignor to empower the assignee to enforce the receivable. The *mandatum agendi* enabled the assignee to sue the debtor without the participation of the assignor, but the assignor remained the creditor, and therefore the debtor could pay to the assignor.<sup>19</sup> Furthermore, the assignor had the right to revoke the mandate. These shortcomings were remedied by various procedural solutions, most importantly the *utilis actio* and the *denuntiatio*, which has led to the result that the assignee was given the right to sue in his own name, the *mandatum* became irrevocable, and the debtor did not have the right to pay to the hands of the assignor once having received notification of the *mandatum agendi*.<sup>20</sup>

<sup>14</sup>Art 244 of Regulation (EU) No 575/2013.

<sup>15</sup>Art. 20 of Regulation (EU) 2017/2402.

<sup>16</sup>Kaser-Knütel (2005) 271, Kaser (1955) 545.

<sup>17</sup>Kaser-Knütel (2005) 271.

<sup>18</sup>Kaser-Knütel (2005) 269–70.

<sup>19</sup>Kaser (1955) 546.

<sup>20</sup>Majer (1954); Windscheid (1875) 370–72.



German law also struggled before accepting that receivables can be transferred similarly to tangibles. German jurists in the Middle Ages were of the view that it is impossible to transfer receivables, as a change in the parties would inevitably lead to the termination of the obligation. German law, therefore, under the influence of Roman law, provided procedural solutions to enable the transferability of receivables. These solutions followed the logic of *mandatum agendi*, *utilis actio* and *denuntiatio*.<sup>21</sup> Legal scholars in the 19th century, however, came to a different conclusion regarding the legal nature of receivables. Whereas earlier it was widely accepted that an obligation is a purely an *in personam* relationship, and therefore a change of the creditor is simply not possible, different interpretations emerged arguing that the substance of a receivable is determined by the obligation of the debtor and not the identity of the creditor. These scholars accepted that the ‘identity’ of the obligation remains the same even if the creditor is replaced. The change in the understanding of *obligatio* has led to the acceptance that receivables can be transferred in the same way as movables.<sup>22</sup> Following this theory, already the very first draft of the [German Civil Code \(BGB\)](#) accepted that receivables can be transferred without the participation of the debtor.<sup>23</sup>

English law also followed a similar logic. The common law, on the one hand, never allowed the transfer of receivables.<sup>24</sup> Similarly to the solutions of the Roman law, the common law accepted novation and the procedural solution of power of attorney as tools that led to similar results as an assignment.<sup>25</sup> Equity courts, on the other hand, accepted and enforced the transfer of receivables, irrespective of the fact whether the receivable was an equitable or a legal claim, although the solutions used in the two cases are different.<sup>26</sup> Parallel to the solution provided by the equity courts, statutes also enabled the assignment of several types of receivables. Section 25 of the 1873 Judicature Act (replaced later by section 136 of the 1925 Law of Property Act) enabled assignees to sue in their own name and not in the name of the assignors. Three requirements were set by the law for enforceability: the assignment needed to be absolute and not by way of charge, the assignment agreement needed to be in writing under the hand of the assignor, and express notice was required to the debtor in writing.<sup>27</sup> Based on this rule, there exist two regimes under English law for the transfer of receivables. If the conditions of the Law of Property Act are met, the assignee may sue in its own name. If these conditions are not met, the assignee may sue in accordance with the requirements of the equity courts, i.e. the assignor needs to join the assignee as a party to the litigation.

In the 21st century, it is easily taken for granted that receivables form part of the creditors’ estate just like other forms of tangible property, and therefore these can also be freely

<sup>21</sup>Luig (1966) 16, Buch (1912) 8.

<sup>22</sup>Luig (1966) 109.

<sup>23</sup>Entwurf eines Bürgerlichen Gesetzbuches. 2. Buch, Recht der Schuldverhältnisse, I. Allgemeiner Theil mit Begründung. 1882. 4. Titel, Begründung 4.

<sup>24</sup>Lampet’s case (1612) 10 Co. Rep. 46b; 77 ER 994.

<sup>25</sup>Smith-Leslie (2018) 216.

<sup>26</sup>Raw v Dawson [1749] 28 ER 487. The difference between the two solutions is not relevant for this analysis. See Smith-Leslie (2018) 225–58.

<sup>27</sup>Beale (2006) 19–007, Smith-Leslie (2018) 373.



transferred. However, from the brief overview above, it can be concluded that it took significant time to accept that receivables are transferable.

#### 4. TRADITIONAL APPROACH: THIRD-PARTY EFFECTS OF NON-ASSIGNMENT CLAUSES

As shown above, the most important concern of legal systems was that the identity of the parties was thought to be of utmost importance. It is not surprising, therefore, that even after the acceptance of the transferability of receivables, as it will be shown below, legal systems typically accepted that the debtor has the right to seek protection against the risks arising from the change of the creditor by inserting a non-assignment clause in the underlying contract from which the receivable arises. Not only did the various legal systems accept the validity of non-assignment clauses, but they also accepted that these have third-party effects, and therefore the receivables will not transfer from the assignor to the assignee if the underlying contract from which the receivables arose contained a non-assignment clause. This section argues that the German, Austrian, Hungarian and English legal systems followed a very similar logic in relation to the third-party effect of non-assignment clauses.

The first draft of the German BGB did not allow for non-assignment clauses rendering the transfer of receivables impossible. This position was based on the insight that the free transferability of receivables had a considerable economic value.<sup>28</sup> However, the position of the German legislator changed during the drafting of the BGB, in favour of the argument that the debtor may have legitimate reasons for prohibiting the transfer of the receivable.<sup>29</sup> Based on this argument, Section 399 of the BGB provides that a claim may not be assigned if the assignment is excluded by agreement with the obligor. The change was based on the assumption that that would only have a limited effect on markets where non-assignment clauses are reasonable (e.g. insurance contracts).<sup>30</sup> As it quickly turned out, this understanding was wrong, and non-assignment clauses became the standard rather than the exception on several markets. Based on the estimate of the Deutsche Faktoring-Verband prepared during the preparation of the law reform in Germany, in 1992 non-assignment clauses have led to the non-transferability of the receivables exceeding 160 billion DM<sup>31</sup> (approximately 80 billion EUR), and almost all large companies as debtors excluded the assignability of the receivables.<sup>32</sup> Legal scholars have argued that Section 399 of the BGB should be amended or repealed, but the courts rejected the attempts to provide purely *in personam* effects to such clauses.<sup>33</sup>

<sup>28</sup>Mugdan (1899) 67.

<sup>29</sup>Mugdan (1899) 573.

<sup>30</sup>Protokolle I 384. and Protokolle II. 772.

<sup>31</sup>Hoop (1992) 15.

<sup>32</sup>Gesetzesentwurf der Fraktion der SPD, Entwurf eines Gesetzes zur Änderung des Handelsgesetzbuches, Deutscher Bundestag, 12/7570. 17 May 1994.

<sup>33</sup>Drobnig (1976), Hattenhauer (2007).



The Austrians followed a similar track. Although originally the Austrian Supreme Court (Oberster Gerichtshof – OGH) did not accept that non-assignment clauses have third-party effect,<sup>34</sup> the court practice quickly changed and the Supreme Court ruled that the consequence of the breach of a non-assignment clause is not simply damages, but invalidity of the assignment.<sup>35</sup> After years of legal discussions, the court confirmed that in the case of non-assignment clauses the receivable cannot transfer to the assignee.<sup>36</sup>

Hungarian law may serve as the third example. The old Hungarian Civil Code adopted in 1959 did not provide any rule on non-assignment clauses. Section 328(2) provided that receivables are non-transferable if the obligation is linked to the obligor, or the transfer is prohibited by the law. However, courts and legal literature interpreted this clause as if it also prohibited transfers in the case of a non-assignment clause.<sup>37</sup> During the preparation of the New Civil Code adopted in 2014, some authors argued that it was not possible without a clear legal provision to accept that a purely contractual agreement has third-party effects.<sup>38</sup> That idea was also reflected in the court practice of the old Civil Code, as some courts concluded that non-assignment clauses only have *in personam* effects, i.e. the transfer of receivables in the case of a non-assignment clause may qualify as a breach, but the receivables will transfer to the assignee.<sup>39</sup>

Finally, English law deserves attention. Although non-assignment clauses have already been examined in the 19th century,<sup>40</sup> they became highly disputed only after a 1978 decision of the Queen's Bench. Croom-Johnson J held in *Helstan Securities* that 'if the parties to a contract, the subject-matter of which was a chose in action, agreed that the chose in action was not to be assigned, any purported assignment was invalid.'<sup>41</sup> The judgment contained a reference to the fact that the 'the assignee must make proper enquiries before he buys a debt,' as the findings will determine the price.<sup>42</sup> The arguments were disputed both by market participants and by legal literature, arguing, among others, that in transactions covering a large number of receivables it is not feasible to conduct due diligence in relation to each and every receivable.<sup>43</sup> However, the court practice did not change as a result of such criticism. Although the exact wording of the provision will have an impact on the effect of the clause (e.g. a mere undertaking not to assign will not render the transfer ineffective),<sup>44</sup> it is undisputed that '[i]n the case of a direct prohibition on assignment, the assignee will be affected, for the effect of the provision will be to render the assignment ineffective.'<sup>45</sup>

<sup>34</sup>OGH 3.11.1908.

<sup>35</sup>OGH 17.9.1912.

<sup>36</sup>OGH Jbl 1984, 311. Koziol-Welser (2001) 115, Apathy (1999) 526.

<sup>37</sup>Gellért (2007) 1179, 2002/1 Decision of the Arbitration Court.

<sup>38</sup>Gárdos (2003).

<sup>39</sup>BDT2011. 2419., LB–H–PJ–2011–15.

<sup>40</sup>Previous authorities were characterised as unclear by Bridge. Bridge (2016) 57.

<sup>41</sup>Smith-Leslie (2018) 580, *Helstan Securities Ltd v Hertfordshire County Council* [1978] 3 All ER 262.

<sup>42</sup>*Helstan Securities Ltd v Hertfordshire County Council* [1978] 3 All ER 262, 266.

<sup>43</sup>Goode (1979) 553.

<sup>44</sup>Tolhurst-Carter (2014) 434.

<sup>45</sup>Smith-Leslie (2018) 579.





Based on this rather summary overview, one can conclude that various European legal systems came to very similar results when they were originally faced with the problem of non-assignment clauses in the 20th century. The next section will show that the economic result of accepting that non-assignment clauses have third-party effects have led these legal systems around the end of the 20th century and the beginning of the 21st century to introduce rules on non-assignment clauses. These rules were similar in the sense that they limited the third-party effects of non-assignment clauses, but the solutions were different in their details.

## 5. NATIONAL AND INTERNATIONAL LAW REFORMS RELATING TO NON-ASSIGNMENT CLAUSES

The first major country that introduced reforms limiting the third-party effects of non-assignment clauses was the United States of America, where the Uniform Commercial Code (hereinafter: UCC) Article 9 provided already in 1952 that non-assignment clauses are ineffective.<sup>46</sup> Although this paper focuses on the solutions of European states, mentioning the US example is relevant as it influenced several law reforms in Europe.<sup>47</sup>

One of the first European countries to reform the civil law rules relating to non-assignment clauses was Germany. In order to remedy the effects of Section 399 BGB, a sectoral rule was implemented in 1994. Section 354a of the Commercial Code (HGB) provides that in the case of certain commercial transactions,<sup>48</sup> the assignment of monetary obligations is valid even if the underlying contract contains a non-assignment clause. However, the debtor may still pay to the hands of the assignor. The parties may not derogate from this provision. The rule intends to balance the interests of all parties. The first part of the provision takes into account the requirement of legal certainty, while the second part, which provides that the debtor may choose whether it wishes to pay to the hands of the new creditor, ensures that the rights and interests of the debtors are not infringed.<sup>49</sup> The first part of the provision was greeted on the market, but several authors raised concerns about the second part of the norm, especially as it provides the right to the debtor to pay to the hands of the original creditor even if it is aware of the assignment and no doubts have arisen about the fact that a legal succession has taken place.<sup>50</sup>

<sup>46</sup>UCC § 9–406(d) provides that ‘a term in an agreement between an account debtor and an assignor is ineffective to the extent that it prohibits, restricts, or requires the consent of the account debtor to the assignment or transfer of [...] a security interest in, the [...] payment intangible, or provides that the assignment or transfer [...] of the security interest may give rise to a default, breach, right of recoupment, claim, defense, termination, right of termination, or remedy under the [...] payment intangible.’

<sup>47</sup>See e.g. the references to UCC Article 9 in the Law Commission’s Company Security Interests report at [link 5](#)., but the UCC has also been influential on the Continent, see e.g. references to the UCC’s rule on non-assignment clauses in [Vékás \(2008\) 851](#).

<sup>48</sup>Either the transaction needs to qualify as commercial transaction (Handelsgeschäft) for both parties, or the debtor needs to be a public law entity (öffentliche Hand, öffentlich-rechtliches Sondervermögen).

<sup>49</sup>Bericht des Rechtsausschusses des Deutschen Bundestags, Beschlußempfehlung und Bericht, [link 3](#). There is legal authority arguing that based on Section 242 of the BGB, the debtor may not pay to the hands of the assignor if paying to the assignee does not impose a significant burden on the debtor. Cf. [Canaris \(2006\) 368](#).

<sup>50</sup>See e.g. [Nörr](#), who argued that ‘if we identify legal principles in the norm, especially its second sentence that should be nothing else than the irony of the unintended consequence of legislation.’ [Nörr, Scheying and Pöggeler \(1999\) 33](#).



Non-assignment clauses that do not fall under Section 354a HBG still prevent the transfer of the receivable to the assignee.

After the German reform, the UNCITRAL also proposed international solutions to the problems created by non-assignment clauses. The UNCITRAL Convention regulates the assignment of trade receivables. Financial transactions, such as transactions on a regulated exchange and financial contracts governed by netting agreements (except a receivable owed on the termination of all outstanding transactions) are excluded from the Convention.<sup>51</sup> Article 9 of the UNCITRAL Convention provides rules for non-assignment clauses, but the scope of this provision is even narrower than the scope of the Convention. This provision applies only to 'assignments of receivables: (a) Arising from an original contract that is a contract for the supply or lease of goods or services other than financial services, a construction contract or a contract for the sale or lease of real property; (b) Arising from an original contract for the sale, lease or licence of industrial or other intellectual property or of proprietary information; (c) Representing the payment obligation for a credit card transaction; or (d) Owed to the assignor upon net settlement of payments due pursuant to a netting agreement involving more than two parties.'<sup>52</sup> Article 9 does not, therefore, apply e.g. to receivables arising from financial services and receivables owed to the assignor upon net settlement of payments due pursuant to a netting agreement involving more than two parties.<sup>53</sup>

Article 9(1) provides that 'An assignment of a receivable is effective notwithstanding any agreement between the initial or any subsequent assignor and the debtor or any subsequent assignee limiting in any way the assignor's right to assign its receivables.' Article 9(2) regulates the *in personam* effects of an assignment in breach of a non-assignment clause: 'Nothing in this article affects any obligation or liability of the assignor for breach of such an agreement, but the other party to such agreement may not avoid the original contract or the assignment contract on the sole ground of that breach. A person who is not a party to such an agreement is not liable on the sole ground that it had knowledge of the agreement.' This solution, supported in the course of the negotiations primarily by the US, was heavily criticised during the preparation of the convention. Several delegations argued that this topic should be left out of the convention, or the parties should have the right to use reservation in relation to this provision.<sup>54</sup> However, the provision remained, and reservation was not made possible. This provision might be one of the reasons why the UNCITRAL Convention did not become a true success.<sup>55</sup> However, the analysis of the UNCITRAL Convention is important as its solutions influenced several national legislations and the same solution is recommended in the UNCITRAL Legislative Guide on Secured Transactions.<sup>56</sup>

<sup>51</sup>UNCITRAL Convention Article 4(2).

<sup>52</sup>UNCITRAL Convention Article 9(3).

<sup>53</sup>UNCITRAL Convention Article 9(3).

<sup>54</sup>UN Doc. A/55/17 Rn. 140, UN Doc. A/CN.9/420, Rn. 62–68, UN Doc. A/N.9/432. 113–126., UN Doc. A/CN.9/434 128–137., 585 UN Doc. A/CN.9/489. 101.

<sup>55</sup>The UNCITRAL Convention was adopted in 2001, but it is not yet in force as there are only three signatories (Luxembourg, Madagascar and the United States of America) and one party (Liberia) to it.

<sup>56</sup>UNCITRAL Legislative Guide on Secured Transactions, 92. and Recommendation 24 of the UNCITRAL Legislative Guide on Secured Transactions Terminology and recommendations at [link 4](#).



In parallel with the UNCITRAL Convention, the 2004 [UNIDROIT Principles](#) also introduced rules on assignment. Article 9.1.9(1) provides that the assignment of a right to the payment of a monetary sum is effective notwithstanding a non-assignment clause, but – in order to balance the interests of the parties<sup>57</sup> – the assignor may be liable to the debtor for breach of contract. The provision only applies to the assignment of a right to the payment of monetary sum, ‘the assignment of a right to other performance is ineffective if it is contrary to an agreement between the assignor and the obligor limiting or prohibiting the assignment. Nevertheless, the assignment is effective if the assignee, at the time of the assignment, neither knew nor ought to have known of the agreement. The assignor may then be liable to the obligor for breach of contract.’<sup>58</sup> The UNIDROIT Principles do not contain special rules based on the type of monetary receivable to be transferred (e.g. financial receivables).

The Austrian legislator followed a different track in 2007 when it introduced Section 1396a of the Austrian Civil Code (ABGB). The law provides that non-assignment clauses are only valid if they are individually negotiated and not grossly detrimental to the creditor. However, even if the non-assignment clause is valid that does not invalidate assignments in breach of such clauses. The debtor may apply the consequences of a breach of the non-assignment clause but set-off is not available to the debtor. The provision applies to non-assignment clauses in contracts for monetary receivables between businessmen (*Unternehmer*). Financial receivables are not excluded, but there is legal literature arguing that current account receivables cannot be assigned as it would make the purpose of the current account impossible.<sup>59</sup>

The [new Hungarian Civil Code](#) adopted in 2013 introduced significant changes in the field of non-assignment clauses. Influenced by the UNCITRAL Convention, Section 6:195 of the [new Hungarian Civil Code](#) provides that non-assignment clauses are valid, but not effective vis-à-vis third parties. If the underlying contract contains a non-assignment clause and the creditor transfers the receivable that qualifies as a breach of contract and usual remedies remain available to the debtor. However, the debtor may not claim liquidated damages or terminate the contract.<sup>60</sup> The Civil Code does not provide exceptions under the rule, however, legal literature argues in relation to current accounts that assignment of receivables that belong to current accounts do not affect the applicability of the rules of the current account, i.e. these current account rules have a quasi-third-party effect.<sup>61</sup>

Most recently, legislation was also passed in the UK to address the issue of non-assignment clauses. In 2005, the Law Commission in its report on Company Security Interests recommended ‘that in a contract between a company and a third party creating a receivable payable to the company, a term that purports to prohibit or restrict assignment of the account should be of no effect against a third-party assignee.’<sup>62</sup> As the recommendation was controversial, it was not implemented back in 2005. The recommendation, however, had a significant impact in recent years on the [Small Business, Enterprise and Employment Act 2015](#), which provided power to the

<sup>57</sup>See the official commentary to Article 9.1.9.

<sup>58</sup>UNIDROIT Principles Article 9.1.9(2).

<sup>59</sup>Bydliński-Vollmaier (2006) 218.

<sup>60</sup>Gárdos (2014) 1657.

<sup>61</sup>Gárdos and Gárdos (2014) 2014.

<sup>62</sup>The Law Commission Company Security Interests, 113, [link 5](#).



appropriate authority to invalidate certain restrictive terms of business contracts.<sup>63</sup> Based on the Act, the Business Contract Terms (Assignment of Receivables) Regulations 2018 were adopted. The general rule of the Regulations is that ‘a term in a contract has no effect to the extent that it prohibits or imposes a condition, or other restriction, on the assignment of a receivable arising under that contract or any other contract between the same parties.’<sup>64</sup> However, the Regulations provide exceptions to the general rule. First, the general rule ‘does not apply and accordingly a term mentioned in that regulation does have effect in relation to the assignment of a receivable if at the time of the assignment the supplier is a large enterprise or a special purpose vehicle.’<sup>65</sup> Second, the Regulations also exempt certain types of contracts under the general rule. The exemptions include contracts for financial services, contracts where one or more of the parties to the contract is acting for purposes which are outside a trade, business or profession, and certain derivatives contracts.<sup>66</sup> The responses to the legislative draft were mixed, only 60 percent of the participants of the Government consultation supported the introduction of the nullification of non-assignment clauses.<sup>67</sup> There were voices arguing that ‘the regulation is injurious to English law, [...] anti-business, [...] risks interfering with set-off and netting, [...] interferes with the freedom of English business contract law.’<sup>68</sup> As the regulation has just entered into force, there is no practice to comment on yet.

## 6. POLICY CONSIDERATIONS

As it was shown above, although less radically than the UCC Article 9, in the last 25 years several European states passed laws to limit the third-party effects of non-assignment clauses. The starting points of law reforms are similar throughout Europe: the various restrictions on the free transferability of receivables are detrimental to the economy as it limits the available forms of credit.<sup>69</sup> The question is, therefore, when should the law accept that the debtor has the right to make the receivable non-transferable.

If we approach this question from an economic perspective, one might ‘presume that it is optimal for contract rights and obligations to be assignable. Just as we like transferable property rights, transferability lets those with contract rights to sell them to those who value the rights more; and it lets those bound by contract obligations to have those obligations performed by someone who can do it at lower cost.’<sup>70</sup> When are non-assignment clauses rational from an economic point of view? The answer of the economic analysis of law is that ‘assuming costless contracting, they will assignment [sic!] if the benefit of assignability to the assigning party exceeds the cost to the non-assigning party of assignability — that is, if (premium x probability)

<sup>63</sup>Section 1 of the [Small Business, Enterprise and Employment Act 2015](#).

<sup>64</sup>Regulation 2. of the Regulations.

<sup>65</sup>Regulation 3. of the Regulations.

<sup>66</sup>Regulation 4. of the Regulations.

<sup>67</sup>Department for Business Innovation & Skills, 4, at [link 6](#).

<sup>68</sup>[Wood \(2018\)](#) 5–6.

<sup>69</sup>See e.g. [Wagner \(1994\)](#).

<sup>70</sup>[Kramer \(2004\)](#) 2.



exceeds (harm x probability). Simplifying, the contract will be made assignable if the premium to be paid to the assignor by the higher-valuing assignee exceeds the harm from assignment to the non-assigning party.<sup>71</sup>

Why do debtors try to limit the assignability of their creditors' receivables? Goode lists the following reasons for using non-assignment clauses: (i) to avoid 'overlooking a notice of assignment [and] be compelled to make a second payment', (ii) maintaining the possibility of set-off by preserving mutuality, (iii) to avoid replacing 'a relatively benign creditor with whom it enjoys a good working relationship [...] by a hard-nosed assignee', and (iv) because the identity of the counterparty is regarded as vital.<sup>72</sup> Taking into account the arguments above, when should a legal system accept that the debtor in a dominant position forces a non-assignment clause on its creditor?

ad (i) It is unquestionable that assignment is burdensome by definition, and leads to administrative inconvenience.<sup>73</sup> The debtor must keep track of the actual creditor, which is especially difficult in cases where the same receivable is transferred in parts or where the same receivable is transferred multiple times. This leads to the risk of mistaken payment.<sup>74</sup> This risk undeniably exists in case of assignments. Still, it would seem to be an excessive measure if we accept that the parties may limit the transferability of a receivable based on this inconvenience. This is especially so as the legislators can protect the debtor's interests by providing clear-cut substantive rules. These rules can make clear in different scenarios to whom the debtor shall pay.<sup>75</sup> Although these rules cannot completely eliminate the administrative inconveniences, they can mitigate a risk of mistaken payment.

ad (ii) The situation is different regarding the argument relating to maintaining the availability of set-off. Set-off, especially in case of financial receivables, is an important risk mitigation tool. This is one of the reasons, why e.g. the UNCITRAL Convention does not apply to assignments of receivables arising under or from financial contracts governed by netting agreements, except a receivable owed on the termination of all outstanding transactions. One way to protect set-off in case of financial transactions is to accept that non-assignment clauses have third-party effect in the sense that the receivable will not transfer to the assignee. However, it is proposed that an equivalent result may be reached, similarly to Hungarian law, by providing set-off rules that ensure the same outcome as if the receivable had not been assigned, i.e. set-off remain fully available also in relation to these receivables irrespective of the change of creditor.

ad (iii) The risk of a hard-nosed assignee is also a real concern. Whereas parties who are in long-term commercial relationship may be reluctant to start enforcement or liquidation taking into account the effect of such steps on the other relationships with the debtor, an assignee that has

<sup>71</sup>Kramer (2004) 17.

<sup>72</sup>Goode (2009) 300.

<sup>73</sup>MacMahon (2020a) 495.

<sup>74</sup>See e.g. Akseli (2009) 656.

<sup>75</sup>See e.g. Section II of the UNCITRAL Convention most importantly on notification (Article 16) and discharge (Article 17). Similar rules can be found in all of the solutions analysed above (see e.g. Article 6:198 of the new Hungarian Civil Code on payment instruction).



no other relationship with the debtor may only focus on the highest return within the shortest time.<sup>76</sup> The assignee will simply step into the shoes of the assignor, therefore from a legal point of view the assignee will not have better rights and the debtor will not be worse off due to the assignment. As the commentary to the Draft Common Frame of Reference formulates this: 'In a sense, every assignment of a right changes the debtor's position in some degree. The debtor has to perform in favour of a different person, and that person may have a more stringent attitude towards enforcement of rights than the original creditor. That by itself is not a sufficient consideration to prevent the assignment.'<sup>77</sup> However, MacMahon, in his recent papers on when contractual rights should be assignable,<sup>78</sup> convincingly shows that 'the identity of one's contractual counterparty is often crucial. Parties choose their business partners based on prior experience with that party, on that party's reputation for trustworthy and reasonable behavior, and on that other party's need to maintain a good reputation in the marketplace. Assignment may render the duty holder liable to suit by someone with whom she has no experience and who has no reputation for trustworthiness and reasonableness.'<sup>79</sup> He explains that 'promisors are often fully aware that a promisee might have a legally enforceable right that is not perfectly calibrated with considerations of fairness or efficiency. [...] When, as so often, it is not possible to use formal enforcement methods, contracting parties rely on social sanctions to avoid opportunistic exploitation of changes circumstances.'<sup>80</sup> These will not necessarily hold true in case of a hard-nosed assignee.

ad (iv) Finally, the argument regarding the importance of the identity of the counterparty needs to be considered. It is true that there are legal relationships where the identity of the counterparty is of crucial importance. This is the reason why several of the above-analysed laws draw a distinction between monetary and non-monetary obligations. Whereas in the case of non-monetary obligations the identity of the counterparty may often be relevant, in case of monetary obligations that is typically not the case. Setting aside the issues discussed above, it is typically irrelevant for the debtor to whom it should pay. This reason should, therefore, not lead to the acceptance of third-party effects of non-assignment clauses. There are, however, solutions, which may be necessary to protect debtors. First, as it is accepted by most jurisdictions, receivables of personal nature shall not be assignable.<sup>81</sup> Second, the debtor shall not suffer costs in relation to the assignment (e.g. by being obliged to pay to a foreign assignee).<sup>82</sup> Therefore, in case monetary receivables the importance of the identity of the counterparty should not lead to the acceptance of third-party effects of non-assignment clauses.

It seems to follow from the above analysis that although all of Goode's arguments refer to valid concerns, three out of the four reasons should not lead to the acceptance of third-party effects of non-assignment clauses. These are either general concerns, which should rather be

<sup>76</sup>See e.g. MacMahon (2020a) 489.

<sup>77</sup>von Bar-Clive (2009) 1039.

<sup>78</sup>MacMahon (2020a) and MacMahon (2020b).

<sup>79</sup>MacMahon (2020a) 490.

<sup>80</sup>MacMahon (2020a) 498.

<sup>81</sup>See e.g. § 399 of the BGB, Section 6:194(3) of the new Hungarian Civil Code and Section III. – 5:109 of the Draft Common Frame of Reference (DCFR).

<sup>82</sup>See. e.g. UNIDROIT Principles 9.1.8, new Hungarian Civil Code Article 6:200.



perceived as the ‘cost’ or ‘inconvenience’ of the transferability of receivables, or relate to risks that may be reduced by well-drafted assignment rules.

It is a question, however, whether the risk of a hard-nosed assignee is so significant that we should accept that the parties can make the receivables arising from their contract to be non-transferrable. MacMahon argues that ‘[i]n normal circumstances, the best evidence as to what serves the parties’ joint interests is their express agreement on the matter,’<sup>83</sup> ‘[i]f transferability serves social welfare, then we can expect parties to bargain for it or, at least, not to agree to a nonassignment clause.’<sup>84</sup>

Although this argument seems convincing, it is worth noting that when the German BGB was amended, the legislator found that almost all large companies successfully excluded the assignability of the claims against them.<sup>85</sup> As the German Factoring Association (Deutsche Faktoring-Verband) found almost 30 years ago, 160 bn Deutsche Mark worth of receivables were made non-transferable, primarily in the insurance, banking, manufacturing and wholesale markets.<sup>86</sup> Experience shows that the inequality of bargaining power leads to the non-assignability of receivables, which may justify legislative intervention.

If we accept that non-assignment clauses cannot prevent the transfer of receivables, two further questions need to be addressed, namely, whether restrictions on the transfer are valid, and if so, what should be the legal consequence of the breach of this provision. As Wood argues, ‘[p]eople don’t trust legal systems which nullify ordinary and routine clauses which are terms they have agreed to and which are legitimate.’<sup>87</sup> Freedom of contract is the fundamental principle of contract law. A provision, therefore, should only be null and void if required by an overriding interest (e.g. protection of the weaker party, public policy reasons). As no such interest exists in case of non-assignment clauses, the invalidity of these clauses is not necessary. It is important, however, to carefully regulate the legal consequences of the breach of non-assignment clauses. If the debtor can freely determine the sanctions, those may be so severe that they, in effect, make the receivable non-transferable. This was the reason why e.g. the UNCITRAL Convention provides that the debtor may not avoid the original contract or the assignment contract on the sole ground of such breach.<sup>88</sup> The Hungarian rule, influenced by the UNCITRAL Convention, excludes the right of avoidance and further the debtor’s right for liquidated damages for the breach of the non-assignment clause.<sup>89</sup>

The legislator may also consider a securitisation specific rule for non-assignment clauses. The securitisation law could provide, e.g., that non-assignment clauses relating to receivables become null and void upon securitisation. However, this solution would be mistaken for two reasons. First, the parties need to be able to determine the validity of a given clause at the time of the conclusion of the contract. Second, the issues of non-assignment clauses are not securitisation-specific issues.

<sup>83</sup>MacMahon (2020b) 294.

<sup>84</sup>MacMahon (2020a) 489.

<sup>85</sup>Gesetzesentwurf der Fraktion der SPD, Entwurf eines Gesetzes zur Änderung des Handelsgesetzbuches, Deutscher Bundestag, 12. Wahlperiode, Drucksache 12/7570.

<sup>86</sup>Wagner (1994) 35–39.

<sup>87</sup>Wood (2018).

<sup>88</sup>Article 9(2) of the UNCITRAL Convention.

<sup>89</sup>Article 6:195(2) of the New Hungarian Civil Code.





These arise in case of all transactions involving the transfer of receivables, whether the transaction entails the transfer of one receivable or the transfer of bulk receivables in a factoring transaction, and the pros and cons for accepting the third-party effects of non-assignment clauses are the same for all such transactions. It does not seem reasonable, therefore, to accept third-party effects as a general rule and provide a special solution for cases of securitisation.

## CONCLUSION

Although we take the transferability of receivables for granted, this is only a recent phenomenon in all of the laws analysed in this paper. These jurisdictions accept that receivables are no longer so tightly linked to the identity of the creditor that a legal succession of the creditor would be impossible, but it has still been accepted until recently that the parties may prohibit the transfer of receivables. Such prohibitions had third-party effects as it prevented the transfer of receivables to the assignee. In the last 25 years several countries amended their laws to limit the effect of non-assignment clauses. Although these rules are different, they typically provide that non-assignment clauses no longer have third-party effects and the assignment only leads to a breach of contract. This development undoubtedly limits the freedom of contract in favour of the free alienation of items of property.

This development is crucial for true sale securitisation. As true sale securitisation requires the transfer of the underlying receivables, securitisation becomes impossible if non-assignment clauses have third-party effects. Securitisation can be most efficiently used if non-assignment clauses do not have third-party effects, and, if the transfer qualifies as a breach of contract, such breach cannot lead to termination or liquidated damages. Although recent reforms may help securitisation, the existing differences in the 28 EU member states regarding non-assignment clauses still make true sale securitisation difficult.

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