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signed by Mr Jordi AYET PUIGARNAU, Director

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To: Mr Jeppe TRANHOLM-MIKKELSEN, Secretary-General of the Council of  
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THE COUNCIL AND THE EUROPEAN ECONOMIC AND SOCIAL  
COMMITTEE on the question of the effectiveness of an assignment or  
subrogation of a claim against third parties and the priority of the assigned  
or subrogated claim over the right of another person

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Delegations will find attached document COM(2016) 626 final.

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**REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE  
COUNCIL AND THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE**

**on the question of the effectiveness of an assignment or subrogation of a claim against  
third parties and the priority of the assigned or subrogated claim over the right of  
another person**

# **REPORT FROM THE COMMISSION TO THE EUROPEAN PARLIAMENT, THE COUNCIL AND THE EUROPEAN ECONOMIC AND SOCIAL COMMITTEE**

## **on the question of the effectiveness of an assignment or subrogation of a claim against third parties and the priority of the assigned or subrogated claim over the right of another person**

### **1. INTRODUCTION**

#### **1.1. Assignment of claims in the perspective of the Capital Markets Union**

The Capital Market Union Action Plan<sup>1</sup> concluded that despite significant progress in recent decades to develop a single market for capital, there are still many long-standing and deep-rooted obstacles that stand in the way of cross-border investments. One of the obstacles identified results from differences in the national treatment of third party effects of assignment of debt claims that complicates the use of these instruments as cross-border collateral particular when bank loans are mobilised as financial collateral in central bank credit operations<sup>2</sup> or in the context of securitisations, and makes it difficult for investors to price the risk of debt investments. To facilitate cross-border investment, the Capital Markets Union Action Plan foresees that 'the Commission will [...] propose uniform rules to determine with legal certainty which national law shall apply to third party effects of the assignment of claims' and that action will be taken by 2017<sup>3</sup>. This report is the first step in identifying the main problems related to the lack of a uniform rule on the law applicable to the third party effects of assignment and the order of priority of the assigned claim and the possible approaches that could be taken to address those problems.

#### **1.2. The concept of assignment of claims**

Assignment of claims is a legal mechanism which enables both simple transfers of claims from one person to another and complex financial operations used to finance the business activity of firms, such as financial collateral arrangements, factoring and securitisation. At its basis, it involves the transfer by a creditor ("assignor") of his claim against a debtor to another person ("assignee"). Examples of typical assignment transactions are set out below (point 2.1).

With the increasing interconnectivity of national markets, assignment often involves a cross-border element, which can lead to a conflict of applicable laws. Legal certainty as to which law applies to the different relationships involved is paramount for the smooth running of assignment operations. Increased legal certainty leads to increased availability of capital and credit across borders and to more affordable rates - particularly beneficial for small and medium enterprises (SMEs), and in the long run, to the facilitation of cross-border movement of goods, services and capital.

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<sup>1</sup> Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of the Regions 'Action Plan on Building a Capital Markets Union' ('CMU Action Plan'), COM(2015) 468 final, p. 23.

<sup>2</sup> See Report from the Commission to the Council and the European Parliament on the appropriateness of Article 3(1) of Directive 2002/47/EC on financial collateral arrangements ('FCD report'), COM(2016) 430 final.

<sup>3</sup> See Capital Markets Union Action Plan, Annex 1: List of actions and indicative timeline, p. 30.

### 1.3. Existing EU legislation

In the European Union, the objective of enhancing legal certainty in the area of assignment of claims has been addressed by harmonising rules on conflict of laws in Regulation (EC) No 593/2008 on the law applicable to contractual obligations (the Rome I Regulation)<sup>4</sup>. These rules provide that the *relationship* between assignor and assignee under a voluntary assignment or contractual subrogation of a claim against the debtor shall be governed by the law that applies to the contract of assignment.<sup>5</sup> The harmonised rules also aim at protecting the assigned debtor by ensuring that he does not owe the assignee more than he owed the creditor/assignor.<sup>6</sup> Consequently, the law governing the claim to which the assignment relates, which is the only law which the debtor can reasonably expect to apply, will also govern the relationship between the assignee and the debtor, the assignability of the claim, the conditions under which the assignment can be invoked against the debtor and the question whether the debtor's obligations have been discharged. However, there is an important element missing in the existing regulation, which concerns the question which law governs the *effectiveness* of an assignment *against third parties*<sup>7</sup>. This question is crucial to ensure legal certainty in cross-border assignment operations.

This Report fulfils the legal obligation<sup>8</sup> under Article 27(2) of the Rome I Regulation which requests the Commission to submit a report on the question of the effectiveness of an assignment or subrogation of a claim against third parties and the priority of the assigned or subrogated claim over a right of another person.

### 1.4. Securities and claims transactions

The Capital Markets Union Action Plan points out, besides the uncertainty in the area of assignment of claims, to the similar uncertainty existing in the context of cross-border securities transactions. Indeed, both securities and claims are frequently the subject of similar financial transactions, such as collateralisation.

Sector specific legislation containing conflict of laws rules has been adopted in the field of securities law with a view to reduce the systemic risk inherent in payment and securities settlement systems<sup>9</sup>, to limit the credit risk in financial transactions through the provision of cash, financial instruments and credit claims as collateral<sup>10</sup>, or to enforce proprietary rights in the event of the reorganisation and winding up of credit institutions<sup>11</sup>. These specific conflict rules apply in the EU Member States and point to the law of the State where the register, relevant account or centralised deposit system is located. These rules have, however, been implemented or are being applied differently in the Member States. This leads to legal uncertainty and additional costs which may create obstacles for the smooth running of financial operations in the internal market.

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<sup>4</sup> See Article 14 of Regulation (EC) No 593/2008 on the law applicable to contractual obligations (the Rome I Regulation).

<sup>5</sup> Article 14(1) of the Rome I Regulation.

<sup>6</sup> Article 14(2) of the Rome I Regulation.

<sup>7</sup> Although Recital (38) of the Rome I Regulation stipulates that the term "relationship" in Article 14(1) extends to the proprietary aspects of assignment as between assignor and assignee in legal orders where such aspects are treated separately from the aspects under the law of obligations, the negotiations in the run-up to the adoption of the Rome I Regulation were conclusive on the fact that no agreement could be reached on a common rule on third party effects of assignment.

<sup>8</sup> The adoption of this report was postponed in order to await the political opportunity to follow its publication by a legislative proposal, which is now undertaken in the Action Plan on a Capital Markets Union.

<sup>9</sup> Directive 98/26/EC on settlement finality in payment and securities settlement systems (SFD).

<sup>10</sup> Directive 2002/47/EC on financial collateral arrangements (FCD).

<sup>11</sup> Directive 2001/24/EC on the reorganization and winding up of credit institutions, OJ 2001 L 125.

Also in the area of securities a general approach to the issue of conflict of laws has so far not been established<sup>12</sup>. Neither has the substantive law on securities been harmonised so far at EU level, notwithstanding the recent development of EU legislation in the area of financial market infrastructure, including European Markets Infrastructure Regulation (EMIR)<sup>13</sup>, Central Securities Depositories Regulation (CSDR)<sup>14</sup> and MiFID II<sup>15</sup>/MiFIR<sup>16</sup> and notwithstanding ongoing work for several years<sup>17</sup>.

In the light of the similar objectives which may be pursued by claims and securities transactions, it may be useful to coordinate any work on the conflict rules regarding both types of transactions. This is even more so since the distinction between a "claim" and a "security" is not always clear in practice.

### **1.5. International instruments**

The conflict of laws problems in the context of claims and securities transactions has been the subject of work at the international level. A United Nations Convention on the assignment of receivables in international trade has been established in 2001. It has not entered into force so far. Its principles have been incorporated in the 2007 UNCITRAL legislative guide on secured transactions. A 2006 Hague Convention on the law applicable to certain rights in respect of securities held with an intermediary also has not entered into force so far.

### **1.6. External study and consultations**

A study<sup>18</sup> examining the question of the effectiveness of an assignment or subrogation of a claim against third parties and the priority of the assigned claim over the right of another person was carried out for the European Commission (hereinafter "the study"). The study based its findings on statistical, empirical and legal data from twelve European Union jurisdictions<sup>19</sup> representing a range of legal traditions, as well as six economically important non-Member States<sup>20</sup>.

## **2. IMPORTANCE OF ASSIGNMENT IN INTERNATIONAL TRADE AND ON CAPITAL MARKETS**

### **2.1. Examples of assignment transactions**

Historically assignment took place in relation to a single claim, which was transferred from the creditor to one or several subsequent assignees.

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<sup>12</sup> Commission withdrew a proposal for a Council Decision concerning the signing of the 2006 Hague Convention on the Law applicable to certain rights in respect of securities held with an intermediary.

<sup>13</sup> Regulation (EU) No 648/2012 on OTC derivatives, central counterparties and trade repositories.

<sup>14</sup> Regulation (EU) No 909/2014 on improving securities settlement in the European Union and on central securities depositories.

<sup>15</sup> Directive 2014/65/EU on markets in financial instruments.

<sup>16</sup> Regulation (EU) No 600/2014 on markets in financial instruments.

<sup>17</sup> Impact Assessment accompanying the Proposal for a Directive of the European Parliament and of the Council on legal certainty of securities holding and transactions, 23.09.2009

<sup>18</sup> The study was carried out by the British Institute of International and Comparative Law in 2011 and is available at: [http://ec.europa.eu/justice/civil/document/index\\_en.htm](http://ec.europa.eu/justice/civil/document/index_en.htm).

<sup>19</sup> These are: Belgium, Czech Republic, Finland, France, Germany, Italy, Luxembourg, the Netherlands, Poland, Spain, Sweden and England.

<sup>20</sup> These are: Australia, Canada, Japan, the Russian Federation, Switzerland and the United States.

### ***Example 1: Outright transfer of a single claim***

The creditor/assignor C assigns his claim<sup>21</sup> against the debtor to assignee A. A may notify the debtor of the assignment, for instance when this is required by the national law of C's place of habitual residence<sup>22</sup>. A then re-assigns the same claim to assignee B. B may decide not to notify the assignment, for instance because this is not required by the law of the underlying claim where such a notification or registration is not necessary to render the assignment effective. C subsequently becomes insolvent and his insolvency administrator tries to ascertain whether B is the valid owner of the claim..

In recent times, assignment transactions have evolved to include assignment of claims in bulk and assignment of both present and future claims. Such transactions have become widely used by businesses in order to obtain capital and credit to finance their business operations.

### ***Example 2: Factoring***

An SME supplier C wishes to assign the bulk of his current and future claims<sup>23</sup> against clients in several Member States to factor A, which in return for a discount against the purchase price is ready to agree to provide cash flow finance, collect the debts and accept the risk of bad debts. To propose an interesting discount to C, A would need to know that the assignment will be effective against third parties in the event of C's insolvency.

A may also be worried that while under the law of the assignment, which governs the proprietary effects between A and C, all claims are assignable, it may be that under the law governing some claims included in the assignment bulk assignments are prohibited<sup>24</sup>.

Legal certainty as to the law governing the effectiveness of the assignment against third parties and the priority of an assignment against other competing assignments has become crucially important in particular in credit transactions involving SMEs which are often unable to obtain finance across borders or are forced to accept unfavourable terms unless they can offer security, often in the form of claims against their debtors.

### ***Example 3: Assignment as security***

An SME C wants to utilise to the maximum extent possible the value of its claims against the buyers of its products to obtain secured credit from both assignees A and B, using the same assets as security.

<sup>21</sup> The claim may result from a contract or from tort, unjust enrichment, *negotiorum gestio*, *culpa in contrahendo* or other legal relationships.

<sup>22</sup> Many Member States do not require a notice or any type of registration for an assignment to be effective against third parties (for example Belgium, the Czech Republic, Germany, Poland, Spain and England), while other require notice to the debtor (e.g. France, Luxembourg) or the acceptance by the debtor in an authentic act (e.g. Italy).

<sup>23</sup> The assignment of future claims is subject to different regimes in the Member States: generally it is accepted that they can be assigned, but under Belgian, Finnish and German laws for example future claims need to be identified or identifiable to be assigned, while Swedish law provides that future claims are obligations clearly contemplated by the relevant security document.

<sup>24</sup> It may also happen that C assigns a claim in breach of a statutory or contractual prohibition to assign. Statutory prohibitions concern for example personal debts such as wages and pensions (e.g. Belgium, The Netherlands, Poland) or bulk assignments (Poland). In some Member States, non-assignability clauses are given full effect (e.g. The Netherlands) while in others exceptions are made for money claims (e.g. Germany). Assignment is subject to the debtor's consent in Czech Republic, Finland and Poland. The situation is not clear under Belgium law.

In order to extend credit to C, A and B would need to know the priority of their security rights in the same asset<sup>25</sup>.

C may also fraudulently assign the same claims to A and B without their knowledge. In the event of C's insolvency, the insolvency administrator would need to ascertain the order of priority between A and B.

A complex mechanism of obtaining cost-effective credit is securitisation. Securitisation is a financing technique by which homogeneous income-generating assets (often claims) – which on their own may be difficult to trade – are pooled and sold to a specially created third party, which uses them as collateral to issue securities and sell them in financial markets<sup>26</sup>.

#### ***Example 4: Securitisation***

A large retail chain C assigns its receivables arising from the use by customers of its in-house credit card to a special-purpose vehicle (A)<sup>27</sup>. A then issues debt securities to investors in the capital markets. These debt securities are secured by the income stream flowing from the credit card receivables that have been transferred to A. As payments are made under the receivables, A will use the proceeds it receives to make payments on the debt securities.

With increased cross-border investment, securities such as bonds are often assigned as collateral to secure credit from investors. The holding chain between investors and issuers is complex: securities can be held through multiple tiers of intermediaries, potentially located in different countries, as may also be the case with investors. This makes it difficult to assess who owns what, with possible serious consequences for financial stability.

### **3. PROBLEMS**

#### **3.1. Current divergence of conflict rules in the Member States**

The substantive rules applicable to assignment in the Member States differ greatly. For example, there are different notice requirements for the effectiveness of assignments<sup>28</sup>, different priority rules, different rules applying to assignment of future claims, as well as different limitations on the assignability of claims. In the absence of harmonisation of these substantive rules, private international law solutions are extremely important in resolving conflicts of laws.

However, in determining the law applicable to third-party aspects of assignment there are several different approaches in the States analysed in the study.

*The law of the contract between assignor and assignee* governs all proprietary aspects of assignment in The Netherlands. This solution favours party autonomy, but it bears the risk that creditors of the assignor can be defrauded. In order to correct such abuses, recourse may be made to the general

<sup>25</sup> In national laws, the rule is generally that priority is given to the first assignee (for example Belgium, Czech Republic, Finland, Germany, Italy, Poland, the Netherlands, England). In England and the Netherlands, the relevant time is the notification of the assignment to the debtor. In England, assignment of debts as security by way of a charge or mortgage needs to be registered with the Registrar of Companies.

<sup>26</sup> Understanding Securitisation, Background – benefits – risks, European Parliamentary Research Service (PE 569.017), January 2016, p. 1.

<sup>27</sup> This example is an adaptation of the illustration used in the UNCITRAL Legislative Guide on Secured Transactions, pp. 16-17.

<sup>28</sup> See *Example 1*. Differences in formal requirements in relation to credit claims are elaborated in the recent FCD report, COM(2016) 430 final.

principle *fraus omnia corrumpit* or to the public policy exception. As to the question of priority in the case of competing assignments, the law governing the second assignment decides upon the protection of good faith second acquirers. This approach has gained some support in other Member States, such as Germany. It is also found in Switzerland.

*The law of the assignor's habitual residence* determines the third-party aspects of assignment in Belgian law. Some Italian scholars support the introduction of the law of the assignor's habitual residence for bulk assignments and assignments of future claims. In Luxembourg, in the specific sector of securitisation, the law applicable to the third-party aspects of the assignment shall be the law of the country in which the assignor is established. Similarly, under U.S. law, the perfection of most assignments is governed by the law of the assignor's location.

*The law of the underlying claim assigned* is favoured in several Member States, such as Spain and Poland. In the absence of a statutory provision, case law and doctrine support this solution in the UK, Germany and Italy. This approach is also found in Australia, Canada, Japan and the Russian Federation.

Other solutions present in the Member States are the *lex rei sitae* (Czech Republic and Sweden) and *the law of the habitual residence of the debtor* (France). In other Member States, for example Finland, there is *no clear rule*.

### 3.2. Legal uncertainty

The absence of a uniform conflict of law rule creates several main areas of legal uncertainty.

The heterogeneity, ambiguity or absence of conflict of laws solutions in respect of third-party effects of assignment can lead to contradictory results. For instance, in *Example 3* above, A may think that his priority is determined by the law of the State of C's habitual residence, while B relies on the law of the assignment contract with A. Each believes that their assignment is effective and that it has priority over the rights of the other. Often, they will not be aware of each other's rights but will rely on checks for the absence of other assignees performed in accordance with the law they presume applicable, i.e. check on the basis of disclosure requirements which may protect potential assignees under the law of one Member State but not under the law of another Member State.

In respect of claims under future contracts, one may not easily determine at the time of assignment the law governing the claim assigned. In *Example 2*, A would not be able to determine in advance the laws of the underlying claims and, faced with the risk of having to comply with yet unknown rules, A may either refuse to finance C or charge a considerably higher premium than he would otherwise.

In addition to the lack of regulation, those aspects of assignment already regulated give rise to certain uncertainties, in particular insofar as financial instruments traded on financial markets are concerned. For instance, it is not clear what is the exact scope of Article 14 of Regulation 593/2008 (Rome I)<sup>29</sup>. In effect, whereas traditional 'securities' (e.g. shares or bonds) are commonly regarded as not covered by

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<sup>29</sup> See R. Plender, M. Wilderspin, *The European Private International Law of Obligations*, 3<sup>rd</sup> edition, Thomas Reuters 2009, paras 13-019 and 13-020.



this provision<sup>30</sup>, rights in securities which are traded [electronically] on some capital markets are believed to be rather included in this conflict-of-laws rule<sup>31</sup>.

Legal uncertainty in establishing the effects of assignment against third parties and the order of priority arises most urgently in the event of an insolvency of the assignor. Thus, even if Article 14 of the Rome I Regulation, clarifies the applicable law between the parties, in the event of an insolvency a third law will very often come into play in determining the effectiveness of assignments and their order of priority: the law applicable to the insolvency proceedings against the assignor.

Regulation 2015/848 on insolvency proceedings (recast) (the Insolvency Regulation (recast))<sup>32</sup> lays down the conflict rules applicable in insolvency proceedings. As a general rule, insolvency proceedings are opened in the State where the centre of main interest of the assignor is located at the time of the opening of the proceedings. By way of derogation from this rule, where the debtor has an establishment in another Member State, secondary proceedings can also be opened in that other Member State but only in respect of assets situated there<sup>33</sup>. The law of the State where insolvency proceedings are opened (*lex concursus*) determines, among others, the assets which form part of the insolvent estate, the rules governing the distribution of proceeds from the realisation of assets, the ranking of claims and the rules relating to the voidness, voidability or unenforceability of legal acts detrimental to the general body of creditors. The Regulation clarifies where assets such as registered shares in companies, book entry securities as well as cash held in accounts are considered to be situated for the purposes of determining the scope of secondary proceedings<sup>34</sup>. Furthermore, where insolvency proceedings are opened in another Member State than that where assets are located, third parties' rights *in rem* and reservation of title are protected<sup>35</sup>.

The law applicable to the effects of assignment on third parties may therefore, in the case of insolvency proceedings opened against the assignor, be determined by the Insolvency Regulation (recast). Insolvency is indeed a situation where ownership questions between competing right holders become particularly important. Consequently, future harmonised rules on third-party aspects of assignment will need to be carefully aligned with the existing *acquis* in the area of insolvency.

### 3.3. Practical problems and high legal costs

The empirical data collected by the study<sup>36</sup> shows that 47% of the stakeholders consulted encounter practical problems in securing the effectiveness of an assignment against third parties. Unlike

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<sup>30</sup> This is common view for 'shares' (see R. Plender, M. Wilderspin, *op. cit.*, para 13-020; H. van Houtte (ed.), *The Law of Cross-border Securities Transactions*, Sweet & Maxwell 1999, p. 7; *Dicey, Morris and Collins on the Conflict of Laws*, vol. 2, 15<sup>th</sup> ed., Thomson Reuters 2012, para 24-066; BIICL Study, p. 244 and 347) and 'bonds' (H. van Houtte (ed.), *op. cit.*, p. 31–32).

<sup>31</sup> This is the prevailing view for the German 'rights in securities', i.e. the 'Gutschrift in Wertpapierrechnung' according to M. Born, *Europäisches Kollisionsrecht des Effektengiros. Intermediatisierte Wertpapiere im Schnittpunkt von Internationalem Sachen-, Schuld- und Insolvenzrecht*, Mohr Siebeck 2014, p. 63. Also R. Plender, M. Wilderspin, *op. cit.*, p. 375 suggest that transfers of 'equitable interests' generally fall within the scope of Article 14 of the Rome I Regulation. However, *Dicey, Morris and Collins on the Conflict of Laws*, *op. cit.*, para 24-067 assume that 'interests in a trust' are outside Article 14.

<sup>32</sup> Regulation (EC) No 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast), OJ 2015 L141/19, repeals Council Regulation (EC) No 1346/2000 of 29 May 2000 on insolvency proceedings, OJ 2000 L 160/1.

<sup>33</sup> See Article 3(2) of the Insolvency Regulation (recast).

<sup>34</sup> See Article 2(9) of the Insolvency Regulation (recast).

<sup>35</sup> Article 8 and 10 respectively of the Insolvency Regulation (recast).

<sup>36</sup> The empirical analysis highlights the practical problems encountered in different market sectors in cross-border assignment and subrogation cases and is based on replies to a questionnaire which was

marketable securities which are generally recorded in electronic accounts, credit claims are evidenced only by a credit agreement. As a result, there is higher risk that the same credit claim might be posted as collateral to more than one collateral taker without the actual knowledge of the latter collateral takers that the credit claim was already pledged in favour of a different person. In addition, the lack of harmonised conflict of laws rules increases the number of substantive laws potentially applicable to the provision of credit claims as collateral, which might make it more difficult to fulfil the eligibility criteria of the Eurosystem<sup>37</sup>.

Furthermore, the average legal costs for cross-border transactions involving assignments, an important proportion of which stem from the need to carry out due diligence in respect of several legal systems, are in many cases very high and can amount to several hundreds of thousands of euros. For example, one factoring business reported legal costs ranging from €350,000 to €1 million per transaction.

## **4. POSSIBLE APPROACHES**

### **4.1. General considerations**

The study<sup>38</sup> shows that, as also set forth in the Capital Markets Union Action Plan, a harmonised conflict of law rule governing the third-party aspects of assignment is needed in order to ensure legal certainty and a balancing of the interests of all parties concerned in a cross-border assignment. Such a rule would also support cross-border trade, in particular by reducing legal costs and due diligence, and facilitating the availability of capital and credit at affordable rates for SMEs.

The study also shows that a single connecting factor may not be appropriate for all types of assignment operations; a combination of connecting factors which would accommodate the interests of various stakeholders may be more appropriate. However, since sector-specific rules carry the risk of inherent complexity and characterisation problems, their use should be limited as much as possible.

Among all possible connecting factors, the law of the contract of assignment, the law of the assignor's habitual residence and that of the law of the claim assigned have been supported by a majority of stakeholders as well as a significant number of Member States.

Some connected matters could also benefit from further clarification, such as the scope of Article 14 of the Rome I Regulation<sup>39</sup>.

In the light of this, three possible approaches have emerged<sup>40</sup>.

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answered by 36 stakeholders representing businesses, trade bodies and associations, financial markets institutions, law societies, legal practitioners, academics and other interested parties.

<sup>37</sup> Guideline (EU) 2015/510 of the European Central Bank of 19 December 2014 on the implementation of the Eurosystem monetary policy framework (ECB/2014/60) (the 'ECB General Documentation'). Article 97 of the ECB General Documentation requires no more than 2 governing laws applicable to (a) the counterparty; (b) the creditor; (c) the debtor; (d) the guarantor (if relevant); (e) the credit claim agreement; (f) the mobilisation agreement..

<sup>38</sup> 80% of the stakeholders participating in the study have expressed a need for a common rule to determine the law applicable to the third-party effects of assignment. As a solution, 44% of the respondents favour the law of the assignor's habitual residence, 30% favour the law of the underlying claim assigned and 11% opt for the law chosen by the assignor and assignee.

<sup>39</sup> On the question which law governs the recovery of the proceeds of a claim or their value, it could be clarified that this matter is governed by the law determined by Article 14 of the Rome I Regulation. Further clarification could also be brought to ensure that all issues which have a direct bearing upon the debtor are regulated by the law applicable to the claim assigned, including the question of whether the assignee has the right to bring a direct claim against the debtor or must join the assignor as a party to such legal proceedings.

## 4.2. The law of the contract between assignor and assignee

Currently, the proprietary aspects of assignment between the assignor and assignee are governed by the law of the contract of assignment<sup>41</sup>. This approach would subject *all* proprietary aspects of assignment – including the effectiveness of an assigned or subrogated claim against third-parties and the question of priority between the assignee and competing right holders - to the law chosen by the assignor and assignee for their contract of assignment. However, to prevent any possible prejudice to third parties, this choice should be limited, in what concerns the effects of the assignment<sup>42</sup>, to either the law of the country in which the assignor has his habitual residence or the law governing the assigned or subrogated claim.

In the absence of a choice of law, or if the law chosen does not correspond to the two solutions envisaged, all the proprietary aspects of assignment would be governed by the law of the country of the habitual residence of the assignor<sup>43</sup>. This solution would avoid the use of sector-specific rules and reduce the number of laws applicable to the same assignment constellation<sup>44</sup>.

The priority issues between competing assignees can be solved by analysing the effects of each transaction in sequence, according to its own applicable law. The analysis would follow the property law principle of "first in time, first in right and rank", which is qualified only by rules on good faith acquisition in the subsequent transactions.

The main advantages of this solution are that it ensures that all proprietary aspects of assignment are governed by the same law as well as flexibility for actors in different market sectors to choose a law which responds to their particular needs. At the same time, the debtor continues to be protected under existing rules. This solution could also accommodate cases of bulk assignments of current and future claims, since the law of the assignor's domicile could be applied either as a result of the choice of the parties or by default.

The main possible disadvantage of this solution is the risk of avoidance of publicity requirements in some Member States. However, this risk is diminished by the fact that the choice of law is limited to two laws, both closely connected to the assignment in question.

## 4.3. The law of the assignor's habitual residence

The third-party aspects of assignment could be determined by the law of the habitual residence of the assignor<sup>45</sup>. Certain financial claims may not be well served by this rule, namely claims under an existing contract concluded within the type of system coming in the scope of under Article 4(h) of the Rome I Regulation or within a multilateral system for the settlement of payments or other transactions between banks and financial institutions or a claim under a financial instrument. This drawback could be mitigated by supplementing the general rule with a specific rule on the third-party effects of

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<sup>40</sup> Three other solutions, the law of the debtor's location, the law of the place of assignment and the law of the forum have little support among stakeholders, create uncertainty, are unsuited for electronic means of transacting or encourage forum shopping (see study pp. 384-385).

<sup>41</sup> See Recital 38 of the Rome I Regulation.

<sup>42</sup> Another law could continue to govern the contractual aspects of the assignment.

<sup>43</sup> In the absence of choice, the applicable law is normally determined by reference to the characteristic performance of the contract which is that of the assignee, as provided for in Article 4 of the Rome I Regulation. This default solution would lead to the application of yet another law to a particular assignment, that of the habitual residence of the assignee.

<sup>44</sup> For this reason, proposal A departs in this respect from the study, which suggests a fall back rule based on the law applicable to the assigned claim, coupled with a sectoral rule for claims under future contracts.

<sup>45</sup> For the purposes of this provision, Article 19(2) and (3) of the Rome I Regulation may need to be disapplied.

assignment of certain financial claims, which would point to the law governing the assigned or subrogated claim at the relevant date.

Questions of priority would be resolved by reference to the date of the last assignment or other event giving rise to a competing right.

The main advantages of this proposal are that it provides a single connecting factor which promotes certainty among secured and unsecured creditors and, in cases of competing assignments, a suitable and predictable solution in determining who has the best title to the assigned debt. The law of the assignor's habitual residence is easy to determine and most likely to be the place in which the main insolvency proceedings with respect to the assignor will be opened. As a result, conflicts between secured transactions and insolvency laws would be easier to address. The proposal is also particularly suitable for bulk assignments and assignments of receivables under future contracts which are an important source of obtaining finance for SMEs. The proposal would furthermore be coherent with the UN Receivables Convention as well as the UNCITRAL Legislative Guide on Secured Transactions<sup>46</sup>, in respect of those types of assignments within the scope of those instruments<sup>47</sup>.

The disadvantages include increased transaction costs and complexity, since this proposal would lead potentially to two laws being applied to the proprietary aspects of assignment, the law of the contract of assignment as between the assignor and assignee, and the law of the habitual residence of the assignor for the third-party aspects. There is also potentially a conflict of connecting factors in cases of joint assignors located in different States and in cases of subsequent assignments, where the same claim is assigned several times by assignors located in different States

#### **4.4. The law applicable to the assigned claim**

Under this proposal, the same law governing the relationship between the assignee and the debtor would also govern the proprietary aspects of assignment in respect of third parties. This general rule would need to be accompanied by a specific rule pointing to the law of the country of the assignor's habitual residence in respect of assignment of claims under future contracts, where the law of the claim cannot be determined at the time of the assignment. This specific rule would also accommodate the factoring and discount invoicing industry, where bulk assignments may otherwise trigger the application of many different laws to the same portfolio of claims.

Questions of priority would be resolved by reference to the date of the last assignment or other event giving rise to a competing right.

The main advantages of this solution are the stability of the connecting factor which is unlikely to change over time and thus the reduced risk of conflicts between connecting factors in the event of competition between assignees or other right holders. In the event of a change in the law applicable to the assigned claim, third parties would not be adversely affected. The proposal leads to a reduction of the number of applicable laws to an assignment, leading to the avoidance of characterisation problems between "debtor" issues and "third party" issues and to the reduction of legal costs associated with assignment. The proposal is particularly suitable for certain financial claims.

The main disadvantages include the potential uncertainty in cases of insolvency of the assignor where the *lex concursus* does not coincide with the law applicable to the assignment. As with the previous

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<sup>46</sup> Adopted on 14 December 2007.

<sup>47</sup> Both the UN Convention and the UNCITRAL Guide exclude from their scope assignment of receivables arising from securities, independent guarantees, bank deposits, derivatives and foreign exchange transactions, and payment systems. The UN Convention further excludes letters of credit.

approach there is also a potential disconnect between the proprietary effects of assignment between the assignor and assignee and in respect of third parties. There is also uncertainty about the applicable law when there is no clear choice of law in the original contract or where the claim assigned is not contractual in nature. In such situations, the applicable law would need to be determined by reference to Article 4 of the Rome I Regulation or by Article 10 of the Rome II Regulation.

## **5. CONCLUSIONS**

Uniform conflict of law rules governing the effectiveness of assignments against third parties as well as questions of priority between competing assignees or between assignees and other right holders would enhance legal certainty and reduce inherent practical problems and legal costs relating to the current diversity of approaches in the Member States.

The Commission presents in this report three possible approaches. The first is based on the law of the contract between assignor and assignee. The second is based on the law of the assignor's habitual residence. The third is based on the law applicable to the assigned claim. All proposals are combined with either fall back or specific rules to take into account the various interests or situations at stake.

In the future, when developing a solution to ensure legal certainty in assignment of claims transactions, due regard should be given to any parallel or similar solution developed to ensure legal certainty in securities transactions. To this end, a study on the law applicable to securities as well as claims traded on financial markets will be completed by mid-2017<sup>48</sup>.

Following the adoption of this report, the Commission will launch, by the end of 2016, a broad public consultation on the issues identified in this report. Any legislative solution proposed to address the lack of legal certainty in this report will be accompanied by an impact assessment, including an adequate quantification of the problem.

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<sup>48</sup> Call for tender No JUST/2016/JCOO/PR/CIVI/0062.