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EUROPEAN HARMONISATION OF PRIVATE LAW

Prohibitions on assignment, a European civil code and business financing

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I. Introduction

Every legal system which has undergone a co-evolution with an economy based on a free market system provides for means of transferring contractual rights - that is, for our purposes, debts or receivables. Where A can claim money from B, he can transfer that right against B to C and thus sooner get hold of the money. A can then proceed to use this money for subsequent business activities, but now B has to satisfy C as his creditor, although he initially contracted with A. This might bring about certain disadvantages for B. On the other hand, C is content to act as factor or creditor, which would not be possible without a legal framework allowing for the transfer of debts. Business is stimulated and economic advantages may be realised if debts are transferable or if they may serve as security (mostly by means of a trust fund), just like other goods or chattels.¹

But referring exclusively to an analogy between debts and chattels has a major shortcoming: the analogy fails to take into account the debtor and his legitimate interests. Therefore, the alienation of debts and the restrictions on such a transfer cannot indiscriminately be subject to the rules governing the alienation of chattels. Statutory law may therefore provide that certain types of debt shall not be assignable, and/or the law may allow debtor B and creditor A to agree that the credi-

tor shall not assign his rights against the debtor. If such an agreement hinders any transfer of rights to a third party C, the interests of B are perfectly safe, as he will only have to deal with his initial creditor. But A and C are prevented from using the debt for their business purposes.

A future European civil code will have to balance these conflicting interests. It is not surprising that various legal systems in- and outside Europe have found a multitude of ways of striking that balance. The most serious problem, however, seems to be that the interests of our parties A, B and C depend on the roles they play in a given legal and economic context. The law should accordingly treat A, B and C differently according to their respective situations. Let us think of A as a wasteful young man and of B as his aunt who wants to make available to him a modest monthly payment from her fortune.² Who would seriously raise any objections if A is prevented from assigning this right to payment in a gambling den due to a prohibition to that effect? But what if A is a small supplier of parts to a car manufacturer B and dependent on B's orders and payments? One could suspect that a prohibition on assignment would put B in a position to control A's liquidity in such a way that would make A more open to follow B's suggestions as to the prices B has to pay under a subsequent supply agreement.³

In the discussion on a future European civil code, it is comparatively easy to hold that prohibitions on assignment should be allowed in cases where the debtor wants to protect his legitimate interests.⁴ However, regard should be had to the fact

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¹ See the preamble of the UNIDROIT Convention on International Factoring, Ottawa, 1988, under www.unidroit.org/english/conventions/c-fact.htm at 1: "[...] factoring has a significant role to play in the development of [...] trade"; as well as the preamble of the UN Convention on the Assignment of Receivables in International Trade, Resolution adopted by the General Assembly, Document A/RES/56/81 of 31 January 2002, under www.uncitral.org/stable/res1681-e.pdf, at 3: "[...] the assignment of receivables [...] promote[s] the availability of capital and credit at more affordable rates and thus facilitate[s] the development of international trade"; and the introduction to UNCITRAL Draft legislative guide on secured transactions, United Nations General Assembly, Document A/CN.9/WG.VI/WP.2/Add.1, under: www.uncitral.org/English/workinggroups/wg_6/wp-2-add1-e.pdf, at 2: "It is well established, [...] that one of the most effective means of providing working capital to commercial enterprises is through secured credit."

² See the French case of the Cour de Besançon, 1870, Recueil Dalloz 1873.2.110 et seq., quoted from Goergen, in: *Das Pactum de non cendo*, Baden-Baden (D), 2000, at 156.

³ This argument was voiced by the parliamentary group of the Sozialdemokratische Partei Deutschlands (German Social Democratic Party) in the Bundestag (Federal parliament in Germany, i.e. the equivalent of the English House of Commons), BT-Drs. 12/7570 of 15 June 1994, at 3; for an account of the political discussion on the prohibition of assignment in Germany see Bauer, in: § 354a HGB - eine geglückte gesetzgeberische Lösung eines rechtspolitischen Problems?, Berlin (D), 2001, at 340.

⁴ Du Perron, in: Hartkamp et al. (eds): *Towards a European Civil Code*, 2nd ed., Nijmegen (NL), 1998, at 319 gives only this suggestion on the present subject.

that small and medium-sized enterprises typically run short of liquidity and that it is consequently of considerable importance for them to make use of claims under contracts for the supply of goods or services by assigning these rights to payment as a means to create working capital. Small and medium-sized enterprises are of paramount importance for the prosperity and wealth of the European Union;⁵ therefore, their interests should duly be taken into account when discussing a European civil code.

What are, on the other hand the “perfectly good commercial reasons for [the debtor to stipulate] that he will not recognise the title of an assignee of the debt”?⁶ It may occur that the debtor overlooks receipt of a notice of assignment and pays his initial creditor. In this case, he will not be discharged and would in effect have to pay twice. In order to avoid this, a debtor must ensure that notices of assignment are not accidentally overseen, so that he can make the proper payment; this is a time-consuming and costly administrative expenditure. Where the debtor pays into escrow, he may find himself in the uncomfortable situation of having to answer to one of the competing claimants regarding the permissibility of the deposit.⁷ In case of partial assignments, the risk of mistakes is even higher. There are further drawbacks for the debtor. In the first instance, a debtor will have an increased administrative burden in order to correctly direct payments where he is unsure about the identity of the creditor. Secondly, an assignee may be “less reasonable”⁸ than the original creditor in dealing with disputes, as the original creditor might take into consideration an ongoing business relationship. Thirdly, the debtor cannot, as a general rule, set up any new equities against the claim of the assignor after he receives notice of the assignment. Fourthly, the debtor might find himself forced to perform the contract in favour of someone with whom he might have refused to contract directly. Furthermore, he might have an interest in keeping secret his business relationship with the original creditor.⁹

This article will give an account of how and to what extent different legal systems allow for the debtor to restrict the assignment of incurred payment obligations. It will demonstrate how the interests of the parties to an assignment and a prohibition or restriction on assignment, respectively, are balanced by various domestic and international legal systems. Afterwards, an outline of how a future European civil code should govern these issues shall be discussed.

⁵ On the significance of small and medium-sized enterprises for the EU economy, see Document COM (2001) 98, in the final version of 1 March 2001 under http://europa.eu.int/comm/enterprise/entrepreneurship/promoting_entrepreneurship/doc/com2001-98_en.pdf as well as in general <http://europa.eu.int/comm/enterprise/entrepreneurship/>. For a definition of small and medium-sized enterprises, see the Recommendation of the Commission of 3 April 1996, OJ 1996 L 107, at 4.

⁶ *Goode*, Inalienable Rights? Note on *Helstan Securities Ltd v Hertfordshire C.C.* [1978] 3 All ER 262; [1979] 42 MLR 553.

⁷ *Holzner*, Weiterhin: Drittwirksamkeit vertraglicher “Abtretungsverbot”, [1998] Juristische Blätter 495, 502.

⁸ *Browne Wilkinson LJ in Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd* [1993] All ER 417.

⁹ On the debtor’s interest, see for Germany: *Wagner* in: Vertragliche Abtretungsverbote im System zivilrechtlicher Verfügungshindernisse, Tübingen (D), 1994, at 41-50; for England: *Allcock*, Restrictions on the Assignment of Contractual Rights [1983] 42 Cambr LJ 328, 344; *Goode* (*supra* note 6), 553.

II. Different provisions in selected legal systems

1. Belgium and France

a) France

In France, the assignment of claims according to the generally applicable provisions of Articles 1689 et seq. Civil Code (French Civil Code) plays a comparatively marginal role in business life, as the formal requirements of the provisions in the Civil Code are cumbersome:¹⁰ For the assignment to be effective against third parties, Article 1690 requires the notification of the assignment to the debtor by a bailiff acting for the assignee, or the acceptance/acknowledgement by the debtor in the form of a notarial act. The historical justification for this procedure lies in the fact that French law considers a claim to be an intangible thing. As ownership of a chattel is generally transferred by handing over the chattel to the new owner, the notification was meant to be the equivalent of the delivery of a chattel. Notification makes the debtor aware of the transfer of ownership of his debt.¹¹ Hence, a transfer of claims by a mere agreement between assignor and assignee is not possible under the Civil Code.

It is of some comfort that case law has done away with some of these formalities since the entry into force of the Civil Code (for instance: delivery of the document is not necessary any more; a writ of summons may replace notification; a private or tacit acknowledgement is enough when no other parties are involved). But the assignment is still only effective as against the debtor and third parties when the debtor has positive knowledge of the fact that the claim has been assigned. A tacit assignment is not possible.

In order to better suit the financing needs of business enterprises, French legislation has provided for more convenient forms of the transfer of claims. In 1967, an invoice could be transferred in the same manner as a negotiable instrument, unless the debtor refused such transfer within two weeks from the receipt of the invoice.¹² However, in 1981 legislation intervened again, abolishing the 1967 act and enacting the *Loi facilitant le crédit aux entreprises*, or *Loi Dailly*,¹³ allowing business enterprises to assign to a credit institution claims arising from their business activities.¹⁴ The *Loi Dailly* does not re-

¹⁰ *Kötz & Flessner*, in: European Contract Law, translated from the German by *Tony Weir*, Volume 1, Oxford (GB), 1997, at 276; *Zweigert & Kötz*, in: Introduction to comparative law, translated from the German by *Tony Weir*, 3rd ed., Oxford (GB), 1998, at 449.

¹¹ *Kötz*, in: Encyclopædia of International Comparative Law, Volume VII (Chapter 13): Rights of Third Parties, Third Party Beneficiaries and Assignment, Tübingen (D), 1992, at 86; *Hoop*, in: Kodifikationsgeschichtliche Zusammenhänge des Abtretungsverbot, Berlin (D), 1992, at 108, 109.

¹² Ordonnance 67-838 of 28 September 1967, quoted from: *Münch*, in: Abtretungsverbote im deutschen und französischen Recht, Frankfurt/Main (D), 2001, at 186.

¹³ Loi 81-1 of 2 January 1981; named after its promoter Senator Etienne Dailly.

¹⁴ *Cour de Cassation* (Court of Third Instance, equivalent to the House of Lords), *Chambre Commerciale*, 3 January 1996, quote taken from *Blaise & Desgorges*, in: Die Forderungsabtretung, insbesondere zu Sicherungszwecken, im französischen Recht, in: *Hadding & Schneider* (eds), Die Forderungsabtretung, insbesondere zu Sicherungszwecken, in ausländischen Rechtsordnungen, Berlin (D), 1999, at 282, 284.

quire the paperwork involved in the transfer of invoices. The formalities are comparatively easy to comply with: The assignor simply hands over to a bank a list of the claims (the *Bordereau Dailly*) in which the exact claims to be assigned are indicated; no notification to the debtor is required to render this assignment fully effective. According to a recent case of the Cour de Cassation,¹⁵ a prohibition of assignment does not prevent the transfer of the claim to the credit institution. As the credit institution, the assignee, was not a party to the prohibition stipulated between debtor and assignor, the prohibition does not have any effect on the assignee (cf. Article 1165 Civil Code, which applies both to assignment under the Civil Code and under the *Loi Dailly*). An assignment contrary to such a prohibition can nevertheless impose a liability for damages upon the assignor towards the debtor (cf. Article 1145 Civil Code).

Due to the formal requirements of assignment, the French legal system had found other ways to transfer claims before legislation intervened in 1967 and in 1981, respectively. The *subrogation personnelle* (Civil Code, Articles 1249 et seq.) provides the legal framework for the French factoring business: The factor pays the debtor's debt to his client, and without any further arrangements the claim is thus transferred to the factor. As this effect is provided for by law, it is not conceivable that any prohibitions on transfer of claims could hinder the transfer of claims by way of subrogation.¹⁶

However, French law provides for an exception to the rule that prohibitions on assignment do not hinder the transfer of a claim. Under Article 900(1) Civil Code, a prohibition will have an effect against third parties if it is temporary and justified by a legitimate interest. In a business context, the provision applies mainly to distribution and subcontracting agreements; and as subrogation provides a means for liquidating claims, this provision does not hinder business financing.¹⁷

b) Belgium

The Belgian law regarding prohibitions on assignment is quite the same as the French law outlined above. But, as early as 1919, Belgian legislation recognised that Articles 1689 et seq. of the Civil Code (Belgian Civil Code), which used to be exactly the same text as the French Civil Code, were not suitable for the financing needs of small enterprises. As a means of mobilising claims and providing security, creditors can assign a claim to a credit institution by endorsement of the invoice.¹⁸

It may be noted that in 1994, the Belgian legislator did away with some of the procedural requirements of the Civil Code as regards assignment: in order for the assignment to be fully

effective against third parties other than assignor and assignee, notification of the debtor is no longer required; the "meeting of the minds" of assignor and assignee transfers the claim to the assignee.¹⁹

c) Conclusion for Belgium and France

The debtor cannot effectively hinder the transfer of his debt to a third party under French or Belgian law. Claims may be sold or used as security for credit. It is remarkable that assignment as a means to provide security is possible under French law, as the Civil Code has quite a reluctant view on fiduciary or security transactions (cf. Article 544 Civil Code, which for a long time was construed to forbid fiduciary ownership). Under Belgian law, the subject of fiduciary ownership is still under discussion; the provisions of the 1919 Act are meant to be an exception to the general rule.

2. The Netherlands

Before 1992, the Burgerlijk Wetboek (Dutch Civil Code) of 1838 mainly followed the Civil Code. For assignment, notification or acknowledgement was required by Article 688(2). This notification requirement has found its way into Article 3: 94 of the Nieuw Burgerlijk Wetboek (New Dutch Civil Code, hereinafter "NBW"), which entered into force on 1 January 1992. Similar to German law at that time, a prohibition on assignment can validly be agreed upon and would accordingly exclude the transfer of the debt, Article 3: 83(2) NBW. The non-transferability of debt under Article 3: 83(2) NBW is effective against third parties.²⁰ The prohibition may extend to the pledging of claims. This is of special interest for business financing. As Article 3: 84(3) NBW has introduced a general prohibition of fiduciary ownership into Dutch law, the pledging of claims is the legal basis for security transfers.²¹ The prohibition of fiduciary ownership can thus be sidestepped, unlike prohibitions on the transfer of claims.

Dutch law therefore effectively offers the debtor everything necessary to avoid the transfer of his debts. Where an assignor falls bankrupt, the assignee/factor who had settled the outstanding debt with the assignor can do nothing but "fish[ing] behind the net"²² in the estate of the insolvent assignor, as he cannot demand payment from the debtor.

3. Germany

Under German law, the assignment of debt is effective as soon as assignor and assignee agree on the assignment, § 398 Bürgerliches Gesetzbuch (German Civil Code, hereinafter "BGB"), furthermore, the law allows for fiduciary assign-

¹⁵ *Cour de Cassation, Chambre Commerciale*, 21 November 2000, Recueil Dalloz 2001.123; cited according to *Münch* (*supra* note 12), at 179, 180.

¹⁶ *Münch* (*supra* note 12), at 208.

¹⁷ *Münch* (*supra* note 12), at 180 et seq. *Remy & Kamina*, in: National Report for France, *Schulze & Verbagen* (eds), *Assignment in Comparative Law*, Manuscript, 2000 (publication pending).

¹⁸ *Loi sur le crédit professionnel en faveur de la petite bourgeoisie commerciale et industrielle* of 25 October 1919 as amended by an Act of 31 March 1958; cf. *Kötz* (*supra* note 11), at 79; *Van den Bergh & Dirix*, in: *Handels- en Economisch Wet in Hoofddlijnen*, Antwerpen (B) et al., at 123.

¹⁹ Act of 6 July 1994, see *Dirix*, *De vormvrije cessie*, [1994-1995] *Rechtskundig Weekblad* 137-145.

²⁰ *Hoge Raad* (Court of Third Instance, equivalent to the House of Lords), 29 March 1993, [1994] *Nederlands Juristenblad* 171.

²¹ The Dutch factoring business makes use of pledging for recourse factoring, that is factoring where the factors do not assume the credit risk. Assignment is only used where the factors carry the credit risk (non-recourse factoring) and in international factoring; *Bewwing*, in: *Factoring*, Zwolle (NL), 1996, at 133/134.

²² *Bewwing* (*supra* note 21), at 133.

ments for purposes of providing security. However, § 399, second alternative, BGB, makes it possible for the debtor to agree with the creditor that the claim shall not be assigned. When the drafting committee for the BGB inserted that provision, it obviously assumed that the restriction would only be applied in a limited number of cases, such as for railway tickets, claims under insurance contracts and certificates of deposits at the national bank.²³ The prohibition on assignment should have an *erga omnes* effect, i.e. against any third party to that agreement, and the debt should thus be a non-assignable debt.²⁴ Neither the case law of the Bundesgerichtshof (the Federal High Court of Justice in Germany, hereinafter “BGH”) nor the majority of legal opinion ever proposed a different construction of prohibition on assignment, i.e. giving such a provision an effect only *inter partes*, i.e. between debtor and creditor.²⁶ Only the minority opinion attributed such an *inter partes* effect from the prohibition on assignment.

Therefore, the “assignee” of a debt which was subject to a prohibition on assignment, obtains nothing but a claim for damages against the “assignor” based on breach of the contractual obligation vis-a-vis the “assignee” to effectively transfer the claim to him (the “assignee”).

However, economists and lawyers have been criticising this state of the law for a long time. As early as 1936/37, the Ministry of Finance issued a recommendation not to insert prohibitions on assignment indiscriminately in all sorts of contracts, as this was held to be disadvantageous especially for small and medium-sized enterprises;²⁷ and in 1941 literature voiced the view that these prohibitions were a “silly custom”.²⁸ Apart from the inhibitory effect on the circulation of claims, prohibitions on assignment under the BGB lead to situations which are hardly justifiable. *Hein Kötz* put in a nutshell, what *Tony Weir* has rendered in English as: “Often the prohibition is not invoked by the debtor [who stipulated] it, but by the assignor’s creditors [seeking] to gain priority over the assignee. Or suppose that the assignor has already paid into escrow and left the game, disclaiming any interest in the outstanding question of priorities; why should the assignor’s creditors benefit from having the assignment declared invalid?”²⁹

For payment obligations which arose from commercial business activity, that is, contracts between business undertakings or merchants, legislation brought a change in the legal regime in 1994. According to § 354a Handelsgesetzbuch (the

German Commercial Code, hereinafter “HGB”), which was newly introduced, a prohibition on assignment does not prevent an effective transfer of the claim to the new assignee. The debtor will nevertheless validly discharge his obligation by paying to the assignor, even if he was duly informed that the claim had been assigned. Any agreement to another effect is to be held invalid.

a) § 354a HGB: scope of application

Only monetary obligations are covered, in accordance with the aim of the provision. Obligations to supply goods or to render services are generally not assignable, but in case such an obligation has been converted into a (monetary) claim for damages after non-performance or any other breach of contract, this secondary obligation falls under § 354a HGB.³⁰ Obviously, monetary obligations arising from tortious conduct do not fall into the scope of the provision.

What sort of restrictions or prohibitions of assignment does § 354a HGB cover? Under § 399 BGB, any prohibition or restriction invalidates the assignment. Even where the debtor merely stipulates that the only condition for an assignment is that notice of the assignment be given to him by the assignor and/or the assignee, the assignment will have no effect until he receives such notice.³¹

A naive approach might suggest that such a notification clause would fall under the scope of § 354a HGB and could thus be disregarded by assignor and assignee. However, a notice is easily dispatched and the creditor cannot deliberately hinder the assignment; furthermore, the clause is said to serve the debtor’s legitimate interest in information. A claim which becomes assignable on condition of notification is still good security – the list of the German banks indicating debtors “excluding assignment or making assignment subject to their express consent” does not refer to notification requirements – and therefore the aim of § 354a HGB is not to bring such clauses under its scope. It has accordingly been held that non-compliance with a notification requirement will result in an ineffective assignment under § 399 BGB.³²

This differentiation, it is argued, may lead to legal uncertainty, as it would be for the parties to decide if, in a given case, the restriction imposed by the creditor is of such a nature or effect as to trigger the application of § 354a HGB.³³ This does not seem too compelling an argument, as it would be relatively simple for the parties to make such a decision: If the debtor wants to retain a right to take influence on the assignment, § 354a HGB will apply, whereas the general rule of § 399 BGB will apply if the debtor only wants to be duly in-

²³ *Hoop* (*supra* note 11), at 77-79.

²⁴ *ibid.*

²⁵ Court of Third Instance, equivalent to the House of Lords.

²⁶ *Busche* in: *Staudinger*, Kommentar zum Bürgerlichen Gesetzbuch, 13th revised edition, Berlin (D), 1999, para. 65 on § 399 with further references; prohibitions on assignment are effective against third parties and hinder the transfer of claims to third parties not only in Germany, but also in Austria and Switzerland: *Bauer* (*supra* note 3), at 295; for Austria: *Holzner* (*supra* note 7), 495 et seq. and *Lukas*, in: *Zession und Syllagamma*, Vienna (A), 2000, at 53 et seq.

²⁷ *Münch* (*supra* note 12), at 81, where he refers to *Serick*, in: *Eigentumsvorbehalt und Sicherungsübereignung*, Band II, Heidelberg (D), 1965, Volume I § 24 III 2, at footnote 96.

²⁸ *Anonymous*, *Der Kampf gegen die Unsitte des Abtretungsverbot*, [1941] *Bankarchiv*, 153.

²⁹ *Kötz & Flessner* (*supra* note 10), at 274.

³⁰ *Schmidt* in: *Münchener Kommentar zum HGB*, Munich (D), 2001, at para. 6 on § 354a.

³¹ *Heinrichs*, in: *Palandt*, Kommentar zum Bürgerlichen Gesetzbuch, 60th ed., Munich (D), 2001, at para. 11 on § 399; *Busche* in: *Staudinger* (*supra* note 26), at para. 62 on § 399, with reference to BGHZ 112, 387, 389; BGH, [1992] NJW-RR, 790.

³² OLG (Oberlandesgericht [Court of Second Instance]) Schleswig, 8 November 2000, [2001] *Betriebs-Berater* 61 et seq. = *Entscheidungen zum Wirtschaftsrecht Kurzkomentare*, Looseleaf, Cologne (D), § 354a HGB 1/2000.

³³ *Koller*, Note on OLG Schleswig, in: *Entscheidungen zum Wirtschaftsrecht Kurzkomentare* (*supra* note 32).

formed and he thus cannot decide whether he wants to accept the assignment. Regard should also be had to the American Uniform Commercial Code § 9-318(4): only terms which prohibit assignment or require the debtor's consent are ineffective under this provision.

Who can rely on the effectiveness of an assignment contrary to a prohibition on assignment under § 354a HGB? Consumers do not enjoy protection against prohibitions on assignment. As the German parliament must respect everybody's right to equal treatment,³⁴ the question arose as to whether consumers are arbitrarily discriminated against by their exclusion from the scope of application of § 354a HGB.³⁵ As employees will not typically use their claims as security for credits supporting their business activities, the legislator had good reason not to make the provision of § 354a HGB generally applicable.³⁶ However, the term "merchant" in the HGB excludes very small business undertakings and professional persons from the scope of application of § 354a HGB. Therefore, lawyers, accountants, tax advisers and architects would be in a position to both force a non-assignment clause upon their suppliers and to be prohibited from assigning their own receivables from clients. It does not seem in accordance with the legislative aim of the provision, that an architect in a building project may be the only supplier of services involved who is not allowed to assign the claims he has earned against his contractor, or that a supplier of office products is not allowed to use his potentially substantive claims against a big law firm, which is typically not a merchant under German law, for his refinancing needs. This unequal treatment does not seem justified in the light of the constitutional guarantee of the right of equal treatment. For these reasons, it is argued that by way of legal analogy, very small businesses and professional persons must be brought under the scope of § 354a HGB.³⁷

b) Effects of § 354a HGB

At the discussions for the drafting of § 354a HGB, it was proposed to render the forbidden assignment effective against everyone apart from the debtor.³⁸ This would have caused a "relative" ineffectiveness of the assignment: for the debtor, the assignor would have remained the creditor, whereas the assignee would not have had the right to demand payment. As against the assignor and his creditors, however, the assignee would have been the creditor of the assigned claim. The reasons for the change to the adopted model cannot be perceived from the materials of the parliamentary law committee. It is suggested that the wording of Article 6 of the UNIDROIT

Ottawa Convention was indeed the model for the final draft.

Under § 354a HGB, the assigned claim does not fall under the estate of the assignor and is transferred to the assignee's estate; the assignment is "absolutely" effective. However, the creditor may still pay to the assignor and thereby discharge his debt. The assignee, on the other hand, then has to recover his money from the assignor by way of an action for unjustified enrichment³⁹ under § 816(2) BGB.

§ 354a HGB is silent on the question whether an obligation not to assign can be effective. Arguing on the basis of the third sentence of § 354a HGB, which provides that deviating agreements shall be held ineffective, it could be said that § 354a HGB must also be concerned with the obligations between debtor and creditor.⁴⁰ But the arguments put forward for the invalidation of a non-assignment obligation, namely pending liability in damages of the assignor or the debtor's right to obtain an injunction preventing the creditor from assigning the claim,⁴¹ are moot points: damage will rarely be done, and where the debtor wanted to protect confidentiality by way of the non-assignment clause, he should not be left empty-handed; injunctions will rarely occur,⁴² as they cannot assist against (bulk) assignments of future claims, a construction which is quite frequently used in Germany. Hence, a mere obligation not to assign does not jeopardise the legislative goal of § 354a HGB, i.e., the transferability of debts. This view seems to be shared by Article 6(3) of the UNIDROIT Ottawa Convention and Article 9(1) of the UN Convention on Receivables Financing in International Trade.⁴³ These rules expressly allow for obligatory effects of the non-assignment clause between debtor and assignor.

c) § 354a HGB and the insolvency of the assignor

As the debtor, under a non-assignment clause, is still free to pay the assignor notwithstanding the assignment, the assignee may find himself in an uncomfortable situation: if the debtor has paid to the assignor and insolvency proceedings over the assignor's estate are opened before transferral of the amount to the assignee, the assignee is left with only a claim for unjustified enrichment against the assignor's insolvent estate. This obligation will hardly ever be fully honoured by the assignor's trustee in the case of an insolvency.

In order to avoid this, the assignee may stipulate that the assignor shall receive payment from the debtor and book this money on a separate account. As the money thus received is still identifiable in the insolvent estate, the assignee can claim that sum of money⁴⁴ under § 48 InsO.⁴⁵ The same applies

³⁴ Article 3, Grundgesetz (Constitution of the Federal Republic of Germany, "GG"). It is binding not only on the government, but also on the parliament and allows for differing legal rules, on condition that the differentiation is justified by the subject-matter of the rule.

³⁵ See Saar, Zur Rechtsstellung des Schuldners nach § 354a HGB, [1999] ZIP 988, 989 and Wagner, [1996] Wertpapiermitteilungen, Supplement 12, 8.

³⁶ Schmidt, in: Münchener Kommentar zum HGB (*supra* note 30), at para. 6 on § 354a; Canaris, in: Handelsrecht, 23rd ed., Munich (D), 2000, at 498.

³⁷ Canaris (*supra* note 35), at 497 and 499; Schmidt (*supra* note 30), at para. 8 on § 354a.

³⁸ Proposal by the Sozialdemokratische Partei Deutschlands (*supra* note 3), BT-Drs. 12/7570, at 3.

³⁹ §§ 812-822 BGB.

⁴⁰ Schmidt in: Münchener Kommentar zum HGB (*supra* note 30), at paras 11 and 32 on § 354a.

⁴¹ Schmidt in: Münchener Kommentar zum HGB (*supra* note 30), at para.32 on § 354a.

⁴² Bruns, Die Dogmatik rechtsgeschäftlicher Abtretungsbeschränkungen im Lichte des § 354a HGB und der UNIDROIT Factoringkonvention, [2000] Wertpapiermitteilungen, 505, 513.

⁴³ See note 1, *supra* and II.6 *infra*.

⁴⁴ Bauer (*supra* note 3), at 332/333.

⁴⁵ Insolvenzordnung (Code of Insolvency proceedings).

where the debtor pays to the assignor's trustee in insolvency after the opening of insolvency proceedings.

d) Assessment of § 354a HGB

An assignee under § 354a HGB is in an unsecured position.⁴⁶ This view is apparently shared by the Association of German Banks,⁴⁷ which still updates its list of enterprises prohibiting assignment or making it subject to their express consent;⁴⁸ this sort of information has obviously not lost its significance in business life in spite of the legislative intervention introducing § 354a HGB. The inalienability of debts under a prohibition on assignment has been replaced by the risk of debtors paying to their initial creditors and not to the assignees. The assignees therefore still lack reliable security for the credit granted. This has an impact on the availability and the price of refinancing for those business undertakings who have to rely on their receivables for their refinancing.

4. England

Under English law, a contractual prohibition on assignment hinders the assignee from acquiring any rights against the debtor;⁴⁹ this applies both for statutory assignments pursuant to Section 136 of the Law of Property Act of 1925 and assignments at law. The assignment is thus "relatively" ineffective towards the debtor. The debtor may ignore a notice of assignment and perform the contract in favour of the creditor.⁵⁰

In contrast to the situation in Germany, creditors of the assignor seeking to garnishee the claim cannot rely on the prohibition on assignment: "[the] judgement creditor is in no better position than the assignor and cannot garnishee anything the assignor could not honourably deal with."⁵¹ As the assignor has obtained consideration from the assignee, honour prohibits dealing with the claim.

English law also provides for a way to side-step a prohibition on assignment.⁵² Notwithstanding such clause, the debt can be the subject-matter of a declaration of trust. It is thus possible for the "assignor" as trustee to hold the contractual rights against the debtor as a trustee for the "assignee", as beneficiary.⁵³ If the "assignor"/trustee then refuses to enforce his right under the contract, the "assignee"/beneficiary can sue the debtor, joining the trustee as a defendant. Furthermore, the old institute of power of attorney would offer a way to sue in the creditor's name, notwithstanding the non-

assignment clause. In both cases, the "assignee" nevertheless remains in an insecure position, as he cannot prevent the debtor from making payment to the creditor.⁵⁴

5. USA

The view that a prohibition on assignment prevents an assignee from acquiring rights against the debtor prevailed for a long time in US case law and doctrine; a host of controversial cases and literature,⁵⁵ as well as Section 151 of the first Restatement of Contracts of 1932 give evidence of this fact. Although private law is a state and not a federal matter in the US, there was political interest on a federal level to cater for the financing problems of small business.⁵⁶ The Uniform Commercial Code brought about a legal regime which suited these interests. A final draft was presented in 1952; since then, it has been put into force, subject to modifications and reservations, in nearly all states; the Code is under periodical review by the American Law Institute and the National Conference of Commissioners on Uniform State Laws.⁵⁷ The UCC is subdivided into nine articles, and Article 9 covers security interests.

Article 9-318(4) reads as follows: "A term in any contract between an account debtor and an assignor is ineffective if it prohibits assignment of an account or prohibits creation of a security interest in a general intangible due or to become due or requires the account debtor's consent to such assignment or security interest." For sales contracts, Article 2-210(2) stipulates that "A right to damages for breach of the whole contract or a right arising out of the assignor's due performance of his entire obligation can be assigned despite agreement otherwise." Hence, assignment is fully effective as against the debtor, despite a prohibition.

In the context of secured transactions, the interests of the debtor are protected to the extent that he is authorised to pay to the assignor until he receives notification that an assignment has taken place; the notification has to reasonably identify the debt which has been assigned.

Apart from this general protection of the bona fide debtor, the UCC provides for a rule which "may do some violence to accepted doctrines of contract law", as the Official Code Comment admits.⁵⁸ It provides for an exception to the rule that the assignor cannot dispose of the claim in any way after the debtor has been notified. By virtue of § 9-318(2), any modification of a contract made by the original parties is effective against the assignee, without his consent, if the right to payment has not yet fully been earned by performance and the modification agreement was made by the parties "in good faith and in accordance with reasonable commercial standards". The agreement is not in good faith where the parties collusively want to deprive the assignee of the benefits of the

⁴⁶ *Bruns* (*supra* note 42), 505, 512.

⁴⁷ Bundesverband der deutschen Banken, BdB.

⁴⁸ The list has last been updated in June 1999 and comprises ca. 900 enterprises, including all car manufacturers and the most renowned retail trading houses.

⁴⁹ *Helstan Securities Ltd v Hertfordshire C.C.* [1978] 3 All ER 262; *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd* [1993] All ER 417.

⁵⁰ *Pane & Frank Ltd. v Discount Bank Overseas Ltd* [1967] Ch 341; *Carl*, in: Die Forderungsabtretung, insbesondere zur Kreditsicherung, in England in: *Hadding & Schneider* (eds) (*supra* note 14), at 204.

⁵¹ *Holt v Heatherfield Trust Ltd.* [1942] 1 All ER 404, 412.

⁵² *Allcock* (*supra* note 9), 328, 343.

⁵³ *Re Turcan*, [1889] 40 ChD 5, CA; *Don King Productions v Warren* [1998] 2 All ER 608.

⁵⁴ *Allcock* (*supra* note 9), 328, 343.

⁵⁵ For references, see *Allcock* (*supra* note 9), 328, 339.

⁵⁶ Financing Small Business. US Congress Report to the Committees on Banking and Currency pp., Washington D.C., 1958, 449,450.

⁵⁷ www.wld.com/conbus/weal/wucc.htm.

⁵⁸ *Kötz* (*supra* note 11), at 85 (86).

assignment. It will be in accordance with good commercial standards if the adjustment, including payment to the assignor, is necessary under the circumstances to enable the assignor to continue the performance of the contract. This is in the interest of all parties involved, as non-performance would give the debtor the right to rescind the contract, in which case the debtor would have a perfect defence against any claim of the assignor; whereas, if the debtor only pays a part of his debt to the assignor, the assignee will still be entitled to demand the other part of the payment from the debtor.

6. International law

Apart from domestic legal systems, there are also two international conventions providing a set of rules on prohibitions on assignment: the UNIDROIT Convention on Receivables Financing, signed at Ottawa in 1988⁵⁹ and the UN Convention on the Assignment of Receivables in International Trade, which was prepared by the UNCITRAL.⁶⁰ Both of these conventions and American law are equally hostile towards these stipulations, which provide that an assignment shall be effective notwithstanding “any agreement prohibiting such assignment” or “any agreement limiting in any way the assignor’s right to assign its receivables”, respectively.⁶¹ Article 6(2) of the Ottawa Convention, however, allows its Member States to declare in accordance with Article 18 that an assignment shall not be effective against the debtor if he has his place of business in that state at the time of conclusion of the contract.⁶²

Although the Conventions provide for the possibility of an effective assignment notwithstanding a prohibition, both Conventions leave it up to debtor and creditor to place the creditor under a mere obligation not to assign.⁶³ Thus, the debtor may have a claim for only liquidated damages.

The scope of application of these conventions is strictly confined to business activities: The Ottawa Convention applies to receivables arising from contracts concerning the sale of goods and the supply of services other than contracts primarily concluded for personal, household or family use, Article 2(1)a); the scope of the UN Convention, as defined by Article 4(1)a), is defined slightly differently, as it does not refer to the purpose of the original contract, but to the purpose of the assignment: it does not cover assignments made for personal, household or family purposes.

Quite similar to UCC Article 9-318(2), Article 20(2)(b) of the UN Convention provides that “after notification, an agreement between the assignor and the debtor that affects the assignee’s rights is ineffective as against the assignee unless the

receivable is not fully earned by performance and either the modification is provided for in the original contract or, in the context of the original contract, a reasonable assignee would consent to the modification.” This provision should apply in cases where UCC Article 9-218(2) would be applicable.

III. Outline for prohibitions on assignment in a future European civil code

Comparing the legal provisions referred to in this article, it appears that all legal systems apart from the Dutch and the English legal system provide for a special set of rules applicable to prohibitions on assignment in the context of business activities and commercial transactions. There seem to be at least two good reasons for that: firstly, the financing needs of business undertakings and merchants are not only bigger in terms of volume, but also of an unequally greater economic significance; and secondly, the payment of money to one party rather than another does not seem a particular hardship for businessmen. This interest might have to be assessed differently in case of an ongoing business relationship, but enterprises and merchants are the first entities to be asked to deal with another creditor than the one they originally contracted with; after all, they are not eligible for the protection consumers can demand. As in the sphere of business life, interests are thus different from the interests consumers may have. It appears to be neither desirable nor adequate to bring prohibitions on assignment under one and the same legal regime for all sorts of claims; in any event, that would not be feasible without providing for one or the other exception to whatever general rule.⁶⁴

Therefore it should be considered to create a different legal regime for the assignment of rights to payment from contracts other than those concluded for the personal, household or family use of either of the parties.

In discussing the *effects of an assignment contrary to a prohibition on assignment*, the following aspects should be considered. If a prohibition on assignment is effective against any third party, like in the Netherlands, or if it authorises the debtor to discharge his obligation by payment to the assignor, as it is the case under German and English law as well as in case of a declaration according to Articles 6(2) and 18 of the Ottawa Convention, it would be no surprise if we could still witness how contractors who are economically more powerful than their creditors hinder these creditors from using their receivables for financing purposes. This has been described as “an eccentric way of retaining control over one’s contractors”⁶⁵ and as “financially straitjacketing the other contracting party”⁶⁶. Some of the disadvantageous effects of payment to the assignor may be avoided by way of special arrangements between assignor and assignee.⁶⁷ But these arrangements have

⁵⁹ See *supra* note 1; the Convention has entered into force (listed in the chronological order of ratifications) between France, Italy, Nigeria, Hungary, Latvia and Germany.

⁶⁰ See *supra* note 1; the Convention has been open for signature since 12 December 2001 and enters into force after five ratifications, Article 45(1). Conflicts with the UNIDROIT Ottawa Convention are governed by Article 38(2) of the UN Convention.

⁶¹ Article 6(1) of the UNIDROIT Ottawa Convention and Article 9(1) of the UN Convention, respectively, *supra* note 1.

⁶² France and Latvia have made such declarations.

⁶³ Articles 6(3) and 9(2), respectively.

⁶⁴ Goergen (*supra* note 2), argues for a general rule.

⁶⁵ Munday, Prohibitions against Assignment of Choses in Action. Note on *Helstan Securities Ltd v Hertfordshire County Council* [1979] 38 Cambridge Law Journal 50, 52.

⁶⁶ Meissner, Validity of prohibitions against assignment, [1952] Wisconsin Law Reports 740, 749, quoted from Goergen (*supra* note 2), at 89.

⁶⁷ Under the Ottawa Convention and under German law by an agree-

an impact on transaction and accounting costs and they will not bring the assignee in a secure position unless he is in a position to control whether the debtor complies with that additional agreement.

The solution adopted under French, American and international law, i.e. to regard as fully effective the assignment against every third party including the debtor, notwithstanding a prohibition of assignment, should therefore be the preferred solution.

The *interests of the debtor should be protected* in two respects: Firstly, the debtor should be free to perform in favour of the assignor as long as he has not been notified, either by the assignee or the assignor, that an assignment has taken place and that payment is to be made to the assignee. This burdens the debtor with keeping track of the notices, but, as an efficient office organisation is in the best interests of any business, the increased administrative costs may well be deemed to be the sole problem of the debtor, as a part of his business expenses.⁶⁸ Such notification should not be a condition for the assignment to be effective as it is under Articles 1689 et seq. of the French Civil Code, and it should be of no significance for the rights of any third party. The legal provisions to be adopted should be guided by UCC Article 9-318(3) and the German case law on notification under § 354a HGB referred to above. The argument of transaction costs cannot be raised in this context: the assignee will only have an interest in ascertaining that no payment is made to the assignor where he has reason to believe that the assignor will not be in a position to honour his obligations towards the assignee. Common and frequent as liquidity troubles and insolvency may be, they are still less frequent than cases where these worries are absent.⁶⁹

Secondly, according to the principle of the freedom of contract, it should be left to the debtor to stipulate an obligation not to assign, which would have an effect merely between debtor and creditor. In case the interests of the debtor are prejudiced by the assignment, it must be for him to seek indemnification from his contractor.

The more the law allows the free circulation of claims, the more likely it is that the law has to *exclude certain debts from free circulation*.⁷⁰ One of the instances in which a prohibition on assignment should hinder the transfer to another creditor of a debt is the case of netting agreements. The parties to a netting agreement agree not to pay for each future claim against each other but to set them off; they will periodically net the sum of the mutual obligations and make a single payment for a multitude of transactions. Where debts in such a netting construction would be transferred to another creditor, this would jeopardise the debtor's legitimate expectation that he will receive payment of his claims against the other party in the netting agreement by way of set-off. Where debts are as-

signed that way, one party is left with claims against the other party, the assignor, and that party must honour claims from the assignee. These legitimate interests should hinder the free transferability of claims in case of netting agreements. Apart from that, the legislative aim of free transferability, i.e. the supply of liquidity to enterprises, is already met by a netting agreement: As no payments have to be made other than a periodic single payment, the parties to the netting agreement have more cash available; the netting agreement itself thus provides increased liquidity for other business activities. Therefore, the UN Convention⁷¹ and German Law,⁷² exempt netting agreements from the rule that prohibitions on assignment do not hinder an effective transfer of the debt to another creditor.

The UN Convention provides for more exceptions than this one; the number and scope of the exceptions to a rule are determined by its scope of application. This proposal for a rule on prohibitions on assignment for a European civil code is mainly concerned with debts resulting from contracts for the sale of goods or the supply of services. The law of banking and the financial markets as well as the rules pertaining to negotiable instruments do not have to be concerned with the financing interests of small and medium-sized enterprises. The rules on prohibitions on assignment as they have been outlined must be strictly confined to commercial activity.

IV. Conclusion

"The social or economic utility of permitting creditors to transfer rights is believed to outweigh the utility of permitting [debtors] to forbid the transfer. That one utility outweighs the other lies beyond demonstration and proof."⁷³ When this sentence was written nearly forty years ago, it may have reflected the facts, and even today it might be correct. However, there are some indications that free circulation of debts is indeed more useful than letting the debtor protect his interest by prohibiting assignment.⁷⁴ Nevertheless, it has to be admitted that legal logic and reasoning alone do not provide for an answer,⁷⁵ as both debtor and creditor can argue on the grounds of the freedom of contract: one wants to be free to contractually restrict the other's freedom of contract in regard to his claims, the other one wants to be free to enter into contracts concerning his claims. Therefore, the legislator's decision in this matter is eventually a political one. The multitude of solutions adopted under different legal systems gives evidence of that, as in each and every legal system, the arguments in this debate are as good as the same.

ment that money paid is to be booked on a separate account, under English law by way of a declaration of trust, see II.3.b and II.4 *supra*.

⁶⁸ Kötz & Flessner (*supra* note 10), at 274.

⁶⁹ Pürner, "Einschränkung des Abtretungsverbotes – der neue § 354a HGB. "Rechtswohltat" für den Mittelstand oder "Wurstelei" des Gesetzgebers? [1995] *Betrieb und Wirtschaft* 257, 263.

⁷⁰ For France, cf. Goergen (*supra* note 2), at 183.

⁷¹ Article 4(2)(b) and Article 5(k)(l).

⁷² Busche, in: Staudinger (*supra* note 26), at para. 55 on § 399.

⁷³ Gilmore, in: Security interests in personal property, Boston (USA), 1965, Vol. I, at 212, 213.

⁷⁴ See the quotes in note 1, *supra*, and for Germany, the economic analysis by Depping & Nikolaus, [1994] *DB* 1199 et seq.

⁷⁵ Allcock (*supra* note 9), 328, 346.