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SHOULD CLAUSES PROHIBITING ASSIGNMENT BE OVERRIDDEN BY STATUTE?

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

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1 The Department of Business, Innovation and Skills has consulted on draft Regulations and further work is continuing, of which the author is a part. *See* Department for Business, Innovation and Skills, Invoice finance: nullifying the ban on invoice assignment contract clauses, https://www.gov.uk/government/consultations/invoice-finance-nullifying-the-ban-on-invoice-assignment-contract-clauses (2015); *see also* Small Business, Enterprise and Employment Act, 2015, c. 26 (U.K.).

2 One of the surveys was carried out by Hugh Beale and Louise Gullifer in 2011 ("2011 Study") with the assistance of Anna Kloeden. The survey was funded by the Asset Based Finance Association (ABFA), which stressed from the outset that it wanted a completely independent view. The second survey was carried out in 2014 as part of the work of the Secured Transactions Law Reform Project ("2014 Study") by Sarah Paterson. I am grateful to both Hugh Beale and Sarah Paterson for

for reasons of space. The model that is likely to be adopted in England and Wales is that found in the Uniform Commercial Code Article 9, which provides that an anti-assignment clause is generally ineffective.[3]

I. The Arguments For and Against an Override

In order to maximize the availability of finance and credit in the economy, it is important that as many sources of wealth as possible can be used as collateral. To do this, the source of wealth (the asset) must be able to be alienated to the secured creditor. The obvious assets which could be alienated are tangible assets: goods and land. However, sources of wealth also include intangible assets, most importantly, rights to be paid by another. Thus, many centuries ago, it became possible to use obligations owed to a borrower as collateral for a loan, first by pledging a document which represented that obligation (a documentary intangible), and then by enabling the benefit of obligations to be assigned, either absolutely or by way of security. A major difference between the use of tangible property as collateral, and the use of such obligations, known in English law as choses or things in action,[4] is that in the latter case there is another person to consider, namely the obligor. There is no real problem when the obligor takes on an obligation that is designed to be transferred, for example, a negotiable instrument. But, where the obligation can be transferred without the agreement, or even the knowledge, of the obligor, a policy imperative arises in competition to that of maximizing available collateral by permitting alienability: that of protection, where necessary, of the obligor. This policy can be seen in English law, for example, by the rule that only an assignee who has taken a statutory assignment can sue the debtor.[5] If an equitable assignment is taken, the assignor must be joined in any action. There are three main criteria for a statutory assignment: (1) the assignment must be in writing; (2) the assignment must not relate to part of a debt or a future debt; and (3)

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permitting me to use the results of the surveys in this paper, and for many useful discussions.

[3] U.C.C. § 9-406(d) (2015).

[4] Also known as intangibles; however, the category of intangibles is potentially wider than just choses in action, e.g., intellectual property and carbon trading units.

[5] Law of Property Act, 1925, 15 & 16 Geo. 5, c. 20, § 136 (Eng.).

notice of the assignment must be given to the debtor. All serve some function in protecting the debtor. Additionally, the policy of protecting the obligor can be seen by the rule that the benefit of a contract for personal services cannot be assigned,[6] and more generally, by the fact that an obligor is permitted to protect himself by restricting the ability of the obligee to assign the benefits of the obligation to another. This permission, though, is justified by the even more fundamental policy of protection of freedom of contract.

Thus, whether there should be a statutory override of anti-assignment clauses can be seen as a matter of balancing competing policy imperatives: alienability of assets, which maximizes available collateral, and freedom of contract, which allows obligors to protect themselves against adverse effects of assignment of the right to which their obligation correlates. On that basis, many jurisdictions and transnational instruments favor alienability.[7] Gilmore described the view in favor of the unrestricted and unrestrictable alienability of contract rights as "so fundamental an order [that] belief is instinctive and irrational, not logical and reasoned."[8] This argument has been used to justify a statutory provision making an anti-assignment clause unenforceable against third parties.

I would like to suggest that the policy position is not so simple. At least from the English law perspective, there is a view that the policy imperatives can be satisfied without any statutory interference and that legislative change has to be justified both by economic arguments (based on the effects of uncertainty of outcome), and by evidence that the availability and cost of borrowing is actually affected by the

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[6] Tolhurst v. Assoc. Portland Cement Mfrs. (1900) Ltd., [1903] A.C. 414 (H.L.).

[7] *See* ANTHONY DUGGAN & DAVID BROWN, AUSTRALIAN PERSONAL PROPERTY SECURITIES LAW 32 (2012) (relating to *Personal Property Securities Act 2009* (Austl.)); UNCITRAL LEGISLATIVE GUIDE ON SECURED TRANSACTIONS, at sec. II par. 107, U.N. Sales No. E.09.V.12 (2010), *available at* http://www.uncitral.org/pdf/english/texts/security-lg/e/09-82670_Ebook-Guide_09-04-10English.pdf; *see also* U.N. Secretary-General, *Legal Aspects of Receivables Financing*, ¶ 23, U.N. Doc. A/CN.9/397 (Apr. 29, 1994); U.N. Secretariat, *Receivables Financing: Analytical Commentary on the draft Convention on Assignment of Receivables in International Trade*, ¶ 100, U.N Doc. A/CN.9/489 (Mar. 13, 2001).

[8] GRANT GILMORE, SECURITY INTERESTS IN PERSONAL PROPERTY 212 (1965).

existence (or potential existence) of anti-assignment clauses in contracts giving rise to receivables. This is for several interconnected reasons. First, the current law, to a large extent, accommodates the protection of the obligor and validity of a proprietary interest of the assignee. Second, receivables financiers in England and Wales have managed reasonably well by adopting "workarounds" to enable themselves to function within the current system. Third, the main concern about anti-assignment clauses relates to borrowers who are small businesses, and is part of a larger problem of inequality of bargaining power. Finally, anti-assignment clauses play an important and justifiable role in loan agreements, derivative contracts, and other financial transactions. In fact, there is real concern about defining the scope of statutory controls so that these benefits are not lost.

II. THE ACCOMMODATION OF THE CURRENT LAW

In analysing the law, terminology can be confusing. In this analysis, terms are adopted that relate to receivables arising from supply contracts, since this is the context in which anti-assignment clauses are said to cause most problems.[9] The parties to the contract giving rise to the receivable are called the "supplier," (the obligee) and the "customer," (the obligor). The supplier is the client of the "financier" to whom it assigns, or attempts to assign, the receivable.

A financier is concerned about three things in relation to the receivables it takes as collateral. First, a financier has a proprietary interest in the receivables and their proceeds, which will survive the insolvency of the supplier. Second, a financier has priority over any subsequent assignee or other person claiming an interest in the receivables. Third, if the customer does not pay, the financier can ensure that the debt is enforced, and it has a proprietary claim to the proceeds of that enforcement.

Under English law, there are two types of assignments. The first type of assignment is a statutory assignment under section 136 of the Law of Property Act 1925, which takes place when certain

[9] Another context, i.e., receivables under loan agreements, is considered *infra* section V.

conditions are satisfied.[10] The most important condition, for purposes of this paper, is that there must be notification to the obligor (the customer). This means that the customer will, and indeed must, pay the financier rather than the supplier.[11] If the customer fails to pay, the financier is able to sue the customer directly. In effect, the supplier drops out of the picture. A statutory assignment will also give the financier a proprietary interest in the receivable in the event of the insolvency of the supplier, or if there are competing interests.[12] There is clear authority that a receivable containing an anti-assignment clause cannot be the subject of a statutory assignment[13] so that the customer can continue to pay the supplier and cannot be sued (at law) by the financier.

The second type of assignment is an equitable assignment. An assignment is equitable when one of the conditions for a statutory assignment is not fulfilled. For example, a valid equitable assignment can occur without notifying the customer. A financier who takes an equitable assignment has a proprietary interest in the receivable, which survives the insolvency of the supplier, and will also have priority over a competing interest, subject to the rules on priority. Until the customer is notified, if it pays it will, of course, pay the supplier and will get a good discharge by so doing. The supplier will then hold those proceeds on trust for the financier.[14] Further, valid set-offs may

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10 *See* Law of Property Act, 1925, 15 & 16 Geo. 5, c. 20 (Eng.).

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

12 The priority rules, which depend on those set out in the nineteenth century case Dearle v. Hall, (1828) 38 Eng. Rep. 475, are somewhat complex. If a receivable is assigned twice, the first assignee to give notice to the debtor will have priority, providing that he did not have notice of the other assignment at the time he took his own assignment. If the debtor has not been notified at all, the assignment that is first in time wins. The position is even more complex if one or both of the assignments is a security interest, as security interests are required to be registered, and registration can, but does not necessarily, constitute notice.

13 *See* Linden Gardens Trust Ltd. v. Lenesta Sludge Disposals Ltd., [1994] 1 A.C. 85, 106-09 (H.L.). Of course, the true effect of any contractual provision (including an anti-assignment clause) will always depend on its exact wording. Thus, the *Linden Gardens* case, though laying down certain principles, was considering a particular form of words.

14 This trust is often expressly declared, but would arise in any event. *See* *G.E. Crane Sales Pty. Ltd. v. Comm'r of Taxation* (1971), 126 CLR. 177, 213-14 (Austl.); Barclays Bank Ltd. v. Willowbrook Int'l Ltd., [1987] 1 F.T.L.R. 386 (Eng.).

continue to arise between the supplier and customer until the customer receives notification of the assignment;[15] after this, only set-offs arising from the contract itself or closely connected claims can arise.[16] If the customer does not pay, the financier cannot, in theory, sue the customer for non-payment without joining the supplier to the action, although this rule is less restrictive than it sounds. It is easy to join a party to an action since no consent is needed if they are joined as a defendant, and the court will not require joinder if there is no good reason.[17] Also, if the financier wishes to enforce, it will first give notice of the assignment to the customer. Doing so will not only require the customer to pay the financier rather than the supplier,[18] but will also, in most cases, convert the equitable assignment into a statutory assignment,[19] thus enabling the financier to sue the customer direct. Of course, where the financing is on a non-notification basis, such as invoice discounting, the financier would normally expect the supplier to enforce against the non-paying customer. If the financing is with recourse, the financier would have contractual rights against the supplier so that the risk of non-payment is on the supplier.[20] It is only when the supplier either refuses to sue or is insolvent that the financier would be concerned to have the right to sue the customer itself. Even then, the financier might not need to enforce directly if there is an

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15 Roxburghe v. Cox, [1881] 17 L.R. 520 (Ch. D.) (Eng.); Gov't of Nfld. v. Nfld. Ry. Co., [1888] 13 App. Cas. 199 (P.C.); Bus. Computers Ltd. v. Anglo-African Leasing Ltd., [1977] 1 W.L.R. 578 (Eng.).

16 Known in English law as "transaction set-off."

17 *See* William Brandt's Sons & Co. v. Dunlop Rubber Co. Ltd., [1905] 2 A.C. 454 (Eng.); Sim Swee Joo Shipping Sdn. Bhd. v. Shirlstar Container Transp. Ltd., (unreported) 17 Feb. 1994; Raiffeisen Zentralbank Österreich AG v. Five Star General Trading LLC, [2001] EWCA (Civ) 68, 60, [2001] 2 W.L.R. 1344 (Eng.). Good reasons include the possibility that the supplier might contest the assignment, or that the assignment is only part of the debt, so that unless the supplier is before the court, the customer might face more than one action.

18 Jones v. Farrell, [1857] 1 De G & J 208; Brice v. Bannister, [1878] 3 Q.B.D. 569; William Brandt's Sons & Co. v. Dunlop Rubber Co. Ltd., [1905] 2 A.C. 454 (H.L).

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

20 *See* HUGH BEALE ET AL., THE LAW OF SECURITY AND TITLE-BASED FINANCING (2d ed. 2012).

efficient means of enforcing against the customer through the insolvency process of the supplier.[21]

If the receivable contains an anti-assignment clause, some, but not all, of the above analysis changes. The customer, who is discharged by paying the supplier before notification of the assignment, is also discharged by paying the supplier after notification: it is entitled to ignore the notification. Once the debt is paid, though, the supplier will hold the proceeds on trust for the financier despite the anti-assignment clause. There is little *direct* authority on this point in English law, but there are a number of dicta[22] and academic support[23] supporting this view. In fact, it is extremely common for invoice discounting agreements to include an express provision that the proceeds are held on trust for the financier, and an anti-assignment clause will not prevent such provision being effective.[24] It is thought that even if the clause purported to prohibit such a declaration, it would be ineffective to prevent such a trust arising since the customer has no interest in preventing the alienation of the proceeds and such a clause would be against public policy.[25] However, this point has never been litigated, so the position is not entirely clear.

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21 *See discussion in the rest of this section.*

22 Re Turcan, [1888] 40 Ch. D. 5, 10-11 (supported by Lord Browne-Wilkinson in Linden Gardens, [1994] 1 A.C. at 106; Barbados Trust Co. Ltd. v. Bank of Zambia, [2007] EWCA (Civ) 148, 28, 77 (C.A.) (Eng.). *See also Devefi Pty. Ltd. v. Mateffy Perl Nagy Pty. Ltd.,* [1993] 113 ALR. 225, 236 (Austl.); Don King Prods. Inc. v. Warren, [2000] 3 W.L.R. 276 (C.A.) (Eng.).

23 *See* Bob Allcock, *Restrictions on the Assignment of Contractual Rights*, 42 C.L.J. 328, 335–36 (1983); Gregory Tolhurst, *Prohibitions on Assignment and Declaration of Trust: Barbados Trust v. Bank of Zambia*, LLOYD'S MAR. & COM. L.Q. 278 (2007); Gerard McMeel, *The Modern Law of Assignment: Public Policy and Contractual Restrictions on Transferability*, LLOYD'S MAR. & COM. L.Q. 483, 507-08 (2004); MARCUS SMITH, THE LAW OF ASSIGNMENT 347 (2007); Peter Zonneveld, *The Effectiveness of Contractual Restrictions on the Assignment of Contractual Debts*, 22 J. INT'L BUS. & F. L. 313 (2007); Chee Ho Tham, *Notice of Assignment and Discharge by Performance*, LLOYD'S MAR. & COM. L.Q. 38, 77 (2010); GOODE ON LEGAL PROBLEMS OF CREDIT AND SECURITY 3-39 (Louise Gullifer ed., 5th ed. 2013).

24 Don King Prods. Inc., [2000] 3 W.L.R. 276; MARCUS SMITH & NICO LESLIE, THE LAW OF ASSIGNMENT: THE CREATION AND TRANSFER OF CHOSES IN ACTION, Part 25.33–25.36 (2nd ed. 2013).

25 Roy Goode, *Inalienable Rights?*, 42 MOD. L.R. 553 (1979); Linden Gardens, [1994] 1 A.C. at 108 (per Lord Browne-Wilkinson at 108). The supplier

If the customer does not pay, it is clear that the financier cannot sue directly, as there can be no statutory assignment. However, provided that the agreement between the supplier and financier can be said to give rise to a trust of the unpaid receivable (either expressly or impliedly),[26] it is likely that the financier can sue the customer, joining the supplier as defendant to the action under a procedure known as the *Vandepitte* procedure. A beneficiary under a trust of a right can bring an action to force the trustee to bring an action to enforce that right for its benefit. The *Vandepitte* procedure merely short-circuits this process by enabling the beneficiary to instigate an action, which brings all parties before the court. In a case dealing with the purported assignment of a syndicated loan containing a restriction on assignment, a majority of the Court of Appeal decided that the *Vandepitte* procedure[27] was available to the "assignee."[28] However, other judges have expressed doubt as to the appropriateness of the *Vandepitte* procedure in this context.[29]

Further, if there is an effective trust of the receivable, the financier will have a proprietary interest which survives the supplier's insolvency, and is effective against competing interests in the receivable. What is not entirely clear, however, is whether it is possible for a well-drafted anti-assignment clause to prevent a trust of the receivable from arising. The judges in *Barbados Trust* were divided on

would be in breach of contract by declaring the trust, but it is hard to see what the damages would be.

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

27 The *Vandepitte* procedure is named after the case of Vandepitte v. Preferred Accident Insurance Corp. of New York, [1933] A.C. 70 (P.C.) (Eng.). Where there is a trust of an obligation, the trustee would usually enforce the obligation by suing the obligor. If the trustee refuses to sue, the beneficiary can sue the trustee to force him to do so. The *Vandepitte* procedure avoids the duplicity of actions, by allowing the beneficiary to sue the obligor direct, providing that the trustee is joined as defendant. If the action is successful, the court will order payment to the trustee, who will then hold those funds on trust for the beneficiary.

28 Barbados Trust, [2007] EWCA (Civ).

29 Don King Prods. Inc., [2000] 3 W.L.R. 276 (Lightman J); Barbados Trust, [2007] EWCA (Civ) at 139 (Hooper LJ).

this issue.[30] A strong case can be made for an analysis whereby the trust is invalid to the extent that it affects the customer, but is valid as between the financier and the supplier.[31] However, there is still considerable uncertainty as to the correct legal analysis.[32]

From the point of view of the customer, the anti-assignment clause protects its position by enabling it to get a good discharge by paying the supplier: it will never be required to pay anyone else. Even if it is sued by the financier under the *Vandepitte* procedure,[33] the order will be that the customer pay the supplier (the trustee), who will then hold the proceeds on trust for the financier. Further, a notice of assignment received by the customer is ineffective to prevent set-offs arising between the supplier and the customer.[34]

Therefore, the overall legal position is that the interests of the financier and the customer can both have a certain degree of protection if an anti-assignment clause is used. This position is subject to several caveats. First, the law is complex and quite uncertain in some areas. There are few cases precisely on the relevant point, and even those that there are have generally not arisen in the context of receivables financing.[35] Second, the legal position will depend on the

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[30] Barbados Trust, [2007] EWCA (Civ) at 44-47, 88, 129-39.

[31] GOODE ON LEGAL PROBLEMS OF CREDIT AND SECURITY 3-42 (Louise Gullifer ed., 5th ed. 2013).

[32] A contrary view is that the clause renders the receivable inalienable so that a valid trust cannot be declared of it. *See* Andrew McKnight, *Contractual Restrictions on a Creditor's Right to Alienate Debts*, 18 J. INT'L BANK. L. & REG., no. 2, 2003, at 43 (2003); Gerard McMeel, *The Modern Law of Assignment: Public Policy and Contractual Restrictions on Transferability*, LLOYD'S MAR. & COM. L.Q. 483 (2004); Gregory Tolhurst & John Carter, *Prohibitions on Assignment: A Choice to Be Made*, 73 C.L.J. 405 (2014); Peter Turner, *Charges of Unassignable Rights*, 20 J. CONT. L. 97 (2004).

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

[34] If, despite the clause, there is a valid declaration of trust, this will break the mutuality required for set-off. If the clause renders a trust invalid to the extent that it affects the customer, then the notification of the trust could be said to be ineffective for all purposes, including preventing set-offs. *See* J. Marshall, *Declaring a Trust Over Rights Under an "Unassignable" Contract*, 12 INSOLVENCY INTELLIGENCE 1 (1999).

[35] Linden Gardens, [1994] 1 A.C. 85; Don King Prods. Inc. v. Warren, *supra* note 23; Barbados Trust, [2007] EWCA (Civ) EWHC (TCC) 530. The one exception is Stopjoin, [2014] EWHC (TCC) 589.

precise wording of the anti-assignment clause and the purported assignment or declaration of trust.[36] Third, even if a financier is protected by the rule that the proceeds are held on trust, this will not help if the supplier has not kept the proceeds in an identifiable state so that they can be traced on its insolvency. A financier might be better off with a proprietary right to a debt owed by a solvent customer, than to proceeds that may or may not be held by an insolvent supplier.

It should be pointed out that the fact that there is a reasonable degree of protection in the current law does not necessarily rule out statutory intervention. For example, Uniform Commercial Code (U.C.C.) (1952) article 9-318(4),[37] which contained an override of anti-assignment clauses, was included in the original U.C.C. (1952) to reflect existing U.S. law rather than to change it.[38] However, this was in the context of a codification of commercial law and the introduction of a new system for secured financing. To make a case for free-standing legislation, a policy imperative is essential.

III. INDUSTRY WORKAROUNDS

Until recently, there were two main types of receivables financing: factoring, which is on a notification basis, and invoice discounting, which is non-notification.[39] Factoring tends to be used for smaller suppliers, where a financier has concerns about the ability of the supplier to run its ledger properly and to operate a trust account, and also where the financier has concerns about the supplier's financial position.[40] Since factoring involves a statutory assignment, it gives the financier much more control over the collection of the debts.

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36 *Id.*

37 Now revised U.C.C § 9-406(d) (2010).

38 This is made clear by the official comment to the original U.C.C. Article 9, which states: "[the provision] can be regarded as a revolutionary departure only by those who still cherish the hope that we may yet return to the view entertained some two hundred years ago by the Court of the King's Bench." However, this is an overstatement. There were contrary cases that were overruled by the legislation, such as Allhusen v. Caristo Construction Corp., 103 N.E.2d 891 (N.Y. 1952).

39 Much of the information in this section comes from the 2011 Study, updated to take into account recent developments.

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

Factoring is more expensive for the supplier than invoice discounting, and a supplier can pay even more for extra services, such as the taking on by the financier of the credit risk of the customer.[41] In invoice discounting, the collection of the receivables is carried out by the supplier, who holds the proceeds in a trust account for the financier.

Recently, two variations on these structures have become more popular, although the details vary in each case. One is discounting of individual invoices over an online platform: this takes place on a non-notification basis, with the platform merely acting as an intermediary. Another is supply chain financing whereby a customer arranges with a financier that the latter purchases receivables owed by the customer to its suppliers at the point when the receivables arise, once the invoice has been confirmed by the customer. This has the advantage that there is less likely to be disputes about the invoice, and also that it allows the financing to be based on the credit rating of the customer rather than that of the (smaller) supplier.[42] Having said this, this kind of financing is usually only offered to established suppliers whose invoices reach a certain, reasonably high, level and is also only offered by large customers.[43] There is also a concern that supply chain financing encourages large customers to extend the credit period they require, forcing small businesses to pay for a longer period of financing, albeit at a lower rate.[44]

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

42 The U.K. Government launched a scheme in 2012 to encourage businesses and government agencies to offer supply chain financing. *See* Prime Minister's Office, *Prime Minister Announces Supply Chain Finance Scheme*, GOV.UK (Oct. 23, 2012), https://www.gov.uk/government/news/prime-minister-announces-supply-chain-finance-scheme.

43 2011 Study, *supra* note 2.

44 *See* John Antunes, *The Supply Chain Finance Scheme: Hit or Miss?*, REALBUSINESS (Nov. 8, 2012), http://realbusiness.co.uk/article/15791-the-supply-chain-finance-scheme-hit-or-miss; James Hurley, *Payment Concerns Over Supply-Chain Finance Move*, TEL. (Oct. 26, 2012 7:00 AM), http://www.telegraph.co.uk/finance/yourbusiness/9634184/Payment-concerns-over-supply-chain-finance-move.html; *Supply Chain Finance Scheme: A Good Idea?* SELECT FACTORING (2012), http://www.selectfactoring.co.uk/supply-chain-finance-scheme.

Although some of the workarounds discussed below are adopted regardless of whether particular receivables arise from contracts containing an anti-assignment clause, English financiers very frequently check for the presence of anti-assignment clauses (and for other problematic clauses) in the invoices they finance.[45] Thus, one of the major arguments for a statutory override made in other jurisdictions (that it is not feasible for a receivables financier to discover anti-assignment clauses, causing the whole cost of financing to rise)[46] is not really made out in England and Wales. However, checking contracts is burdensome and takes time, particularly if it is necessary to consult lawyers about the effect of a particular clause.[47] The need to do so clearly increases costs, although it is probably the case that some checking would still take place even if there were to be a statutory override of anti-assignment clauses. It is also the case that most supply contracts are on a customer's standard terms, and financiers get to know the terms of large customers and whether they contain an anti-assignment clause, so checking involves merely looking at who the customers are rather than reading individual contracts.

If the financing is on a non-notification basis, the presence of an anti-assignment clause does not create problems for the financier on a day-to-day basis, since the customer does not know of the assignment and continues to pay the supplier.[48] Of course, the supplier would be in breach of contract: this may be of concern if, for example, the breach entitled the customer to terminate the supply agreement.[49]

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45 Those interviewed for the 2011 Study all said that they checked for the presence of anti-assignment clauses. The picture was more mixed in relation to the 2014 Study, although most said that they checked at least in many cases.

46 *Personal Property Securities Act 2009* (Austl.); ANTHONY DUGGAN & DAVID BROWN, *supra* note 7.

47 2011 Study, *supra* note 2.

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

49 Although such a breach is unlikely to be repudiatory, it could fall within a clause entitling the customer to terminate for "any material breach" (which is quite common) or could trigger a cross-default clause. The absence of a general duty of good faith in English law could mean that a customer could rely on such a termination clause even if its real motivation for termination was something entirely

The financier might worry about two situations: (1) if the supplier becomes insolvent, and (2) if the customer does not pay and the supplier refuses to enforce.[50]

In relation to the first situation, financiers almost universally protect themselves by taking a security interest over all assets of the supplier.[51] This has the effect, under English law, of enabling the financier to appoint an administrator of the supplier should it become insolvent.[52] The financier is then in a good position to direct the administrator to collect the receivables and pass the proceeds to it. There seems to be little concern among financiers about the collecting in of debts if an administrator is appointed (even if not appointed by that particular financier), although the costs are sometimes a problem if the supplier is a very small business.[53] Financiers also see an "all assets" security interest as having an additional benefit, namely that it will cover receivables that are not assigned to the financier because of an anti-assignment clause. Sometimes, financiers specify that such "non-vesting debts" fall within a fixed charge, while much of the all assets security interest will be a floating charge. However, depending on the wording of the clause, to the extent that it prevents a valid assignment, an anti-assignment clause may also prevent the creation of a valid security interest.[54]

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different. In theory, a breach could entitle a customer to obtain an injunction to prevent further breaches (although this is unlikely) or to sue for damages. However, it is usually hard to see what loss is suffered.

50 The 2014 Study indicated that the latter concern is at least as important, and, for invoice discounters, more important than the 2011 Study, although the sample for this particular question was small.

51 2011 and 2014 Study, *supra* note 2.

52 The Insolvency Act 1986 provides that a qualifying floating charge holder can appoint an administrator out of court. The Insolvency Act 1986, c. 45, sch. B-1, ¶ 14 (U.K.).

53 Seminar to explore and discuss the merits of an online register for all security interests, including outright assignments of receivables, Secured Transactions Law Reform Project, May 8, 2014; 2014 Study, *supra* note 2.

54 Although a charge is not, in theory, an assignment, many charges are drafted as equitable mortgages, which involve an equitable assignment of the receivables. A fixed charge has been treated as an assignment in a number of cases. *See* Biggerstaff v. Rowatt's Wharf Ltd., [1896] 2 EWCH 93 C.A. (U.K.); N W Robbie & Co. v. Witney Warehouse Co., [1963] 1 W.L.R. 1324 (C.A.) (U.K.); Foamcrete (UK) Ltd. v. Thrust Engineering Ltd., [2000] EWCA (Civ) 351. *See also Re Turner*

Another mode of protection often coupled with the all assets' security interest is for financiers to take a personal guarantee from the directors of the supplier company.[55] Of course, the effectiveness of such guarantee depends on the credit-worthiness of the directors, and also may entail costs in enforcing the claims under the guarantees, to which there could be arguable defenses.

Yet another possibility is for the financier to take a power of attorney enabling it to sue the customer in the name of the supplier.[56] This protection tends to be more useful in the second situation: when the supplier is solvent but refuses to sue. For the power of attorney to be irrevocable on the insolvency of the supplier, the financier must have some sort of proprietary right in the receivables or must be owed the receivables directly.[57] Where there is an anti-assignment clause, the latter is clearly not the case, and it is unclear whether a right under a trust is a sufficient proprietary interest to render the power irrevocable. The legal position is uncertain and untested.[58]

An anti-assignment clause causes much greater problems for financiers who operate on a notification basis. Here, there is a likelihood that the customer will refuse to pay the financier when notified, and will, instead, pay the supplier. The financier is then at risk of the proceeds being dissipated by the supplier, leaving the financier at the credit risk of the supplier. As a result, such financiers often refuse to finance receivables arising from contracts containing such clauses, or demand that the customer agrees to a waiver.[59] The evidence from the 2014 study is that financiers only sometimes pursue a waiver. There was considerable agreement[60] that the time and effort

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Corp. Ltd. (In Liq), [1995] 17 ACSR 761 (Austl.) (where the Federal Court of Australia took the view that a clause prohibiting assignment also prohibited a charge).

55 2011 and 2014 Study, *supra* note 2.

56 2014 Study, *supra* note 2.

57 Powers of Attorney Act, 1971, c. 27, § 4 (Eng.).

58 *See* M. BRIDGE, L. GULLIFER, G. MCMEEL & S. WORTHINGTON, THE LAW OF PERSONAL PROPERTY 29-43 (2013).

59 2011 Study, *supra* note 2. It should be pointed out that invoice discounters also sometimes refuse to finance receivables if they contain an anti-assignment clause, will only finance them on a factoring basis, or will demand a waiver. This is particularly true if, for some reason, a security interest over the supplier's assets is not taken.

60 Twelve out of the eighteen respondents agreed.

involved in obtaining a waiver was substantial or significant, and that by no means all customers were willing to agree to a waiver. Some customers would only agree to a waiver on terms that were disadvantageous to the supplier: this depended on the bargaining power between them and also on whether the financing was being sought at the beginning of the supplier/customer relationship.

In one sense, the increasing availability of supply chain financing is a workaround. This is customer driven: the customer waives the anti-assignment clause to enable supply chain financing with its nominated financier, but relies on the clause to prevent the supplier obtaining financing elsewhere. This means that the supplier is locked into the supply chain financing deal, which could be seen as anti-competitive. The discount rate for such financing is usually reasonably low since it is based on the credit rating of the (large) customer, but the period for which financing is required may be increased.[61] Nevertheless, supply chain financing does achieve protection for the customer; only invoices approved by the customer are financed, which reduces disputes, and the customer does not have to deal with a financier with whom it has no relationship.

It can be seen that the receivables industry has developed a number of workarounds which mean that, with the exception of the situation where factors cannot or do not try to obtain a waiver, receivables containing anti-assignment clauses are actually being financed. The workarounds, however, are costly in terms of time and effort, and also create more uncertainty, which can lead to costly disputes. In fact, one concern of the industry is that the existence of an enforceable anti-assignment clause may give a customer traction in disputes which it would not otherwise have, or will enable the customer to negotiate benefits for itself which would otherwise not exist. Although it is hard to prove, it seems likely that the existence of enforceable anti-assignment clauses will increase the cost of financing.[62]

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61 *See* above, [text to notes 43 – 45].

62 In the 2014 Study, eleven out of eighteen answered "always" or "sometimes" to the question: "Do you consider that (a) receivables are purchased at a greater discount to face value, or (b) the advance rate applied to the purchase of receivables will be reduced, as a result of the possibility that the contract governing

IV. INEQUALITY OF BARGAINING POWER

At this point it is necessary to consider the reasons why a customer might want to include an anti-assignment clause in a supply contract. The reasons usually given in the literature are that the customer wishes to avoid paying the wrong party, that the customer wishes to make sure that set-offs can continue to arise between it and the supplier, and that the customer wishes to continue to deal with the supplier rather than the financier, who is an unknown quantity.[63] The information gathered from the two surveys (which came from all three constituencies: customers, suppliers, and financiers) shows that the motivations are more mixed. There appeared to be little concern about paying the wrong party per se,[64] but there did appear to be genuine concern about incorrect invoicing and the sorting out of disputes.[65] It was thought that financiers would be more concerned that the invoice was paid, and would wish disputes to be sorted out afterwards between the customer and the supplier. The problem of incorrect invoicing was being tackled both by self-invoicing and electronic invoice platforms.[66] However, the desire to retain the relationship with the supplier in order to sort out disputes is ongoing.[67] Not surprisingly, opinions varied as

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the receivable may contain a valid prohibition on assignment than would apply if such prohibitions on assignment were not binding as against an assignee?" However, only a small minority answered "yes" to the question: "Do you consider that the cost of finance is increased as a result of the inclusion of a prohibition on assignment within funded ledgers?" This discrepancy may be explained by the latter question being interpreted as relating only to where receivables with anti-assignment clauses were actually included in the funded ledger, which is seldom the case in factoring arrangements.

63 *See*, *e.g.*, Orkun Akseli, Contractual Prohibitions on Assignment of Receivables: an English and UN perspective, 7 J. BUS. L. 650, 656 (2009); LOUISE GULLIFER & JENNIFER PAYNE, CORPORATE FINANCE LAW: PRINCIPLES AND POLICY 378–79 (2011); Roy Goode, *Contractual Prohibitions against Assignment*, LLOYD'S MAR. & COM. L.Q. 300, 302 (2009).

64 This was only mentioned by the financiers in the 2011 Study, but by no one else.

65 Especially evidence from customers. 2011 Study, *supra* note 2.

66 *See*, *e.g.*, TUNGSTEN, http://www.tungsten-network.com/uk/en/expertise/e-invoicing/ (last visited Jan. 22, 2015).

67 This desire was mentioned by a number of respondents to the 2014 Study.

to how helpful the financiers were in sorting out disputes and how aggressively they sought payment.

Perhaps surprisingly, the issue of set-off did not seem to be of great importance to the parties.[68] This may reflect the fact that transaction set-off, that is, set-off of cross-claims arising out of the same contract or closely related to the claim, is not affected by assignment of the receivable. The desire to lock the supplier into a supply chain finance agreement was mentioned by one respondent to the 2014 Study and one respondent to the 2011 Study mentioned one customer who wanted total confidentiality and did not want its identity revealed to a financier. However, there seemed to be considerable consensus that, in many cases, customers did not include anti-assignment clauses to prevent receivables financing, but rather to prevent "assignment" (or sub-contracting) of suppliers' obligations under the contract. Of course, under English law an obligation cannot be assigned, and so such a clause would be unnecessary, but it might be included out of ignorance or in order to make the sub-contracting of obligations a repudiatory breach, which would entitle the customer to terminate the relationship. In any event, many financiers felt that the clauses, in the form in which they precluded receivables financing, were included without a great deal of thought: out of habit or fear of the unknown or out of an over-abundance of caution by lawyers who drafted the boilerplate contract.[69]

It is certainly the case that anti-assignment clauses are generally found in standard form contracts used by large companies for their small and medium-sized suppliers.[70] The suppliers cannot negotiate the terms of the contracts and, as previously discussed, may find it difficult to obtain a waiver. Where the balance of bargaining power is reversed so that the supplier is a large company and the customer is a small company or consumer, the latter are not able to bargain for the protection of an anti-assignment clause. Control of anti-assignment clauses therefore raises the broader question of protection of small

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

[69] 2014 Study, *supra* note 2.

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

businesses against potentially unfair terms. Under English law, unreasonable exclusion and limitation clauses in standard form contracts are unenforceable against businesses of all sizes[71] and penalty clauses are sometimes unenforceable,[72] but otherwise any control of unfair terms relates to consumer contracts. The Law Commission suggested in 2005[73] that some control should be extended to contracts with micro businesses,[74] but this suggestion has not been implemented. Some of the suppliers who responded to the 2011 Study suggested that there was a problem with unfair terms in supply contracts[75] which was wider than just with anti-assignment clauses, and that either legislation or wider codes of practice[76] were needed.

If it is right that inequality of bargaining power enables large customers to impose potentially unfair terms on small suppliers, then statutory control of anti-assignment clauses could have the effect that, deprived of this protection, the customers just imposed more swingeing terms in other areas.[77]

V. The Role of Anti-Assignment Clauses in Financial Transactions

In many financial transactions, there are specific reasons for the inclusion of anti-assignment clauses that are important for the proper functioning of the market. In some cases, the clause does not ban assignment, but permits it to certain entities and requires consent

71 Unfair Contract Terms Act 1977, c. 50, §§ 3, 6(3), 7(3) (U.K.).

72 GUENTER H. TREITEL, THE LAW OF CONTRACT 20-129 to 20-145 (Edwin Peel ed., 14th ed. 2015).

73 THE LAW COMMISSION AND THE SCOTTISH LAW COMMISSION, UNFAIR TERMS IN CONTRACTS, 292 (2005).

74 Micro businesses are defined as businesses with nine or fewer employees.

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

76 *See*, *e.g.*, GROCERIES CODE ADJUCIATOR, GROCERIES SUPPLY CODE OF PRACTICE, 2009 (U.K.), *available at* https://www.gov.uk/government/publications/groceries-supply-code-of-practice.

77 For example, a term that an invoice for goods or services is not payable until the invoice has been approved by the customer. This possibility was discussed with the respondents to the 2011 Study, but is, of course, speculation because there can be no hard evidence.

for assignment to others. Thus, for example, in syndicated loan agreements, it is very common for the relevant clause to permit assignment to certain financial institutions, but require consent for assignment to others. This stems from a concern that were the loan to be assigned to, for example, a hedge fund specializing in distressed debt, it would be enforced in a much more aggressive way than it would be by a bank.[78] It also stems from a concern that a loan might be sold to one of the competitors of the borrower.[79] In derivatives contracts, which depend on close-out netting to protect against credit risk and for enforcement, it is critical that mutuality of parties is maintained and so restrictions on assignment are very important.

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

VI. SHOULD THERE BE A STATUTORY OVERRIDE?

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

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

79 THE LAW COMMISSION NO. 296, COMPANY SECURITY INTERESTS, 2005, Cm. 6654, at126, (U.K).

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

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

It is reasonably clear from both surveys[80] that some small suppliers, whom financiers will not finance on the basis of invoice discounting because of concerns about their ability to collect in the receivables and hold them on trust for the financier, are unable to have certain invoices financed because they contain anti-assignment clauses. The only way round this problem is for the customer to waive the clause, and this is only possible on some occasions. Often it will not be possible, either because the costs of waiving outweigh the benefits to both the supplier and the financier, or because the supplier has little bargaining power compared to the customer. The U.K. Government is very concerned about the funding of small businesses at the moment: they are seen as critical to economic recovery.[81] The effect on small businesses, then, is a good reason for a statutory override of anti-assignment clauses.

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[80] It should be born in mind that both surveys were fairly small-scale.

[81] *Small Business, Big Support Confirmed by Prime Minister*, GOV.UK (Jan. 27, 2014), https://www.gov.uk/government/news/small-business-big-support-confirmed-by-prime-minister.

It is also clear that the presence of such clauses leads to costs for the financing industry. While it should not be overemphasized,[82] there is the cost of discovering such clauses. Waivers can also be costly, as is the development and execution of the workarounds discussed above. Moreover, the existence of the workarounds themselves increases *ex ante* uncertainty, both in terms of the law[83] and also in that it increases the possibility of disputes. Finally, the law itself is complex and uncertain. A financier cannot be sure that it has a valid interest in a receivable containing an anti-assignment clause. It is clearer that it has an equitable interest in the proceeds, but this is not any good if the proceeds are not traceable.

Are these costs outweighed by the benefits of the clauses? It is clear that such clauses are of value in the context of financial contracts. However, some of the reasons why customers seem to include them in their contracts are of little or no merit,[84] and the results from the (small-scale) surveys suggest that some do not seem of concern in the real world.[85] The concern about preserving a relationship with the supplier in the event of dispute or incorrect invoices is a real one. Yet, the latter concern can be overcome with modern invoicing techniques, and the former argument is undermined by the fact that customers are prepared to permit assignment to a financier of their choice under a supply chain finance scheme. The argument that a financier might be more aggressive than a supplier in enforcing invoices is also flawed, since the risk of a third party influencing enforcement is an ever present one: the supplier could be taken over by more aggressive management. The customer's concern to remain in a relationship with the supplier may have more to do with the fact that the supplier is a small business compared to the customer, and therefore the customer is more likely to have the upper hand in negotiations than it would with

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

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

84 The prevention of sub-contracting does not require an anti-assignment clause, and the "habit" or "fear of the unknown" reasons seem unmeritorious.

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

a financier. The use of an anti-assignment clause to lock a supplier into supply chain financing also seems unmeritorious. If the supply chain financing was sufficiently attractive to the supplier, it would choose it over other sources of financing.

This brings us to the argument that a statutory override would do little harm, and could do some good in clarifying the law. One possible harm, however, is that the override is not sufficiently limited and might cause problems in the financial markets. This is a serious risk, but could be overcome by careful drafting, even if this were at the expense of not including some borderline cases within the override. Another possibility is that an override may lead to harsher terms being imposed by large customers on small suppliers in other areas. This again would be serious, but could be controlled by a code of practice.[86] It therefore seems that the benefit in clarifying the law would outweigh any possible detriment.

CONCLUSION

This paper has sought to elucidate the arguments both for and against a statutory override of anti-assignment clauses in English law. It is suggested that the arguments are not ones of principle, or even policy, but are more pragmatic. Since such clauses have not ever been the subject of statutory intervention, the common law has developed in such a way as to give all parties limited protection, and the industry has worked around the law to enable receivables financing to take place. However, on the basis of two recent surveys, the pragmatic arguments are assessed, and it appears that a statutory override would be beneficial.

[86] *See*, *e.g.*, GROCERIES CODE ADJUCIATOR, GROCERIES SUPPLY CODE OF PRACTICE, 2009 (U.K.), *available at* https://www.gov.uk/government/publications/groceries-supply-code-of-practice.