THE CITY OF LONDON LAW SOCIETY

4 College Hill
London EC4R 2RB

Telephone 020 7329 2173
Facsimile 020 7329 2190
DX 98936 – Cheapside 2
mail@citysolicitors.org.uk
www.citysolicitors.org.uk

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Mrs Jean McMahon
Ministry of Justice
Private International Law Team,
International Directorate 5.38,
Fifth floor 102 Petty France
London SW1H 9AJ

By post and email: jean.mcmahon@justice.gsi.gov.uk

Dear Mrs McMahon

Response by the City of London Law Society's Financial Law Committee to the Discussion Paper by the Ministry of Justice entitled "European Commission Review of Article 14: Assignment"

The City of London Law Society ("CLLS") represents approximately 13,000 City lawyers, through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi-jurisdictional legal issues.

The CLLS responds to Government consultations on issues of importance to its members through its 17 specialist Committees. A working party of the CLLS Financial Law Committee, made up of solicitors who are experts in their field, have prepared the comments below in response to the proposals contained in the discussion paper by the Ministry of Justice entitled "European Commission Review of Article 14: Assignment".

The members of the working party comprise:

- Dorothy Livingston (Chairman) – Herbert Smith LLP
- Tolek Petch – Slaughter and May
- Andrew Dickinson – Clifford Chance LLP
- Richard Calnan - Norton Rose LLP
- Ian Falconer – Freshfields Bruckhaus Deringer LLP

Our responses to the questions listed at the end of the consultation paper are as follows:

United Kingdom compromise
Question 1: Is the general scheme of the proposed solution satisfactory?

1. We agree with the general proposition that the same law that applies to "paragraph 2 issues" should also apply to "paragraph 3 issues", i.e. the law governing the assigned or subrogated claim. We believe that this would

   (a) avoid the artificial differentiation between the assignability of the debt and the question to whom the debtor needs to pay the assigned debt (paragraph 2 issues) and the question who has the better "proprietary" right to the debt (paragraph 3 issue) and, consequently, the difficulties arising from a need to classify an issue as falling either within paragraph 2 or paragraph 3;

   (b) be fairer to the assignee, whose rights should not be effected by the subsequent involvement of a third party outside of the assignee's control;

   (c) be both logical (that was the law by which the debt was created) and result in enhanced certainty, as the law applicable to the claim is normally clear (it will be specified in the contract) and remains constant, while the law of the habitual residence of the assignor will differ, in particular in the case of subsequent assignments;

   (d) give the best effect to the principle of the parties' autonomy to choose the law applicable to all aspects of the debt that they have created.

2. We do not believe that a sufficient case has been made out for the inclusion of exceptions to the proposed general rule with respect to factoring or consumer assignors, for the following reasons:

   Relevant to both exceptions

   (a) The thrust of EU law and other Directives in the field of private international law is to recognise the vulnerability of consumers and to afford them the convenience of being able to litigate in their home courts and, while respecting the right of party autonomy in commercial contracts, protect them in key areas from exposure to complex issues in which a foreign law may be involved. It is our understanding, in the areas where exceptions are sought and the transaction involves consumers (or private individuals operating unincorporated businesses), that the consumer will typically be the primary debtor, not the assignor or assignee, although sometimes the assignor and/or assignee might also be an individual.

   (b) Further, we see no logical or practical reason to introduce exceptions to the proposed general rule, and we set out below how we have reached this view in relation to the proposed exceptions. The more exceptions that are made to the rule, the more uncertainty is created and the greater the opportunity for arbitrage.

   Factoring

   (c) It is understood that the practice in (discounted) factoring is for factors not to concern themselves with the assignability or enforceability of the debt against the debtor and that their main concern is whether or not they have a better right compared to e.g. a competing assignee or charge holder.

Otherwise (if they were concerned about assignability and enforceability) the application of the law of the assignor's habitual residence simply to paragraph 3 issues would not assist factors and the same law would need to be applied to paragraph 2 issues (which is not being suggested and would be unacceptable to the debtor).

(d) The application of the law of the assignor's habitual residence to paragraph 3 issues is nevertheless likely to affect the debtor in cases where competing assignees (one of which may be a factor) pursue the debtor for payment based on their respective assertions that they have the better ultimate right to the debt. This may be the case where the assignor is no longer able to collect in the debt on behalf of the factor (e.g. has been wound-up or ceases to trade) and the factor is required to pursue the debt in competition with any other assignees or charge holders. In this case the involvement of a second law unconnected with the debt governing the question of who has the best title to the debt (and is ultimately entitled to the proceeds) would potentially be onerous upon the debtor and complicate any litigation in which the debtor is likely to be embroiled. We have had the benefit of considering Professor Goode's arguments for a separate rule (attached to his email of 4 February 2010: "A note on Article 14 of Rome I") but cannot see how the debtor can be kept out of the equation where the debt has not yet been discharged (his examples are based on scenarios in which the debt has already been discharged) and the debtor is faced with competing assignees.

(e) Regardless of the point made above we are not convinced that the issue raised on behalf of the factoring industry is of sufficient practical importance to merit an exception. We would expect that in most cases factors will take a bulk assignment of debts originating from, and likely governed by the laws of, one country (and enquire about the law of that country) rather than originating from a number of different countries. We suspect that the issue has been raised predominantly by the factoring industry in the US where assignment may indeed be taken of debts originating from different (federal) states (rather than different countries). However, differences between the national laws of EU member states relating to the assignment of receivables will potentially be far more pronounced than those within the US and the potential application of a third country's (rather than another federal state's) law to paragraph 3 issues is therefore likely to result in greater complications in any proceedings brought against the debtor, whether in the debtor's jurisdiction or elsewhere.

(f) If an exception were to be proposed for factoring we agree that such an exception would need to be drafted with extreme care to limit the exception to factoring, to avoid uncertainty as to its application to other forms of bulk assignment (e.g. securitisations).

Consumer Assignors

(g) It is unclear how the proposed exception will benefit the consumer assignor, unless it is proposed that both paragraph 2 and paragraph 3 issues are governed by the law of the assignor's habitual residence (which would be unacceptable both as a matter of principle and as undermining party autonomy, from the debtor's perspective).

(h) In any event, we cannot see how the issue raised is of sufficient practical importance to merit an exception to the general proposed rule. Although in certain exceptional circumstances a consumer might be the assignor of a debt, typically the consumer will be the debtor rather than the creditor. In this case, it will be in the debtor consumer's interest to have both paragraph 2 and paragraph 3 issues governed by the law of the assigned debt.

(i) If there are jurisdictions where assignments by consumers to commercial parties (e.g. to create a form of security) are common, then the "consumer protection rule" might be thought to justify this exception. But even then the assigned claims may be against other consumers whose rights as primary debtors should prevail. Therefore any exception should not be applicable with regard to any assignment of rights against a consumer, where the law of the original debt should be paramount.

(j) Although a claim against a commercial party, there are also difficulties for insurance policies related to land which may be assigned in the context of a mortgage and where it is more appropriate to have the law of the policy (which is likely to be the law of the country in which the land is situated) to govern both paragraph 2 and paragraph 3 issues, rather than introducing the law of the country of the insured's habitual residence into the equation. See also below under Question 6.

Judgment debts

Question 2: Should there be a rule that the assignment of judgment debts is governed by the law of the court that granted the judgment; and should this apply to paragraph 2 issues as well?

We see no need for a special rule for judgment debts and believe that the general rule already contained in Article 14(2) (regarding paragraph 2 issues) and the proposed general rule (regarding paragraph 3 issues), i.e. that both paragraph 2 and paragraph 3 issues be governed by the law of the obligation assigned (i.e. the law of the judgment debt rather than the law of the obligation adjudicated upon) should also apply to judgment debts. The proposed reference to the "law of the country in which the court was situated " has the potential of causing confusion and uncertainty e.g. where a judgment is recognised for enforcement in several different jurisdictions by different courts or courts of different instances are involved which are not situated in the same state or country (e.g. in the case of federal states or the Privy Council). At the most, a recital should confirm that Article 14 applies to the assignment of judgment debts.

Intellectual property

Question 3: Should special provision be made for assignments of intellectual property? If so, should the applicable law be that under which the IP right arose or was created? Should this apply to paragraph 2 issues as well?

One view is that Article 14 does not apply to the primary assignment of intellectual property rights and it is perhaps more appropriate to clarify that Article 14 does not apply, as the assignment of intellectual property rights does not involve a "debtor" in the normal sense.

However, if it is considered beneficial to bring the assignment of intellectual property rights within the scope of Article 14 (which would require clarification and an examination of its compatibility with existing international conventions and other EU intellectual property legislation) we agree that the proposed rule is sensible and we see no need for and are opposed to exceptions being made to this rule either for factoring or natural persons acting as consumers for the reasons set out above.

Shares

Question 4: Should special provision be made for assignments of shares in companies? If so, would it be satisfactory to apply the law governing the share agreement, normally that of the habitual residence of the company? If so, should there be a further exception to the proposed paragraph 3(b) under which shares are also excluded from the rule in that paragraph?

1. We suggest that, if there is to be a rule, the most sensible rule is to apply the law of the place of incorporation of the company both to paragraph 2 and paragraph 3 issues. We see no need for and are opposed to the provision of factoring or consumer exceptions in relation to this rule. We believe this to be the most sensible rule, as this will

   (a) normally be the law that will govern all other constitutional matters;

   (b) provide for the greatest certainty as the place of incorporation will be easily determinable and will be constant.

   This would be the position as a matter of company law and, given the separate suite of EU company laws, it may be simpler to continue the (assumed) exclusion of such assignments from Article 14.

2. However, if a rule is introduced, we believe that the above rule should only apply to shares that are held directly by shareholders and that intermediated securities should be excluded from the scope of Article 14 and, indeed, the scope of the Regulation generally. Intermediated securities are already the subject of special regulations (Financial Markets and Insolvency (Settlement Finality) Regulations 1999 and Financial Collateral Arrangements (2) Regulations 2003), and the application of the proposed rule would cut across the approach taken in these regulations.

Letters of credit

Question 5: Is it necessary to make special provision for letters of credit? Should letters of credit be excluded from the rule in paragraph 3(b)?

Question 6: Should there be a further exception to the proposed paragraph 3(b) under which insurance policies are also excluded from the rule in that paragraph?

As set out above we do not believe that a sufficient case has been made out for a consumer exception to the general proposed rule. The suggestion that these exceptions may have to be made to the proposed consumer exception is a further factor that militates against a consumer exception which causes such complications.

Tort or delict claims

Question 7: Should the proposed paragraph 3 apply to the subrogation (both by operation of law and under a contract) and assignment of claims in tort or delict? If so, should the applicable law be determined by the general rules or is special provision necessary?

Our view is that paragraph 3 issues should be governed by the law of the tort. This would provide for reasonable certainty (the law of the tort will be determinable under Rome II once the tort claim arises) and would avoid unfair preference being given to one assignment or subrogation over another.

This response is not confidential and we have no objection to its public disclosure.

Yours sincerely

David McIntosh
Chair
CLLS

THE CITY OF LONDON LAW SOCIETY
FINANCIAL LAW COMMITTEE

Individuals and firms represented on this Committee are as follows:

Ms. D.K. Livingston (Herbert Smith LLP) (Chairman)

R.J. Calnan (Norton Rose LLP)

M. Campbell (Clifford Chance LLP)

J. Curtis (Denton Wilde Sapte LLP)

J.W. Davies (Simmons & Simmons)

D.P. Ereira (Linklaters LLP)

M.N.R. Evans (Travers Smith LLP)

J. Naccarato (CMS Cameron McKenna LLP)

A. Newton (Freshfields Bruckhaus Deringer LLP)

R.E. Parsons (Sidley LLP)

Ms J. Paterson (Slaughter and May)

S. Roberts (Allen & Overy LLP)

N.T. Ward (Ashurst LLP)

P.R. Wood (Allen & Overy LLP)(Emeritus)

G.B.B. Yeowart (Lovells LLP) (Deputy Chairman)