Patience is a virtue – The third party effects of assignments in European Private International Law

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The third-party effects of the assignment are one of the "most discussed questions of international contract law" as it concerns the "most important gap of the Rome I Regulation". This gap is regrettable not only for dogmatic reasons, but above all for practical reasons. The factoring industry has provided more than 217 billion euros of working capital to finance more than 200,000 companies in the EU in 2017 alone. After a long struggle in March of 2018, the European Commission, therefore, published a corresponding draft regulation (COM(2018)0096; in the following Draft Regulation). Based on a recent article (ZEuP 2019, 41) the following post explores whether the Draft Regulation creates the necessary legal certainty in this economically important area of law and thus contributes to the further development of European private international law (see also this post by Robert Freitag).

Legal background and recent case law

Although Article 14 of the Rome I Regulation provides for a rule governing the question regarding which law is applicable to the voluntary assignments of claims, it is the prevailing opinion that the third party effects of assignments are not addressed within the Rome I Regulation. According to Article 27 (2) of the Rome II Regulation, the European Commission was

under the obligation to submit a report concerning the question of the effectiveness of an assignment or subrogation of a claim against third parties and the priority of the assigned or subrogated claim over a right of another person. Said report should have been published no later than 17 June 2013. In March 2018, almost nine years after the Rome I Regulation came into force, the Commission finally presented said report in form of the Draft Regulation subject to this article. The practical importance and the need for a harmonized European approach have also been demonstrated by recent case law proving the rather unsatisfactory status quo in European PIL. Two recent decisions of the Higher Regional Court of Saarbrücken (dated 8 August 2018 – 4 U 109/17) and of the Norwegian Supreme Court (see IPRax 2018, 539) gave striking examples of how the diverging requirements for the effectiveness of the assignment vis-à-vis third parties lead to different solutions within the respective PIL rules of the member states. The preliminary reference to the ECJ of the Higher Regional Court of Saarbrücken concerns a multiple assignment, while the ruling of the Norwegian Court of Justice deals with the question whether unsecured creditors of the assignor can seize the allegedly assigned claims of the assignor in insolvency (see also this post by Peter Mankowski).

The material scope of the proposed regulation

Art. 5 of the Draft Regulation determines the material scope of application of said Draft Regulation with regard to the effectiveness of an assignment as well as its priority vis-à-vis third parties. The effectiveness vis-à-vis third parties is regularly determined by registration or publication formalities (lit. a), while priority conflicts for the assignee arise vis-à-vis various persons. Lit. b) concerns multiple assignments, while lit. c) regulates the priority over the rights of the assignor's creditors. In addition, lit. d) and e) assign priority conflicts between the assignee and

the rights of the beneficiary of a contract transfer/contract assumption and a contract for the conversion of debts to the Draft Regulation.

In essence, Art. 5 of the Draft Regulation covers notification requirements to the assignee. Most legal systems require a publicity act for binding effects vis-à-vis third parties and the debtor, such as a notice of assignment to the debtor or a registration in a public register. Whereas under German law the assignment becomes effective immediately between the assignor and the assignee as well as against third parties, in other jurisdictions this only applies once the debtor has been notified of the assignment (*signification* in French law pursuant to former Art. 1690 of the Code civil or within the framework of legal assignment in the UK).

Connecting factor: habitual residence of the assignor combined with sectorial exceptions

The connecting factors employed by current national PIL rules considerably vary between the member states. In principle, three connecting factors compete with each other: the habitual residence of the assignor, the law applicable to the transfer agreement (assignment ground statute) and the law applicable to the transferred claim. Furthermore, the law at the debtor's domicile might also be considered an important factor.

Art. 4 (1) of the Draft Regulation unties this gordic knot as it specifies the law of the country in which the assignor has his habitual residence "at the relevant time" as the primary connecting factor. The goal of the European Commission is to create legal certainty and, above all, to promote cross-border trade in claims. By way of sectoral exceptions, the law of the transferred claim is to be applied if either (i) "cash collateral" credited to an account or (ii) claims from financial instruments are transferred (Art. 4 (2) of the Draft Regulation).

A downside of the link to the law of habitual residence is its changeability, which may lead to a *conflit mobile*. By altering the connecting factor, the applicable law may also change leading to legal uncertainty. To overcome such conflict, so called meta conflict of laws rules are also provided for in the Draft Regulation. In this case, it is a matter of determining the relevant point in time in order to make a viable connection. This rule has been implemented in Art. 4 (2) of the Draft Regulation.

An unsolved problem is the determination of the "material point in time" cited in Art. 4 (1) of the Draft Regulation. Accordingly, the third parties' effects are determined by the assignor's habitual residence at the relevant time. However, neither a recital nor the catalogue of Art. 2 of the Draft Regulation give an adequate definition of this relevant point in time so far. It is therefore advisable to replace the term "at the relevant time" with "at the time of conclusion of the assignment contract" in the final regulation. This is also reflected in the EP's legislative resolution of 13 February 2019 (P8_TA-PROV(2019)0086, p. 12). The advantage of this clarification would be that the same point in time would be relevant in the legal systems of the member states which follow the principle of separation as well as those which follow the principle of unity.

A step forward?

The Draft Regulation would represent a major step forward in the trade of cross-border receivables in the EU. It closes a large gap within European PIL, while at the same time aiding EU member states to partly adapt their domestic legal system accordingly. Even if the European Commission did not comply with the (unrealistic) deadline for the review cited in Art. 27 (2) of the Rome I Regulation, the legal debate made this essential progress possible demonstrating the EU's ability to reach compromises. Although the Draft Regulation solves many problems, it may also raise new ones. That is again good news

for lawyers interested in PIL. Nevertheless, the enactment of the Draft Regulation would eventually answer “one of the most frequently discussed questions of international contract law”. The old saying “patience is a virtue” would be proven right again.

This blog post is a condensed version of the author’s article in ZEuP 2019, 41 et seqq. which explores the new Draft Regulation in more detail and contains comprehensive references to the relevant literature.