

**REPORT OF THE COMMITTEE TO HARMONIZE
NORTH AMERICAN LAW WITH REGARD TO THE
ASSIGNMENT OF RECEIVABLES IN INTERNATIONAL
TRADE CONVENTION**

NATIONAL CONFERENCE OF COMMISSIONERS
ON UNIFORM STATE LAWS

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WITH REGARD TO THE ASSIGNMENT OF RECEIVABLES IN
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REPORT OF THE COMMITTEE TO HARMONIZE NORTH AMERICAN LAW WITH REGARD TO THE ASSIGNMENT OF RECEIVABLES IN INTERNATIONAL TRADE CONVENTION

The Committee to Harmonize North American Law with regard to the Assignment of Receivables International Trade Convention (the “*Committee*”) was formed as a joint undertaking of the National Conference of Commissioners on Uniform State Laws (the “*Conference*”) and the American Law Institute (the “*ALI*”) to work with the Uniform Law Conference of Canada and the Uniform Law Center of Mexico with a view to harmonizing the commercial laws of all three countries consistently with the United Nations Convention on the Assignment of Receivables in International Trade (the “*Convention*”). This paper is the report of the Committee to the Conference in connection with the 2007 annual meeting of the Conference in Pasadena, California.

The report first provides some background relating to the Convention and the Convention’s relationship to Article 9 of the Uniform Commercial Code as promulgated by the Conference and the ALI (“*Article 9*”). It then provides some background relating to the project and a description of the process by which the Committee carried out its work. It then explains the product of the Committee and the future processes for achieving the harmonization objective. It concludes with some general remarks.

Background Relating to the Convention

The Convention addresses the assignment of receivables. “Receivables” are defined in the Convention as contractual rights to payment, and “assignment” is defined to include both the creation of a security interest in receivables to secure an obligation and an “outright sale” of receivables. The scope limitations in the Convention exclude transactions in securities, derivatives and other financial assets, assignments of deposit accounts, and assignments of claims under letters of credit and independent guaranties. Additional rules in the Convention protect those who are holders of negotiable instruments or assignees of certain real estate lease receivables. Accordingly, the Convention rules relate primarily to assignments of trade, loan and similar commercial and consumer receivables arising in asset-based lending, factoring, securitization and project finance transactions.

For the Convention to apply to an assignment of a receivable, either the assignment or the receivable must be international; i.e., the assignor and the assignee must be located in different countries or the assignor and the account debtor must be located in different countries. Also, for the Convention to apply, the assignor must be located in a country that has adopted the Convention. For the rights or obligations of the account debtor to be affected by the Convention, either the account debtor must be located in a country that has adopted the Convention or the contract from which the receivable arises must be governed by the law of a country that has adopted the Convention. The Convention provides specific rules to determine where an assignor, assignee or account debtor is “located”. Once the Convention applies to an assignment of a receivable, it applies to a subsequent assignment of the receivable.

The Convention was approved by the United Nations General Assembly on December 12, 2001. The Convention has been adopted by Liberia. It has been signed but not adopted by Luxembourg, Madagascar and the United States. Five adoptions are required for the Convention to enter into force. A copy of the Convention may be found at www.unictr.org and is also attached to this report.

Relationship of the Convention to Article 9 of the Uniform Commercial Code

Many of the transactions in receivables covered by the Convention are those that are, as a matter of state law in the United States, largely governed by a Conference and ALI product - Article 9. Fortunately, the drafting process for both the Convention and the recent revisions to Article 9 coincided. Those from the United States who negotiated the Convention also participated in the drafting of the Article 9 revisions.¹ Issues raised in negotiating the Convention were considered by the Article 9 drafting committee, and issues raised in the Article 9 drafting committee meetings were considered in the negotiation of the Convention. The result was a desirable harmony between the rules of the Convention and provisions of the Article 9.

The main differences between the rules of the Convention and the provisions of Article 9 relate to scope and choice-of-law. Some assignments of receivables are excluded from the scope of the Convention but are included within the scope of Article 9. Examples would be assignments of receivables consisting of security interests in deposit accounts or in security entitlements. Other assignments of receivables are included within the scope of the Convention but are outside of the scope of Article 9. An example would be an assignment of an insurance claim that is neither a health-care-insurance receivable nor an insurance claim that arises out of a casualty loss to collateral covered by Article 9.

The differences in choice-of-law-rules are largely confined to a small subset of the rules that determine which jurisdiction's law governs the perfection and priority of a security interest in a receivable. To be sure, both the Convention and Article 9 generally look to the law of the location of the assignor to determine the perfection and priority of a security interest in a receivable. There are three differences, though, between the Convention choice of law rules and the parallel Article 9 rules. First, in the relatively uncommon situation in which an assignor that is a U.S. corporation or other registered organization has its place of central administration outside the United States, the Convention provides that that assignor is located in the country of central administration rather than in the U.S. state of organization. Second, the Convention applies the law of the country in which the assignor is located even if that law does not meet the criteria set out in Section 9-307(c) of Article 9.² Third, the Convention rule for determining which law governs perfection and priority applies to "reified" receivables, such as tangible chattel paper and Article 9 instruments. However, under Article 9, priority for those types of

¹ The United States delegation was led by Harold Burman of the State Department. The other United States delegates were Professor Neil Cohen, Harry Sigman and Edwin E. Smith, all members of the drafting committee that revised Article 9 from 1993 to 1998, and Professor Peter Winship, who participated in many of the drafting committee meetings.

² Section 9-307(c) in some circumstances would view a foreign assignor to be located, for Article 9 purposes, in Washington, D.C.

collateral is governed by the law of the state or country in which the collateral is located, as is perfection in the case of possessory security interests.

Nevertheless, the Convention and Article 9 are largely consistent with each other. The differences in scope do not suggest any inconsistency between the Convention and Article 9. Inconsistency is a concern only in the case of a transaction that is within the scope of *both* the Convention *and* Article 9. Furthermore, with the exception of, in some cases, choice-of-law for determining the perfection and priority of security interests in receivables, the other substantive and choice-of-law rules of the Convention are substantially consistent with those of Article 9.³ As further explained below, consistency with Article 9 will be maximized through the use of declarations⁴ to the Convention that the Committee proposes.

Background Relating to the Project

As part of the efforts of the Conference to explore possible joint products with the Uniform Law Conference of Canada and the Uniform Law Center of Mexico, the Uniform Law Conference of Canada and the Uniform Law Center of Mexico expressed to the Conference's leadership in the Summer of 2005 an interest in working with the Conference and the ALI on a project for Canada, Mexico and the United States to harmonize their domestic laws to conform to the rules of the Convention so that cross-border receivables financing among the three countries could receive the benefits of the Convention.

Of course, for members of the Conference, the benefits of harmonization of laws are well known, especially in the field of commercial law. Cross-border harmonization of commercial laws provides greater certainty for transacting parties and reduces transaction costs. These benefits are much like those experienced by the states of the United States from the uniform law process when the states enacted the Uniform Commercial Code and other uniform state laws in the commercial law field.

After approval of the project by the Conference's executive committee and the ALI Council, the Committee was formed, with Commissioner Edwin E. Smith acting as the U.S. Chair, Ms. Kathryn Szabo acting as the Canadian Chair and Carlos Sanchez-Mejorada y Velasco acting as the Mexican chair. Steven O. Weise served as the U.S. reporter. Conference members consisted of Professor Carl S. Bjerre, Dimitri Karcazes and Professor Kathleen Patchel. ALI members consisted of Professors Neil B. Cohen and Steven L. Harris. The Committee benefited greatly from the participation of the Canadian and Mexican members and a wide variety of advisors and observers.

At first the project was contemplated as a domestic law harmonization process whereby the laws of the three countries would be harmonized insofar as necessary to bring about the same results, in transactions among the three countries, as would be the case if all three countries had

³ For a fuller discussion of the provisions of the Convention in comparison to Article 9, see Sigman and Smith. "Toward Facilitating Cross-Border Financing and Securitization: an Analysis of the United Nations Convention on the Assignment of Receivables in International Trade", 57 *The Business Lawyer* No. 2 (Feb. 2002).

⁴ By a "declaration" the adopting country modifies or supplements a provision of the Convention in a manner permitted by the Convention.

ratified the Convention. Under this approach, consideration was given to the preparation of supplementary choice-of-law rules for Article 9 that would apply to these situations. A copy of the Committee's draft of these supplementary choice-of-law rules is attached to this report. Of course, it was envisioned that such rules would not preclude any of the three countries from adopting the Convention on a national or federal level, whether as part of the harmonization process or as a second step.

However, as the project proceeded, interest in the Convention among Committee members, advisors and observers grew to the point that ratification by all three countries appeared to be most efficient method of achieving harmonization. Ratification of the Convention quickly appeared to be the preferred approach in Canada and Mexico. The representatives of the Uniform Law Conference of Canada explained that, because of Canada's federal system, adoption of the rules of the Convention would be most efficient if the Convention were adopted at both the federal level and at the provincial and territorial level in the Canada. The representatives of the Uniform Law Center of Mexico explained that, because commercial law is federal law in Mexico, adoption of the Convention by Mexico would be the most efficient method for Mexico to implement the rules of the Convention.

Members of the Committee from the Conference and the ALI were likewise persuaded to proceed on a tentative basis with recommending a ratification approach. Their views were largely influenced by a determination by the State Department that ratification of the Convention by the United States was a distinct possibility. Moreover, given the changes that would need to be made to the choice-of-law rules of Article 9, there was significant concern that transactions could be disrupted or become more expensive if not all states enacted the changes at a substantially identical time. Accordingly, a process involving enactment of state law amendments to Article 9 in more than 50 jurisdictions in the United States to obtain harmonization was viewed to be less efficient and, indeed, more highly disruptive to ongoing affected transactions than ratification itself.

Members of the Committee also were persuaded by the view of the State Department that no implementing legislation would be required in connection with ratification of the Convention, either at the state or the federal level. The Convention did not itself require implementing legislation by state or other territorial units in the United States as part of the ratification process in contrast to some treaties that do require such implementing legislation. Nor, following the tradition of the United Nations Convention on Contracts for the International Sale of Goods and the recently ratified Cape Town Convention on International Interests in Mobile Equipment, did the State Department see the need for any implementation of the Convention by federal legislation. For practitioners familiar with Article 9 but who might not be otherwise aware of the Convention, the Committee understood that the Permanent Editorial Board of the Uniform Commercial Code would consider expanding the Official Comments to Article 9 to point out those areas where the Convention choice-of-law rules might lead to a different conflict of laws result than the result obtained by following strictly the choice-of-law rules of Article 9.

Once the tentative decision was made to recommend ratification of the Convention without separate implementing legislation, the work of the Committee consisted in formulating

recommendations for declarations and understandings⁵ by the United States designed to maximize the consistency between the rules of the Convention and the provisions of Article 9.

The Process

The Committee's deliberations proceeded in three steps. The first was a series of Drafting Committee meetings held on April 21-23, 2006, in Detroit, June 17 and October 16, 2006, in New York City and November 17-18, 2006, in Chicago, at which representatives from all three countries, in consultation with advisors and observers, accomplished a number of tasks. First, they educated each other on their own domestic laws pertaining to transactions contemplated by the Convention. Second, they educated each other on the processes in their own countries for reforming their domestic laws to be consistent with the rules of the Convention. Third, they explored ways in which they might shape their own domestic law changes so as to lead to the most transparent and consistent results among the three countries.

The representatives of each country benefited significantly from comparing issues confronting them in their own countries and, where an issue was not isolated to a particular country, seeking common solutions among the three countries.

Once the decision was made to work on ratification of the Convention, the Committee proceeded to a second step in the United States to "test the market". With the joint sponsorship of the Conference, the State Department's Legal Advisor's Office for Private International Law and other organizations,⁶ the Committee held open symposiums in New York City on October 16, 2006, and in Los Angeles on December 20, 2006, which a number of legal practitioners and representatives from financial institutions attended.⁷ At these symposiums, the rules of the Convention were explained in the context of specific hypothetical transactions.⁸ The overwhelming reaction of the audiences was favorable to the efforts of the Committee and reinforced the view of the State Department that ratification by the United States was a distinct possibility.

Following its "market testing", the Committee proceeded with a third step. The third step consisted of a series of conference calls that included advisors and observers,⁹ occurring two or three times each month, to draft the declarations and understandings that would be recommended to the State Department for submission to the United States Senate in connection with the

⁵ In an "understanding" the adopting country sets forth its interpretation of a particular provision of the Convention without modifying or supplementing it.

⁶ The other co-sponsoring organizations were the American Bankers Association, the American Bar Association (Business Law Section), the American College of Commercial Finance Lawyers, the Bankers' Association for Finance and Trade, the Commercial Finance Association and the New York City Bar Association.

⁷ In addition to representatives of various law firms, the October 11, 2006, meeting was attended by representatives from Bank of America, Citicorp, Cardozo School of Law, Columbia University School of Law, GMAC, JPMorgan Chase, Merrill Lynch, PNC Bank, UBS, Wachovia and US Bank as well as Standard & Poor's.

⁸ Participating on the panels at the October 16, 2006, meeting were representatives from the American College of Commercial Finance Lawyers, the Commercial Finance Association, the Loan Syndication and Trading Association and the American Securitization Forum. Panelists included Canadian and Mexican participants as well as U.S. participants.

⁹ The conference calls took place on February 1, February 8, February 26, March 19, March 28, April 5, May 1, May 8, May 21, June 5, and June 11, 2007.

Convention ratification process. In addition, the Committee drafted various background papers for consideration by the State Department for inclusion in its report to the United States Senate recommending ratification. In this third step, the expertise of the Conference and the ALI was critical in providing the technical skills to address how the Convention could be implemented by the United States in a manner that was most consistent with Article 9.

The Product

The product of the Committee, for consideration by the State Department, consists of (a) draft declarations and understandings to accompany ratification of the Convention by the United States, (b) a draft report of the United States Senate Foreign Relations Committee to the United States Senate recommending ratification of the Convention and (c) a draft of an article-by-article summary of the Convention for submission by the State Department to the President of the United States. The draft of the declarations and understandings and the draft Senate Foreign Relations Committee report are attached to this report. It is anticipated that a draft of the article-by-article summary will be available at the 2007 annual meeting of the Conference.

The draft report contains the proposed declarations and understandings. The most significant of these are the declarations permitted by articles 36 and 37 of the Convention. These declarations are designed to allow the Article 9 choice-of-law rules for perfection or priority of security interests in receivables within the scope of Article 9 to operate within the United States when the Convention requires that the law of a jurisdiction within the United States govern the perfection or priority of the security interest.

The Future Processes

It is envisioned that the State Department will consider the product of the Committee in formulating its report to the United States Senate recommending ratification of the Convention. The Senate Foreign Relations Committee will consider the State Department's report and submit its own report to the United States Senate. If the Senate ratifies the Convention, the Convention will become effective for the United States six months after the instrument of ratification has been deposited with the Secretary-General of the United Nations or, if less than five countries have by then adopted the Convention, then six months after the fifth adopting country has deposited its instrument of ratification or adoption with the Secretary-General.

The process in Canada will likely proceed concurrently with the United States ratification process. Even though under the Canadian federal system each Canadian province or territory must accede to the Convention for the Convention to be effective in that province or territory, it is contemplated that the accession document will be structured so as to become effective when a requisite number of provinces and territories have acceded.

It is unlikely that Mexico will seek to adopt the Convention in the near term. However, the adoption of the Convention by Canada and United States will likely encourage adoption by Mexico, with the work of the Committee providing much of the groundwork.

Concluding Remarks

The Committee appreciates that the project was an extraordinary effort of the Conference in the international field. While the approach taken by the Committee was one of facilitating the implementation of federal law through a treaty ratification process rather than drafting a recommended uniform state law, the Committee felt that it carried out its work in the finest tradition of the Conference in protecting and preserving much of state law.

This is the case for several reasons. The first is that the Convention itself rests largely on principles, if not the substantive law itself, developed by the Conference and the ALI through the Uniform Commercial Code. The second reason is that, through the development of the declarations and understandings to accompany the United States Senate's ratification of the Convention, the Conference and the ALI maximized the consistency of the rules of the Convention with the provisions of state law, particularly Article 9. Third, the Committee was able to employ the historical skills and expertise of the Conference in harmonizing laws reflecting principles embodied in Conference products such as Article 9.