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**The Legal Position of an Assignee in Assignor's  
Insolvency**

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## The Legal Position of an Assignee in Assignor's Insolvency

Belarusian law does not recognize security consequences of outright assignment of claims (assignment of receivables). By contrast, a pledge is the method to create a security interest in receivables, where a pledgee does not acquire title to the encumbered property. Classical assignment mechanism (*cessio*) results in a transfer and has never been addressed as a security instrument.

Articles 353-361 of chapter 24 'Substitution of parties in obligations' of the Republic of Belarus Civil Code N 218-Ç of 07.12.1998 (Hereafter Civil Code) sets out the following rules:

- Rights (claims) belonging to a creditor on the ground of an obligation may be transferred to another person by contract or by law (art. 353 (1)).
- Debtor's consent is not required (art. 353 (2)).
- Where debtor was not notified about the transfer assignee shall bare the risk of adverse results of assignment (art. 353 (3)).
- Transfer of personal rights is not allowed (art. 354).
- The amount of the right transferred shall be determined according to the moment of the transfer (art. 355).
- The debtor is allowed to decline discharge of his obligation until he is provided with a proof of the transfer, and the assignor shall deliver to the assignee the documents evidencing the assigned right (claim) that are in his possession (art. 356).
- The debtor can raise against the assignee all defenses arising out of the original contract he has by the moment of the notification (art. 357).
- Assignment shall not contradict the law, other regulations or the contract, assignment is not allowed in case assignor's personality is crucial for the debtor (art. 359).
- If the original contract is concluded in writing or notarized, assignment shall also be concluded in writing or notarized (art. 360).
- The assignor is bound to guarantee the validity of the right (claim) at the time of the assignment. The assignor does not answer for the solvency of the debtor, unless he has undertaken to guarantee it (art. 361).

Chapter 24 of the Civil Code does not mention assignment except addressing it within articles 353-361. No security elements of assignment are dealt with by the Civil Code. By contrast, § 3 of Chapter 23 of the Civil Code (articles 315-339) deals with pledge as a security tool.

Article 317 'Subject of Pledge' of the Civil Code clearly establishes that 'any property, including things and property rights (receivables) can be subject to a pledge'. Thus, the Civil Code lists receivables among the types of property that can be subject to a pledge. Some provisions that specifically address issues relating to the pledge of receivables are contained in the Law of the Republic Belarus 'On pledge'. In particular, Chapter 10 of the Law of the Republic Belarus 'On pledge' (articles 52-56) specifies the rules governing pledge of receivables.

Pledge is defined within article 315 of the Civil Code. Accordingly, under a pledge, the creditor (pledgee) in case of default by the debtor can meet his claim out of the encumbered asset. He has priority over the other creditors that have ownership in respect of all or part of the encumbered asset (pledgor).

Belarusian legal concepts do not recognise pledge as a transaction aimed at transferring rights in receivables, unlike an assignment transaction which is understood as a mechanism of replacement of a creditor's obligation. In an assignment transaction, the will of the parties is directed towards the transfer of property, whereas in cases where the asset is pledged, the encumbered asset is of interest only because of its securing value. Assignment (according to the rules set by the Civil Code explicitly) is devoid of security nature. By contrast, according to the statutory provisions of the Civil Code, the only aim of a pledge is to create a security right over the encumbered asset.

A closer look into the Civil Code and insolvency regulations allows disclosing the security functions of outright assignment and the security elements in an assignee's right.

In case of the assignor's insolvency, the position of an assignee (transferee) is different to that of a buyer of a tangible thing. Once entitled to acquire possession immediately after assignment, i.e. after

the transfer, an assignee becomes a new creditor and insolvency of the assignor does not affect the assignee's financial position. The transferred receivable shall be taken out of the insolvency mass.

The ownership in tangible property may typically pass due to a sales contract; receivables are transferred by assignment. Under the Belarusian law the assignee is not a mere "buyer of a claim" and in comparison with a buyer within a sales contract has a more stable position and additional guarantees deriving from the essence of an assignment. At this stage it is essential to go into details comparing the position of the buyer (before and after the transfer of property) and that of the assignee in an insolvency proceeding brought against the assignor.

When a contract relates to the delivery of tangible goods in a standard (non-default) situation, a creditor will expect a debtor to perform (i.e. deliver goods, or other property) according to the agreed contractual conditions. If the debtor follows the contract accurately, there should be no difficulties arising out of the transaction. The situation is different where the debtor defaults or becomes insolvent and is not able to perform all its obligations. Before the performance on behalf of the creditor has been accomplished the latter remains a mere creditor possessing a contractual claim against the debtor. If the debtor (seller) has failed to deliver before the insolvency procedure started the creditor cannot claim for the contracted goods or payments under the title of the ownership. His claim in this case will be settled from the total insolvency mass available for distribution to all the creditors.

According to article 224 of the Republic of Belarus Civil Code rights in tangible things pass upon delivery: 'A purchaser acquires ownership over a thing after delivery'. Article 225 specifies that hand over or handing the goods over to the first carrier for transmission to the buyer is essential to accomplish the delivery.

In case of the seller's insolvency, when the seller fails to deliver before the insolvency procedure started, the purchaser (creditor) cannot claim the contracted goods under the ownership title. His claim is referred to the insolvency mass. According to the Republic of Belarus Law 'On insolvency (bankruptcy)' claims of unsecured creditors are allowed in the sixth instance after the claims of secured creditors, compulsory payments, wages and royalties, claims for injury to life and the like claims' are settled.

The insolvency mass indicates the amount of the debtor's property available. 'Property' is defined through article 128 of the Civil Code: 'Among the objects of civil rights are things, including money and negotiable papers, other property, including rights and claims; works and services; protected results of intellectual activity and similar rights (intellectual property); non-property rights'. The term 'property', thus, in legal terms covers things and claims, i.e. account receivables.

The Regulations issued by the Ministry of Economics of the Republic Belarus N 159 of 28.06.2004 with respect to insolvency proceedings defines the insolvency mass as follows:

"Insolvency mass – all the property of the debtor available on the date when the insolvency procedure was opened; or the property revealed during the bankruptcy proceedings"

This definition covers all the property (including receivables) 'available on the date when the insolvency procedure was opened'; even if the property has already been subject to a contract but the ownership has not yet passed.

In case of an assignor's insolvency (i.e. the insolvency of a seller of a receivable), the position of an assignee (transferee) is different. The essential feature of intangibles is that no physical actions influence creation or movement of rights in intangible assets. Only *actiones juris* are capable of creating, changing or ceasing rights in receivables. The obligation to assign is a contractual obligation which is normally executed upon its conclusion ('consensual' contract). In other words, upon conclusion of a contract to assign two *actiones juris* are accomplished simultaneously: (1) the contract creating (among others) an obligation to assign and (2) the transfer (*cessio*). The transfer (*cessio*) may be referred to a future moment, for example, in case future receivables are dealt with. Absent such a reference, intangible property (receivable) is transferred at the moment the contract to assign is concluded.

The assigned receivable (after the transfer), therefore, shall be considered out of the insolvency mass. This is where the security elements of the assignee's right turn out.

It is important to mention that according to the new Belarusian factoring rules (Chapter 19 of the Republic of Belarus Banking Code N 441-Ç of 25.10.2000 (Hereafter Banking Code) yet only mentions though explicitly the security function of assignment. Article 153 of the Banking Code sets out the rules. Under a factoring contract, a bank or a financial organization (factor) is obliged to pay to the creditor the monetary obligation of the debtor with the discount. Discount is the difference between the obligation of the debtor and the sum paid by the factor to the creditor. The monetary claim to the debtor may be transferred to the factor for the purpose of securing the obligation of the creditor before the factor.

This means that a factor by law can not only 'buy' the monetary claim, but also receive a security obligation from the 'creditor' with the monetary claim (receivable) as the encumbered asset. Under factoring rules security is created by transfer.

This rule, however, is rather an exception than a general rule of the Belarusian civil law. First, this rule is structured within the Banking Code and not the Civil Code. Second, according to article 153 of the Banking Code 'factor' is a bank or a licensed financial organization. Factoring rules therefore under Belarusian law relate to banking contracts and not civil law contracts. In addition, the above rule is a singular provision with no further statutory elucidation. That is why one should assert that according to the Civil Code the security consequences of outright assignment (articles 353-361 of the Civil Code) are not explicitly recognized as far as general assignment rules are concerned. Security elements of assignment in Belarusian law are implicit.

At the same time academics agree that factoring rules under the Banking Code (as a transfer of a monetary claim from the creditor to the factor) is a particular case of the civil law assignment of receivables in general. This view is implicitly supported by the provisions of the Banking Code where article 153 mentions factoring as a 'transfer'.

### ***International outlook***

The issue of assigning security effects is well known in 'western' laws. This is also seen in the UNCITRAL texts. Keeping in mind the interest towards intangible security recourses launched by the UNCITRAL it is extremely important to understand that the Belarusian law in its nature is not alien to the latest international law developments.

The General Assembly of the United Nations at its sixty-third session issued Resolution A/RES/63/121 of 15 January 2009 and recommended the Legislative Guide on Secured Transactions<sup>ii</sup>. The Guide remains the most detailed international set of model legal rules for secured financing touching specifically security rights in receivables. The concept underlying the Guide resembles the approach introduced within the UN Convention on Assignment of Receivables<sup>iii</sup>. In the Guide with respect to the account receivables as assets UNCITRAL reaffirmed adherence to the concept embracing three kinds of relationships under the unified treatment:

- (i) Creation of a security right in receivables
- (ii) Assignment of receivables for security purposes and
- (iii) Outright assignment of receivables whether for security purposes or not<sup>iv</sup> (earlier this concept was introduced in the UN Convention on Assignment of Receivables).

Following the work on security and insolvency undertaken by UNCITRAL throughout decades as well as the most recent international work on security and insolvency done by other international organisations,<sup>1</sup> the UNCITRAL Guide does not address 'pledge of receivables'. Rather, the Guide addresses 'creation of a security rights in receivables' as a separate concept coincided with the corresponding rules on assignment, in particular, with the UN Assignment Convention. The draft text offers a comprehensive treatment of the three spheres where receivables are dealt with.

This concept, designed in order to develop the availability of the account receivables as assets, does not remain a mere theoretical recommendation. Recently it influenced changes in the legislation of the European Union: article 14 (3) of the Rome I Regulation 593/2008 which provides that assignment for

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<sup>1</sup> Bazinas, S. V., "Harmonization and modernization of secured transactions law: The UNCITRAL draft legislative Guide on secured transactions" (2007) 7-8 *DeCITA; derecho del comercio internacional, temas y actualidad* (Buenos Aires), at p. 101.

the purpose of the Regulation includes 'outright transfers of claims, transfers of claims by way of security and pledges or other security rights over claims'.

The most historically important first example of material law inspiring the above mentioned concept is the American Unified Commercial Code (UCC), article 9 'Secured transactions; sales of accounts and chattel paper'. The article 'applies to any transaction which is intended to create a security interest in personal property or fixtures including goods, documents, instruments, general intangibles, chattel papers or accounts [...]'. Following § 9-202 of the UCC the title to the collateral is immaterial: 'Each provision of this Article with regard to rights, obligations and remedies applies whether title to collateral is in the secured party or in the debtor'. In other words, whether the parties actually transfer the title to the property or not, the provisions of article 9 apply in both cases. The UCC rules on security, thus, include assignment provisions as an integral part.

### ***Transaction planning notice***

In the course of the (focused on the Belarusian law) reasoning aimed at underlining the security element in the assignee's right, the crucial point is the *moment* when a receivable is transferred. Account receivables are intangible and only jural facts influence creation and movement of rights in receivables. Belarusian law on assignment (Chapter 24 'Substitution of parties in obligations' of the Civil Code) does not specify any other legal fact but the conclusion of a contract to assign to indicate the moment of the transfer. The parties therefore should take care and specify the legal fact in order to save the security effect of outright assignment.

If the moment of the transfer is not specified it can lead to a situation when assignee, similarly to a buyer of a tangible thing, can be considered a mere creditor under a contract to assign, and not a new owner of an assigned receivable. In this case the security element of assignment is lost because, unlike a new possessor, a mere creditor (assignee) in order to meet his claim in case of the assignor's insolvency shall address his claim to the insolvency mass, not to the value of the asset.

With respect to the moment of the transfer the crucial point is the wording of the contract to assign. In order to preserve the security function of outright assignment the parties should avoid a so called 'real' contract. In theory it is reckoned that a 'real' contract is the contract where parties do not actually transfer the asset at the time the contract is concluded, but agree to transfer. In such a contract the parties agree that the assignor *'is obliged to transfer the receivable'*. Instead, in order to preserve the security function of assignment, the parties should use a 'consensual' clause. This means that the contract should read as follows: 'the assignor *transfers the receivable'*. In this case the contract to assign is 'consensual'. This means that the parties agree to transfer the receivable at the same time as they conclude the contract to assign. The assignee is secured from the assignor's insolvency or default by the title of ownership over the transferred receivable. Whereas in a 'real' contract a separate act of transfer is required before the ownership in the receivable passes to the assignee. In case insolvency of the assignor occurs after the contract, setting an obligation to assign is entered into but before the act of transfer is accomplished the assignee is not secured against the assignor's insolvency.

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<sup>i</sup> Article 144 of the Republic of Belarus Law 'On insolvency (bankruptcy)' N 423-3 of 18.07.2000.

<sup>ii</sup> UNCITRAL Legislative Guide on Secured Transactions ('the Guide on Secured Transactions' or 'the Guide'), A/CN.9/WG.VI/ WP.31/Add.1. The latest text of the Guide is available at: [http://www.uncitral.org/uncitral/en/uncitral\\_texts/payments/Guide\\_securedtrans.html](http://www.uncitral.org/uncitral/en/uncitral_texts/payments/Guide_securedtrans.html).

<sup>iii</sup> United Nations Convention on Assignment of Receivables in International Trade ('the Assignment Convention' or 'the Convention') was adopted by the United Nations General Assembly and opened for signatures on 12 December 2001. The text of the Convention is available at: [http://www.uncitral.org/uncitral/en/uncitral\\_texts/payments/2001Convention\\_receivables.html](http://www.uncitral.org/uncitral/en/uncitral_texts/payments/2001Convention_receivables.html).

Article 2 (a) of the Convention defines assignment: 'For the purpose of this convention 'Assignment' means the transfer by agreement from one person ('assignor') to another ('assignee') of all or part of or an undivided interest in the assignor's contractual right to payment of a monetary sum ('receivable') from a third person ('debtor'). The creation of rights in receivables as security for indebtedness or other obligation is deemed to be a transfer'.

<sup>iv</sup> Recommendation 3 of the Guide on Secured Transactions reads as follows: 'The law should apply to outright transfers of receivables despite the fact that such transfers do not secure the payment or other performance of an obligation'.

<sup>v</sup> Bridge, M., Stevens, R. Cross-border security and insolvency, 2001, Oxford University Press, Oxford, New York, at p. 49.