



Department
for Business
Innovation & Skills

Nullification of Ban on Invoice Assignment Clauses

Summary of responses

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Nullification of Ban on Invoice Assignment: summary of responses

Introduction

Invoice finance allows a business to assign the right to future payment of an invoice (known as a “trade receivable”) to a finance provider in exchange for a loan up to the full value of the invoice. Businesses are reliant on a strong cash flow and even a profitable business can come into serious difficulties if it has to wait a long time for payment.

A ban on invoice assignment refers to a clause in a debtor’s terms of sale which prohibits the supplier from selling the debt from an accounts receivable, typically from an invoice, onto a third party financier. Where businesses encounter bans on invoice assignment clauses they can still often obtain invoice finance by seeking waivers or workarounds. But this can expose businesses to higher interest and administrative fees. Sometimes no waiver or workaround can be achieved, which may stop businesses accessing the finance.

At the moment invoice financing is used to obtain a small proportion of the finance small and medium sized businesses borrow. Figures from the Asset Based Finance Association (ABFA) show that in the third quarter of 2014, £18.3bn worth of invoice finance was being used by businesses, an 18% increase on the same period two years ago¹.

In 2005 the Law Commission recommended removing this contractual barrier as part of a package of recommendations on secured transactions law reform. In December 2013, we published a discussion paper, *Building a Responsible Payment Culture*, on issues related to prompt payment and respondents were clear that removing contractual barriers to selling invoices would help to increase access to invoice financing.

In response to this discussion paper, the Government committed to introduce legislation to tackle contractual barriers such as ban on assignment. We are now seeking to achieve this through powers in the Small Business, Enterprise and Employment Bill which will allow the Secretary of State to make regulations to invalidate anti assignment clauses.

The consultation *Nullification of Ban on Invoice Assignment Clauses* set out our initial views on what should be in the secondary legislation. The proposal we tested proposed to nullify the term outright with some exemptions. Our consultation asked whether we should limit this proposal to business to business contracts and exclude financial services.

This document provides a summary of the responses received to the consultation. It does not set out the Government response to responses received. We will publish amended regulations and an accompanying document outlining how the regulations have changed based on the responses received to the consultation after the election.

¹ Quote from ABFA, data available from <http://www.abfa.org.uk/members/statistics.asp>

Responses received

We received 20 responses to the consultation, coming mainly from business representative bodies, invoice financiers and law practitioners. We also had some responses from large businesses in the retail and construction industry. A full list of respondents is set out in Annex A.

One response was supported by five other organisations who agreed with its conclusions. These have been counted as individual responses to the consultation. Where arguments from this response are cited, we have flagged that this view was supported by the five separate organisations.

During the consultation period, we held a number of roundtable discussions gaining stakeholder feedback on the proposals outlined in the consultation. This feedback is not reflected in this document.

Summary of responses

1. Comments on Draft regulations

Overall, there was support for the proposals, but some concerns were expressed about the consequences of this measure to contract law. Detailed comments on the draft regulations are set out in the relevant sections below.

Principles of the Proposal (questions 2-6)

2. Introducing the nullification of ban on invoice assignment

Our consultation proposed that nullifying anti-assignment clauses in contracts would be the most efficient way to implement this measure. The intention of this method was to keep costs to business low; it would prevent debtors from having to retrospectively revise their contracts. Suggested alternative approaches were:

- Sectoral regulation
- Amendments to competition law rather than the proposed contractual law change.
- More work to promote supply chain finance
- The creation of a trust account between a supplier and an invoice financier where the financier could access the funds paid into the account.

Responses to this approach of nullifying anti-assignment clauses in contracts were as follows:

- 12 responses supported this approach
- 8 responses did not support this approach.

Ten of the respondents who supported this approach did not elaborate on why they supported this method of implementation. The other two responses thought that simplifying access to invoice finance without asking debtors to revise their contracts would be the most effective way to introduce the measure.

There were concerns from the eight respondents who did not support this approach that there may be unintended consequences to preventing anti-assignment clauses. One respondent argued that it would place a limit on contract law and this particular response was endorsed by five other organisations. The respondent suggested an alternative approach, which would see the change implemented through competition law or alternatively through sectoral regulation. The respondent considered that, in any case, its scope should be limited to contracts that are enforced in England and Wales. The response argued that parties from all over the world use our contract law in order to do business and so there may be legitimate reasons why overseas businesses included a ban on assignment clause in debtors' contracts.

One response suggested a different approach entirely, which called for the Government to do more to promote supply chain finance.

The final response suggested that suppliers create a trust account between themselves and the invoice financier.

3. Business to Business contracts

We asked consultees whether the proposal should be limited to business to business contracts. We received the following responses.

- 6 responses agreed with the proposal
- 8 responses disagreed with the proposal
- 6 responses did not respond to the question

The six respondents who agreed with the proposal thought that it should be limited to business to business contracts, with two commenting that excluding consumer contracts was correct.

One response argued that overriding the ability for businesses to freely agree contracts was undesirable and this particular response was endorsed by five organisations. Two other respondents disagreed with the proposal because they felt the scope should be widened to sole traders and to Government contracts.

4. Excluding Financial Services Contracts

Our consultation sought views on whether financial services contracts should be excluded from the scope of our proposed regulations. The responses were as follows:

- 12 responses agreed with the proposal
- No responses disagreed with the proposal
- 8 responses did not answer the question

Seven responses agreed that financial services products are different from business to business payment contracts and the measures should not apply to financial services contracts. Those seven agreed with the examples quoted in the consultation, a business may want to ensure that it maintains a direct relationship with a bank issuing a loan or there may be uncertainty about the credit rating of a third party in assignment of derivative

products. The remaining five did not elaborate on why they agreed with excluding the financial services.

Finally, a response stated that excluding other types of contracts would make the law difficult to interpret and that it would be difficult to capture all the different types of contracts defined in law. This particular view was supported by five other organisations.

5. Do you agree with the list of Financial Services?

We asked participants if we should exclude financial services as listed in section 40 of the Terrorist Asset Freezing etc. Act 2010.

- 11 responses agreed with the list
- 9 responses did not respond to the question

All respondents who answered agreed. Six respondents agreed that the list from the Terrorist Asset Freezing etc. Act 2010 was a thorough list of financial services. However, two issues were raised by two invoice financiers, firstly, that invoice discounting be included in the list, and secondly, that invoice financing be recognised as distinct from lending.

6. Other activities that should be excluded or special provisions that need to be taken into account

Thirteen responses raised no other issues. We received seven responses which relayed concerns to the proposal to nullify anti-assignment clauses. One respondent stated that it would be impossible to list all the contracts that could be caught under the nullification. This response was endorsed by five other organisations; however, they did not provide an example to support this view.

Exemptions from the nullification (questions 7-10)

7. Tenancy agreements

We asked for views on the exclusion of tenancy agreements and interests in land from the proposals. The responses were as follows:

- 9 responses agreed
- 2 responses disagreed
- 9 responses did not respond to the question

Three respondents agreed with this proposal without elaborating on why they believed tenancy agreements and interest in land should be excluded. The other six respondents in agreement stated that there were clear and established rules on subletting arrangements in legislation that should not be interfered with. The two respondents in disagreement with the proposal thought that a landlord should be able to assign their right to receive rental income to a third party.

8. Supply Chain Finance

Our consultation proposed that the nullification of anti-assignment clauses should not extend to contracts which included exclusivity clauses for supply chain finance. Such exclusivity clauses allow a supplier to only access the creditor's own supply chain finance scheme and prevent an assignment of an invoice to a third party financier. We received a range of different views on this exemption. The responses were as follows:

- 7 responses agreed that contracts with exclusivity clauses should be exempt
- 11 responses objected to this exemption
- 2 responses did not respond to the question

One respondent who agreed to the proposition explained that regulations should not interfere with the free negotiation of contracts between parties. This view was supported by five other organisations. No other views were expressed in support to the proposal.

Eight of the responses which objected were clear that they viewed the nullification of anti-assignment clauses as being unfairly restrictive on a business wishing to assign a debt which would limit the financial options available to SMEs. Invoice financiers, who in some cases also provided supply chain finance, thought that it would not be uneconomical and would remain commercially viable without legislation. They also voiced concerns that debtors would place exclusivity clauses into contracts for disingenuous reasons. Two responses mentioned that other jurisdictions with laws which nullify anti-assignment clauses do not have provisions which protect the interests of supply chain finance.

9. Commercial Confidentiality

We also considered the issue of debtors wishing to keep commercially sensitive information confidential when an assignment of their invoices was made. Our consultation set out to test this assumption. We proposed that debtors wishing to keep their commercially sensitive information private should be able to ban assignment of invoices.

- 9 respondents agreed that protecting commercially sensitive information was grounds to prevent an assignment
- 11 respondents objected to this exemption

One response argued in support of this exemption and stated that contracting parties should be free to negotiate terms. This response was endorsed by five other organisations. Similarly, seven responses stated that large companies had a right to protect their commercial confidentiality. The remaining two responses did not elaborate on why they supported this exemption. None of the responses that agreed with the exemption were able to give examples of where their commercial confidentiality could be impinged by an assignment. One respondent who objected to the exemption thought that there should be a way to protect commercial confidentiality for national security reasons.

Seven responses which objected to the exemption expressed similar arguments to the exclusivity clauses for supply chain finance. Invoice financiers generally thought that commercial confidentiality clauses could be used frequently and disingenuously by debtors to prevent assignments. One respondent went further and stated that normal invoice information is already exempt from confidentiality for VAT purposes by HMRC and the

supplier's auditors, insolvency practitioners and legal advisers. Other issues cited were that this would not prevent invoice financiers from seeking out waivers and workarounds, therefore maintaining costs. One respondent explained that banks are bound by a duty of secrecy to keep commercial practices confidential, and that this duty has to date not been significantly breached.

10. Linked Contracts

Contracting parties often agree a master contract setting the overall terms and conditions for business before issuing an individual contract for batches of goods and services. The anti-assignment clause can be contained in these master contracts rather than in specific contracts. Our proposal stated that the nullification of anti-assignment clauses should extend to those contracts as well. We received the following responses to this proposal:

- 15 responses agreed that the nullification should extend to linked contracts
- No respondents disagreed that the nullification should extend to linked contracts
- 5 responses did not respond to the question

Fifteen responses from other organisations agreed with this principle without elaborating on why they agreed with the proposal.

Effects on the Market (questions 11-15)

11. Invoice Finance Beneficiaries

The Small Business, Employment and Enterprise Bill allows the Government to choose to prohibit assignment of invoices, for example, to any organisation other than dedicated invoice financiers. The consultation instead proposed that the regulations should not prescribe who an invoice could be assigned to. The responses were as follows:

- 15 responses agreed with the proposal not to prescribe who should benefit from assignment
- No respondents disagreed with the proposal not to prescribe who should benefit from assignment
- 5 responses did not respond to the question

Three of the invoice financier responses argued that invoice finance was not recognised in law, therefore making it difficult to enact this proposal without considerable legislative amendments. Two responses similarly thought that not enacting this proposal would enable finance providers to compete on a level playing field and allow new businesses to enter the market.

12. Damages to Debtors

Our consultation asked whether the secondary legislation should include provisions to protect the debtor from damages where an invoice is assigned to a third party. The responses were as follows:

- 7 responses agreed that no further provisions needed to be created in order to protect debtors
- 6 responses disagreed and thought that terms needed to be in place to protect debtors
- 7 responses did not respond to the question

Four of the responses which agreed with the proposal in the consultation document believed that adding additional terms to protect debtors would add unnecessary complexity. All invoice finance respondents were concerned that large debtors would use terms to prevent assignment of invoices for disingenuous reasons.

One respondent who disagreed with the question raised a concern that a debtor may need to pay an invoice financier more than they had initially agreed with their supplier. One respondent raised concerns that a nullification of invoice assignment would prevent efforts to tackle money laundering, sanction laws or regulations. These concerns were supported by five other organisations who wrote in support of this response.

13. Contractual Disputes

We consulted on whether invoice financiers should raise disputed invoices with the supplier of the goods or services. We received the following views:

- 4 responses agreed with our statement on contractual disputes
- 10 responses disagreed with our statement on status quo of contractual disputes
- 6 responses did not respond to the question

We were told by three invoice financiers that they raised disputes with the debtor party, in consultation from suppliers. One of the law practitioners believed that any dispute between debtors and suppliers would have to be resolved between them and should not involve an invoice financier as a party to the dispute at all. They reiterated that ban on assignment clauses may be put in place deliberately so that the relevant parties could resolve complicated contractual disputes. This particular response was endorsed by five other organisations.

14. The Right to Set-Off

Set-off is a legal right for a debtor to settle the cost of an invoice against costs incurred to the debtor of a previous invoice. Set-off is dependent on the principle of mutuality. Our proposal was that mutuality is not affected when an invoice is assigned. We received comments which both supported and did not support this interpretation:

- 7 responses supported our proposal on set-off
- 10 responses did not support our proposal on set-off
- 3 responses did not respond to the question

Two responses from invoice financiers were clear that mutuality was not affected by assignment. They also considered that the law was clear that a debtor cannot be placed in a worse position by an assignment. Conversely, one response also explained that debts up to and including the last assignment could be set-off against each other. New debts

post notification could be regarded as part of a separate contract and thus could not be set off against debts payable under a previous contract. It was explained that this scenario rarely occurred.

One response disagreed with the proposal in the consultation. They stated that a debtor should have all the rights to set-off that an assignment would prohibit, and explained that this was the position adopted under general law. This particular response was endorsed by five other organisations. One respondent asked us to consider the implications of supplier insolvency in relation to set-off.

15. Other issues to consider

Respondents raised a few additional points for consideration. Invoice financiers asked if we could consider the issue of applying the nullification of anti-assignment clauses to contracts retrospectively rather than from commencement.

Another respondent requested that we consider a communications plan to support the launch of the policy and offered guidance to businesses on potential changes, in order to provide clarity.

One response agreed that the nullification of anti-assignment clauses should apply in legislation to Government contracts.

One respondent expressed concerns about the territorial extent of the regulations. They argued that the effect of the regulation would affect international contracts agreed under the law of England and Wales where there was no UK business involved in assignment. We were asked to clarify this issue and state in the regulations whether we intended to apply the measure to contracts only governed by the law of England and Wales. Five further responses were written to endorse this point.

Changes to legislation and Enforcement (questions 16-17)

16. Changes to existing law

We asked for views on whether existing legislation should be amended in order for us to change the law. We received one request to review a piece of legislation - the Law of Property Act 1925.

17. Government enforcement

We consulted on the proposal that Government should not have a role in enforcing the nullification. There were no dissenting opinions to this proposal. We noted arguments that future regulations may be needed if unintended consequences to business were to occur.

- 9 responses agreed
- 11 responses did not respond to the question

Costs to the Market (questions 18-19)

18. Costs of Workarounds and waivers

Our consultation asked if the nullification of anti-assignment clauses would negate the cost of waivers and workarounds and therefore benefit the overall invoice finance market. We received views which agreed and disagreed with this assumption:

- 5 responses agreed that the costs of waivers and workarounds would be negated
- 8 responses disagreed
- 7 responses did not respond to the question

The respondents who agreed with our conclusion thought that the nullification would simplify access to invoice finance. Invoice financiers disagreed, however, arguing that exemptions on supply chain finance and commercial confidentiality would maintain their need to conduct due diligence checks.

One respondent raised the possibility that debtors will work to find loopholes to the regulations and costs associated with the use of these loopholes would be transferred to suppliers. They also believed that the loss of the right to set-off would damage suppliers further. This view was supported by five other organisations.

19. Costs of an assignment to business

We outlined our reasons for assuming low costs for implementing the nullification of anti-assignment clauses. Debtors would not need to retrospectively amend contracts. The only cost we believed would be incurred would be to invoice financiers who would have to familiarise themselves with this policy.

- 3 responses agreed with our calculations
- 9 responses disagreed with our calculations
- 8 responses offered no opinion on the subject.

Arguments for envisaging costs were varied. Invoice financiers argued that if the exemptions of supply chain finance and commercial confidentiality were left in the regulations, the invoice finance market would be weakened with debtors seeking to include frequent and disingenuous exemptions, therefore preventing an assignment. More broadly, one respondent felt that changing an important principle of contract law would damage the economic interests of the UK. This particular response was supported by five other organisations.

Those responses that agreed with our cost assumption believed in the case that was stated in the consultation and did not offer any other explanations to agree with the consultations points.

Next steps

We will use the findings from the consultation to prepare a Government Response, which we will publish in due course.

Annex A – Responses Received

Asset Based Finance Association

Allen & Overy LLP

The Association of Professional Staffing Companies

Carillion PLC

Chartered Institute of Credit Management

City of London Law Society (Financial Law Committee)

City of London Law Society (Litigation Committee)

Clifford Chance LLP

Federation of Small Businesses

Fujitsu Ltd

GLI Finance Ltd

Herbert Smith Freehills LLP

HSBC

The Institute of Chartered Accountants in England and Wales

Professor of Commercial Law, Louise Gulliver (responding on behalf of Professor Hugh Beale and Assistant Professor Sarah Paterson)

Lloyds Bank Commercial Finance Limited

MarketInvoice Limited

Peter Graham

John Davies

Travers Smith LLP



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