

Journey to the Future: The Assignment of Future Receivables in China

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Abstract: The legality of the assignment of future receivables in Chinese law has undergone a significant transformation, representing another instance of Chinese law continuously updating itself to meet transactional demands. Chinese law does not recognize the independent juristic act of real rights, thus offering a more flexible legal framework for explaining the assignment of future receivables. To eliminate the negative externalities of the assignment of future receivables, it is essential to continuously refine the certainty standard to exclude assignments of future receivables that lack any determinability and to establish a unified registration system. The effect of future receivables assignment occurs immediately at the time of agreement, at which point the future receivables will become the enforceable assets of the assignee.

Keywords: Future Receivables, Legal Acts, Certainty Standard, Unified Registration System.

1. Introduction

The assignment of future rights was once seen as a perilous concept: in traditional view, it was considered impossible to assign a receivable that did not yet exist. Moreover, the mere assignment of "expected benefits" was seen as potentially speculative or not serious enough: if a heavily indebted debtor could assign all his future rights, there would be further risks, as he might impair the economic freedom of others. This caution towards the assignment of future benefits is also reflected in the legislation and practices of various countries, with some judicial cases in China also opposing the assignment of future receivables and judicial authorities once rejecting to recognize the legality of such transactions. Happily, just as Tang Sanzang and his companions completed their Journey to the West, China has recognized the importance of acknowledging the assignment of future receivables and has launched its Journey to the Future in this field. This article will introduce the shift in China's attitude towards future receivables and provide an outlook on the legal framework of future receivables in China. At the same time, this paper will also elaborate on the supporting systems to eliminate the negative externalities of the assignment of future receivables and provide research conclusions on the practical issue of the effective time of the assignment of future receivables.

2. The Legality of the Assignment of Future Receivables

Future receivables can be classified into two categories based on certainty: One category includes future receivables that have an existing contractual relationship as their basis, such as receivables contingent upon a condition or future receivables arising from ongoing contracts. These future receivables are based on existing contracts, such as ongoing contracts. For example, there are judicial decisions that have recognized future monetary receivables generated from the income rights of a sewage treatment project as future receivables, where the right to claim sewage treatment service fees is based on an existing sewage treatment service contract.

The other category includes future receivables that do not have a contractual basis, such as receivables arising from contracts that have not yet been concluded, like sales and leases, referred to as "pure future receivables." Examples include toll fees and utility charges, which are essentially future license fees or franchise fees and can also be recognized as future receivables.

The inherent uncertainty of future receivables has led judicial authorities and financial regulators to maintain a skeptical attitude towards them for a long time. Even when their validity is recognized in some particular cases, it is often accompanied by hesitation and excessive caution.

The "Interim Measures for the Administration of Factoring Business of Commercial Banks" issued by the former China Banking Regulatory Commission is a reflection of the regulatory authorities' overly cautious attitude. This regulation defines future receivables in Article 13 as "expected receivables under a contract where the seller's obligations have not yet been fulfilled" and restricts commercial banks from conducting business based on them, despite the fact that the regulation already provides an overly narrow definition of future receivables.[11] The attitude of the regulatory authorities naturally influenced the courts' judgment on the compliance of banking operations. In *China Exim Bank v. Kailuan Group International Logistics Co., Ltd. Import and Export Branch, Kailuan Group International Logistics Co., Ltd.*, the court held that factoring business based on future receivables constituted non-compliant business (2017 Yue 01 Min Chu 133 No. 1, Guangdong High People's Court).

However, the conservative stance of the regulatory authorities has not formed a consensus within the industry. On the contrary, most judgments are reluctant to outright deny the transferability of future receivables, whether by negating the strength of the regulations issued by regulatory authorities or reasoning about its legitimacy.

Indeed, the free circulation of future rights is an inevitable outcome of the development of modern finance. Even without explicit legal provisions, financial practice will create various forms of such transactions. For instance, China's real estate mortgage business involves the assignment of future

receivables, such as homeowners' installment repayment claims. Factoring, asset securitization, and other financial services are all manifestations of the mature development of future rights assignments. The principle behind this is that the increasing degree of financial liberalization inevitably stimulates financial practitioners to maximize the vertical value of property interests. This financial innovation in the assignment of future rights will eventually be addressed by legislation. Article 9.1.5 of the UNIDROIT Principles of International Commercial Contracts follows the international trend by recognizing the assignment of future receivables. The Restatement of the Law, Second, Contracts, Section 321 conditionally acknowledges the assignment of expectant payment rights. The Uniform Commercial Code Section 9-204 more clearly endorses the possibility of assigning future rights. Japanese courts have recognized the assignment of future receivables within a one-year period, and in 1999, the Japanese Supreme Court even overturned this one-year limit, allowing assignments to cover receivables arising within an eight-year period, as long as the beginning and end periods of such assignments were sufficiently certain. This stance was ultimately codified in the 2017 amendments to the law.

In this sense, discussing whether to recognize the assignment of future receivables is pointless; it is an inevitable transaction form that emerges with the development of the financial industry. The key lies in how to substantiate its legal foundation.

So, it is not surprising that the restrictions on the transfer of future receivables were completely removed in the "Notice on Strengthening the Supervision and Administration of Commercial Factoring Companies" issued by the regulatory authorities in 2019.[12] The Civil Code, arguably the most important legislation for China's factoring industry in recent years, which was enacted in 2020, includes future receivables in the definition of factoring contracts under Article 761, ultimately confirming the legitimacy of conducting factoring based on future receivables.[13]

3. The Legal Framework of the Assignment of Future Receivables

Based on whether the effect of receivables assignment should be distinguished from the receivables assignment contract, that is, whether an independent juristic act of real rights (*Dingliches Rechtsgeschäft*) or the juristic act of disposition (*Verfügungsgeschäft*) is recognized, there are two positions:

The view that recognizes the independent juristic act of disposition holds that the effect of receivables assignment occurs based on an independent juristic act.[14] It affirms the independent existence of the intent to dispose of receivables and advocates for the principle of separation in the field of receivables assignment. Since the current law does not recognize the consensus on juristic acts of real rights, it is referred to as a quasi-real right contract. The theoretical basis for the quasi-real right contract lies in the formalism or principle of distinction in real right changes. Therefore, it can be said that the debate on the nature of receivables assignment is greatly influenced by the debate on the nature of real right change models.

The view that denies the independent juristic act of disposition holds that the effect of receivables assignment occurs directly based on the effectiveness of the receivables assignment contract and does not particularly distinguish the

intent to dispose of receivables.[15] In this sense, once the receivables assignment contract takes effect, the receivables are immediately transferred to the assignee. The proponents of denying the act of disposition of receivables have long struggled to properly address the status of the right of disposition in the receivables assignment contract and to respond to the issue of unauthorized disposition of receivables, thus being at a disadvantage in debates for a long time. However, the latest research on creditor formalism has provided a strong response to this issue, advocating for the independence of the right of disposition to achieve the separation of receivables establishment and real right changes.[16] The theory of denying the quasi-real right contract can be used as a reference, not distinguishing the intent to dispose of in the receivables assignment contract.

The theory of juristic act of receivables has an inherent disadvantage when explaining the reality of the assignment of future receivables. According to the traditional theory of the civil law system, an independent juristic act naturally needs to be directed at existing receivables. Recognizing the disposition of expected benefits would undermine the refined theory of juristic act derived from German law, forcing it to invent the concept of "post hoc correction" or reluctantly admit that this is a theoretical exception.

In contrast, the tradition in Chinese law of not recognizing the independent juristic act of real rights has an advantage when explaining new types of transactions. According to the existing analytical framework of Chinese law, parties in a contract based on future receivables only need to generally include the intent to enter into the contract and the intent to dispose of the rights.

The effect of the receivables assignment requires meeting additional requirements for the disposition right, typically the disposition right. The disposition right is not a necessary requirement for entering into a valid contract. For example, the intention of a party without the disposition right to assign specific receivables can still be recognized; however, they need to obtain the disposition right for the transfer to take effect. The separation of the discussion on the effect of the parties' agreement and the effect of rights transfer renders China law more easily incorporating future receivables into the legal framework.

4. Certainty Standard and Unified Registration System for the Assignment of Future Receivables

The assignment of future receivables is essentially an advance on future assets. In a free market of individual liability, how an assignor advances their future assets should naturally not be interfered with. However, the unique nature of future receivables assignments makes them inherently internal transactions. On one hand, they are difficult to publicize, making it hard for other transaction parties to be aware of the reduction in responsible assets. On the other hand, the expected benefits from future receivables are not controlled by the assignee. For example, in cases of future receivables without a foundational contract, such as utility contracts, the expected benefits the assignee receives depend on the assignor's business operations. The assignment of future receivables, involving issues of excessive assignment, dissolution of publicity, and credit downgrades, needs to be restricted based on considerations of transaction security.[3] This is mainly reflected in two aspects: first, excluding the

assignment of future receivables that lack any identifiability to prevent the risk of commercial speculation; second, establishing a unified registration system to provide the necessary information for transactions.

4.1. Criteria for Determining the Transferability of Future Receivables

The freedom to assign future receivables has its boundaries, necessitating appropriate criteria to exclude assignments that harm public interest. The first viewpoint agrees that the ability to be identifiable should be the criterion for determining the transferability of future receivables.[4] This means that future receivables must be recognizable as being covered by the previous receivables assignment contract when they actually arise. As long as there are identifiable standards for receivables, such as all receivables in a certain transaction, all receivables from a particular entity, or receivables within a specific time period, they can be assigned. The scope of the effect of ownership change depends on the scope of publicity. The second viewpoint holds that the core criterion for determining the transferability of future receivables is reasonable expectation and certainty. In practice, some courts have refused to recognize the validity of future receivables assignments based on the lack of reasonable expectation due to false records.[17] However, some scholars argue that the reasonable expectation standard is vague and inconsistent, as the expectability of future receivables fundamentally depends on the number of debtors, without a uniform standard.[18] For example, abstractly, the expectability of utility project income rights is greater than that of POS machine fee rights. However, in individual cases, if the POS machine fee rights come from a merchant in a popular business district, even if the scale is small, it still possesses the necessity to confer transferability.

Although the identifiability standard and the reasonable expectation standard appear distinct, they share a similar essence. Both standards focus on the need for future receivables to have identifiable criteria, which may be based on the reasons for the occurrence of future receivables or significant life facts at the time of occurrence. These two viewpoints can be integrated into a "certainty standard," suggesting that transferable future receivables either need to have certainty in their occurrence reasons or contractual foundational relationships, such as accounts receivable with foundational contracts, or be identifiable by other means, such as service fee rights of well-operated business units. This verification should be based on the nature of the subject, the condition of the debtor, the nature of the right, and other factors in individual cases. The level of certainty required to grant transferability to future receivables involves the judicial system's discretionary scope and the regulatory authorities' intervention in financial markets.[19] Additionally, the certainty standard considers the perspectives of both the creditor and the assignor, as there are separate protective rules for the debtor.[20] As long as future receivables can be determined from the perspective of a generally rational person in similar situations and typical transaction intentions, they can be considered transferable, regardless of the actual cost of confirming the receivables.

4.2. Publicity System for the Assignment of Future Receivables

Receivables assignments do not have a natural appearance of publicity. Therefore, in general receivables assignments, notification as a means of publicity is a requirement for it to

be effective against third parties. In the assignment of future receivables, the debtor is not always identifiable, leading to different methods of publicity. For future receivables with a foundational contract, notification to the debtor can achieve publicity, but it may not satisfy the certainty needs of commercial transactions. Moreover, for future receivables without a foundational contract, using notification as a means of publicity is impractical. Thus, establishing a registration system to achieve publicity for future receivables is necessary.

A unified registration system should be established to include future receivables such as accounts receivable, infrastructure, commercial property, or real estate income rights. In practice, prudent transaction parties in future receivables transactions like factoring have already adopted self-registration. Legislatively, the "Receivables Pledge Registration Measures" are insufficient in terms of scope and hierarchy of effectiveness to clearly use registration as a prerequisite for priority. A unified registration system is needed, as some court cases have ruled that "registration of receivables assignments in the central bank registration system does not have mandatory exclusive opposable effect" due to the lack of relevant laws and regulations (Shanghai No. 2 Intermediate People's Court, 2012, Hu Er Zhong Min Liu (Shang) Zhong Zi No. 147).

Comparatively, the Uniform Commercial Code (UCC) establishes that U.S. law uses perfected public registration as a condition to oppose third parties. Japan previously adopted newspaper publicity and later transitioned to electronic registration under the "Act on Special Provisions, etc. of the Civil Code Concerning Claims for Indemnity for Losses." Chinese law can fully reference foreign experiences and put the establishment of a publicity system for the assignment of future receivables on the legislative agenda:

First, a unified registration system for future receivables should be established. The assignment of future receivables is a highly commercialized transaction form, and establishing a registration system around the People's Bank of China or other registration authorities is feasible. Second, for future receivables with a foundational legal relationship and some purely future receivables where the future debtor is specific, "notification to the debtor" can still be used as a means of publicity for the assignment. However, considering the existence of a unified registration system, the scope of publicity through notification should be narrower, and its effectiveness should be subordinate to unified registration. Lastly, in cases where the assignment of future receivables has not completed any registration and the debtor has not received any notification, priority should be determined based on the sequence of assignment agreements.[3]

5. Time of the Assignment of Future Receivables

As long as the assigned receivable is transferable, the mainstream view in academia holds that, unless otherwise agreed, the assignee acquires the receivable once the assignment contract takes effect.[21] However, opinions differ regarding the timing of the effect of future receivables assignments. The first view holds that the effect of future receivables assignments occurs when the receivables actually arise. Intuitively, legislative examples that adopt the theory of juristic act of real rights seem more inclined to consider that future receivables take effect only when they become a reality. Such a stance indeed aligns more closely with the theoretical

logic of the juristic act of real rights. German law maintains the distinction between the obligational act and the act of disposition, and the act of disposition only takes effect when the future receivable becomes a reality. Tai Wan, China follows Germany's detailed formal logic, attaching a suspensive condition to the effect of the disposition of future receivables, which takes effect only when the condition is fulfilled or the term arrives. The second view holds that the assignment of future receivables takes effect at the time of agreement. For example, U.S. law recognizes the prior assignment of receivables and can simultaneously transfer the rights. The mainstream view in international practice also leans towards the second perspective. The Working Group on International Contract Practices believes that "a future receivable is deemed to be transferred at the time of the conclusion of the contract of assignment." The United Nations Convention on the Assignment of Receivables in International Trade ultimately reflects this viewpoint, asserting that the timing of the transfer of receivables does not fundamentally differ based on their current existence or not; in principle, it occurs at "the time of the conclusion of the original contract."

It has been argued that issues such as the timing and scope of the effect of receivables assignment are formal issues related to the nature of the assignment itself.[22] From this perspective, the extent to which different countries' legislations accept the juristic act of real rights directly determines the distribution of benefits within the receivables assignment system. The reason Germany holds the view that the transfer of receivables occurs when future receivables arise is that it recognizes the act of disposition. In short, the time of assignments is essentially determined by whether the juristic act of real rights is supported.

However, it should be noted that within the theoretical framework of recognizing or opposing the independent juristic act of real rights, there are multiple approaches to constructing the effects of receivables assignments. Rather than saying that formal logical differences determine system construction, it is more accurate to say that the sensitivity of various national legislations to transaction risks, views on the extent of financial market freedom, and preferences for market transaction rules, determine which interpretative path is adopted based on the original logical consensus. From the perspective of institutional economics, market operations have costs. The core issue of all system designs is how to reduce the "friction" in resource allocation and more efficiently lower transaction costs. The timing of the occurrence of future receivables assignments essentially determines the point of asset risk isolation. The assignee is the most vulnerable and most in need of protection among the transaction parties because they rely entirely on the assignor's ability to fulfill the expected performance at the time of the contract to ensure the realization of certain interests. They always hope that "the road to the future" is as short as possible: the closer the transfer timing of the receivable is to the time of agreement, the less transaction uncertainty the assignee has to bear. The assignor is the least deserving of protection among the various transaction parties because they control the expected benefits, honesty and diligence of who directly determine whether the transaction objectives of the other parties are fulfilled, making providing any additional protection for them unnecessary. At the same time, other transaction parties of the assignor, or the so-called third parties, also need a certain degree of protection. The

assignment of future receivables lacks transaction visibility, significantly interfering with the assessment of the debtor's responsible assets and inducing the risk of backdating contracts. Even if the effect of receivables assignment is permitted to occur before the receivables become a reality, it is still necessary to prevent corresponding transaction risks through other systems. Therefore, the process of choosing a legislative model should be transformed into weighing the interests between the assignee and the third party. If the effect of receivables assignment occurs at the point when the receivables become a reality, it certainly protects the interests of third parties. However, it imposes unavoidable transaction uncertainties on the assignee and ultimately hinders the development of the future receivables assignment as a transaction model. If the timing of the receivables becoming a reality is used as the point of change in ownership, it imposes an additional transaction risk on the assignee that requires evaluation and supervision.

Upon weighing the factors, it is more appropriate to affirm that the effect of receivables assignment occurs immediately at the time of agreement. Clarifying that the assignee acquires the receivables at the agreed time helps to define the ownership of rights clearly, and this protection for the assignee cannot be substituted. Furthermore, the establishment of the unified registration system, as advocated above, is sufficient to ensure the transaction security for third parties. In the United States, where future receivables are transferred at the time of contract signing, financing has been extremely successful because this approach provides certainty of ownership for future receivables, reducing uncertainties for the assignee. For instance, in the case of asset securitization, this rule of ownership change effectively isolates the risks between the special purpose entity and the original assignor. This can serve as another important factual argument.

One significant practical implication of specifying the time the assignment of future receivables take effects is that it helps clarify the status of future receivables in enforcement and bankruptcy proceedings. In the current Chinese enforcement law, the subject of enforcement is textually limited to existing receivables. Whether expected interests can be included in enforcement proceedings remains a legislative gap. Based on the above discussion, future receivables can be strongly justified as enforceable assets. This is because, as long as they pass the certainty standard test, future receivables acquire the attributes of property interests and gain circulation properties. There is no reason to automatically exclude property interests that are transferred based on mutual agreement from being subjects of enforcement. Additionally, since the assignment of future receivables takes effect immediately at the time of agreement, the future receivables are removed from the assignor's enforceable assets and become part of the assignee's enforceable assets at the time the contract is concluded.

As for bankruptcy proceedings, more disputes are likely to arise. As a form of collective enforcement, bankruptcy proceedings will not differ from enforcement proceedings regarding the eligibility of future receivables as enforceable assets and the time when the future receivables are removed from the assignor's enforceable assets. However, future receivables represent a potential credit overdraft, making them particularly suspicious in bankruptcy proceedings. The certainty standard established in judicial practice is inevitably a lenient one. Therefore, the transfer of future receivables

with certainty may not constitute sufficiently honest transactions from the perspective of bankruptcy enforcement and is more likely to be considered fraudulent transfers and thus subject to avoidance. Notably, Chinese law only recognizes the bankruptcy trustee's right to avoid unperformed contracts. If the debtor engages in transactions involving excessively overdrafted credit for expected benefits, the only remedy would be to determine such transactions as "unreasonable condition transactions," with the specific standards to be gradually refined through judicial cases.

6. Conclusion

One of the founders of New Institutional Economics, Professor Steven Cheung, once described China's market economy reforms as "the greatest program for economic reform in history." Over the past 40 years, China's civil and commercial law system has continuously updated itself, shouldering the responsibility of ensuring the smooth operation of the market economy and guarding this "greatest reform". The process of securing a legitimate status for the assignment of future receivables is another example of Chinese law continuously adapting to changes in transaction realities, balancing market transaction efficiency and transaction security. Furthermore, the highly inclusive concept of "contract" in Chinese law has allowed it to avoid the historical burdens of the civil law system. With judicial practice continuously exploring, refining, and implementing the "certainty standard", the establishment of a unified registration system, and the determination of the immediate transfer of future receivables, the transaction form of future receivables assignment will have a brighter future in Chinese law.

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