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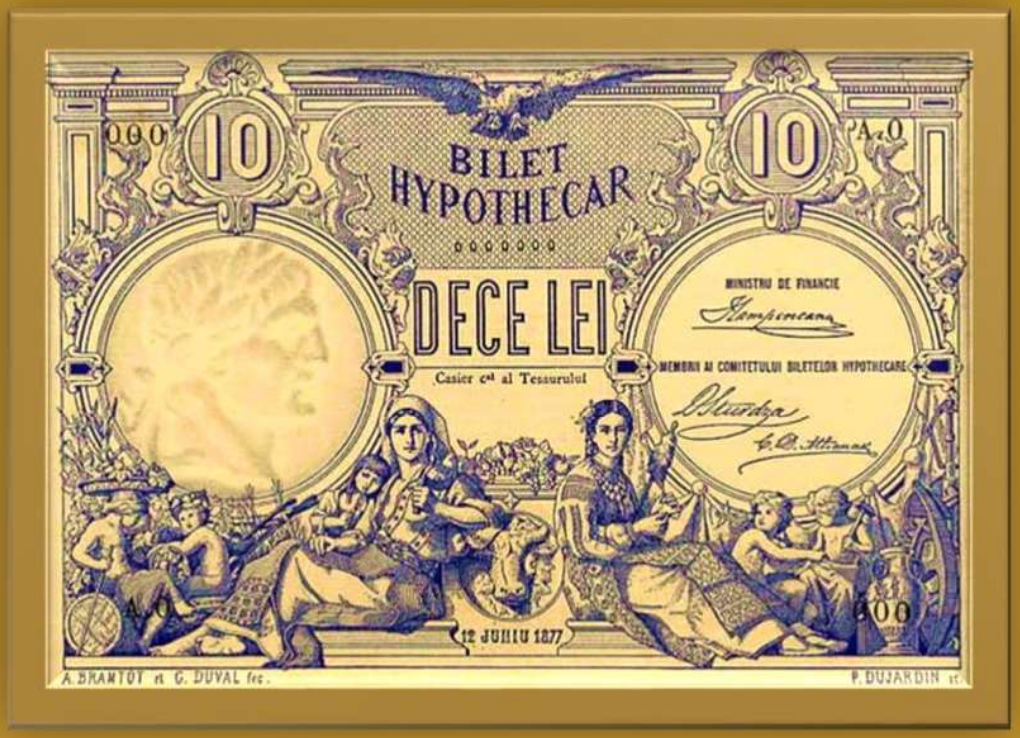
Banking Law in the 21st Century



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A contemporary overview of the factoring agreement

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Abstract

Modern factoring resulted from the adaptation, in the 15th and 16th centuries, of the Atlantic trading posts to the commercial activity between England and the United States, in which, by virtue of their intensity, commercial warehouses took on a more financial than commercial feature. In the course of this evolution, these intermediaries, in addition to the distribution and consultancy tasks, began to guarantee the fulfilment of the transaction (del credere factors), often granting advances to European producers on the price of goods before sold. The factors thus became known as the 'financiers of European industry'. This sophistication of the intermediary conceived in European merchant schemes was at the origin, between the 16th and 19th centuries, of the colonial factoring, the predecessor of the modern factoring, in which the factor, in addition to distributing the products of European exporters, with special focusing on the textile field, in the New World markets, start collecting its credits, which in the meantime were assigned to it, and financing, through the provision of advances on sales. Later, colonial factoring gave way to old line factoring, which has assumed since the beginning a financial nature, providing a new range of services. In the old line classic scheme, the factor thus assumes four essential tasks: collection and management of assigned credits; provision of consultancy services; financing through the granting of advances on assigned credits and guarantee of the debtor's compliance and solvency. The financing role is undoubtedly one of the main reasons that motivate the use of this contract. Indeed, the need to attain financing, in addition to banking, with a greater incidence in times of credit restriction, is pointed out by many authors as one of the main justifications for the use of factoring in Europe. The crisis currently experienced worldwide following the Pandemic COVD 19 and the role that this contract can play in the economic recovery, through the financing the SMEs, justifies the analysis of the evolution of this contract, as well the legal framework in Portugal.

Keywords: *factoring, financing, contract, Portugal.*

JEL Classification: K20, K22, K42

1. Introduction

Factoring is "*the product of the contemporary needs of commercial management*"[2] whose contours and evolution were traced by mercantile practice and contractual freedom and not by the skillful hand of the legislator.

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[2] Menezes Cordeiro, *Da cessão financeira (Factoring),* Lex-Edições Jurídicas, 1994, p. 25.

Modern *factoring* resulted from the adaptation, in the 15th and 16th centuries, of the model of the Atlantic trading houses, to the mercantile activity between England and the United States, in which, due to their intensity, trading posts took on a more financial than commercial feature.

European traders began by copying the traditional mercantile mechanisms, which were essentially based on the delivery of goods to third parties, resident in the colonies, who sold the traders' products, either on the domestic or foreign market, in their own name but on behalf of the traders, from whom they charged a commission. These third parties were true agents acting on behalf of the principal.

The British colonies in North America soon revealed themselves to be potential markets for the metropolis' products and not to mere transit points for goods and raw materials. However, these colonies were a new, unknown and distant world, and it was necessary that these "*commissioners",* who gradually settled on the coast, took on a wider function than that of a mere distributor and started to provide consultancy services regarding the strategy to be followed in the sale of products, taking into account factors such as clientele, price, interest and the size of the market.

In the course of this evolution, these intermediaries, in addition to their distribution and advisory functions, began to take on the task of guaranteeing the proper performance of the transaction (*del credere factors*), often providing European producers with advances on the price of goods before they were sold[3]. These new functions are explained by the personal knowledge of the financial capacity and honesty of their clientele and the fiduciary relationship that was established with the principal[4]. The factors thus became the "*financiers of European industry"*[5].

2. The emergence and evolution of factoring

2.1. Colonial factoring

This sophistication of the intermediary conceived in the European mercantile schemes was at the origin of the appearance, between the 16th and 19th centuries, of the embryo of the current factoring, the *colonial factoring* in which the factor, apart from distributing the products of the European exporters, with special focus on the textile area, in the markets of the New World, also assumed the functions of collection of their credits, which, in the meantime, were assigned to him, and financing, through the concession of advances on sales.

The economic agents then had the perception that *"There are many ways*

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[3] Rolin, S., *El Factoring* (tradução espanhola Galvez –Piñero y Pidal), Madrid, 1975, p. 16.

[4] See Fossati /A. Porro, *Il factoring*, p. 4 ff and Zuddas, *Il contratto de factoring*, p. 5.

[5] See Zuddas, *Il contratto di factoring*, p. 5 and Aldo Frignani, *Prime decisioni dei giudici italiani* p. 5.

of raising cash besides borrowing. One is by selling book debts"[6].

However, as the factor assumed a more financial function, the English legal system had to adapt to overcome limitations traditionally imposed on factors, such as the impossibility of selling assets entrusted to them by the principal on credit or through exchange, the most serious being the prohibition on pledging the principal's assets[7].

In this context, English jurisprudence recognized, in order to protect the factor, the existence in his favour of a special security, the *Factor's Lien,* over the merchant's property in order to overcome the fact that, under *Common Law,* possession of the debtor's property had, until the beginning of the 19th century, been the only valid form of guarantee[8].

The creative and flexible English jurisprudence, as early as 1755, admitted, in the case of *Kruger v. Wilcox,* the existence of the *factor`s lien* on the goods of the merchant deposited in the warehouses of the *factor,* as a means for the latter to guarantee the claims which it held against the former. In 1775, in *Drinkwater v Goodwin,* the factor was recognized as having *"a lien on the price of goods in the hands of the buyer"*[9].

The growth of the English textile industry supported by *colonial factoring* and the obstacles created by *common law* principles eventually triggered the need for *factoring to* be the object of legislative treatment. Thus, in the period between 1823-1889, numerous laws known as *Factors Acts* were enacted, which provided for special forms of guarantees for the *factor,* even when he was not in possession of the goods and documents relating to the commercial transactions in which he intervened[10].

Curiously, it was at the end of the 19th century that *factoring* began a period of decline in England. In fact, the development of means of communication, the appearance of alternative forms of credit and insurance, the development of large factories and the closer relationship between industrialists and suppliers of raw materials eventually reduced the use of services provided by factors[11].

The same, however, did not happen in the United States.

The declaration of independence in 1776 and the consequent adoption of

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[6] *Chow Young Hong v. Choong Fah Rubber Manufactory,* cited by Freddy Salinger, *Factoring: The Law and Practice of Invoice Finance*, 3rd Edition, Sweet & Maxwell, London, 1999, p. 5.

[7] See R. Munday, *A legal history of the factor*, p. 244.

[8] Peter Coogan, *Article 9º - An Agenda for the next decade*, 1977, Yale LJ, Vol. 87, 1977-78, p. 1014 ff, refers that "*the only way to create a valid security interest in personal property was by physical pledge – the transfer of possession of property (collateral) by the debtor (the pledgor) to the creditor or secured party (the pledgee)".*

[9] *Kruger vs Wilcox,* (1755) and *Drinkwater v Goodwin (1775).* Cfr. Giuseppe Tucci, *Garanzie sui crediti dell'impresa e tutela dei finanziamenti – L´esperienza statunidense e italiana*, Giuffrè Editore, Milano, 1974, p. 52 ff.

[10] For a detailed analysis of *Factors Acts* of 1823–1889, see R. Munday, *A legal history of the factor*, cit, p. 246-250 and *Anson´s Law of Contract*, updated by J Beatson, 28th edition, Oxford University Press, Oxford, 2002, p. 673.

[11] See Roderick Munday, *A legal history of the factor*, p. 250.

protectionist measures made *factoring* flourish in the former colony.

Under the influence of the protectionist measures imposed by the United States at the end of the 19th century, which practically put an end to the import of textiles from Europe[12], and with the development of means of communication and transport[13], factoring loses its initial vocation for the external market and for commercial distribution, turning towards the internal market. As a result of this protectionism, the American industrial expansion began, with characteristics that would also end up favouring *factoring*.

In fact, this new clientele, with special focus, again, on the textile industry, presented some financial shortcomings. American textile companies, despite enjoying a reasonable distribution network, had no alternative means of financing than banks. As they needed to borrow money to buy expensive machinery, they soon ran out of bank credit[14]. The lack of liquidity of these companies was aggravated by the practice of very long credit maturity periods, equal or superior to 180 days[15].

In addition to these features of the American industrial fabric, it should be noted that the American banking system has no knowledge of the discount banking system[16].

Thus, the factors, which until then had represented English fabric producers, although timidly beginning to develop the role of financier, taking advantage of the experience they had gained, their knowledge of the market and their own capital, began to increase their financial function, which included managing and collecting their customers' debts, guaranteeing their fulfilment and granting advances on the debts assigned to them. The *trade factor was about* to give way to the *finance factor*[17]. The *old line factor* that inspired European *factoring was* born[18].

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[12] A *"McKinley Tariff Act*" of 1890 imposed very strong restrictions on European imports, subject to a 49.5% customs tax on the value of imported European textiles. See Peter Biscoe, *Law and Practice of credit factoring*, Butherworths, London, 1975, p. 34.

[13] Merchants undertook the storage, selling and shipping the products, taking the traditional distribution functions away from the factor. See Aldo Frignani, *Prime decisioni dei giudici italiani,* cit., p. 6 and Renato Clarizia*, I contrati per il finanziamento dell´impresa*, cit., p. 419.

[14] Zuddas, *Il Contratto di Factoring*, cit., p. 6 notes that it was because of the factoring association to companies that had already exhausted their respective credit ceilings with the Bank, that it became a common opinion that only companies with financial and economically weak problems resorted to factoring.

[15] See Fossati /A. Porro*, Il factoring,* p. 4.

[16] Ibid., p. 4.

[17] Omar Pace/Daniele Cherubini, *Il factoring quale strumento della finanza d´impresa*, Jandi Sapi Editori, 2001, p. 4 ff.

[18] Regarding the sophistication of primitive factoring by the Americans, S. Rolin, *El factoring*, p. 21 refers *"Que tentacion la de devolver la pelota al viejo continente y hacerle descubrir de nuevo esta técnica, corregida y aumentada".*

2.2. Old line factoring

As we have already analysed, the fact that the United States was in the midst of a period of industrial growth, aided by the absence of discounting in commercial practice, contributed greatly to the triumph of the *old line factor*[19].

As we have already mentioned, the textile and clothing companies that the factor knew so well were also the ones that most needed the *finance* and guarantee from the *finance factor* to face the everlasting market volatility and lack of financial solidity. It is not surprising, therefore, that *factoring* companies were concentrated around major textile centres such as *New York* and *Boston*[20]. To illustrate this link between the textile industry and *factoring,* Skilton's phrase "*Factors and the textile trade go together" is a perfect example*[21].

Old line factoring is distinguished from *colonial factoring* by the financial nature assumed by the factor and the functions it provides to its customer.

In the classic *old line* scheme, the customer assigns to the factor part or all of the credits arising from his commercial activity, the latter assuming the management and collection of such credit. The factor, at the request of the customer, grants him advances on the value of the credits assigned, assuming the fulfilment and solvency of the debtor. At the same time, the *factor* provides consulting services. We would like to make a brief parenthesis here just to point out that, for the overwhelming majority of the doctrine[22], the rendering of commercial advisory services is not seen as an autonomous function, the *old line factor* being attributed a *"triple function*[23]*"* (management and collection, financing and guarantee of the debtor's *del credere* risk). In our opinion, the provision of consulting services is a fourth function of the *old line factor*[24], since it was the knowledge of the market and of the clientele acquired by *colonial factoring* that enabled the factor to cope with the end of the colonial market following the independence of the United States and the application of protectionist measures, evolving into the scheme of the *old line factor*, then limited to the American domestic market.

In return for providing these services, the *factor* receives a commission and interest when funds are advanced.

The *old line* thus assumes four essential functions: collecting and managing the assigned credits; providing consulting services; financing the customer by granting advances on the assigned credits; guaranteeing the debtor's compliance and solvency. This does not mean that all these functions are provided simultaneously.

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[19] When it was introduced in 1913 by the Federal Reserve Act it had little impact since its function was ensured by the old line factor and accounts receivables finance companies.

[20] Roderick Munday, *A legal history of the factor*, p. 252.

[21] *The factor´s lien on merchandise*, Wisconsin LR, 1955, p. 368.

[22] Garcia-Cruces, *El contrato de factoring,* cit, p. 48, José Carlos Pires, *O contrato de factoring,* p. 33.

[23] Expression used by José Carlos Ferreira Pires, *O contrato de factoring*, p. 16

[24] Luís Miguel Pestana Vasconcelos, *Dos contratos de Cessão Financeira (Factoring)*, p. 69.

As far as the financing function is concerned, the *old line factor* may take the form of *conventional factoring in* which financing is provided to the customer through the granting of advances on the invoices assigned, or the form of *maturity factoring* in which the factor does not grant any advances on the credits assigned, only crediting the value of the invoices assigned, in the current account of the assignor, on their due date. In the latter modality, the factor does not provide any financial function to the client, although it may assume the credit guarantee. On the other hand, the *old line,* in a diametrically opposed field to *maturity factoring,* can take the form of *credit cash factoring* or *discounting factoring* in which the financial function reaches its full extent, since all the ceded credits are anticipated.

In relation to the function of guaranteeing the fulfilment and solvency of the debtor, *factoring* may assume more than one modality, namely non-recourse and recourse factoring. In the first modality, the risk of insolvency or financial incapacity of the debtor is transferred to the factor, while in the second, the grantor guarantees the factor the risk of the solvency of the debtor. In the latter, the factor, in the event of insolvency or incapacity of the debtor, has a right of recourse against the assignor. These different modalities focus on the insurance function of the factor and the assumption of the *del credere risk* by the factor.

Although *old line factoring* may assume some deviations, as we have analysed, with regard to the financing and guarantee function, its mandatory feature is that the assignment of credits is notified to the debtor.

Bearing in mind that, as we will analyse, it was the classic scheme of the *old line* that became successful in Europe in the sixties and began to be practised by European *factoring* companies, it therefore seems appropriate to us to make a detailed analysis of each of the functions that the *old line factor* traditionally performs.

2.2.1. Collection and management of assigned credits

Within the scope of this function, the factor, once the credit has been assigned, is responsible for managing and collecting it on the due date.

In this way, the client transfers a large part of the administrative and collection services to the factor, and his customers' accounts are centralised in a single account, managed by the factor, which sends him the respective statement on a monthly basis. This service has benefited small and medium-sized companies, which have been able to transform a fixed cost, that was often extremely expensive due to their weak structure and organisational capacity, into a variable cost. Small and medium-sized companies are thus free to focus on their core business and improve their productivity.

As regards the recovery of credits, the intervention of the factor promotes the success of the underlying commercial operation, especially when credits are assigned without recourse, a situation in which the factor assumes the default of

the debtor, leaving him, in the face of his default, to resort to the courts to obtain payment of the credit. The collection is, therefore, fully assumed by the factor.

When the credit is assigned with recourse, in the case of default by the debtor, the right assigned is retransferred to the assignor, being charged by the factor, if there was an advance granted. In this type of *factoring,* the judicial collection of the credit falls to the assignor, and it is certain that the factor, in many situations, places its legal service at the disposal of the assignor, although the respective cost is charged to the latter[25].

2.2.2. The guarantee of compliance and solvency of the debtor

In relation to the function of guarantee of the debtor's solvency and compliance, if certain requirements of the factoring contract are met, the factor may accept the assignment in the aforementioned non-recourse modality, transferring to its legal sphere the risk of insolvency or mere non-compliance of the debtor. This function allows the entrepreneur to transfer to the *factor,* in situations of economic crisis, the losses resulting from the insolvency of the debtor. In this operation, the *factor* must necessarily make a careful analysis of the economic and financial situation of the debtor assigned. In light of this analysis, a ceiling is set by the factor within which it assumes the risk of insolvency and default of the debtor[26].

2.2.3. Financing

The financing function is, without a doubt, one of the main reasons that motivate the use of this contract. In fact, the need to obtain financing, other than bank financing, with greater incidence in times of credit restriction, is pointed out by many authors as one of the main justifications for the use of *factoring in* Europe.

This financing function consists of the factor granting advances of between 80% and 100% of the nominal value of the credits transferred. These advances allow the monetisation of trade receivables which companies have against their debtors, since it is commercial practice for the seller to grant the buyer a certain period of time for payment after delivery of the goods. However, this practice often causes serious liquidity problems for the company, particularly in small and medium-sized enterprises characterised by their lack of financial solidity, in expanding companies and at times of restrictions on bank credit.

Old line factoring has thus made it possible for companies to obtain immediate liquidity without having to resort to banks and securities. This financing is beneficial for both the assignor and the assignee. The assignor finds a safe and

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[25] R Ruozi/B Rossignoli, *Manuale del factoring*, Milano, 1985, p. 46.

[26] Luís Pestana Vasconcelos, *Dos contratos de cessão Financeira (Factoring)*, p. 71, note 140, maintains that, among us, the factor guarantees compliance and not just the debtor's solvency.

constant way of keeping its treasury balanced, benefiting from the management and consultancy services of the assignee, who, as Luís Miguel Pestana Vasconcelos underlines,[27] has every interest in the success of the activities of the assignor company, as he is the guarantee of the profitability of his investment.

Liquidity, on the other hand, as highlighted by the same author, brings the transferor a series of advantages, namely, it allows the entrepreneur to have the financial cash flow to make immediate purchases, placing him in a position that allows him to negotiate, with his suppliers, the best contractual conditions and discounts, which can go up to 4% of the business value[28]. Also, according to the same author, it improves the company's *current ratios,* which allow estimating the company's capacity to satisfy future obligations. At the same time, it enables the reduction of short-term debts without recourse to bank debt and, simultaneously, creates favourable conditions for the granting of credit by the banks.

We cannot, however, fail to mention that financing obtained through *factoring,* rather than substituting bank financing, has come to serve as a complement to it. In fact, the scope of *factoring* is limited to short and medium term credits, while the need for bank financing for long term investments and operations remains[29].

Financing plays such an important role in *old line factoring* that, as we have already mentioned, it has even led to the splitting of the same into dogmatic categories, depending on whether or not there was financing of the grantor.

Conventional factoring corresponds to the most typical and complete expression of the *old line,* in which the factor acquires the credits it has approved, for which it has assumed the risk of the debtor's default, simultaneously providing management, accounting, collection and consultancy services. In some situations, it is the factor that notifies the debtor. In this type of arrangement, the factor may grant the assignor advances on the transmitted credits, normally between 80% and 100% of their value[30] .

On the other hand, there is *maturity factoring,* whose main difference is the provision of all *conventional* services, with the exception of financing. The assignor only receives the amount corresponding to the credit assigned, through two forms: F. M. P. (*fixed maturity period)* in which an average maturity period is defined by the *factor* for the assigned credits, in which the assignor is credited with the value of the same, and P. A. P. *(pay as paid)* in which the assignor only receives the value of the credit after the factor has successfully collected the credit

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[27] *Dos contratos de cessão Financeira (Factoring)*, p. 73.

[28] Ibid., p. 73 ff.

[29] See José Manuel Bracinha Vieira, *Alguns aspectos económico-financeiros do factoring*, Lisboa, 1970, p. 33, Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão Financeira (Factoring)*, p. 74. On the confrontation between bank financing and factoring see José Bracinha Vieira, *Alguns aspectos,* p. 31.

[30] Also known as "complete factoring", it is considered, among us, the most current modality. José Fernando Sousa, *O factoring em Portugal*, p. 266 ff.

from the assigned debtor[31]. Coexisting with these categories of *factoring* is *credit cash factoring* or *discounting factoring* whose main function is financing, with the assignor being granted advances on the nominal value of the credits assigned[32].

Factoring is often given a pejorative connotation and associated with companies in poor financial health, particularly because of its strong link with the fragile textile industry. However, this does not seem correct to us because the factor is, above all, an investor who wants to recover the investment made, and, therefore, has no interest in subsidising financial weaknesses.

2.2.4. Provision of consultancy services

The factor's interest in the success of its client credit led it to assume and develop a commercial consultancy function, through which, taking advantage of the in-depth knowledge it acquires of the companies needs and potential of the various markets in which it operates, offers advice and recommendations to the assignor that will enable him to make the activity profitable. This function is an important contribution towards characterizing the financial solvency of the companies with which the assignor intends to do business. As we know, small and medium-sized companies have great shortcomings in the area of management and market knowledge and have few means of information about the economic and financial situation of their clients, often being limited to information provided by banks and market reputation. The factor fills lack of SME's in the area of management, organisation, promotion and commercial planning. The factor, as has already been said, is an element of simplification, specialisation, rationalisation and information[33].

In short, *old line factoring,* as we have analysed, was conceived for short term credits whose underlying legal operation consists of the transfer of commercial credits from the respective holder to the factor, as a rule, through the assignment of credits, with the necessary notification of the debtor. The factor, within the scope of this contract, may assume the financing of the assignor, by providing advances on the assigned credits, the guarantee of compliance and solvency of the debtor, the latter depending, obviously, on the verification or not of an assignment of credits without recourse, the collection and management of credits and, with increasing relevance, the function of commercial advisor. This varied range

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[31] On this distinction, we follow closely Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão Financeira (Factoring)*, p. 41 ff and João Caboz Santana, *O contrato de factoring. Sua caracterização e relações factor-aderente,* Ed. Cosmos, Lisboa, 1995, pp. 29 ff, José Fernando Sousa, *O factoring em Portugal*, p. 266 ff.

[32] Garcia-Cruces, *El contrato de factoring*, p. 58, Considers this modality a figure close to the discount with provision of typical factoring services. Also in this sense, Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão Financeira (Factoring),* p. 42.

[33] Slogan created by C Galvada/J Stoufflet, *Le contrat dit de factoring*, JCP, I, 1966, 2044, n.º 29 ff.

of services offered by the factor, which is not exhausted in mere financing, has been responsible for the growing recourse to *factoring,* even after the credit crisis of the eighties was overcome[34].

2.3. New line factoring

Due to the requirements of the North American market and the introduction of *factoring* in markets as diverse as the clothing, electronic instruments, mechanical equipment, furniture and pharmaceutical industries, factoring companies took on a very broad credit dimension, becoming true financial operators, offering, in addition to the traditional *old-line* services, a varied and complex set of financial services and products. Some are closer to traditional *factoring,* such as *non-notification factoring* and *undisclosed factoring,* while others have little to do with it, such as *commercial financing, inventory financing, hire purchase financing, confirming, renting and leasing.*

2.3.1. Non-notification factoring

This type of *factoring* contrasts with *notification factoring* or *factoring with notification,* characteristic of *old line factoring,* in which the assignor is - obliged to notify the debtor of the assignment of the credits to the factor, to which is added, generally, the duty to mention on the invoices that the obligation will only be considered fulfilled through the payment to the factor. The factor assumes the collection of the credits.

Non-notification factoring is a form of *factoring* used in the United States whereby the debtor is not notified of the assignment of the credit.

In this modality, the client transfers to the factor all his credits, which, in turn, assumes the risk of insolvency of the debtor and grants him advances on the values of the credits assigned. The assignment is not, however, notified to the debtor, nor does the creditor assume the collection of the credits, which remains in the hands of the client, who acts as an agent without representation of the factor, being required to transfer to him the amounts received for payment of the funds advanced and the commission for the services rendered by the creditor[35]. These services correspond to the traditional functions of financing and guaranteeing credits and consultancy[36]. Once the credit is collected, the factor compensates with the advance payments with it and debts the *factoring* commissions and

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[34] See José Gallardo Rodriguez, *El factoring como figura económico-financiera,* in "Jornadas sobre Factoring", Universidad Complutense, Madrid, 1992, pp. 37 ff, Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão Financeira (Factoring),* p. 78.

[35] Cfr. Theodore Silbert, *Financing and Accounts Receivables*, Harvard BR, 1952, p. 46.

[36] These are the functions that distinguish Non-Notification factoring from Accounts receivable financing, a very similar figure, but in which the guarantee of the transmitted credit is not assumed by the financing entity. See Zuddas, *Il contratto di factoring*, p. 18 and 19. G. Tucci, *Garanzie sui credit*, p. 63 ff.

other expenses, crediting the remaining amount to the assignor 's account[37].

It should be noted that, in certain situations, it is the factor itself that has an interest in resorting to this modality, since, for companies with many small amounts of credit, the effort made by the factor to obtain the respective collection is disproportionate to the value of the credits, making the *factoring* commission extremely expensive[38].

Non-notification factoring was born in the United States to remedy the bad reputation resulting from recourse to *factoring,* which, since the beginning of the 20th century, has been seen as a sign of a lack of economic solidity and as a solution of last resort for companies in a very precarious economic situation. This is accentuated by the fact that many companies have their own means of collection and are unwilling to pay the factor a commission for a service that they are capable of providing themselves[39] .

It should, however, be pointed out that this modality carries more risks for the factor since there is less control of the assignor account, which increases the possibility of fraud and damaging administration. The factor must take special precautions, namely by developing a more demanding analysis of the counterparty in these contracts.

This modality has seen reasonable development in Europe, and is widely used in export *factoring*, where there is a fear that the presence of the factor in the operation may hurt the susceptibilities of the foreign client, but where it is important to have the guarantee of good payment[40].

2.3.2. Undisclosed factoring

In Great Britain, for the same reasons that led to the use of *non-notification factoring in the USA, undisclosed factoring* emerged in the early 1960s.

This contract consists of the conclusion of two contracts, a contract of sale, whereby the factor purchases the goods from its customer, and a contract of commission whereby the customer resells the goods to the purchasers, in its own name, but on behalf of the factor. In this way, he obtains the advanced payment of the credits assigned and is not liable for the proper conclusion of the operation, acting as a simple commission agent. The factor, in this modality, does not assume the management and collection of credits, only performing a guarantee, financing and consulting function.

This contract is essentially financial in nature and the final cost of the operation is lower since, as we have seen, not all the services of traditional *factoring* are provided.

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[37] Cfr. R Ruozi/B. Rossignoli, *Manuale del factoring*, p. 26.

[38] See Gianluigi de Marchi/ Giuseppe Cannata, *Leasing e Factoring*, 4ª ed., Milano, 1986, p. 275.

[39] This modality of *non-notification factoring,* the called confidential *factoring*, has little expression in the Latin market and none in Portugal.

[40] *Vd.* João de Sousa Uva, *Factoring – Um instrumento de gestão*, Texto editora, 1991, p. 21.

As in *non-notification factoring*, there are, in this contract, greater risks for the factor, as the customer in a difficult situation may make the result of the sale of goods already sold to the factor its own, which imposes greater demands on the factor in the analysis of the customer's financial situation and reputation[41].

This figure also known as *money without borrowing* does not contain global clauses, which is why the client is always free to decide whether or not to contract with the factor[42].

The factor may, through this contract, finance long-term operations, provided they do not exceed five years and capital amounts above certain minimum values are involved[43]. This type of *factoring is* essentially aimed at the trade of industrial equipment, allowing the purchaser to pay in the long term, while the seller, who is the factor's client, receives cash[44].

Italian legal theorists classify this contract as *quasi-factoring*[45].

In fact, this contract does not use the traditional figure of the assignment of credits but uses different legal techniques. However, this is not a reason to separate this contract from *factoring,* because if we consider the functions that it performs, we will verify that it performs all the functions of traditional *factoring,* with the exclusion of the management and collection of the credits[46].

2.3.3. Bulk factoring

In this modality, the client of the factor assumes the management of its credits, and the factor may provide financing and credit guarantee services.

Normally, the factor only advances funds and does not provide any services. In practical terms, this modality is very close to the discounting of invoices with the difference that the credits are effectively assigned to the factor, with a corresponding notification to the debtors by means of a imprint on the invoice informing the debtor that payment should be made to a bank account in the name of the factor.

This method is essentially used by companies belonging to the same economic group, which have their own collection services and take their own risks. It is also often used when very small invoices are involved, which would make

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[41] On the *Undisclosed Factoring*, Zuddas, *Il contratto di factoring*, p. 126.

[42] Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão Financeira (Factoring)*, p. 47.

[43] It seems to us that this modality of factoring is not admissible in our legal system since n.º 1 of the article 2.º in DL n.º 171/95, of 18.07, conditions the factoring activity to the acquisition of short-term credits, which obviously is not compatible with the undisclosed factoring 5-year terms.

[44] This figure is very similar to forfaiting, which we will analyse later. See Zuddas, *Il contratto di factoring*, p. 127.

[45] Cfr Zuddas, *Il contratto di factoring*, p. 126.

[46] There are authors who have divided factoring into two large groups: distributive credit factoring, which includes contracts with conventional notification, and industrial credit factoring, which includes this contract of British origin. See Renzo Bianchi, *Il factoring e i problemi gestionali che comporta*, Torino, 1970, p. 99.

the *factoring* commission excessively onerous[47].

In view of paragraph b) of n.º 2 of article 1 of the Unidroit Convention, in which it is required as a condition for the qualification of the legal transaction as a *factoring* contract that the factor renders at least two of the functions originally rendered by the *old line factor,* it seems to us that this modality, in the majority of the cases, cannot be qualified as *factoring,* since often only the financing service is rendered[48].

2.3.4. Partial factoring, split factoring and split risk factoring

These modalities originated in the United States, where they are still practised exclusively.

In *partial factoring,* the customer assigns only a part of his credits and is responsible for managing the remainder[49].

In *split factoring,* part of the receivables is assigned to one factor, while the other part is assigned to another factor. Often this division is due to the nature of the products.

In *split risk factoring,* the factor and the customer share the credit risk.

2.3.5. Selective transfer credit

This modality has the particularity of excluding the globality clause. In effect, it is the transferor who chooses which credits to cede to the factor. The *factoring* company reserves the right to approve or not the credit and not to grant any postponement and only delivers the amount of the credit twenty days after its maturity[50].

In the meantime, a new modality has appeared, *factoring by exception, which is* similar to the one we have just discussed, but in which advances can be granted[51].

2.3.6. Mill agent factoring or drop shipment factoring

This modality is essentially intended to meet the financial requirements of small and medium-sized enterprises that want to launch new products on the market, but do not have the necessary structure for their production and marketing.

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[47] This modality is not used among us, although a similar system is used in other financial services. See João de Sousa Uva, *Factoring – Um instrumento de gestão*, Texto editora, 1991, p. 20.

[48] See Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão Financeira (Factoring),* p. 49.

[49] G de Marchi e G Cannata, *Factoring e Leasing,* p. 277.

[50] Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão Financeira (Factoring),* cit, p. 50, refers that the period between the payment of the credit and its maturity exists to face the risk that the factor bears, given the non-existence of a globality clause.

[51] In this respect, G de Marchi/ G Canatta, *Leasing e Factoring*, p. 53 ff.

In this case, the factor, the *jobber* and the *manufacturer* are involved in the operation. The factor guarantees the manufacturer, with whom its client has signed a production contract, the payment for all supplies previously approved. The manufacturer sends the goods directly to the purchasers, but always on behalf of the jobber, who, in his relations with the purchasers, appears as the real seller. The manufacturer issues an invoice and sends it to the jobber, who then draws up his own invoices which he sends to the customers and in which he must indicate the assignment of credits to the factor. The jobber and the manufacturer send the invoices issued to the factor, who will settle the amount in full with the producer and pay the designer the difference between the two invoices, corresponding to the profit of the operation, after deducting the *factoring* commission and any interest.

Some authors reconcile this operation to *factoring*[52]. However, other authors believe that it is no longer possible to frame it within the already vast limits of the *factoring* contract[53].

In fact, only two of the traditional functions of *factoring* are present in this operation, namely financing and collection, the latter being only a consequence of the construction used.

As Luís Miguel Pestana Vasconcelos observes, the function of a factoring *agent* is to finance the production of a small company that does not have the means to manufacture its products. If we think of the financing function of *factoring,* we can see that it is quite diverse, consisting essentially of providing liquidity to short term credits, solving the cash-flow problems of companies with long payment terms[54].

On the other hand, the function of the guarantee provided is also different. Firstly, because the guaranteed credits are not those of the designer, but those of the manufacturer, arising from the production contract entered into with the factor's client and subject to approval by the *factor*.

Thus, although this figure has some similarities with *factoring,* it has a very different purpose.

2.4. Indirect factoring

This system originated in Italy in the early 1980s. Some industrial groups joined forces with *factoring companies* to set up *factoring* companies that would provide their services exclusively to companies in the group[55].

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[52] Ruozi/B Rossignoli, *Manuale del factoring*, Milano, 1985, p. 26 ff.

[53] See Luís Miguel Pestana de Vasconcelos, *Dos contratos de cessão Financeira (Factoring),* p. 51.

[54] Ruozi/Rossignoli, *Manuale del factoring*, Milano, 1985, p. 27.

[55] In March 1980, Olivetti Fin – Factoring, SpA was formed. This was the pioneer and had, as its exclusive corporate purpose, the financing through factoring of the suppliers of the Olivetti group, as well as of the Olivetti concessionaires with regard to the purchase of Group products. Later

The operation essentially consists of the following: the factor guarantees to the seller the acquisition of the credits arising from the supply contracts concluded with the factor's customer and settles them immediately. As regards the buyer, the factor grants a deferment of payment. The customer pays the commission and interest, while benefiting from certain advantages, such as a discount[56].

This model has some particularities in relation to traditional *factoring.* Firstly, the client and debtor are the same company and the services are provided not to the client, but to third parties.

As Luís Miguel Pestana Vasconcelos observes, this modality is a way of providing financial resources, characteristic of bank credit, through the use of credit assignments[57].

The author[58] considers that although this operation is practiced under the name of *factoring* and by *factoring* companies of the *old line,* it should not be included in the already broad concept of *factoring,* since it is a purely financial business, entered into by these companies, due to market demands and competition from financial companies. However, the typical financing function of *old-line factoring* is quite distinct, since it essentially consists of making advances on short-term debts.

3. The legal framework of the factoring contract in Portugal

The first legislative reference to *factoring* occurs in DL n.º. 46/302, of 27.04.1965, with reference to para-banking institutions[59]. Article 1.º, n.º 4 identifies as one of the four types of para-banking institutions, *"Companies whose object is to effect the collection of credit from third parties, in whatever form used for this purpose, particularly those carrying on any system of activity known as factoring"*[60].

Merchant Factors International S p A. followed the example of Olivetti, Cfr. Zuddas, Il *contratto di factoring,* p. 74.

[56] See R. Ruozi, *Il factoring indirecto*, in "Il factoring" (coord por Roberto Ruozi e Gian Guido Oliva), Milão, 1971, p. 77 ff, R Ruozi/R Rossignoli, *Manuale del factoring, Milano, 1985,* cit p. 82 ff

[57] Luís Miguel Pestana de Vasconcelos, *Dos contratos de cessão Financeira (Factoring),* cit, p. 53.

[58] Ibid, p. 53.

[59] These institutions were admitted, albeit not expressly, for the first time in DL nº 41.403 of 27/11/1957. See Menezes Cordeiro, *Da cessão financeira (Factoring)*, cit, 31.

[60] This diploma, as already mentioned, was intended to regulate parabanking institutions, and the contract and factoring activity remained unregulated. However, despite this lack of regulation, the foundation of two factoring companies was authorized, *International Factors Portugal, S. A.* in 1965 and *Heller Factoring Portuguesa*, S A, in 1972. See João de Sousa Uva, *Factoring - um instrumento de gestão*, cit, p. 12. As referred by Teresa Anselmo Vaz, *O contrato de factoring*, cit, p. 58, these companies adopted, as regards the transfer of credits, the credit assignment institute as a legal instrument, without this being legally required. This is in line with the evolution of *factoring*, outlined by us in Section II, in relation to the other countries in Europe, with the exception of France and Belgium, for the reasons set out there. These companies adopted, as regards the transfer of credits, the credit assignment institute as a legal instrument, without this being legally required.

In 1986, DL n.º 56/86, of 18.03 was published, with the purpose, according its official summary, to systematize *"the juridical-economic bases of factoring activity in the country"*. The legislator, modestly, assumes in the preamble that, given the embryonic phase of *factoring* in our country, "*it was considered preferable, in this first systematization test, to establish very general parameters of the activity by law"*.

After reading its 29 articles, we can only agree with Menezes Cordeiro and consider that the articles went beyond what was intended in the preamble[61].

In fact, the law devotes more attention to factoring companies, imposing on them "an extensive and sometimes duplicated web of rules"[62], referring only in Articles 1.º, 3.º, 4.º and 5.º to the factoring activity and the respective contract[63].

Thus, Article 1.º stated that *"The factoring activity consists in the acquisition, in accordance with the applicable legislation, of short term credits, derived from the sale of products or the provision of services, in the internal and external markets*"[64]. The n.º 2 stated that *"The factoring activity includes complementary actions of collaboration between the companies involved and their clients, namely credit risk studies and legal, commercial and accounting support for the good management of the credits transacted"*.

Article 2.º contained a light reference to *factoring* activity, defining in nº. 2 the concepts of factor, adherent and debtor for the purposes of the law.

Article 3.º, under the heading "Factoring Contracts", stated in n.º 1 that "*The set of relations between the factor and each of the adherents is governed by factoring contracts"*, requiring, in n.º 2, that the credits transmitted under factoring contracts must be supported by invoices or equivalent documentary representation.

Articles 4.º and 5.º dealt with the payment of the claims transferred and the factor's remuneration.

By virtue of Articles 19.º and 20.º and of article 21.º of the Lei Orgânica do Banco de Portugal, approved by DL n.º 644/75, of 15.11[65], *factoring* companies and their respective activity were subject to the regulatory and supervisory

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[61] Menezes Cordeiro, *Da cessão financeira (Factoring),* cit, p. 34.

[62] Ibid, p. 36.

[63] The summary, somewhat pretentious, proves to be out of step with the slightly more modest reality of the diploma, which, despite its 29 articles, devotes few provisions to the contract, striving more to regulate companies that have such an activity for object. See Rui Pinto Duarte, *Notas sobre o contrato de factoring,* cit, p. 142, Damião Vellozo, *Sociedades de factoring, Sociedades de risco,* Editora Rei dos Livros, Lisboa. 1990, p. 20 ff, João Caboz Santana, *O contrato de factoring, Sua caracterização e relações factor-aderente*, p. 35.

[64] The concept of short-term credits in the writing of this article is an indeterminate one. However, the literature marks the short term in the period between 30 to 180 days. See Mauro Bussani/Paolo Cendon, *I Contratti Nuovi*, cit, p. 260.

[65] Subsequently, articles 22 and 23 of the Organic Law of Banco de Portugal, approved by Lei Orgânica do Banco de Portugal, approved by DL n.º 337/90, of 30.10. With the changes introduced by Lei n.º 5/98, of 31.01 to the Lei Orgânica do Banco de Portugal, having In view of its integration in the European System of Central Banks, this matter is now regulated in articles 15.º and 17.º.

powers of the Banco de Portugal. These powers were exercised through Aviso n.º 5/86 of 18.04 and, subsequently, Aviso n.º 4/91 of 25.03. In addition to imposing the written form of the contract, they governed certain aspects relating to the execution of the contract, not considered in DL n.º 56/86[66].

This law has been much criticised by legal scholars.

In this sense, Rui Pinto Duarte considers that the legal concept set out in Article 1.º of DL n.º 56/86 is both excessive and flawed[67].

In excess, to the extent that the Author classifies as redundant the reference that the *factoring* activity is exercised, "*under the terms of the applicable legislation*", and unnecessary the allusion to "*internal and external market*", as he understands that nothing indicated that its absence could lead to a restrictive interpretation[68].

In the Author's opinion, it is also flawed because it does not make any reference to the services provided by *factoring* companies, considering that the acquisition of credits referred to in Article 1 is nothing more than the legal form by which such services are provided[69].

Teresa Anselmo Vaz also considered that, in this diploma, the legislator relegated the *factoring* contract to second place, not taking a position on the legal questions underlying it, opting instead to focus on its economic and financial aspects[70].

Menezes Cordeiro considered this diploma as a reflection of the prolixity of the Portuguese economic legislation[71], pointing out that it is the most extensive regulation of the countries legally close[72].

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[66] Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão Financeira (Factoring),* cit, p. 107, note 259, refers that Banco de Portugal, through these notices, made it mandatory to include certain clauses in the contracts entered into by factoring companies, contributing unquestionably to regulate the content of the contractual type of factoring. The fact that factoring contracts must be written, imposed by al a) of article 1.º of Aviso n.º 5/86 of 18.04 and maintained in al a) of article 1.ç of Aviso n.º 5/86 of 18.04 and the mandatory transmission of credits opened by a factoring contract through periodic proposals by the adherent to the factor imposed by paragraph c) of article 1.º, al. c) of article 1.º of Aviso 4/91 of 25.03. The Author considers this obligation imposed in al. c) of art. 1.º of Aviso n.º 4/91 is extremely criticized, as it made it impossible for the factor to be agreed with the client in the sense that the latter make a global assignment of future credits. We cannot forget, however, that these notices did not intend to establish the legal regime of the factoring contract, being certain that nothing prevented the factor from entering into factoring contracts in spite of the impositions contained in the Notices. This is so, because the violation of these rules, as the Author refers, did not result in the nullity of the contract, but only the penalty of the infringer by Banco de Portugal.

[67] *Notas sobre o contrato de factoring*, cit, p. 143.

[68] Ibid, p. 143.

[69] Ibid, p. 143.

[70] Teresa Anselmo Vaz, *O contrato de factoring*, cit, p. 58 ff.

[71] Menezes Cordeiro, *Da cessão financeira (Factoring),* cit, p. 36.

[72] Menezes Cordeiro, *Manual de Direito Bancário*, p. 761.

The Author considers that this diploma *"was victim of a double philosophy of strict speciality and detailed regulation"*[73].

The solution adopted by this Author was not to regulate the *factoring* contract, whose regulation should depend on the autonomy of the parties and the application of general principles[74].

João Caboz Santana, in opposition to Rui Pinto Duarte, maintains that Article 1.º, by itself, does not provide sufficient elements for the construction of a concept of *factoring*. The Author explains that the contours of the factoring contract are found from the combination of Article 1.º, which describes the *factoring* activity, with Article 2.º, which defines the subjective requirements for *factoring,* as well as the legal concepts of factor, adherent, and debtor, the subjects involved in the contract and, in the specific case of the debtor, affected by *factoring.* In the author's opinion, Article 4.º, in which the legislator addresses the form of payment for the credits transmitted also offers elements for defining the contract, although the possibility of the transmission of credits being *pro solvendo* or *pro soluto* is left open[75].

Thus, the Author sustains, from subjective and objective elements, the existence of a concept of *factoring* as being the contract "*by which one of the parties (the adherent) undertakes to assign to the other, for consideration, the totality of his present and future short-term credits resulting from his professional activity, which, if he accepts the assignment, assumes or not the risk of the debtor's solvency and receives in exchange, a determined commission, calculated on the value of the credits assigned, which will also pay the accounting and legal support inherent to the good collection of those credits*"[76].

This Author ends up recognising, in some contradiction with the position taken about the existence in the law of sufficient contours for the construction of the concept above mentioned, that the legislator limits himself to describing the *factoring* activity, not providing sufficient elements in the references that he makes to the contract to characterise, its content and regime, under the legal point of view[77].

At this point, we must agree with the Author, and with all those who consider that this law did not bring anything new as to the legal framework of *factoring in* relation to what already existed, arising from the business *praxis.* So much so that Article 3.º, dedicated to the factoring contract, states a Lapalisse's truth, paraphrasing José Carlos Pires[78], ruling that the *factoring* companies celebrate *factoring* contracts with their clients. In fact, no reference is made to the

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[73] Menezes Cordeiro, *Direito Bancário – Relatório*, Almedina, Coimbra, 1997, p. 98.
[74] Ibid, p. 98.
[75] João Caboz Santana, *O contrato de factoring,* cit p. 27.
[76] Ibid, p. 27 ff.
[77] Ibid, p. 35. The Author ends up considering this contract atypical. In our opinion, in view of the position adopted by the author, it seems to us that it would be more coherent for him to admit the existence of an open legal type, in the DL nº 56/86, de 18/03.
[78] *O contrato de factoring*, cit, p. 87, note 236.

material content of the *factoring contract.*

However, it will always be said that, in our opinion, this law may be accused of having erred by excess in the sense that it went much further than what was intended: to launch the economic-legal bases of the *factoring* activity.

We do not agree with the criticism made by Rui Pinto Duarte and, implicitly, by Teresa Anselmo Vaz, relative to the absence of the material content of the *factoring* contract and of an answer to the legal questions it raises.

Firstly, we must not forget that in Law *omnis definitio periculosa est*[79] and secondly, it does not seem to us, from the reading of the preamble and the articles, that the legislator intended to regulate the *factoring* contract, but the *factoring activity*[80].

This clear lack of a specific legal regime has led literature to consider the *factoring* contract atypical, notwithstanding DL n.º 56/86 of 18.03[81].

With the enacting of DL n.º 298/92 of 31.12, which approved the Regime Geral das Instituições de Crédito e Sociedades Financeiras (General Regime of Credit Institutions and Financial Companies), also known by RGICSF, the *factoring* company changed from a para-banking institution to a financial institution, according to h) of Article 3.º, having also been extended the exercise of *factoring* to banks, through b) of n.º 1 of Article 4.º. The detailed regulation that DL n.º 56/86 offered regarding to *factoring* companies was transferred to the RGICSF[82].

DL n.º 58/86 of 18.03, in the sequence of the reforms undertaken after the publication of the RGICSF, was finally revoked in 1995, as had been anticipated, by DL n.º 171/95, of 18.07[83]. The legislator expressly refers in the respective preamble that he intended with the alterations introduced to *"clarify and deregulate the factoring contract regime"*, seemingly accepting Menezes Cordeiro's

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[79] As reminds Maria João Tomé, *Algumas notas sobre a natureza jurídica e estrutura do contrato de factoring,* DJ, 1992, p. 253.

[80] Rui Pinto Duarte, *Notas sobre o contrato de factoring*, cit., p. 143, admits the dangers of the definition in law and the intelligence that resides in the decision not to regulate certain aspects.

[81] Teresa Anselmo Vaz, *O contrato de factoring*, cit, p. 78, Maria João Vaz Tomé, *Algumas notas sobre a natureza jurídica*, cit, p. 273, Caboz Santana, *O contrato de factoring,* cit, p. 35, José Carlos Pires, *O contrato de factoring,* cit, p. 86.

[82] The DL n.º 298/92 of 31.12, has, however, been altered by several diplomas, the most recent and profound change imposed by DL n.º 201/2002, of 26.09.

[83] With the entry into force of DL n.º 171/95, there are authors who maintain that Aviso n.º 4/91 issued under arts. 19.º and 20.º of DL n.º 56/86, was tacitly revoked, since it was issued under a diploma that was revoked (art. 10 DL n.º 171/95), a position to which we also adhere. See António Pinto Monteiro/Carolina Vicente, *Sobre o contrato de cessão financeira ou de factoring*, BFDUC, Volume Comemorativo, 2003, p. 531. These Authors draw attention to the fact that the RGICSF attributes, among others, the competence to Banco de Portugal to issue notices, which will not be exclusively addressed to factoring companies, but to credit institutions in general. In favor of maintaining Aviso n.º 4/91 in everything that does not contradict the DL n.º 171/95, see Mafalda Oliveira Monteiro, *O contrato de factoring em Portugal,* cit., p. 36. With some doubts raised by the fact that the issuance of this notice derives from the Organic Law of Banco de Portugal, but pending for the tacit revocation of the notice, see Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão financeira (Factoring)*, cit, p. 195, note 259.

criticism.

In this law, the legislator dedicates only two articles, Articles 7.º and 8.º, to the *factoring* contract and its operation, limiting itself to imposing in Articles 7.º, n.º 1 the written form, in n.º 2 requiring the assignment of credits to be accompanied by the respective deeds and in Article 8.º stating some rules relating to the payment of the credits assigned, namely the anticipation of payments[84].

In n.º 1 of Article 1.º , the legislator refers to *factoring* or financial assignment[85], in a vague way, as being *"the acquisition of short term credits derived from the sale of products or rendering of services, in the internal and external markets".* The second paragraph adds that factoring activities include "*complementary actions of collaboration"* between *factoring* companies and their clients, "*namely the study of credit risks and commercial and accounting legal support for the good management of the credits transacted"*[86].

Article 4.º, on the other hand, established the principle of exclusivity, that is, only *factoring* companies and banks could normally conclude *factoring* contracts[87]. This article was expressly revoked by Article 4.º of DL n.º 186/2002 of 21.08 that introduced in Article 1.º the Credit Financial Institution, abbreviated

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[84] With regard to art. 8, which practically reproduces Article 4 of DL n.º 56/86, Menezes Cordeiro criticizes the way in which the legislator established limitations on the payment of the credits transmitted, alerting to the possibility that doubts may arise regarding the interpretation of the article. Indeed, nº 3 seems to prevent advance payments in relation to the due date, although n.º 2 allows them. In the Author's interpretation, only prepayments for non-existent credits are not allowed, and prepayments on account of the assigned credits are allowed, even if they are not overdue. This is for Menezes Cordeiro one more example that it would be all easier if the Portuguese legislator, following the example of the legislators of industrialized and post-industrialized countries, abandoned the idea that everything has to be regulated in detail. We agree with the author. See Menezes Cordeiro, *Manual de Direito Bancário*, cit, p. 761 and 773.

[85] The legislator seems to accept the term financial assignment suggested by Menezes Cordeiro to translate factoring. In that regard, Romano Martinez, *Contratos Comerciais*, *Apontamentos*, Principia, Lisboa, 2001, p. 66, note 10, Expresses doubts about considering the factoring contract as named, taking into account the use by law of two designations - factoring and financial assignment. Conversely, considering the factoring or financial assignment contract named see Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão financeira (Factoring)*, cit, p. 182. Pinto Monteiro/Carolina Cunha, *Sobre o contrato de cessão financeira ou de Factoring,* p. 17 and José Carlos Pires, *O contrato de factoring,* cit, p. 91. It is curious to note that in Article 3.º, dedicated to the identification of the subjects involved in the activity of factoring or financial assignment, the legislator attributed the designation of "factor" or "assignee" to the factoring companies or banks referred to in n.º 1 of Article 4.º to who recognizes, in paragraph 2, the designation of a factoring or financial assignment company. However, they keep the expression "adherent" to designate the client. For the sake of consistency, we understand that, when referring to the client, the legislator could have included the term assignor. Thus, there would be total harmony with the fact that it admits two expressions form the same contract, reflected in double naming of *factoring* legally accepted.

[86] This Article 2.º is quite similar to Article 1.º of DL n.º 56/86, with the difference that the legislator, perhaps sensitized by the criticism of Rui Pinto Duarte, decided to delete the expression "under the terms of the applicable legislation"

[87] With the exception of Caixas de Crédito Agrícola Mútuo.

to IFIC, with the objective that these institutions could develop the activities allowed to *factoring* companies. These IFIC, by virtue of an Article 2.º of the above-mentioned law, are subject to the RGICSF.

In relation to the deregulation promised in the preamble, we verified that DL n.º 171/95 abolished the reference, existing in Article 5.º of DL n.º 56/86, to the factor's retribution and the redundant definition of *factoring* contract contained in n.º 1 of Article 3.º of DL n.º 171/95.

DL n.º 171/95 kept the obligation for *factoring* contracts to be made in writing, an obligation already imposed by the Bank of Portugal in Aviso n.º 5/86 of 18.04 and later in Aviso n.º 4/91 of 25.03.

Factoring is also included in the Stamp Duty Code and its General Table. In effect, the customer of a factoring company*, by virtue* of the provisions of articles 1.1, 2.2 and 3.f) or 3.g) and of item 17.1 of the General Tax Table (TGIS) approved by Law 150/99, of 11th September, as amended by DL n.º 287/2003, of 12.11, Law n.º 12-A/2010, of 30.06, is obliged to pay stamp duty. However, it is not enough to enter into a *factoring* contract*; it* is essential, as stated in the above-mentioned article, that any form of finance to the customer by the factor results from that contract. Therefore, tax will only have to be paid under the terms of Item 17 of the TGIS in the hypothesis of the factor paying the client all or part of the credits in advance, under the terms of the provisions of n.º 2 of Article 8.º of DL n.º 171/95[88].

There are authors who consider that, given the fact that the regulation of the *factoring* contract in this diploma is so vague, it remains an atypical contract[89].

4. Legal typicity

Before investigating whether a *factoring contract* is a socially typical contract, we believe it is essential to distinguish between a legal type and a social type. Thus, it is necessary to keep in mind that contractual types may be legal or extra-legal. In a simplified manner, we may consider that legal types are those typified in law and extra-legal types are those typified in business practice[90].

Under the principle of private autonomy, enshrined in Article 405.º of our Civil Code, the parties may enter into contracts other than the types pre-established by law and simultaneously modify the rules governing a certain type of

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[88] It should be noted that the factoring contract, as a contract reduced to writing, is subject to the payment of stamp duty, under the terms of n.º 8 da TGIS. See Ac of RP of 15.06.1999, CJ, Year XXIV, Tomo III, 1999, p, 219 ff.

[89] Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão financeira (Factoring)*, cit, p. 183 ff, José Carlos Pires, *O contrato de factoring - Estrutura e Causa,* cit., p. 89 ff.

[90] Cfr. Mota Pinto, *Cessão da posição contratual*, cit, p. 94, Maria Helena Brito, *O contrato de concessão comercial*, Almedina, 1990, p. 155, Pinto Monteiro/Carolina Vicente, *Sobre o contrato de cessão financeira. ou de Factoring*, cit, p. 521 ff and Pedro Pais de Vasconcelos, *Contratos Atípicos*, Almedina, Coimbra, 1995, p. 59 ff.

contract according to the interests which they intend to satisfy with the contractual relationship created. The economic foundation of this principle lies in the need for the parties to be able, at their discretion, to adapt the contract to the concrete purposes they intend to pursue[91].

For this reason, the legal types do not exhaust the contractual types. In fact, in addition to the types typified in the law, there are other contract types in practice. These types are the social types, types that emerge from business practice[92].

Thus, if, traditionally, contractual typicality, herein understood as a means of regulation through types, was identified and exhausted in the legal typicality, with the consequence that only the contracts governed by the legislator were considered typical, nowadays it also encompasses social typicality[93].

There are no exact criteria for assessing whether or not a contractual practice constitutes a business type, not least because social typicality itself is gradable[94]. There is, in fact, a set of indications collected by legal scholars which make it possible to distinguish the social type from other situations of business practice.

The social typicality proves to be, from the outset, quite important in the discovery of Law, because through the reconnection of concrete contracts to the corresponding extra-legal types of the criteria for the interpretation and integration of the stipulated regulation are found. Basically, as Pedro Pais Vasconcelos states, "*the regulatory model constituted by the social type functions as the dispositive law in the legal type*"[95].

The social type, besides being a phenomenon that imposes itself on the legal order, is an instrument of rationality, economy and evolution, facilitating the negotiation between the economic operators, simplifying the discussion on the validity and legal discussion of the contract in question, since the respective discipline will be drawn up by literature and jurisprudence[96].

Thus, it is possible to find contracts that are legally atypical but socially typical, nevertheless some authors, following the admissibility of social typicality, reserve the category of atypicality only for contracts that do not correspond neither to legal types nor to social types[97].

In this sense, the *factoring* contract, as in other legal systems, is not an

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[91] Cfr. Maria Helena Brito, *O contrato de concessão comercial*, Almedina, 1990, p. 155.
[92] Pedro Pais de Vasconcelos, *Contratos atípicos,* cit, p. 59 ff.
[93] In this respect, see Pinto Monteiro/Carolina Vicente, *Sobre o contrato de cessão financeira ou de Factoring*, cit, p. 521. On the admissibility of social typicality, see the biography named by Maria Helena Brito, *O contrato de concessão comercial*, cit., p. 169, note 57 and referred by Rui Pinto Duarte, *Tipicidade e atipicidade dos contratos*, Almedina, Coimbra, 2000, p. 33, note 63.
[94] Pedro Pais de Vasconcelos, *Contratos atípicos,* cit, p. 60 ff.
[95] Ibid, p. 62.
[96] See Maria Helena Brito, *O contrato de concessão comercial,* cit, p. 169 and Pedro Pais de Vasconcelos, *Contratos Atípicos*, cit, p. 60 ff, Against the relevance of social typicality in the Portuguese context, see Rui Pinto Duarte, *Tipicidade e atipicidade dos contratos*, cit, p. 42, note 82.
[97] Maria Helena Brito, *O contrato de concessão comercial,* cit, pág. 169-170.

atypical contract, in the sense that it has no model either in law or in practice.

The *factoring* contract performs a relevant socio-economic function, is uniformly designated, apart from exceptional attempts at translation, has a very high degree of dissemination, presents contractual clauses common to the various legal systems and has merited much attention from case law, although in our country this is still scarce, and from literature, which recognises its social typicality[98].

In relation to the type, more important than detecting the presence or absence of the essential elements, is to ascertain whether or not the specific case, *e.g.* a contract, can be traced back to the general framework, being essential to determine the intensity with which those elements exist in the specific case. The question of the submitting a concrete case to a type is no longer posed in terms of alternative but in terms of degree or intensity. Thus, it is possible to submit it to types that are in a relationship of similarity and not of identity. A complex reality can be led to a type and not be subsumed into the concept[99].

In Legal Science, concepts are used preferentially, because, by allowing an operation in exclusively logical terms, they provide, therefore, a guarantee of certainty and security to the system.

Thus, the legislator, even in matters such as contracts where the type could be relevant, chose to privilege concepts. Our legislator, similarly, to the German, French and Spanish legislator, constructs contract types as authentic concepts, as will be the case of the contracts typified in our Civil Code[100].

The legal types, by default, are open, without a determined and fixed number of characteristics. However, the legislator, in attention to the value of certainty in Law, did not receive the open types from the practice, having them closed, crystallized in concepts[101]. This transformation of the open type into a closed type makes subsumption possible[102].

Thus, it is necessary to bear in mind that when we refer to contracts and

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[98] Cfr. Maria Helena Brito, *O «factoring» internacional e a Convenção do Unidroit*, cit, p. 17, Menezes Cordeiro, *Da cessão financeira (Factoring),* cit, p. 84, José Carlos Pires, *O contrato de factoring - Estrutura e Causa*, cit, p. 90, Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão financeira (Factoring)*, cit, p. 188, Pinto Monteiro/Carolina Cunha, *Sobre o contrato de cessão financeira ou de Factoring*, cit, p. 523, Pedro Pais de Vasconcelos, *Contratos at*ípicos, p. 213, Zuddas, *Il contrato di factoring,* p. 205 admits that the factoring contract is a social type, but no longer a jurisprudential type. It should also be noted that the factoring companies' use of general contractual clauses, in the general part of the contracts, leads to a natural uniformity that enhances the social character of the contract.

[99] See Maria Helena Brito, *O contrato de concessão comercial,* cit, p. 159 ff.

[100] The tendency is for jurisprudence to bring the contract back to a legal type. See Sacco, *Autonomia contrattuale e tipi,* RTDPC, part II, 1966, p. 798 ff. In this way, Pinto Monteiro/Carolina Cunha, *Sobre o contrato de cessão financeira ou de Factoring,* cit, p. 524, note that the interpreter has a tendency to deny the existence of a legal typification where he does not find a closed type.

[101] As refers Maria Helena Brito, *O contrato de concessão comercial,* cit, p.162, typical contracts are not 'types' in the technical sense.

[102] Ibid, p. 162; Pedro Pais de Vasconcelos, *Contratos atípicos*, cit, p. 39 ff.

inquire about the respective legal type, we can find the *closed type,* i.e. a concept, formed by a set of elements - all of equal importance - whose subsumption requires the verification of all of them. The subsumption of the contract to the type is made by means of an alternative judgment of application or non-application of the concept.

However, we can also find the legal type in a technical sense, being certain that these are, by essence, open, elastic, not having, therefore, defined and firm boundaries, not being possible to determine with certainty where the type begins and where it ends. As they do not contain definitions, they are not susceptible of subsumption[103]. As to the latter, it is not a matter of assessing whether the concrete case is or is not subsumable, but rather, whether the latter, to a greater or lesser extent, is in line with it.

Bearing these introductory considerations in mind, the first impression caused by DL n.º 171/95, of 18.07, with the consequent revocation of DL n.º 56/86 and the Avisos that regulated it, is that there is no legal definition of the contract, being practically exempt from regulation in the Portuguese legal system[104].

In effect, it seems to us that we can safely say that DL nº. 171/95, of the 18.07, does not contain any definition of a *factoring* contract, nor does it establish the application of a legal regime. The complexity of the social type that we analysed above is not, in any way, regulated by this law.

However, there are authors who maintain that DL n.º 171/95 contains elements that, from the point of view of the subjects and contents of the contract, are sufficient to delimit a global framework for the contract, not in the sense of a detailed legal framework, proper of a closed type *factoring* contract, but fit to an *open type.*

Pinto Monteiro and Carolina Vicente[105], develop, in this sense, a very interesting position because, although they sustain that DL n.º 171/95 does not establish a closed legal type, they understand that the legislator, when in Article 1.º mentions that "*the present law regulates factoring companies and the factoring contract",* wanted to provide a legal type of *factoring,* although open. The legislator disciplined the subjects, the object and the services. Thus, the Authors maintain that the content of the contract is given through the definition of the services to be provided by the factor, in Article 2.º(2) (management services), Article 8.º(1) (collection of credits) and Article 8.º(2) (anticipation of funds); the

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[103] Cfr. Pedro Pais de Vasconcelos, *Contratos atípicos,* p. 43.

[104] Menezes Cordeiro, *Da cessão financeira (Factoring), cit*, p. 34–36, 82-84, Rui Pinto Duarte, *Notas sobre o contrato de factoring*, cit, p. 141 ff, Maria João Tomé, *Algumas notas sobre a natureza jurídica e a estrutura do contrato de factoring*, cit, p. 251 ff, 270 ff, Teresa Anselmo, *O contrato de factoring*, cit, p. 78, already considered the factoring contract to be legally atypical, before DL n.º 171/95.

[105] Pinto Monteiro, *Sobre o contrato de cessão*, cit p. 524 ff.

definition of the services to be provided by the customer in Article 2.º(1) (assignment of credits) and Article 7.º(2) (forwarding of documents); the definition of the subjective element in Article 4.º(1) when attributing the exclusivity of the factoring to banks and *factoring* companies and Article 2.º(1)when attributing the quality of supplier or service provider to the counterparty and, finally, by defining the objective element, specifying in n.º 1 of Article 2.º which credits are the object of the contract

For the Authors, these typifying elements provide the global image of the contract. The Authors explain that it is not enough for the factor to be one of the entities referred to in Article 4.º and he contract to have a financial component, considered essential in Article 2.º n.º 2, to qualify it as a factoring contract. As an example of the openness of the type, it is accepted that a contract that does not include credits management, but offers risk coverage, a function that is not even mentioned in the law, or includes an assignment of credits of medium and long-term credits may be considered as factoring contract according to DL n.º 171/95.The qualification as an open type is not an alternative between *yes* or *no,* but a *more* or *less that* can only be verified in the concrete case[106].

Despite being very coherent, we view this position with many reservations, since DL n.º 171/95 does not even contain all the functions of the *factor,* for example, the function of guaranteeing the credit risk and also because with the revocation of article 4.º by Article 4.º of DL n.º 186/2002 of 21.08, *factoring* activity is no longer exclusive to banks and *factoring* companies, one of the strongest arguments used in defence of this position.

However, we do not consider this to be a settled issue, and it is certain that until the revocation of Article 4.º of DL n.º 171/95, we had more doubts in rejecting the existence of a very open type of legal *factoring* contract.

Thus, even if we were to consider the *factoring contract as* approximating to an *open type,* in light of the insufficiency of the text of the law, we cannot conclude that there exists in our legal system a legal type to which the factoring contract could be subsumed. In our opinion, in order to consider the *factoring contract* to be legally typical, it would be necessary that DL n.º 171/95 contained "*the complete model of the typical discipline of the contract",* a regulatory model that can be of greater or lesser scope, being, however, necessary that the legal regulation correspond, at least approximately, to the social type in order to provide the parties with the basic discipline of the contract[107].

However, in light of the reading of the legal text, this is far below the complex of rights and duties established between assignor and factor in contractual *practice,* namely the existence of an exclusivity and globality clause, the mechanisms of credit approval, the modalities "with recourse" and "without recourse" of the assignment of credits and the respective particularities regarding,

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[106] Pinto Monteiro/Carolina Vicente, *Sobre o contrato de cessão financeira ou de Factoring*, cit, p. 526 ff.

[107] Pedro Pais de Vasconcelos, *Contratos atípicos,* p. 210.

for example, the factor's right of recourse.

Only, we can extract that the *factor* will always have to exercise the function of management and collection of the rights ceded (Article 8.º, n.º 1) and provide commercial consulting services (Article 2.º, n.º 2). This will be the minimum scheme that the factoring contract, concluded between the parties, could assume. It will, however, be far below the business practice, which prevents a legal type being inferred from it[108].

As Menezes Cordeiro observes[109], the *factoring contract,* pursuant to Article 7.º of DL n.º 171/95, is subject to being concluded in writing, everything else resulting from the autonomy of the parties and general principles. The legislator, in our opinion, left the *factoring contract to the* free regulation of the parties, under contractual freedom[110].

This lack of legal regulation means that the *factoring* contract, from a legal point of view, must be considered atypical[111].

It should only be pointed out that, at this moment, we can already conclude that the rules existing in the Civil Code relative to the assignment of credits (Article 577.º and ff), the rules of the Commercial Code relative to the current account (Article 344.º and ff) are applicable to the *factoring* contract, as it is clear that within the scope of this contract a current account is established for the updating of credits and debts that arise during the course of the contract[112].

However, and as we have already mentioned, the fact that the *factoring*

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[108] See Luís Miguel Pestana de Vasconcelos, *Dos contratos de cessão financeira (Factoring)*, cit, p. 173.

[109] Menezes Cordeiro, *Direito Bancário - Relatório*, cit, p. 98.

[110] Menezes Cordeiro, *Do contrato de franquia («Franchising»): autonomia privada versus tipicidade negocial*, ROA, Ano 48, Lisboa, Abril 1986, p. 66, warns against the excesses of legal typicality in contracts.

[111] Luís Miguel Pestana Vasconcelos, *Dos contratos de cessão financeira (Factoring),* cit, p. 183 ff, considers this contract atypical since it does not have its own legal regime, an idea that is immediately reinforced by the dynamics and functions that the factor may or may not assume. Also, in the sense of atypicality, see Romano Martinez, *Contratos comerciais, Apontamentos*, cit, p. 66 and José Carlos Pires, *O contrato de factoring - Estrutura e Causa*, cit, p. 90.

A different question is whether we should consider it a pure atypical contract or a mixed atypical contract in the sense that this atypical result from the modification of a certain type or the combination of several types. Pais de Vasconcelos, *Contratos atípicos,* p. 211. Menezes Cordeiro, *Manual de Direito Bancário*, cit, p. 763, mentions a mixed typicality with elements of promise to sell future credits, risk-taking, provision of various services. In the sense of the mixed atypicality of the factoring contract, see Ac of RL, of 27.05.2001, CJ, XXVI, III, p. 102 ff.

[112] Pinto Monteiro/Carolina Vicente, *Sobre o contrato de cessão cessão financeira ou de Factoring,* cit., p. 537, observe that it will be more difficult to apply rules that integrate the discipline of certain contracts, in particular, the purchase and sale, mutual, mandate. Such difficulty does not result, in our opinion, from the affirmation of the legal characteristic, which, for the reasons already mentioned, does not occur, but because it is an autonomous contract whose social characteristic is evident. Thus, such standards can only be applied analogously. The same happens with the provisions regarding the agency contract that some doctrine, as already mentioned, intends to apply to the factoring contract, namely, art. 28 and 30 referring to the termination and termination of the contract., See Menezes Cordeiro, *Manual de Direito Bancário*, cit, p. 771.

contract is not a legal type does not prevent it from being a social type, raised by business *praxis*[113].

There is therefore no legal type of *factoring* contract, but rather a social type[114].

5. Conclusions

As we have seen, from the historical evolution of factoring from the 16th century to the present day, this contract reveals great versatility, assuming several outlines.

The historical evolution of *factoring* was the criterion that we decided to use for the presentation of the various types of *factoring*.

In effect, the literature has pointed out several criteria to establish the typology of *factoring,* namely the type of *factoring* company, the method of execution, the financing function and the geographic area, criteria that, despite not being autonomous, are present in our exposition.

Following Menezes Cordeiro, we concluded that the factoring contract, under the terms of Article 7.º of DL n.º 171/95, is subject to written celebration, everything else resulting from the autonomy of the parties and the general principles. The legislator, in our opinion, left the factoring contract to the free regulation of the parties, under contractual freedom.

This absence of legal regulation means that the factoring contract, from a legal point of view, has to be considered atypical.

The fact that the factoring contract is not a legal type does not prevent it from being a social type, built by the praxis.

There is, therefore, no legal type of factoring contract, but a social type.

Finally, the analysis of the characteristics assumed by the factoring contract, allowed us to conclude that it has a complex, articulated and variable cause, depending on the conditions negotiated by the parties.

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[113] Maria Helena Brito, *O contrato de concessão comercial, cit.,* p. 168 ff.

[114] The analysis of national jurisprudence courts, among which we highlight the decisions of Supremo Tribunal de Justiça 05.06.2003, Proc. n.º 03B1466, 3.05.2012, Proc. 6018/05.0TBSXL.L1.S1, STJ 13.09.2012, Proc. 384/09.5TVPRT.P1.S1, 15.01.2013, Proc. 345/03.8TBCBC.G1.S1, Tribunal da Relação do Porto 15.11.2018, Proc. nº 596/15.2T8PVZ.P1 Tribunal da Relação de Lisboa 13.07.1995 Proc. nº 0083866, 27.11.1997, Proc. n.º 0018742, 14.05 2015, Proc. 649/13.1TVLSB.L1-8, available at www.dgsi.pt , allow us to sustain that there is a jurisprudential type. The decisions of Supremo Tribunal de Justiça 18.11.2010, Proc. nº 129/03.0TVLSB.L1.S1, Tribunal da Relação de Guimarães 4.03.2010, Proc. 196831/ 08.0YIPRT.G1, Tribunal da Relação do Porto 11.10.2018, Proc n.º 24142/16.1T8PRT.P1 considerer applicable to factoring contract the assignment of credits framework. Jurisprudence seems to have absorbed the social type of factoring, although it still reveals ignorance of the special complexities of the contract and avoids dwelling, with some exceptions, on the legal nature of the contract. Thus, it seems to us that there is some identity between the social and jurisprudential type, the latter not deserving particular emphasis in the absence of treatment of the legal nature of the contract. See Sacco, *Autonomia contrattuale*, cit, p. 790, regarding the separation between legal, social and jurisprudential types.

In fact, the factoring contract can operate a basic set of functions (financing, credit risk taking, consultancy, management and collection), which are articulated differently in the different individual credit transmission contracts.

Among other advantages, provides immediate cash inflow as this sort of finance shortens the cash collection cycle, provides analysis and useful information about the credit standing of the customers, reduces the bad debt and the administrative and management costs.

For this reason, it can be particularly relevant for companies in the economic recovery after the COVID pandemic

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