

Finance for Development

Banking Commission

Position paper of the Legal Committee on Irrevocable Payment Undertakings (IPUs)

There is set out below a summary of the points discussed by the Legal Committee in relation to IPUs.

There follows the Legal Committee recommendation to the ICC Banking Commission as drafted by a working group led by Geoffrey Wynne and endorsed by the ICC Legal Committee.

Discussion points

Nature of IPUs

It is agreed that IPUs should mean irrevocable payment undertakings, not independent payment undertakings.

IPUs have limited usage (i.e. in relation to receivables arising under sale and services contracts and perhaps other commercial contracts). Their use is mainly for receivables finance transactions. They may also serve as security or quasi security in commodity self liquidating transactional trade finance facilities. This would be wider than supply chain finance. IPUs are not to replace promissory notes (**PNs**). A PN is an irrevocable promise to pay that is separate from but often connected to another transaction. An IPU is a promise to pay under a commercial transaction.

IPUs = waiver of Buyer's rights (except defective goods claim which could be pursued separately): a promise to pay without withholding /deduction /set off /counterclaim.
IPU is to remain classified as a trade debt, not a bank debt.

An IPU is a bankable undertaking but not a bank debt (which takes the payment obligation outside of the purpose for which it was intended) since it is used to evidence an IPU arising out of the sale or services contract – therefore we can seek to avoid any recharacterisation risk.

Delivery of IPUs

An IPU is a payment obligation given by the Buyer of goods and services to the Seller, and not by a third party (e.g. Guarantor) and not given to a third party (eg. a financier).
It should be fully assignable by the Seller.

Specimen IPU

A typical **Specimen IPU Statement**: *"I irrevocably agree to pay you the amount due under this contract/invoice, without any right to withhold payment, make deductions, or set off or counterclaim in respect of the amount due."*

Issues

Issues to be considered include: (i) applicable law of the IPU; (ii) commerciality of having a Buyer sign IPUs; (iii) reclassification between trade debt and bank debt; and (iv) assignability of IPUs.

Discussions surrounding the applicable law of IPUs

- The irrevocable nature of the payment obligation is dependent and should be specified in and follow the relevant commercial contract, therefore what may be needed is a separate set of rules or, at least, guidance for IPUs.
- This also raises questions as to the enforceability of such undertaking (which is dependant upon applicable law) as it is up to the courts of each jurisdiction to take a view as to what type of instrument an IPU is as it is up to the relevant court to interpret the undertaking.
- Options:
 - 1) The undertaking does not need to be a separate instrument. Ultimately what the Seller wants from the Buyer is for the Buyer to give a statement along the lines of: *“I will irrevocably and unconditionally pay you this amount for the good/services”*. The Specimen IPU Statement could appear in an invoice acknowledgment or be built into the underlying contract. We are not trying to create an independent instrument, but to evidence what an IPU is. If it appears in a contract, it will be governed by the law of underlying contract.
 - 2) When a Buyer gives the Specimen IPU Statement, this would mean that, whatever the applicable law is, the ‘new rules’ would provide that the Buyer will pay (and will not deduct anything (credit note, tax or otherwise) from the payment) – therefore an IPU can be seen as highly valuable in receivables financing since it improves the bankability of such receivables.
- What if the Buyer does not pay under the IPU, under which law would we examine the Buyer’s liability to the financier? If you do not specify a law to govern the IPU, the assumption is that the IPU will follow the law of the underlying contract.

Discussions surrounding the commerciality of IPUs

- If the Buyer provides the Specimen IPU Statement, this would mean that they are giving up the rights they would otherwise have. This raises questions as to the commercial viability of the IPUs (e.g. would a Buyer be prepared to give this statement, especially without financing?).
- Arguments:
 - An IPU does not seek to prevent the Buyer from utilizing its rights to claim against the Seller for defective goods, but it does give up the right to withhold payment of an invoice.
 - A Specimen IPU Statement from the Buyer will be commercially challenging, but if the Buyer understands the bankability of such statement, it may be interested.

Discussions surrounding the reclassification of IPUs from trade debt to bank debt

If the Specimen IPU Statement is given to the financier, then there is a risk of reclassification from trade debt to bank debt.

- The Specimen IPU Statement should be given to the Seller.
 - An IPU is given to the Seller. The Seller can then use this characteristic of the trade debt, and the assignability of it in a financing.

- On this basis, the Buyer would see that if they give the Specimen IPU Statement to the Seller, the debt will remain trade debt.
- Would the characteristic change if a financier intervenes?
 - This is something to be addressed in the Paper. It can deal with the question as to whether trade debt transforms into bank debt if the Specimen IPU Statement is given to or held by the financier. The Paper could seek to influence the basis on which the IPU could remain as trade debt.

Discussions surrounding the assignability of IPUs

Assignability should solve the issue of not needing to provide the IPU directly to the financier.

Summary

The consensus is that there is appetite in the market for at least a position paper (the **Paper**) (perhaps with agreed wording for the IPU) and perhaps even new rules to apply to receivables evidenced by an IPU within sale or service contracts.

The purpose of the Paper is to tease out whether there is demand for guidance on IPUs, a form of IPU or even legally binding rules for IPUs.

Next steps

This Paper is supported by the ICC Legal Committee.

One further step would be to produce a relevant sample form of IPU as a form of template that would be seen as trade debt but also a bankable document. This IPU could be used in contracts or on invoices for example.

The IPU Working Party within the Legal Committee consisted of Frieder Bauer, Philippe Berta, Angelia Chia, Patrick Eberhardt, Sean Edwards, Lorna Strong, Ron van Staten and Geoff Wynne.

ICC LEGAL COMMITTEE