

ICC Global Banking Commission

Drafting ICC Rules for Supply Chain Finance

Position Paper

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1. Introduction

To satisfy the market demands of trade finance practitioners and standardise supply chain finance (SCF) practice globally, the Global Supply Chain Finance Forum (GSCFF)¹, facilitated by the ICC Global Banking Commission, set up the ICC Rules Workstream for SCF in 2018. After thorough investigation and careful consideration, the GSCFF has decided to issue this position paper exploring the need to draft ICC rules for SCF as a whole.

The paper concludes that the GSCFF recognises the market demand for ICC SCF rules. While it considers the conditions for drafting such rules as pre-mature at this stage, the GSCFF will continue to monitor the industry's feeling towards ICC rulemaking for SCF in the future.

The GSCFF defines SCF in the **Standard Definitions for Techniques of Supply Chain Finance**² as “the use of financing and risk mitigation practices and techniques to optimise the management of the working capital and liquidity invested in supply chain processes and transactions. SCF is typically applied to open account trade and is triggered by supply chain events. Visibility of underlying trade flows by the finance provider(s) is a necessary component of such financing arrangements, which can be enabled by a technology platform. SCF is a portfolio of financing and risk mitigation techniques and practices that support the trade and financial flows along end-to-end business supply and distribution chains, domestically as well as internationally. This is emphatically a ‘holistic’ concept that includes a broad range of established and evolving techniques for the provision of finance and the management of risk.”

The importance of SCF as a key growth area in both domestic and cross-border commerce has increased over the past couple of years. Market participants consider it as one of the key mechanisms to help bridge the gap in financing of trade for small- and medium-sized enterprises (SMEs). The demand for SCF has been driven by multiple factors including economic, regulatory and technological with varying impact in different countries. In particular, the extension of global supply chains and maturing trading relationships have contributed to an increased use of open account settlement methods driven by a demand for alternative risk and liquidity solutions. This is especially true for SMEs with challenging balance sheets when it comes to obtaining other forms of financing. These factors are summarised in a WTO paper where it was noted that “the expansion of global supply chains through the growth of open account trade involving ecosystems of small- and medium-sized enterprises (SMEs) embedded in ‘made-in-the-world’ product assembly processes; a tightening of bank lending since the great financial crisis of 2007-9, particularly for SMEs”³.

SCF is widely considered as one of the areas showing significant opportunity and the greatest potential for growth, and as a strategic priority by providers of trade finance solutions. The 2017 ICC Global Trade Finance Survey indicated that almost 30% of respondents identify SCF as the most important area for development and strategic focus in the coming 12 months. The 2018 ICC

¹ The Global Supply Chain Finance Forum is a collective group representing a number of industry associations with members around the world, with participating organisations such as the ICC Global Banking Commission, Bankers Association for Finance and Trade (BAFT), Euro Banking Association (EBA), Factors Chain International (FCI), and the International Trade and Forfeiting Association (ITFA).

² Drafted by GSCFF in 2016

³ Marc Auboin, Harry Smythe and Robert Teh, Supply Chain Finance and SMEs: Evidence from International Factoring Data, WTO Working Paper ERSD-2016-04

Global Trade Finance Survey shows that this figure increased to 38% of respondents identifying SCF as a highly strategic priority expected to drive significant growth, and 43% of respondents (compared to 35% in 2016) reported that SCF business rose. The 2020 ICC Global Trade Finance Survey revealed further increased figures, with 53% of respondents indicating SCF as an immediate (in the next 12 months) and 33% of respondents as a near-future priority (in the next one to three years). Global banks expected a significant increase in the usage of SCF over the next five years with one-third expecting a growth of over 50%.

The 2018 ICC Global Trade Finance Survey further highlighted that, among the eight SCF techniques presented in the **Standard Definitions for Techniques of Supply Chain Finance**, the four most popular techniques were payables finance, receivables discounting, factoring and loans or advances against receivables. The share of these four receivables finance techniques accounts for 85% of all the eight techniques, with payables finance becoming increasingly popular (top share of 28%). Notably, 43% of global survey respondents indicated that payables finance is one of the fastest-growing areas of trade finance. The 2020 ICC Global Trade Finance Survey found that receivables discounting (71%) is the SCF technique most demanded by clients, followed closely by payables finance (54%), loans/advances against receivables (46%), and factoring (45%).

The advantages of SCF propositions are widely acknowledged by buyers and sellers who seek to enhance their efficiency through physical and financial supply chains with alternative risk mitigation techniques in supply chain management and finance schemes. The unique features of SCF propositions, such as payables finance, make SMEs ideal candidates for providing access to adequate and affordable levels of financing that may help to narrow the global trade finance gap, which is estimated at about US\$1.5 trillion.

Nonetheless, SCF is still in development. Looking at SCF propositions globally, varying levels of evolution can be observed across different regions in terms of market awareness, product maturity, standardisation (target market, pricing, operating models, legal, regulatory and compliance aspects etc.), and technology.

SCF providers operating in different parts of the world face diverse regulatory, compliance, capital, tax and accounting requirements and standards. For example, according to the 2018 ICC Global Trade Finance Survey, 40% of respondents identified Know Your Customer (KYC) and Know Your Customer's Customer (KYCC) requirements as persistent challenges in SCF delivery. According to the 2020 ICC Global Trade Finance Survey, 34% of respondents identified KYC and KYCC as challenges, and 24% of respondents indicated the lack of clarity in accounting and regulatory treatment of SCF solutions as some of the major challenges in SCF delivery.

2. Overview

Inter-governmental organisations and industry associations, including the United Nations, European Commission, ICC, BAFT, FCI, Wolfsberg Group and the GSCFF have developed rules or rule-like documents, definitions, guidance papers and reports related to SCF, which are described in the following.

2.1 SCF techniques related rules

2.1.1 ICC rules

The ICC Global Banking Commission has successfully set up universally adopted rules for traditional trade finance products such as Letters of Credit (UCP), Standby Letter of Credit (ISP98), Demand Guarantees (URDG) and Documentary Collections (URC). Additionally, ICC has issued new electronic rules ([eRules](#)) to advance the digitalisation of letters of credit and collections, namely eUCP Version 2.0 and eURC Version 1.0. With the development of SCF, ICC has also focused on SCF in rulemaking decisions in recent years as follows:

Uniform Rules for Forfaiting

ICC **Uniform Rules for Forfaiting** ([URF](#)) have been in force since 2013. Forfaiting is one of the eight SCF techniques outlined in the SCF definitions released in 2016.

Uniform Rules for Bank Payment Obligations

In 2013, ICC developed the **Uniform Rules for Bank Payment Obligations** ([URBPO](#)) deploying the technology platform (the Trade Services Utility), which is hosted by SWIFT and limited solely to bank-to-bank interactions. With the increasing development of SCF, these rules respond to market demands for new solutions to deal with the growing use of open account in trade and the increasing move to digital processes.

Uniform Rules for Digital Trade Transactions

Due to the limitation to bank-to-bank interactions, a single technology platform and engagement with four parties at most, the URBPO in their existing format are not considered suitable to accommodate emerging technologies.

On 5 December 2018, the ICC Global Banking Commission Executive Committee approved a proposal to draft a new set of rules under the working title Uniform Rules for Digital Trade, serving as a high-level framework with obligations, rules and standards for the digitalisation of trade finance. Pursuant to feedback from the ICC national committees, the title of the rules was changed to **Uniform Rules for Digital Trade Transactions** (URDTT).

The objective is to codify those events in a commercial transaction that support the roles and obligations of participants in a digital trade transaction regardless of the underlying technology supporting the transaction.

Version 1.0 of the URDTT came into force on 1 October 2021.

2.1.2 Convention on International Factoring by UNIDROIT

In 1988, the International Institute for the Unification of Private Law (UNIDROIT) drafted and promulgated the **Convention on International Factoring**, which took effect on 1 May 1995. The Convention addresses elementary aspects of factoring.

2.1.3 Model Law on Factoring by UNIDROIT

In May 2019, the UNIDROIT Governing Council approved the project of developing a **Model Law on Factoring** for the UNIDROIT 2020-2022 Triennial Work Programme proposed by the World Bank Group (WBG) in December 2018.

The WBG made this suggestion for three main reasons:

- (i) To facilitate the use of factoring as an important form of financing to allow quicker access to credit;
- (ii) To address the constraints in access to credit, which limit economic growth, particularly in developing countries and emerging markets; and
- (iii) To address the gap that currently exists in international standards regarding factoring.

The proposal noted that existing instruments largely focus on international or cross-border transactions and do not provide sufficient guidance to states to develop functional domestic factoring frameworks.

The Model Law will be a standalone instrument for states looking to reform their domestic law to facilitate factoring. The focus will be on developing states and emerging markets that want to reform their existing domestic factoring laws, but are not yet in a position to undertake a full reform of their secured transactions law.

In July 2020, the Factoring Model Law Working Group started discussions on issues to consider when preparing the Model Law.

The draft **Model Law on Factoring** was approved by the UNIDROIT Governing Council at its 101st session in June 2022. A three-month online [public consultation](#) on the draft Model Law on Factoring was conducted between July and October 2022.

It is anticipated that the Model Law on Factoring will be finalised and published in 2023.

2.1.4 United Nations Convention on the Assignment of Receivables in International Trade by UNCITRAL

To make financing of international trade easier and more accessible, the United Nations Commission on International Trade Law (UNCITRAL) published the United Nations Convention on the Assignment of Receivables in International Trade in 2001, as well as a Legislative Guide on Secured Transactions in 2007, and a Guide on the Implementation of a Security Rights Registry in 2013. These laws include regulations on issues such as the forms and legal effects related to receivables assignments.

2.1.5 General Rules for International Factoring by FCI

As the largest factoring business industry association⁴, Factors Chain International (FCI) released the Code of International Factoring (formerly the Shield Agreement) in 1969. It regulates the operations of international factoring. Following numerous revisions, the rule was renamed to **General Rules for International Factoring** (GRIF) in 2002 and specifically addresses the operations of two-factor international factoring among FCI members.

FCI created the **Rules of Arbitration** in 1976, as all disputes between members are required to be resolved via arbitration.

The Rules of FCIreverse and Rules for Islamic Factoring were published by FCI in recent years.

2.1.6 Model Factoring Law by IFG

The International Factoring Group (IFG), a global trade association based in Belgium, created the Model Factoring Law in 2014. FCI refrained from further developing the IFG Factoring Model Law after FCI and IFG merged in 2016. Instead, FCI supported an initiative by the World Bank for the creation of a new global model law on factoring by the UNIDROIT.

2.2 SCF techniques definitions, guidance and reports

2.2.1 Standard Definitions for Techniques of Supply Chain Finance by GSCFF

To establish a common global understanding and international standardisation of SCF techniques, the GSCFF published the **Standard Definitions for Techniques of Supply Chain Finance** in 2016.

They have been shared among the members of the contributing organisations which represent more than 1,000 leading banks, factoring and forfaiting companies as well as technology and services providers. Relevant institutions like banking associations, media, the educational sector, regulatory and government agencies, law firms, accounting firms and other important stakeholders were informed about the definitions.

2.2.2 SCF techniques guidance papers by GSCFF

To raise further awareness of the SCF terms and techniques and achieve adoption of the generally accepted SCF practices across the industries, the GSCFF drafted a series of guidance documents on major SCF techniques based on its 2016 Standard Definitions for Techniques of Supply Chain Finance. On 19 June 2019, the GSCFF released its first guidance document, **Market Practices in Supply Chain Finance: Receivables Discounting Technique**.

⁴ Over the past 20 years, factoring has grown on a CAGR basis of nearly 10% p.a. By the end of 2018, world factoring volume is over €2.76 trillion, while Factors Chain International members accounted for nearly 60% of global factoring volume, and nearly 90% in international cross border volume. (Factors Chain International, *Annual Review*, 2019)

To address the concerns on payables finance raised from 2019 onwards – particularly following the collapse of certain companies and the alleged role of payables finance – the GSCFF released its factsheet paper **Payables finance – How It Helps Global Supply Chains** in March 2020. The paper defines payables finance and addresses concerns raised by rating agencies and accounting firms.

In response to the increased criticism on payables finance, the GSCFF released a document containing the most frequently asked questions and answers in August 2020. The report **Ensuring Payables Finance Remains a Force for Good** aims to address criticisms across three key areas: the potential adverse impact on suppliers, issues relating to financial reporting and transparency, and overall programme risk.

2.2.3 BAFT/GTIC Principles Paper on Payables Finance

To raise further awareness around payables finance, the BAFT/GTIC issued a principles paper in September 2020. This paper outlines acceptable practices that qualify a product as payables finance as described in the Standard Definitions for Techniques of Supply Chain Finance.

2.2.4 The Wolfsberg Group, ICC and BAFT Trade Finance Principles 2019 amendment

In 2017, the **Wolfsberg Group, ICC and BAFT Trade Finance Principles**⁵ were published, covering trade finance products like Documentary Credits, Documentary Collections, Demand Guarantees and Standby Letters of Credit. The document specifically relates to trade-based money laundering guidelines.

With increasing focus on SCF, the trade finance industry called for additional guidance on SCF techniques, which the 2017 version document did not cover. As a result, the **Trade Finance Principles 2019 Amendment** was enhanced with a section on open account trade (defined for payables finance and receivables discounting in the ICC Standard Definitions of Supply Chain Finance).

2.2.5 ICC Trade Register Report

To reflect the shift in trade financing from documentary trade finance towards open account term and to provide banks, investors and regulators visibility on the credit risks in SCF, the **2018 ICC Trade Register Report** expanded its scope to include supply chain finance techniques. The ICC Trade Register provides loss given default (LGD) estimates based on the data provided by participating banks. Payables finance was selected as a pilot.

⁵ A joint ICC-Wolfsberg Group Trade Finance Principles Drafting Group was set up in April 2014 to redraft and update the Wolfsberg Trade Finance Principles paper in the style of ICC guidance, with a view to raising and standardising the practice level of Financial Crime Compliance (FCC) within the trade finance industry. The drafting group includes members of Wolfsberg Group banks, ICC and BAFT.

The SCF data set in the Trade Register for the first two years is relatively small, but it evidences that the probability of default for SCF is comparable to other short-term trade finance products.⁶

ICC will further expand the scope of the ICC Trade Register to include operational and fraud risks and collect data to substantiate and disaggregate these results so they can be used to satisfy the requirements set out by regulatory, capital or accounting policies.

3. Premature conditions for drafting ICC SCF Rules

Greater standardisation, transaction rules as well as legal and regulatory frameworks in the area of SCF are required to help promote sound SCF practices, guarantee better data quality and bring transparency to SCF providers, regulators, legal bodies, accounting firms, investors and other SCF stakeholders.

The GSCFF members should actively advocate for the use of the **Standard Definitions for Techniques of Supply Chain Finance** and SCF techniques practice guidance papers to achieve standardisation, a wider global adoption of the practice and consensus over SCF techniques in the market.

3.1 Preconditions for ICC Rulemaking

As a rulemaking body for global commerce, ICC monitors the global market development and drafts new rules or revises existing ones to accommodate market demands and respond to the needs arising as global trade keeps evolving. This includes, for example, transportation, insurance, technology, accepted practices, new practices or responses to serious issues resulting from a lack of rules or ambiguous interpretation of rules.

To justify and initiate a new rules-drafting process, it is paramount that a business plan is in place. Only once the ICC Global Banking Commission Executive Committee has approved the business case, the process can commence.

3.2 Targets and Benefits for Future ICC SCF Rules

Similar to other ICC publications, ICC rules for SCF should aim at delivering globally accepted rules, which will benefit all parties involved in SCF activities, and should promote developments in risk assessment, the legal and regulatory framework.

⁶ 2018 ICC Trade Register Report: Exposure-weighted default rates for SCF in 2017 were 0.11%, comparable to the long-term average of trade finance products of 0.15%. The obligor-weighted default rate is also 0.11%, hence, below all trade finance products except for export L/Cs.

2019 ICC Trade Register Report: Exposure-weighted default rates for SCF in 2018 were 0.13%, a slight increase from 0.11% in the previous year and comparable to other trade finance products. The obligor-weighted default rate increased from 0.11% to 0.23% (below all documentary trade finance products except for export L/Cs). Defaults weighted by transactions rose to 0.01% in 2018 from <0.01% in the previous year.

ICC rules for SCF should focus on various issues related to supply chain finance techniques not covered by local laws or regulations, reflect and promote generally accepted sound and standard industrial practice, reduce confusion and act as references for all parties concerned.

Any proposed ICC rules for SCF must also be in alignment with the format and structure of other ICC rules while stringently complying with ICC rulemaking procedures.

3.3 Preconditions for ICC SCF Rules

To make sure any proposed ICC rules for SCF are as successful as existing ICC rules, for example, UCP 600 for Documentary Credits, URDG 758 for Demand Guarantees and other ICC rules, the drafting of ICC rules for SCF will first need to, at the least, take into consideration the following preconditions:

- a. The need for uniform industry-wide adoption of the standard definitions of SCF techniques and common practice;
- b. Collection of sufficient market feedback which may provide substance to the potential ICC rules for SCF;
- c. Acceptance by market participants (i.e. ICC national committees);
- d. Liability of acting parties if rules are applied;
- e. Feasibility of the rules being applied in both domestic and/or cross-border practice;
- f. Rulemaking approaches as to include general SCF techniques or specific SCF techniques and the structures of the rules;
- g. Dialogue and engagement with regulators;
- h. Sufficient market demand.

While standard terminology by the GSCFF is available, there is a market demand for clear rules due to different interpretations existing among market participants. In this context, it is worth noting the large grey area between 'classic' payables finance as the GSCFF promotes it and various shades of payment undertakings, where a receivable may be purchased or not. Different interpretations may still exist due to historical, technical or competitive reasons.

Under the current market conditions, it seems unlikely that all above preconditions for rules can be fulfilled. There are, however, indications for steps towards more standardisation, which may ultimately also make ICC rules for selected SCF techniques more realistic in the future.

4. Conclusion

Without doubt, market demand for ICC SCF rules exists. It is expected that SCF rules would be similarly successful as existing ICC rules for other trade finance products. The industry-wide adoption of the standard definitions of SCF techniques and common practice has made considerable progress thanks to advocacy efforts. Yet, wider adoption of such definitions and common practice must be evidenced before meeting the requirements of rulemaking. Generally, an industry-wide consensus on the basics of rulemaking must be achieved to ensure the rules

satisfy an actual market demand and are applied and adopted by the international trade finance community. More market research may be required to better understand the exact market demand.

After assessing the development of ICC Rules for SCF, the GSCFF workstream on ICC rules found that the landscape for developing SCF rules is still premature at this stage.

In the meantime, ICC will drive the subject forward and continue to work together with the GSCFF and other industry organisations on advocacy and promotion to drive broad adoption of the standard definitions of SCF techniques and practice. At the same time, they will collect market feedback on the customs and practices, including the use of digitalisation to advance SCF, to be considered in any future ICC rules for SCF.

To further establish the definitions published by the GSCFF, market participants are asked to incorporate the standard definitions into their daily operations and align their products and services accordingly, while retaining their freedom in differentiated products and services in the market.

Once the GSCFF together with its sponsoring organisations considers the preconditions for drafting ICC rules for SCF as fulfilled, the formal drafting work will be initiated in accordance with ICC's rulemaking procedures.

About the International Chamber of Commerce

The International Chamber of Commerce (ICC) is the institutional representative of more than 45 million companies in over 130 countries. ICC's core mission is to make business work for everyone, every day, everywhere. Through a unique mix of advocacy, solutions and standard setting, we promote international trade, responsible business conduct and a global approach to regulation, in addition to providing market-leading dispute resolution services. Our members include many of the world's leading companies, SMEs, business associations and local chambers of commerce.



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