

# CLIENT GUIDE TO TRADE FINANCE DISPUTES: RECEIVABLES

**Receivables are a key aspect of commodity finance. They provide liquidity to sellers, extended payment terms to buyers and investment opportunities for banks and non-bank financiers. This guide outlines what receivables are and some key aspects of receivables financing; highlights legal issues that commonly arise under English and other common law systems; and identifies where disputes are most likely to occur, drawing on recent case law and market experience.**

## What are receivables?

A receivable is a right to receive payment from another party for goods sold or services provided. From the seller's perspective, it is an asset; from the buyer's perspective, it is a liability.

Receivables financing is a collective term for a range of techniques by which receivables are sold, assigned or used as collateral to raise financing.

In a typical trade receivables financing:

- A seller supplies goods or services to a buyer and issues an invoice on extended payment terms.
- The seller enters into a receivables purchase agreement (“**RPA**”) with a financier.

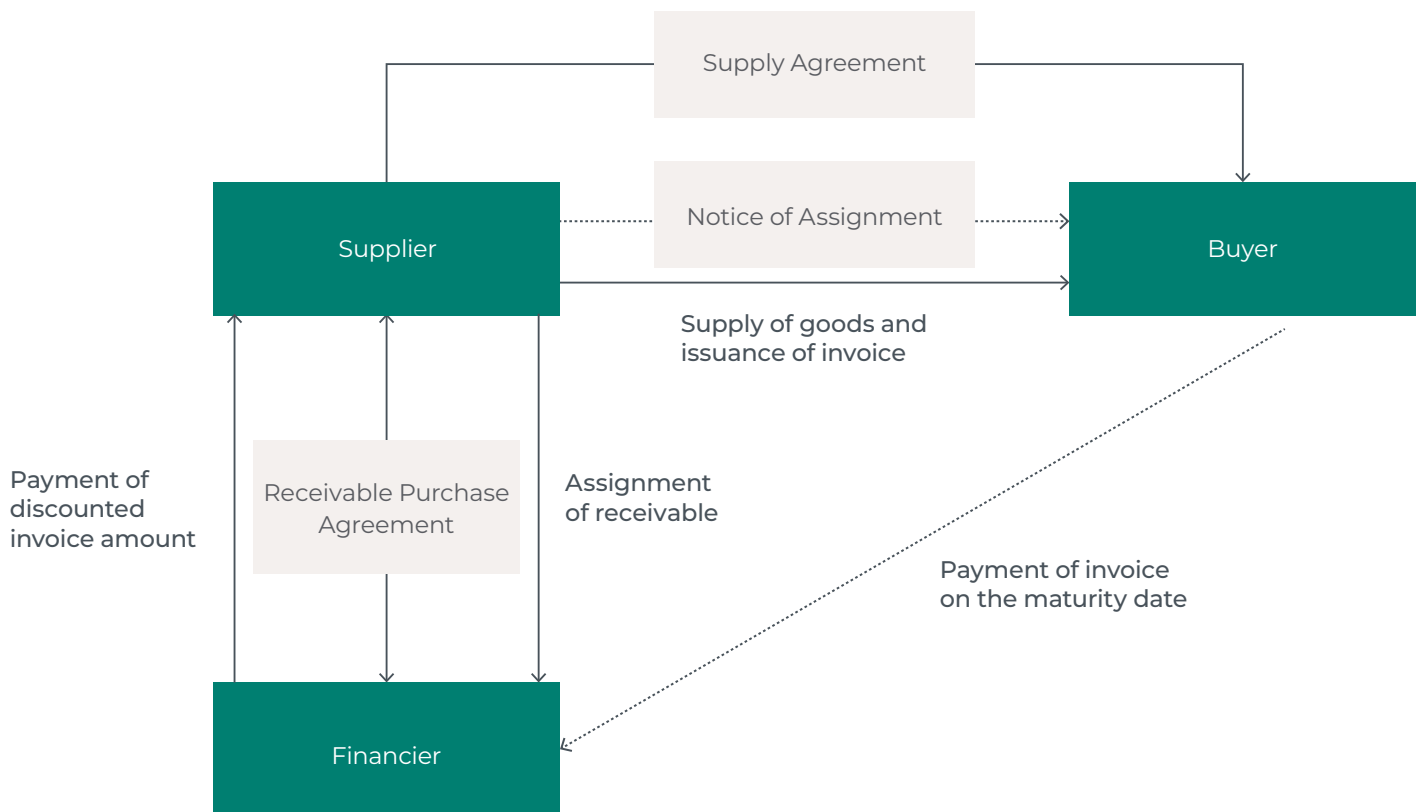
- The receivable is sold or assigned to the financier, usually at a discount.
- The financier is repaid when the buyer pays the invoice at maturity.

The commercial drivers are straightforward. Sellers wish to convert sales into cash quickly and reduce days sales outstanding (“**DSO**”). Buyers often seek longer payment terms to improve working capital and increase days payable outstanding (“**DPO**”). Receivables financing seeks to reconcile these competing objectives.

## Types of receivables

Receivables broadly fall into two categories:

- **Negotiable instruments:** These include bills of exchange and promissory notes. They are independent of the underlying trade transaction and create an unconditional obligation to pay. They are transferred by delivery.
- **Contract receivables:** These include invoices and contractual payment rights. Unlike negotiable instruments, they are not independent of the underlying contract. This means that there may be resistance to payment demands on the grounds of, for example, non-performance or set-off. Transfer usually occurs by way of assignment, which may be legal or equitable. Contract receivables require closer analysis of the underlying contract and carry greater legal and credit risk.



## Assignment

The assignment of contract receivables can be by way of legal or equitable assignment. This will have consequences for the way in which assignment is achieved and how any claim is enforced, as well as the priority of any claim in the event of insolvency. Where trade receivables are assigned, issues to consider include counterparty performance risk, insolvency of the customer or their buyer and the timing and effectiveness of any notice of assignment, particularly where there is an anti-assignment clause in the underlying contract.

## Recourse

Although many transactions are described as “non recourse”, this typically means limited recourse, rather than no recourse at all. Financiers sometimes retain recourse for risks within the seller’s control, such as misrepresentation, breach of warranty, invalidity of the receivable, a failure by the seller to perform the underlying contract or fraud. The extent of recourse rights can have an impact on whether a transaction is characterised as a true sale or a loan.

## Key legal issues – where can disputes arise?

Disputes in receivables financing typically arise when a receivable is not paid and the financier seeks to enforce payment, assert recourse against the seller, or claim under a trade credit insurance policy.

## Insolvency

Insolvency is where disputes relating to receivables most often crystallise. Where receivables are insured, insolvency can also trigger claims and corresponding coverage disputes.

## True sale or secured lending?

A key issue in receivables financing disputes is whether a transaction amounts to a true sale or a secured loan. Although the threshold for recharacterisation is high, the consequences are serious: an intended purchaser may ultimately be treated as an unsecured creditor if the arrangement is viewed as a financing rather than a sale. This distinction matters most in cases of insolvency. If a true sale has occurred, the receivable should be outside the seller’s insolvency estate. However, if the transaction is recharacterised as secured lending, the financier may rank only as a secured (or even unsecured) creditor of the seller.

Under English law, there is no single legal test to determine whether a transaction constitutes a true sale. Broadly, a transaction will generally be seen as a true sale if it is structured in substance as a sale and documented accordingly. However, if certain provisions are inconsistent with a sale, the Courts will examine the agreement as a whole in order to reach a decision, relying on defined parameters to differentiate between a sale and a transfer by way of security. These parameters include whether there is an obligation to return surplus proceeds or to make good on shortfalls, for example. Greater recourse rights generally increase the likelihood of a transaction being recharacterised as secured lending. For more information on both English and New York law in this area, see our article [here](#).

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## Assignment

Disputes may arise where:

- The underlying sale contract prohibits or restricts assignment.
- Pre-existing rights of set-off exist between the supplier and buyer in the underlying sale contract, such as master netting and set-off arrangements.
- Notice of assignment is defective or ineffective under local law.
- Competing assignments or security interests exist.
- In cross-border transactions: whilst it may be possible to assign a receivable freely under English law, that may not be the case under the law governing the underlying contract or the buyer's jurisdiction.

## Fraud and sham transactions

In recent years, a series of high profile credit failures in the trade finance sector exposed a pattern of underlying sophisticated fraudulent practices. Investigations uncovered schemes such as the double financing of cargoes and the use of sham transactions. The risks are magnified in receivables financing, which is largely paper-based and therefore particularly vulnerable to fraud. For example, issues in relation to assignment can give rise to disputes where it transpires that a cargo is either non-existent or has been financed multiple times.

A recurring theme in major insolvencies and trade finance frauds is the question of whether the underlying trade ever truly existed. If no goods exist, buyers may claim that no payment is due – leaving the bank exposed. Insurers have relied on this when disputing claims, arguing that no genuine trade took place and that the documents presented masked an artificial or non-existent transaction. This issue has arisen before the courts in a number of common law jurisdictions, including Singapore, Australia and England.

The courts have set a high threshold for establishing a sham transaction:

*“For acts or documents to be a “sham”...all the parties thereto must have a common intention that the acts or documents are not to create the legal rights and obligations which they give the appearance of creating. No unexpressed intentions of a “shammer” affect the rights of a party whom he deceived.”<sup>1</sup>*

The challenge of meeting this threshold has been borne out in recent cases in Singapore, in which the courts have, in most cases, declined to find that there was a sham.

Some purchasers of receivables have sought to address this risk by requesting an acknowledgement of assignment from the buyer which may confirm, for example, that the underlying trade is genuine (and, depending on timing, has been performed), that there are no disputes under the relevant contract and/or that the buyer will make payment in accordance with the notice of assignment. Depending on the contents of the acknowledgement and the circumstances of the underlying trade, a buyer may be estopped from subsequently claiming that the underlying trade was not genuine and/or had not been properly performed.

## Example Cases

### Assignment: non assignment clauses

In *First Abu Dhabi Bank PJSC v BP Oil International Ltd*<sup>2</sup>, the English Court of Appeal considered the effect of a contractual non assignment provision in the context of a receivables financing transaction. The case is an example of receivables related claims arising in the context of insolvency and demonstrates that anti-assignment clauses may not always operate as restrictively as they appear.

BP Oil International Limited (**BP**) sold the majority of a receivable owed to it by a Moroccan refinery, SAMIR, to First Abu Dhabi Bank PJSC (**the Bank**) under an

<sup>1</sup> Diplock, LJ in *Snook v London and West Riding Investments Ltd* [1967] 2 QB 786

<sup>2</sup> [2018] EWCA Civ 14

RPA. The underlying supply contract between BP and SAMIR contained a clause prohibiting assignment without SAMIR's consent (which was not obtained). Following the receivables sale, SAMIR entered insolvency proceedings in Morocco. With recovery prospects against SAMIR limited, the Bank sought to rely on the warranty in the RPA, which provided that BP was not "*prohibited by any security, loan or other agreement*" from disposing of the receivable. The Bank argued that BP had been contractually prohibited from disposing of the receivable by virtue of the non-assignment clause, and that this amounted to a breach of warranty and triggered a recourse event entitling it to reimbursement of the purchase price.

The English Commercial Court found in favour of the Bank and BP appealed. The Court of Appeal held that, while the non assignment clause prevented BP from effecting a legal or equitable assignment of the receivable without SAMIR's consent, it did not prohibit them from disposing of the economic benefit of the receivable by other means. In particular, the clause did not prevent BP from:

- agreeing to pay to the Bank sums received from SAMIR.
- holding such sums on trust for the Bank pending payment.
- providing for subrogation in favour of the Bank.
- granting a funded sub participation in respect of the receivable.

None of these mechanisms amounted to an assignment as a matter of English law. Accordingly, BP was not contractually prohibited from disposing of the receivable "as contemplated" by the RPA and was not in breach of warranty.

The decision illustrates that a non assignment clause will generally be construed narrowly. Where a clause restricts assignment alone, it will not, without clear and express wording, prevent other methods of transferring the economic benefit of a receivable. If a debtor wishes to prohibit all forms of transfer or risk sharing, this must be made explicit in the underlying contract. The case ultimately turned on construction, demonstrating the importance of precision in drafting.



### Assignment: pre-existing rights of set off

In *CIMB Bank Berhad v World Fuel Services (Singapore) Pte Ltd*<sup>3</sup>, World Fuel Services (Singapore) Pte Ltd (**WFS**) bought marine fuel from Panoil Petroleum Pte Ltd (**Panoil**). CIMB Bank Berhad (**CIMB**) had provided banking facilities to Panoil, secured by a debenture issued over all receivables, goods and documents representing goods financed by CIMB. Panoil subsequently went into administration and relying on the debenture, CIMB gave notice of assignment to WFS and then demanded payment of sums outstanding. WFS refused to pay and the claim went to the Singapore courts. The Singapore High Court agreed with WFS that CIMB had failed to prove the authenticity of the debenture and dismissed CIMB's claim. CIMB appealed and the Singapore Court of Appeal overturned the High Court's finding. However, CIMB nevertheless failed in its appeal because WFS was found to have a right of set-off under an underlying agreement with Panoil. This case illustrates the impact of provisions in underlying contracts (here, rights of set-off) on the security offered to financiers by the assignment of contract receivables.

### Fraud and trade credit insurance

In *BCC Trade Credit Pty Ltd v Thera Agri Capital No 2 Pty Ltd*<sup>4</sup>, the Court of Appeal of New South Wales held that a party's uncommunicated fraudulent intention does not render a contract a sham. Thera Agri Capital No 2 Pty Ltd ("**Thera Agri**") purchased credit insurance from BCC Trade Credit Pty Ltd ("**BCC**"). Thera Agri was an Australian non-bank structured credit financier specialising in agricultural commodities and the insurance was to cover a guarantee supporting a supply chain finance facility advanced to the Phoenix Group, a commodity trader operating out of Dubai. Thera Agri advanced USD 7.3 million in four drawdowns; shortly afterwards, both Phoenix Dubai and its guarantor entered liquidation without repaying any amounts.

BCC denied cover, alleging that some drawdown documents were fraudulent. The first instance court held that the presence of fraud did not extinguish the insurer's obligation. The New South Wales Court of Appeal upheld that decision, with some helpful analysis on the relevance of allegedly sham contracts to the issue of trade credit insurance cover and whether fraud on the part of the buyer (here, Phoenix) could deprive an innocent insured of cover. The key question was whether the contract between Thera Agri and Phoenix giving

rise to the receivable was enforceable, not whether Phoenix acted fraudulently. Thera Agri had entered into a genuine contract and was unaware of Phoenix's fraudulent conduct. Its contractual loss was therefore covered. The judgment aligned with the policy's fraud exclusion, which barred claims arising from the insured's fraud – but not from fraud committed by the buyer.

### HFW Comment

Receivables financing offers clear commercial advantages but also carries significant legal risk for financing banks, particularly in a market susceptible to insolvency and fraud. Case law shows that courts are willing to uphold genuine trade finance structures and to hold parties to the bargains they have made. It also illustrates the importance of taking legal advice in order to minimise the risk of disputes arising – and to maximise the chances of succeeding where they cannot be avoided.

For English law transactions, it is important to ensure that transactions are structured and documented as true sales to reduce the risk of recharacterisation as secured lending, with the associated exposure to an increased credit risk in the event of an insolvency.

Assignment should be approached with care, with appropriate due diligence undertaken and advice sought to ensure that notices are compliant and that there are no restrictions on assignment or set-off clauses in underlying contracts which would impact the value of security for the financing bank. Consideration should be given to whether an acknowledgement of assignment is required, and to the contents of any acknowledgment. Where a receivable owed by a foreign entity is to be transferred by assignment, the bank should take local law advice on the law governing the underlying contract and/or of the buyer's jurisdiction to ensure that the assignment is effective. Clear and expert drafting should ensure that receivables agreements adequately reflect the parties' intentions.

Given the number of disputes arising from fraud and/or insolvency, we recommend thorough risk assessments and counterparty due diligence, regularly updated, to protect against these risks.

HFW regularly advises on receivables financing structures, disputes arising from non payment and insolvency, and related coverage issues under trade credit insurance policies.

<sup>3</sup> [2021] SGCA 19 2017

<sup>4</sup> *BCC Trade Credit Pty Ltd v Thera Agri Capital No 2 Pty Ltd* [2023] NSWCA 20

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