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ALERT MEMORANDUM

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European Union Approves Hague Convention on Choice of Court Agreements

On June 11, 2015, the European Union approved the Hague Convention on Choice of Court Agreements (the "Convention"), triggering the countdown to the Convention's entry into force, which is scheduled to occur on October 1, 2015. Thereafter, the Convention will be in force between all EU member states (except Denmark) and Mexico, which acceded to the Convention in 2007. This marks the culmination of more than 20 years of research, drafting and negotiation conducted under the auspices of the Hague Conference on Private International Law.

The Convention aims to ensure that, where commercial parties have agreed to resolve their disputes exclusively in a specific court, that agreement will be honored and a judgment subsequently rendered by the chosen court will be widely recognized and enforced. The goal is to put into place an international legal foundation for choice of court agreements similar to that established for arbitration agreements by the New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards (the "New York Convention").

Due to the limited number of parties who have so far acceded to the Convention and a combination of other factors discussed below, this goal remains more an aspiration than a reality. As a result, the Convention is unlikely to alter the calculus that goes into deciding between choice of court agreements and arbitration agreements, at least for the time being. This could, however, change if the EU's approval of the Convention spurs a cascade of ratifications by other economically important states.

The Convention's Three Pillars

The Convention's attempt to ensure the enforceability of choice of court agreements and judgments rendered thereunder rests on three pillars:

First, the Convention ensures that the parties' chosen court will hear their dispute. Article 5(1) provides that a court specified in an exclusive choice of court agreement "shall have jurisdiction" over a dispute within the scope of that agreement and Article 5(2) bars that court from declining jurisdiction "on the ground that the dispute should be decided in a court of another State," for example under the doctrines of *forum non conveniens* or *lis pendens*. These provisions will not, however, be enforced where the choice of court agreement is "null and void" under the laws of the state in which the chosen court is located, nor do they override rules that (i) restrict the chosen court's subject matter jurisdiction or (ii) govern the allocation of cases among courts in the same state. (Art. 5(3).)

Second, the Convention directs courts other than the chosen court to "suspend or dismiss proceedings to which an exclusive choice of court agreement applies," except in certain limited circumstances, including where "the agreement is null and void under the law of the

State of the chosen court," "giving effect to the agreement would lead to a manifest injustice or would be manifestly contrary to the public policy of the State of the court seised," and "the chosen court has decided not to hear the case." (Art. 6.)

Third, the Convention provides that a judgment issued by the chosen court will be recognized and enforced by the courts of other Contracting States, unless one of the specified grounds for refusal applies. (Art. 8(1).)[1] The Convention prohibits the court where recognition and enforcement is sought from conducting a "review of the merits of the judgment," except where necessary to assess the applicability of the Convention, and provides that the "court addressed shall be bound by the findings of fact on which the court of origin based its jurisdiction, unless the judgment was given by default." (Art. 8(2).)

Several of the grounds for refusal of recognition and enforcement mirror those available under the New York Convention and the UNCITRAL Model Law on International Commercial Arbitration (the "Model Law"), including invalidity of the choice of court agreement (Art. 9(a)), incapacity of either party in concluding the choice of court agreement (Art. 9(b)) and lack of notice to the defendant of the relevant proceedings (Art. 9(c)). A similar public policy exception is also present, permitting a court to refuse recognition and enforcement of a judgment where it "would be manifestly incompatible with the public policy of the requested State, including situations where the specific proceedings leading to the judgment were incompatible with fundamental principles of procedural fairness of that State." (Art. 9(e).) This language appears to set a higher bar than the equivalent language in Article V.2(b) of the New York Convention and Article 36(1)(b)(ii) of the Model Law, which provide that recognition and enforcement of an arbitral award may be refused where it would be "contrary" to the public policy of the requested state.

The Convention also provides grounds for refusing recognition and enforcement of a judgment that have no equivalent in either the New York Convention or the Model Law, such as where the judgment:

- is "inconsistent" with another judgment between the same parties rendered in the same state where recognition/enforcement is sought. (Art. 9(f).)[2]

- is "inconsistent" with another foreign judgment (i) between the same parties; (ii) based on the same cause of action;[3] (iii) rendered earlier in time; and (iv) that

[1] The Convention leaves the mechanics of recognition and enforcement of judgments to the law of each Contracting State. (Art. 14.)

[2] The Convention does not define "inconsistent" nor does it indicate which parts of the two judgments must be inconsistent for this provision to be triggered. However, the Explanatory Report issued by the Hague Conference states that the Convention "never requires" the enforcement of rulings on "preliminary questions," suggesting that the intent of the drafters was that inconsistency would be assessed only with respect to the final, dispositive section of the judgments at issue. Trevor Hartley & Masato Dogauchi, Explanatory Report ¶ 195 (*available at*: http://www.hcch.net/upload/expl37final.pdf). That said, there is nothing in the Convention that would prohibit a Contracting State from adopting a broader definition of "inconsistent" in its implementing legislation.

[3] Neither the Convention nor the Explanatory Report provides any guidance on the meaning of "cause of action," including as to whether the facts underlying two causes of action must be identical in order for the causes of action to be considered "the same."

could be recognized in the state where recognition/enforcement is sought. (Art. 9(g).)

- awards damages "that do not compensate a party for actual loss or harm suffered," *e.g.*, exemplary or punitive damages. (Art. 11(1).)

- relates to a matter excluded from the scope of the Convention. (Art. 10(2) and (4).)

Finally, it is important to note that the Convention only requires Contracting States to recognize and enforce judgments "given by a court of a Contracting State designated in an exclusive choice of court agreement." (Art. 8(1).) Thus, if parties designate a state not party to the Convention in their choice of court agreement and the chosen court subsequently renders a judgment pursuant to that agreement, the Convention will not govern the recognition and enforcement of the judgment, even if sought in a Contracting State. By contrast, the New York Convention does not restrict recognition and enforcement of an arbitral award on the basis of where the award was rendered. Likewise, Article 35(1) of the Model Law states expressly that "An arbitral award, *irrespective of the country in which it was made*, shall be recognized as binding and … shall be enforced …."

As the foregoing demonstrates, the Convention establishes a robust framework for choice of court agreements, which, if widely adopted, could increase their appeal and put them on a more level footing with arbitration agreements in the context of enforceability. However, as will be discussed in the next section, the Convention's scope is narrower than that of the New York Convention, meaning that many choice of court agreements will not benefit from its application.

Scope of the Convention

There are four important limitations on the scope of the Convention. Together, they ensure that the Convention's primary effect will be on choice of court agreements in business-to-business contracts dealing with straightforward commercial matters, *e.g.*, the buying and selling of goods and services. In deciding between dispute resolution mechanisms, parties will therefore need to carefully consider whether the Convention will apply, given the nature of their relationship and the types of disputes likely to arise between them, if they opt for a choice of court agreement.

The first limitation on the Convention's scope is that it applies only to "exclusive choice of court agreements." (Art. 1(1).) A choice of court agreement is "exclusive" if it designates "the courts of one Contracting State or one or more specific courts of one Contracting State to the exclusion of the jurisdiction of any other courts." (Art. 3(a).) Significantly, the exclusion of other courts need not be made explicit: Article 3(b) of the Convention provides that a choice of court agreement will be deemed exclusive if it designates "the courts of one Contracting State or one or more specific courts of one Contracting State … unless the parties have expressly provided otherwise." In other words, a choice of court agreement specifying "the courts of France" or "the U.S. District Court for the Southern District of New York" will be deemed exclusive absent express language to the contrary. Note that, as a result of the way Article 3 of the Convention is

drafted, it does not cover asymmetric choice of court agreements that provide one forum for claims brought by one party (*e.g.*, a lender) and a different forum for claims brought by another party (*e.g.*, a borrower), unless both fora are in the same Contracting State.

The second key limitation is that the Convention applies only in "international cases." (Art. 1(1).) What constitutes an international case differs depending on the Convention chapter at issue. In the "Jurisdiction" chapter (*i.e.*, Articles 5-7, which relate to the jurisdictional implications of a choice of court agreement for the chosen court and other courts) a case is considered international unless the parties are resident in and all elements of the dispute are connected to the same state. (Art. 1(2).) In the "Recognition and Enforcement" chapter (*i.e.*, Articles 8-15, which relate to the recognition and enforcement of judgments rendered by the court designated in a choice of court agreement) the definition is more expansive: "a case is international where recognition or enforcement of a foreign judgment is sought." (Art. 1(3).) A state can, however, make a declaration under Article 20 permitting its courts to refuse recognition and enforcement of a judgment where a dispute, even though heard in a foreign court pursuant to a valid choice of court agreement, is otherwise purely domestic.

The third limitation is that the Convention does not apply to choice of court agreements concluded with natural persons "acting primarily for personal, family or household purposes" or relating to employment contracts, whether individual or collective. (Art. 2(1).) This provision distances the Convention from some of the more controversial choice of court agreements contained, for example, in contracts of adhesion between corporations and consumers.

Fourth and finally, the Convention excludes from its scope a wide range of substantive matters (Art. 2(2)) and permits a state to expand on this list by making a declaration "clearly and precisely" defining those additional matters that the state would like to exclude. (Art. 21(1).) The matters excluded by default include "family law matters," "insolvency, composition and analogous matters," "anti-trust (competition) matters" and "the validity of intellectual property rights other than copyright and related rights." (Art. 2(2).)

In approving the Convention, the EU declared that it would also exclude most insurance contracts from the Convention's scope, making exceptions for, among other things, reinsurance contracts and contracts covering certain commercial risks, such as losses related to the operation of aircraft and seagoing vessels. The EU noted that it may at a later date reassess whether it is necessary to maintain its Article 21 declaration.[4]

The Convention and the EU

The Convention contains in Article 26 a series of rules governing its interaction with other international instruments. Of particular relevance in light of the EU's recent approval of the Convention is the way conflicts will be resolved between the Convention and the Brussels Regulation, which covers some of the same ground. The Convention identifies two situations in which it will give way to regulations adopted by Regional Economic Integration Organisations ("REIOs") like the EU:

[4] EU Declaration, *available at*: http://www.hcch.net/index_en.php?act=status.comment&csid=1044&disp=resdn

First, the Convention will give way in cases "where none of the parties is resident in a Contracting State that is not a Member State of the Regional Economic Integration Organisation." (Art. 26(6)(a).) This provision is not easily parsed, but its purpose is to ensure that the Convention will not interfere in situations where all states with an interest in the dispute are (i) subject to a conflicting REIO regulation and/or (ii) not parties to the Convention. A state is assumed to have an interest if one or more of the parties to the dispute (and to the applicable choice of court agreement) is resident in the state.

As an illustrative example, imagine that Company A, incorporated in Germany, and Company B, incorporated in France, conclude a contract designating the courts of England and Wales as the exclusive forum for resolving disputes. Company A then initiates proceedings against Company B in Cologne and, thereafter, Company B sues Company A in London. In this situation, the Brussels Regulation – and not the Convention – would govern the jurisdiction of the courts involved because both parties are resident in Member States of the EU and thus subject to the Regulation. The Convention would likewise give way to the Brussels Regulation if Company A were incorporated in the United States because Company A is not resident in a Contracting State and Company B is resident in a Member State of the EU. By contrast, if Company A were incorporated in Mexico, which acceded to the Convention in 2007, then the Convention would prevail because one of the parties is resident in a Contracting State that is not a Member State of the EU.

Second, the Convention will give way to REIO regulations to the extent they concern "the recognition or enforcement of judgments as between Member States of the Regional Economic Integration Organisation." (Art. 26(6)(b).) This means that if the court that issued the judgment and the court where recognition and enforcement is sought are both located in EU Member States, then the Brussels Regulation will prevail over the Convention.

Though the provisions of Article 26 are a sensible way of dealing with conflicts between the Convention and REIO regulations, at the moment they deprive the Convention of much force because the vast majority of Contracting States are also EU Member States. Relations between parties in EU Member States will continue to be governed by the Brussels Regulation, confining the Convention's current role to commerce between the EU and Mexico. Of course, each additional approval/ratification of the Convention will expand its applicability.

No Retroactive Application

The Convention does not apply to choice of court agreements that designate a court in a state where, at the time the agreement is concluded, the Convention has not entered into force. (Art. 16(1).) The Convention likewise does not apply in "proceedings instituted before its entry into force for the State of the court seised." (Art. 16(2).) As a result, any choice of court agreement concluded or proceedings initiated before October 1, 2015 will fall outside the Convention's scope. For each subsequent state that ratifies, accepts, approves or accedes to the Convention, it will come into force "on the first day of the month following the expiration of three months after the deposit of [the state's] instrument of ratification, acceptance, approval or accession." (Art. 31(2)(a).)

Conclusion

The Convention is an important step towards a global enforcement regime for judgments rendered under exclusive choice of court agreements. Though relatively modest in scope, it nonetheless covers an important category of commercial agreements. Whether this Convention will be as impactful as the New York Convention has been with respect to the enforceability of arbitral awards depends in large part on whether more states become parties to it. So far, the United States (in January 2009) and Singapore (in March 2015) have both signed the Convention, but neither has ratified it. And while ratification seems imminent in Singapore, the process in the United States has long been delayed by a debate over the proper method for implementing the Convention in domestic law. It is possible that the EU's approval of the Convention will increase its acceptance by other members of the international community and break the ratification deadlock in the United States, but that remains to be seen.

If you have any questions, please feel free to contact Thomas Buhl, Richard Kreindler, Matthew Slater, Christopher Moore, Nat Jedrey or any of your regular contacts at the firm. You may also contact our partners and counsel listed under Litigation and Arbitration located in the "Practices" section of our website at http://www.clearygottlieb.com.

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