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Drafting international commercial contracts: Lessons from recent European Union case laws

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Abstract
Choice of law and choice of forum clauses of an international commercial contract may sometimes be used to evade the application of any domestic or international law. This is so done by the principle of party autonomy. However, the parties cannot avoid the mandatory rules of such laws. Lawyers drafting commercial contracts should be mindful of this limitation on the autonomy principle. The recently decided English and German cases depict this tension and sends a note of caution for international commercial lawyers. This paper makes a brief review of those cases and highlights the said limitation coupled with some suggestions.

Keyword: Choice of law clause, choice of Forum clause, Party Autonomy, Freedom of Contract, Pacta sunt servanda, Mandatory rules, Commercial Agents (Council Directive) Regulation 1993.

Introduction

The principle of party autonomy is a basic principle of international commercial contract law. It posits that the parties are free to choose and agree upon the terms and conditions of their contract (Ramberg,2011; Meiselles, 2013). The lawyers who draft the contract should couch them carefully so that they reflect exactly the intents of the parties (Fox, 2009). Once signed, sealed and delivered, the terms and conditions are sacred. The principle of *pacta sunt servanda* dictates that parties are bound by the contract; no departure is allowed unless consented to by both parties (Sanson, 2005; Zahid and Shapiee, 2010). However, mandatory rules are an important limitation of the autonomy doctrine (Ramberg. 2011; Bortolotti, 2010). Those rules are such as cannot be avoided by the parties. Even if the parties do not incorporate them in the

contract, they (mandatory rules) shall apply in the event of a dispute. National and international public policy justifies their application.

Given the importance of mandatory rules, it is a must for international commercial lawyers who are engaged in drafting contracts to educate themselves in the applicable mandatory rules to avoid likely hassles their clients may face, if there ensues a dispute. In this respect, the recent English and German case law is instructive.

English Cases:

Fern vs Intergraph

Facts of the Case

In this case, Fern was the agent of Intergraph in the European Union (EU). Fern was based in Derbyshire, England, while Intergraph is a US software company based in Texas. The agency agreement between them contained the law and forum clause as follows:

> THIS AGREEMENT SHALL IN ALL RESPECT BE INTERPRETED AND CONSTRUED IN ACCORDANCE WITH AND GOVERNED BY THE LAWS OF THE STATE OF TEXAS USA (EXCLUDING ITS CHOICE OF LAW PROVISIONS) REGARDLESS OF THE PLACE OF ITS EXECUTION OR PERFORMANCE. For the benefits of {Intergraph}, {Fern} hereby irrevocably agrees that any legal action, suit or proceeding arising out of or relating to this Agreement shall be brought in the courts of the State of Texas sitting in Houston, Harris County, Texas or in the United States District Court for the Southern District of Texas. By the execution and delivery of this agreement, {Fern} hereby irrevocably consents and submits to the exclusive jurisdiction of such courts in any such action, suit or proceeding arising out of or relating to this agreement in the courts of the State of Texas sitting in Houston, Harris County, Texas or in the United States District Court for the Southern District of Texas, and irrevocably waives any claim that any such action, suit or proceeding brought in any such court has been brought in an inconvenient forum.

Intergraph terminated the contract with Fern. Fern claimed that it was a commercial agent for Intergraph, and as such, was entitled to compensation under the UK *Commercial Agents (Council Directive) Regulations 1993* (http://www.legislation.gov.uk).[i] It filed two claims- one for compensation for breach of the Regulations, and the other for unpaid claim under the agency contract in the High Court of England and Wales, despite the clear wordings of the law and forum clause as above.

Because the Defendant is based in Texas, Fern filed an application to serve out of jurisdiction. Under such an application, the claimant had to satisfy the court that the claim could pass through any one of the gateways under Civil Procedure Rules (CPR) 6, and that the claim had merits. Fern was claiming that it could pass through the gateway because the contract was governed by English law, and because of the fact that the contract was breached within the jurisdiction. Leave to serve out of jurisdiction was obtained on 29th October 2013.

In order to pass through the gateway, Fern relied on the decision of Tugendhat J in *Accentuate case (2010)* discussed further below, which also concerned a claim under the above Regulations. In Accentuate, the permission to serve out of jurisdiction was allowed under sub-paragraph (6)(c) of the Practice Direction to CPR 6, which provides that 'a claim is made in respect of a contract where the contract… is governed by English Law.'

Fern's leave to serve out of jurisdiction had been given on the grounds that the English Courts were the proper place to hear the claim, there was serious issue to be tried, and the claim satisfied the said sub-paragraph (6)(c).

When Intergraph became aware of the order, it filed this application to set aside the said order granting leave to serve out of jurisdiction. In this application, the English Court was asked whether a clear Texas governing law and Texas jurisdiction clause should be set aside on the basis of an alleged infringement of the UK implementation of the Regulations.

Intergraph argued that the Regulations did not apply because the contract was governed by Texas law, as per the law and forum clause, which, in the present scenario, was unchallengeable. So, Fern could not pass the gateway in sub-paragraph 6(c) of the Practice Direction to CPR 6. In doing so, Intergraph was relying on the sanctity of party autonomy principle and the doctrine of *pacta sunt servanda.* Fern, on the other hand, invoked domestic law to escape the unfavorable effect of the law and forum clause.

Court's Judgment and Rationale

With regard to Fern's first claim, the judge held the view that a claim for compensation under the Regulations was not contractual, rather statutory, which could not be avoided given its mandatory nature as provided for in Paragraph 19 of the Regulations. It (Paragraph 19) provides that the parties cannot derogate from regulations 17 and 18 (i.e. entitlement of commercial agent to indemnity or compensation on termination of agency contract, and grounds for excluding payment of indemnity or compensation under regulation respectively). As such, any attempt to avoid the statute (Regulations) would be void and attract the jurisdiction of the English court. In coming to this view, the judge referred to the *obiter dicta* by Lord Hoffman in the case of *Lonsdale (2007)*. At paragraph 38 of his judgment, he said

> A close study of the Regulations confirms that they are not themselves directly contractual. .. They acknowledge the existing contract as an actual higher or parallel contract and (as observed above) they are not implemented by means of an implication into the contract. They acknowledge the existence of the contract to which they relate as a separate legal concept … and override it to the extent that there are frequent bars on derogation from the regulations. Any attempt to derogate from them would be likely to be via a contract, and the effect of the Regulations is to bar the operation of a contract in that respect. So the rights given by the Regulations are definitely not contractual as that word would normally be understood. This conclusion is supported by the speech of Lord Hoffman in Lonsdale vs Howard & Hallam Ltd [2007] 1 WLR 2055 … where he contrasts the claimant's "contractual entitlement" with his additional "statutory entitlement to compensation.

The UK Regulations in questions have implemented *EU Council Directive 86/653/EEC on the Co-ordination of the Laws of Member States Relating to Self-employed Commercial Agents (http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX:31986L0653)*. The spirit behind the Directive

and hence the Regulations is to protect the commercial agents in the European Union. To quote the European Court of Justice in the case of *Ingmar (2001)*,

> 24. The purpose of the regime established in Articles 17 to 19 of the Directive (same as the UK Regulations provisions in questions) is thus to protect, for all commercial agents, freedom of establishment and the operation of undistorted competition in the internal market. Those provisions must therefore be observed throughout the Community if those Treaty objectives are to be attained.
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> 25. It must therefore be held that it is essential for the Community legal order that a principal established in a non-member country, whose commercial agent carries on his activity within the Community, cannot evade those provisions by the simple expedient of a choice-of-law clause. The purpose served by the provisions in question requires that they be applied where the situation is closely connected with the Community, in particular where the commercial agent carries on his activity in the territory of a Member State, irrespective of the law by which the parties intended the contract to be governed. (emphasis added by the Distributor).

As for the second part of Fern's claim, the judge held that the claim for unpaid remuneration was a claim under the agency contract. Since parties had agreed that the governing law for the contract would be the law of Texas, and the forum would be a court in Texas, he did not interfere and rightfully refused to open the gateway for Fern to pass.

The Judge's view about the first claim, however, opened up new possibilities for future litigation for claims made under the Regulations, at least in the English jurisdiction. The judge was not comfortable in this respect (*Fern vs Intergraph 2014*). According to him, the Regulations apply in relation to the activities of commercial agents in Great Britain. In light of *Ingmar* and the arguments of Intergraph's counsel, the Judge maintained that the breach of a statutory duty could conceptually be a tort for the purposes of CPR 6. As such, he ruled out possibilities that a claim to serve out could be made in respect of a tort where, inter alia, damage is sustained within the English jurisdiction under gateway 20.

While ruling that the leave to serve out obtained earlier be set aside, the judge had, therefore, adjourned the hearing in order to give opportunity to both parties to submit on whether Fern should be allowed to amend the application so as to be able to argue on this point.

In order for the Judge to open the case for further submission, he established the merits of the case in that the software in the CD were goods and Fern is a commercial agent within the meaning of the Regulations.

Accentuate Ltd v Asgira Inc

In this case, Asgira, a Canadian company, engaged, by an agreement concluded on 17th January 2004, Accentuate, an English company, as its agent to distribute its software in the UK. The parties chose the laws of Ontario and federal laws of Canada to govern their contract and Toronto as the forum for dispute settlement by arbitration. Asgira sought to terminate the contract in November 2006. At this, Accentuate notified Asgira that it was preparing a claim against the latter for a claim for breach of the contract and with a further claim for compensation under the *Commercial Agents (Council Directive) Regulations 1993*. Asgira sought a declaration from

the Toronto arbitral tribunal that Accentuate did not have any claim under the distribution agreement. On the other hand, the High Court in England declared the choice of law and forum clause null and void as that would not enforce the mandatory law of EU, namely the said 1993 Regulations. Confirming its jurisdiction over this case, the High Court declared the unenforceability of the Canadian arbitral award on grounds of public policy.

German Cases

In several German cases, a similar line of mandatory rules approach, as in the UK, has been taken. Whenever the German courts had the fear that the selected law and forum would not honor her mandatory rules, they declined to relinquish their jurisdiction. For example, in a German Supreme Court Case (2013), in November 2095, an American company based in Western Virginia entered into an agency contract with a German sales agent to sell its products in Europe. The parties submitted the agreement to Virginia law and chose Virginia as the forum for dispute settlement. In April 2009, the American principal terminated the agency contract. As Virginia law did not provide for any right to post-termination indemnity, the German agent brought the matter to a German court (District Court in Heilbronn) under the *German Commercial Code (GCC),* which implements the same EU Commercial Agents Directive referred to above. Later, the case went to appeal (the Higher Regional Court of Stuttgart) and then, to the German Supreme Court. All the three courts accorded an overriding effect to the mandatory rule of commercial agent's right to indemnity established by the EU Directive. In doing so, they relied, in the same way as English courts did, on the public policy argument of the ECJ *Ingmar* case mentioned above.

Conclusion: Comments and Suggestions

As noticed above, the EU Commercial Agents Directive has designated its provision of indemnity for termination of agency contract as non-derogatory. *Ingmar* case has upheld this as a public policy of the European Union. As such, the national courts, particularly English and German courts, have taken the matter seriously. They have gone to the extent of invalidating the choice of law and forum clause or arbitration agreement of the parties concerned. Instead, they have applied their jurisdiction and enforced the mandatory rules principle on the public policy ground. This is a new trend in the EU, which is a disregard to the party autonomy principle. That is why, this is critiqued as "tension" creating in international litigation and arbitration (Antomo, 2013). To address this issue, it has been suggested that an EU court should not, in the first, entertain any matter that has been submitted to a non-EU jurisdiction and law even though it involves mandatory rule(s). It may interfere only when it is *certain* that the chosen forum or arbitral tribunal shall not apply the mandatory rule or shall not apply any other rule with similar result (Antomo, 2013). However, this suggestion is not above question. That is, before the final disposal of the matter by a foreign court or arbitral tribunal, how can an EU court be sure that the foreign court or tribunal shall not apply the mandatory rule or a similar rule of similar effect? Rather, it (EU court) should wait until the non-EU court finally disposes of the case. If the non-EU court or tribunal does not apply the mandatory rule or a similar rule, the EU court may refuse to enforce the judgment or award and may try it afresh (See Bortolotti, 2010). In this way, it is submitted, the ends of both autonomy principle and mandatory rule principle will be served in a balanced and justified way.

Now, the EU courts have two alternative ways to follow in respect of a matter that entails a mandatory rule(s). One, they may persistently disregard the parties' choice of law and

forum/arbitration clause and decide cases according to their own law. Or, they may adopt the suggestion given above. In either case, the contract drafters have lessons to learn. They must educate themselves of the mandatory rules both of the chosen law and jurisdiction, and also of the law of the jurisdiction where the judgment or award will be enforced. With that knowledge, they should draft the applicable law clause in such a way that mandatory rule of the EU law is respected and there remains no scope or need of interference by the jurisdiction responsible for enforcement of the judgment or award.

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Endnotes:

[i] The Regulations set out the rights and obligations as between commercial agents and their principals (regulations 3 to 5) and deal with remuneration (regulations 6 to 12), and the conclusion and termination of the agency contract (regulations 13 to 16).They contain provisions relating to the indemnity or compensation payable to a commercial agent on termination of his agency contract (regulations 17 to 19) and also to the validity of restraint of trade clauses (regulation 20). The Regulations provide for minimum notice periods and compensation to be paid in most situations to an agent unless termination results from material breach by the agent. The full text of the Regulations is available at http://www.legislation.gov.uk/uksi/1993/3053/made/data.pdf