Brexit Essentials: Dispute resolution clauses

In this briefing, we consider the potential impact of Brexit on contractual dispute resolution clauses. EU law underpins these clauses. When that law ceases to apply in the UK, the nature of the likely replacement regime is clearer in some areas than in others. The questions and answers below are intended to help businesses understand the position better and, where necessary, take practical steps to limit uncertainty.

A dispute resolution clause sets out the mechanism by which contractual counter parties intend for any disputes that may arise between them to be resolved. It generally does so by specifying:

A. which legal systems are to provide the rules and infrastructure to hear and determine their disputes. This means, for example, stating which governing law is to apply to the contract and its terms, and which court or courts will hear disputes or supervise their conduct; and

B. which method or methods of dispute resolution they wish to have resort to (e.g. litigation, arbitration, expert determination, mediation) and in which order and in which circumstances they wish those methods to be available.

At the moment, various rules derived from the UK's membership of the EU provide the legal framework underpinning the elements of dispute resolution clauses described at sub-paragraph (A) above. Those rules are designed to create a harmonised, predictable, cross-border system the purpose of which is:

1. to determine the law which governs parties' contractual and non-contractual obligations;

2. where the parties have elected to litigate their disputes in a court, to confer jurisdiction on the EU member state court deemed best qualified to determine a dispute, so avoiding competing litigation in different EU countries' courts; and

3. to ensure that judgments of member state courts can be enforced quickly and easily across all member states.

The current versions of these EU rules have direct effect in the UK. When the UK leaves the EU, the default position is that these rules will cease to apply. The Government's current intention is to legislate, in a so-called "Great Repeal Act", to convert EU law in force at the moment of withdrawal into domestic UK law "wherever practical"[1]. The Government would then be able to consider and propose amendments to or repeals of that domesticated law at a later date.

The Government has yet to publish details of its proposed saving legislation or the position it proposes to adopt in negotiations with the EU. For the moment, that must inevitably give rise to a degree of uncertainty. However, the extent of that uncertainty should not be over-stated: in some areas, the shape of the future will be very like the present. For example, even before Brexit negotiations begin or a draft "Great Repeal Bill" is published, it is possible to say with a high degree of confidence that, post-Brexit, English governing law clauses will continue to be upheld, both here and on the continent.

Even in areas where there is greater uncertainty, there are strong and mutually-applicable arguments in favour of an EU-UK arrangement which provides for a continuation of the current regime. In the event such an agreement is not possible (or at least not in the short-to-medium term), there are steps the UK could take unilaterally and swiftly that would preserve at least some of the benefits of the current regime.

[1] Statement to the House of Commons by David Davis MP, Secretary of State for Exiting the European Union, on 10 October 2016.

1. Will an English choice of law clause in a contract still be valid post-Brexit?

Yes. It is important to remember that, where parties choose English law to govern their contracts, the courts of EU member states generally respect that choice. Brexit should not change that, in the EU or the UK.

This is because the relevant EU rules, which the remaining member states' courts will continue to apply, are not concerned with whether the law which parties choose to govern their contracts is or is not that of a member state. Similarly, where the parties have not chosen a governing law, the EU rules set out a procedure for its determination under which the question of EU membership is irrelevant.

Meanwhile, as we have noted above, the UK Government intends to introduce legislation to convert, where practicable, existing EU law into domestic law. That would, in theory, mean the legal position in this area would remain the same in the UK post-Brexit (at least as an interim measure). This is not unexpected: the current European regime was itself heavily influenced by the longstanding policy of English law and English courts to seek to respect the right of parties to choose which law should govern their contracts.

2. Does English law remain a good choice as the governing law of a contract?

Yes. English law is a highly sophisticated, commercially-aware, flexible system of laws pre-eminent in international business relations. These strengths will remain following Brexit. The English courts are of course best placed to understand and apply English law; the judiciary are rightly known for their impartiality, independence and quality. These strengths will remain post-Brexit. That said, it is always prudent for commercial parties (regardless of Brexit) to be mindful of their particular circumstances when selecting a governing law for new contracts. That will include an assessment of where they are likely to wish to sue, what causes of action may arise, the particular industry the contract relates to and where they may wish to enforce any judgment. That assessment will no doubt often confirm English law as being appropriate, regardless of whether the English courts end up with jurisdiction over any disputes.

3. Should I still be agreeing English jurisdiction clauses?

Parties to a contract use a jurisdiction clause to nominate a court (or courts) which they wish to hear and give judgment on disputes which arise out of their contract. The ability of a court in the EU to accept jurisdiction over a case is determined by the application of EU rules. The same rules provide a mechanism for the enforcement of one member state court's judgements in another member state. Thus the UK's exit from the EU gives rise to two particular issues in the context of jurisdiction clauses:

A. the risk that courts in remaining EU states will not respect the parties' choice of the English courts as the forum for their disputes; and

B. the risk of not being able to enforce an English court judgment in a relevant foreign jurisdiction.

Although these risks deserve appropriate consideration, and particular cases will turn on their own facts, in our view there are now, and will continue to be, strong reasons for adopting English jurisdiction clauses.

We begin by noting that, following the Prime Minister's statement that the UK will make a notification under Article 50, TEU, before the end of March 2017, the current regime will continue in force in the UK for at least the next two years. Thereafter, any unilateral move by the UK to seek to preserve the current regime in UK law will be of limited effect, because the essence of the jurisdiction and enforcement regime is its reciprocity. Continuation of the status quo, or an approximation of it, would therefore need some kind of agreement. That would plainly

be in the interests of all parties. Litigants in all member states, not just the UK, benefit from the current regime of mutual respect for jurisdiction and enforcement, including through the ability it offers to enforce local judgments in England easily.

However, even if the UK and the EU are not able to reach agreement on such a regime (or there are delays in its agreement) there are steps the UK could take unilaterally relatively quickly that would preserve at least some of the benefits of the current system. Some or all of these steps might be pursued in parallel with negotiations with the EU in order to seek maximum stability and continuity for commercial parties. Accession to the Hague Convention on Choice of Court Agreements is the most straightforward of these options, because it does not require the UK to secure the consent of any other party. Accession to the Lugano Convention would preserve more of the benefits of the current regime, but would require the consent of those states which are already party to the Convention.

Issues relating specifically to point (B) above – enforcement – are considered further in answer to question 4 below.

4. Will European courts enforce my English court judgment? What can I do to reduce uncertainty?

For the moment, of course, the UK is a full member of the EU and will remain so for two years at least. Judgments obtained during that period will be fully enforceable in accordance with the current European regime. As noted in answer to question 3 above, there is also considerable incentive for EU member states to maintain the current regime post-Brexit so that their local judgments continue to be easily enforceable in the UK. Further and in any event, the Hague Convention on Choice of Court Agreements, should the UK become a party to it, would provide another post-Brexit means by which English judgments in disputes arising from qualifying exclusive jurisdiction agreements would continue to be enforceable in EU member states.

5. Should I consider a non-exclusive jurisdiction clause?

One option for parties entering into contracts now is to consider giving the English court non-exclusive jurisdiction over disputes. That would allow each party the flexibility to choose at the appropriate time whether to sue in England or to try to sue in the courts of one of the continuing member states of the EU. The ability to sue in an EU court instead of in England might, in theory, be useful in the event that the UK is not immediately able, post-Brexit, to secure a continuation of the current regime whereby English judgments are easily enforceable across the EU.

However, a non-exclusive jurisdiction agreement carries its own risks which might negate its perceived benefits. Such a clause should be drafted carefully by reference to the circumstances of the case and a clear understanding of what each party wishes to achieve. Particular issues relevant in the context of the EU and Brexit are as follows:

First of all, a party can only sue in a member state court if that court has jurisdiction under the EU rules. In other words, a jurisdiction clause that merely confers non-exclusive jurisdiction on the English courts does not automatically confer a right to sue in another, member state court.

Second, it is in the nature of a non-exclusive jurisdiction clause that parties have a choice where to start a claim. The result might be that a party is obliged to defend proceedings in a jurisdiction it might rather have avoided – the EU rules require member state courts to defer (in the first instance, at least) to the court first seised. With the UK outside the EU, there might be greater potential to enlist the help of the English court in resisting litigation overseas, but that would also involve extra time and cost (with no guarantee of success).

Third, in the event that a party chose to sue in England (or was unable to sue elsewhere), the fact of the non-exclusive jurisdiction clause might impair its ability to enforce the resulting judgment outside England. That is because non-exclusive jurisdiction clauses fall outside the scope of the Hague Convention on Choice of Court Agreements. Signatories to the Hague Convention (which include the EU and which the UK could easily and unilaterally accede to post-Brexit) agree to permit mutual enforcement of in-scope judgments. It is likely that the UK will wish to accede to the Hague Convention, if only to provide litigants with a jurisdictional safety net pending a fuller co-operation agreement with the EU.

In short, parties considering adopting a non-exclusive jurisdiction clause should consider carefully in which country the particular circumstances of their contract indicate they might need or be able to sue. Is the apparent flexibility enough to compensate for the risk of jurisdictional disputes and the possibility of not being able to sue in England (or another preferred jurisdiction)?

6. Will I still be able to serve a claim issued in the English court on a defendant in Europe post-Brexit?

In summary, yes. The legal position is summarised below. It has always been possible, however, to avoid the various technicalities and delays of service overseas by ensuring that, where a party to a contract is not domiciled in England, provision is made in the contract for the appointment of an agent in England to accept service on that party's behalf. Often, this agent for service will be the relevant party's English lawyers. Parties may consider such an approach all the more desirable in the context of Brexit.

By way of background, service is the process by which a party is given legal notice of documents used in court proceedings. Where the parties are in the jurisdiction where the proceedings were issued, service is generally straightforward (though subject to precise rules). Where a defendant to English proceedings is outside England, service can be a more complicated and time-consuming affair.

Sometimes, as a first step, the court's permission is required. Where the party to be served is in the EU (and the English court has jurisdiction by virtue of the pan-European regime discussed above[2], it is not necessary to obtain the English court's permission. However another EU instrument, the Service Regulation, sets out compulsory rules for effecting service in another member state. Absent some special agreement, the Service Regulation will cease to apply in the UK when the UK leaves the EU. Various pre-existing conventions, bilateral treaties and local law rules of service will remain in place, although they can sometimes be more cumbersome in their operation than the Service Regulation.

7. Should arbitration be the default dispute resolution choice for cross-border contracts and transactions?

The regime governing cross-border enforcement of arbitral awards is not linked to the EU and will be unaffected by Brexit. In some circumstances, then, arbitration could offer a more certain and more appropriate dispute resolution process.

However, it is important to recognise that an arbitration clause is not a universal panacea. Parties thinking of incorporating an arbitration clause in contracts should still weigh up the relative pros and cons of choosing arbitration, both generally and for the type of dispute(s) that may materialise under the specific contract in question including, for example, limited rights of appeal, and the ability to obtain urgent relief. Parties should also consider carefully the different arbitral institutions and rules available to determine which may be appropriate for their circumstances.

[2] or the Hague Convention on Choice of Court Agreements.

8. Will one-sided jurisdiction clauses still be valid?

A one-sided (or asymmetric) jurisdiction clause requires one party to bring proceedings in the courts of a particular state while typically affording the other party the flexibility to sue in any court which will accept jurisdiction.

One-sided jurisdiction clauses have been upheld by the English courts. However, a series of decisions in the French courts have led to some doubt over whether one-sided jurisdiction clauses (at least in their broadest form) are, in fact, consistent with the current European regime. The inconsistent approaches among different member state courts make it likely that the CJEU will at some stage be asked to opine on the validity of one-sided jurisdiction clauses. If the UK is still part of the EU when that happens, the English courts would be bound to apply the CJEU's interpretation. If the CJEU opines after the UK has left, we would expect the English courts to continue to respect party autonomy and uphold one-sided jurisdiction clauses. Given the prevalence of one-sided jurisdiction clauses in, for example, financing agreements, the likely pragmatism of the English courts may be attractive to commercial parties.

9. Should parties consider including hybrid clauses providing for arbitration as well as litigation in the English courts?

A hybrid jurisdiction clause can provide for the English courts to have jurisdiction over disputes while also giving one party the right to elect for arbitration. (Giving both parties such a right would be impracticable and would likely lead to further disputes.)

Although superficially attractive for their apparent flexibility, such clauses may in fact do little to mitigate the risks they are designed to guard against. This is because hybrid clauses are a type of one-sided jurisdiction clause: although the English courts have upheld such clauses, courts in certain EU member states, most notably France, have found them to be unenforceable in some circumstances.

As a result, entering into such a clause creates not only the risk that the enforcement benefit of an arbitral award will be removed, as the clause underpinning the arbitration will itself be unenforceable, but also raises the prospect of additional challenges at the jurisdiction stage by competing tribunals within the EU. In the absence of a clear indication that the courts of all potentially relevant jurisdictions will uphold such a clause, they are unlikely to be suitable. Please seek specific advice if you are considering making use of such a hybrid clause.

10. EU case law is relevant to my business. After Brexit, will judgments of the CJEU / ECJ continue to be relevant in English law?

For so long as the UK is a member of the EU, it is subject to EU law. One aspect of this is the right of the English court to ask the CJEU questions on the interpretation and validity of EU law. All member state courts are bound by the interpretative rulings of the CJEU.

After the UK leaves the EU, the default position is that the English court will lose the right to refer questions of EU law to the CJEU and it will no longer be bound by the CJEU's jurisprudence. But in all likelihood that jurisprudence will continue to be highly relevant to the English courts for some considerable time. This is because, where English courts consider matters which arose pre-Brexit, they will need to consider and interpret the law as it was pre-Brexit. Even in respect of disputes relating to matters arising post-Brexit, the UK Government has indicated that its preferred approach upon Brexit is to retain in UK law, to the extent possible, all EU laws and then repeal or amend them at a later date as deemed necessary. The Government's position, coupled with the pervasive nature of EU or EU-derived laws, makes it likely that a considerable volume of English law will continue to be interpreted by reference to

European legal concepts and case law for some time to come.

Although dependent in part on the future relationship agreed between the UK and EU, it is also possible that, over time, the English courts and CJEU may adopt or develop different interpretations of similar legal issues and concepts.

11. Are the English courts likely to be more reluctant to make references to the CJEU now that the UK is leaving the EU?

The UK is currently a full member of the EU and it will remain so until the conclusion of a withdrawal agreement between the UK and the EU or the expiry of two years from the date the UK gives formal notice of its intention to leave. Until then, the English courts are entitled under the EU Treaties[3] to ask the CJEU questions on the interpretation of EU law and the validity and interpretation of acts of EU institutions, where an answer is necessary to enable the English court to give judgment on the matter before it. In the language of the Treaty, these questions are known as "references for a preliminary ruling".

None of the EU Treaties, the Statute on the CJEU, or the CJEU's rules of procedure specifically contemplates the implications of withdrawal of an EU member state on references by that state's courts to the CJEU. However, the CJEU's rules of procedure[4] provide that the court is seised of a request for a ruling insofar as it has not declared that the conditions of its jurisdiction are no longer fulfilled. The CJEU would have no jurisdiction to rule on a request from a court that was not a member state. On this basis, it would appear that, where a reference to the CJEU from the English court is outstanding at the time the UK ceases to be a member state, the CJEU shall be entitled (but not obliged) to decline to render a ruling in respect of that reference.

In practice, it is likely that any agreement between the UK and the EU by which the UK ceases to be a member state will provide for some kind of transitional arrangements in respect of UK court references to the CJEU.

In the meantime, the right of the English court to make a reference is unencumbered, and there is no reason to think that English judges will not continue to make references on EU law where they consider it necessary in order to enable them to give judgment in cases before them.

It is possible that, as we move closer to the UK's formal withdrawal from the EU, the number of references to the CJEU from the English court may increase as parties rush to litigate matters which touch on disputed or ambiguous provisions of EU law. Given that the timeframe for obtaining a decision from the CJEU can be very lengthy, anyone considering whether a reference to the CJEU may be necessary or desirable as part of their litigation tactics would be prudent to try to expedite proceedings to obtain such referral as soon as possible.

[3] Article 267 of the Treaty on the Functioning of the European Union.
[4] Article 100.

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