

# THE BASICS: WHAT TO CONSIDER WHEN NEGOTIATING GOVERNING LAW AND JURISDICTION CLAUSES

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Articles

Parties negotiating any contract of substance, especially one with a cross border element, should consider the most appropriate form of dispute resolution for any disputes arising under it. Where litigation is the chosen forum, parties should agree both a governing law and a jurisdiction clause to help interpret the contract and resolve any future disputes. Too often, such clauses are only given proper consideration after a dispute has arisen and a party finds itself litigating in a jurisdiction it would not have chosen with its rights and remedies restricted by an unfamiliar law.

We consider the basics of what you need to know.

- Governing law clauses, what they do and when Rome I and II may apply;
- Jurisdiction clauses, what they do, when the European Regime for determining jurisdiction applies and the position if there is a conflict;
- The possible effect of Brexit;
- Factors to consider when choosing a jurisdiction clause; and
- Some drafting tips.

## GOVERNING LAW CLAUSES

### What does the governing law clause do?

It enables the parties to specify what substantive law will govern the rights and obligations of the parties. It will be applied to interpret the contract and its effects if a dispute arises, thereby reducing uncertainty for both parties.

## **What are the consequences?**

If you choose a governing law - which can cover both contractual and non-contractual obligations and disputes (subject to certain exceptions) - make sure you know the consequences of that choice. Some legal systems have very different rules on, for example, the recoverability of damages and the circumstances in which you can terminate a contract and the consequences of termination.

## **What if there is no governing law clause?**

If no governing law clause is included and a dispute arises, the court hearing the dispute is likely first to have to determine what law applies to the contract (and any non-contractual obligations) before it can resolve the dispute.

Where at least one of the parties is based in an EU Member State, the Rome I Regulation (for contracts concluded on or after 17 December 2009) and Rome II Regulation (which has applied from 11 January 2009 for non-contractual disputes - such as negligence, misrepresentation, product liability) provide a prescriptive set of rules to determine the governing law. Under Rome I, specific rules apply to different types of contract but in most cases the applicable law is that of the country where the party with characteristic performance of the contract has his/her/its habitual residence. Under Rome II the applicable law is generally the law of the country in which the damage occurs or is likely to occur. However, it may also be that of the country in which both parties have their 'habitual residence' or the country most 'closely connected' to the underlying tort. There are also specific rules for certain types of claims under Rome II.

Invariably, costs and delay can be incurred in arguing over 'habitual residence' and 'close connection' and the ultimate result may be that a very unfamiliar law governs the contract or tortious claim (and remedies) and those rules may not favour you.

Where a court outside the EU has jurisdiction, the conflict of law rules that will be applied to determine the governing law vary from country to country, again introducing an element of uncertainty and potential costs.

## **Are parties always free to choose the governing law?**

In some situations, even if you do choose a governing law, Rome I and II will not allow the parties to use their choice of governing law to get around certain "mandatory rules" of the country where the case is to be heard or where all the relevant elements at the time of the choice are situated.

## **Can there be more than one governing law?**

It is possible, but rarely sensible, and will almost always lead to confusion.

## **Should the governing law accord with the jurisdiction?**

It is usual for the governing law to coincide with the jurisdiction clause but there is no requirement for it. Although the English courts are experienced in applying foreign law, the foreign law must be pleaded and proved as a fact, usually through evidence of a qualified lawyer from the relevant jurisdiction. Again, this can add uncertainty, time and costs to the litigation.

## JURISDICTION CLAUSES

### What does the jurisdiction clause do?

It enables the parties to agree at the outset of the contract which country's courts will hear any disputes that arise under it. This means parties can avoid (generally) jurisdictions that they might consider less desirable or predictable. Failure to agree your chosen forum could mean that even a strong case is commercially not worthwhile pursuing. If the parties agree a particular court within the EU has exclusive jurisdiction this will generally prevent claims being brought in any other courts within the EU.

### What if there is a dispute over the jurisdiction clause?

Although a jurisdiction clause will not always prevent a party from issuing proceedings in another court, if there is any disagreement as to venue that dispute must be resolved first.

### What if there is no jurisdiction clause?

Where there is no clause, the basic rules of the Recast Brussels Regulation (for proceedings instituted on or after 10 January 2015) or 2001 Brussels Regulation (for proceedings instituted before 10 January 2015) (together the European Regime) apply. Under the European Regime, an EU domiciled defendant must be sued in the courts of the Member State of his/her domicile (in the case of an individual), or its place of statutory seat, central administration or principal place of business (for a company), subject to certain exceptions and constraints. In contractual claims, a defendant may be sued in the place of performance of the obligation in question.

Courts outside the EU will apply their own rules to determine whether they have jurisdiction. Non EU domiciled defendants may be sued in the English court if one or more certain prescribed connections to England are established.

### What if there is a conflict between a jurisdiction clause and the European Regime?

Member States have exclusive jurisdiction in relation to some types of dispute regardless of domicile (for example claims relating to immovable property, certain questions of company law etc). Where the Member States have such exclusive jurisdiction this will override anything the parties may have otherwise agreed in a contractual jurisdiction clause and the court nominated will decline jurisdiction if claims are issued before them in breach.

Where one party is from an EU Member State (except Denmark) and another is from Mexico or Singapore, then the rules of the Hague Convention on Choice of Court Agreements (the Hague Convention), under which exclusive jurisdiction clauses are required to be recognised and enforced, will need to be considered.

## WHAT WILL BREXIT DO TO THE EUROPEAN REGIME?

The UK's position is that when it exits the EU, the European Regime will cease to apply. Although both parties seem keen to replicate the existing system in some way, it may be that other agreements to which the UK is party (for example the Hague Convention) take on new importance. With this uncertainty, it is all the more important to understand the consequences of governing law and jurisdiction and to specify English law and jurisdiction in a contract if that is appropriate.

## WHAT FACTORS SHOULD BE CONSIDERED WHEN CHOOSING A JURISDICTION CLAUSE?

- **Which court is the most practical and convenient?** Your home court? Where would any witnesses be located? Are there language issues?
- **What are the respective procedural systems for the competing jurisdictions?** Some jurisdictions have onerous disclosure obligations (the U.S.), some have very little in the way of disclosure (France). Costs follow the event in some places (England & Wales) but not in others (the US). Consider also the rules of evidence, whether the system is inquisitorial (many continental European countries) or adversarial (most common law countries), whether there are specialist courts and judges, the speed of the litigation process and cost generally, the availability of appeals and the quality of the judges (and lawyers). The English judiciary has a reputation for quality, independence, impartiality and integrity.
- **How easy is enforcement?** Claimants should consider litigating in the place where the assets are located to avoid having to transport a judgment from elsewhere: the rules on enforcing foreign judgments can be complex.
- **Should the jurisdiction clause be exclusive (i.e. the parties can only go to that location) or non-exclusive (the parties can litigate elsewhere)?** This is a question of certainty (exclusive) against flexibility (non-exclusive). In some cases an asymmetric jurisdiction clause may be agreed, so that party A can sue party B in any jurisdiction, but party B can sue party A only in the specified jurisdiction. This clause typically occurs where there is an imbalance of bargaining power, for example between a lender and borrower. However, this is not universally accepted - the law of some countries does not recognise these as valid jurisdiction clauses making enforcement difficult or potentially impossible.
- **Is a jurisdiction clause appropriate at all?** Is arbitration or some other form of Alternative Dispute Resolution (ADR) more appropriate to resolve the dispute?

## CONSIDER THE FOLLOWING DRAFTING TIPS

- Include express governing law and jurisdiction clauses in the contract; seeking to imply them by reference to other contracts or documents can prove difficult.
- Draft the clause so that it is wide enough to cover both contractual and non-contractual disputes which may arise, for example for misrepresentation claims. Specify whether it is exclusive or non-exclusive.
- Unless there is good reason not to do so, ensure the governing law and jurisdiction clauses are compatible with each other.

The inclusion of clear provisions on governing law and jurisdiction in a contract as referred to above, should ultimately assist in any dispute being determined under the law and in the courts chosen by the

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