3VB'S FINANCE COLUMN: ENFORCING FINANCE AGREEMENTS IF THE UK CANNOT JOIN THE LUGANO CONVENTION

In this column Victor Steinmetz, of 3 Verulam Buildings considers how cross-border enforcement of English law contracts might be affected if the UK does not join the Lugano Convention and suggests practical steps parties to finance agreements should take to prepare for this eventuality.

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Following Brexit, the UK has lost the benefits it previously enjoyed under the Brussels Regulation (Recast). As a result, it is hoped that the UK will accede to the 2007 Lugano Convention on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (the "**Lugano Convention**"), which provides for a similar (albeit not identical) regime. The UK was a party to the Lugano Convention through its EU membership and applied to join it in its own right on 8 April 2020.

However, these hopes now appear to be waning as a result of the *EU Commission's recommendation* to reject the UK's application on the basis that it is not a member of the EEA or EFTA and lacks any special link to the internal market. The recommendation is not binding and the ultimate decision lies with the Council of the European Union, which is still outstanding.

This note outlines:

- The rules that would apply if the Council were to follow the EU Commission's recommendation.
- What lenders can do to limit any risks that would arise as a result.

THE HAGUE CONVENTION AS A FALL-BACK SOLUTION

If the EU Council rejects the UK's application to join the Lugano Convention, dispute resolution clauses and the recognition and enforcement of judgments will be governed by a combination of both the 2005 Hague Convention on Choice of Court Agreements (the "**Hague Convention**") and the national laws of the relevant countries in question.

Accession to the Hague Convention does not require the unanimous agreement of the contracting parties and the UK acceded to the Hague Convention in its own right on 1 January 2021 (CET). The scope of the Hague Convention is however not as extensive as the Brussels and Lugano regimes.

THE LIMITS OF THE HAGUE CONVENTION

The Hague Convention only applies to cases where:

- The parties agreed to an exclusive jurisdiction clause in favour of the courts of a contracting state; and
- That agreement was entered into after the Convention came into force in that state.

In such a case, the chosen court cannot decline to exercise its jurisdiction on the basis that the dispute should be decided in a court of another state, and except in specific circumstances, the courts of other contracting states must suspend or dismiss any proceedings that were brought before them (*Hague Convention, article 5.2*).

The contracting parties to the Hague Convention are the EU member states, the UK, Mexico, Singapore and Montenegro, but does not include any of the EFTA countries (Iceland, Liechtenstein, Norway and Switzerland). A large number of subject matters are also expressly excluded from the scope of the Convention, including consumer and employment contracts, insolvency and arbitration related proceedings (*Hague Convention, article 2*) and it should also be noted that the Hague Convention does not provide for the recognition and enforcement of interim orders, such as freezing orders and injunctions (*Hague Convention, articles 4 and 7*).

Where the Hague Convention does not apply, jurisdiction and enforcement issues are governed by the national laws of the relevant country, which may result in more burdensome enforcement procedures and may be more time consuming and expensive.

THE NEED FOR AN EXCLUSIVE JURISDICTION CLAUSE

The fact that the Hague Convention only applies to exclusive jurisdiction clauses throws doubt on a party's ability to rely on non-exclusive and asymmetric jurisdiction clauses (see *Practice note, Governing law and jurisdiction clauses: Choosing a jurisdiction clause*).

The contracting states have the option to declare that they will recognise and enforce judgments given pursuant to non-exclusive jurisdiction clauses but none have done so (*Hague Convention, article 22*). These clauses therefore currently fall outside the scope of the Convention and jurisdiction and enforcement issues will be determined by the relevant domestic laws.

It is currently uncertain whether asymmetric clauses, which are popular in finance and other transaction documents, should be regarded as exclusive jurisdiction clauses. The Explanatory Report on the Hague Convention appears to exclude such clauses from the scope of the Convention and their validity has been doubted by the courts of EU member states, in particular by the French *Cour de Cassation*. Recent (obiter) comments from the (English) Court of Appeal also suggest that the English courts will probably not consider that the Hague Convention applies to such clauses (*Etihad Airways PJSC v Lucas Flother [2020] EWCA Civ 1707*). If this position were to be applied, a court's jurisdiction and the enforcement of a judgment handed down pursuant to such a clause would again be a matter of national law.

WHEN DID THE HAGUE CONVENTION COME INTO FORCE IN THE UK?

Another issue concerns the date on which the Hague Convention entered into force in the UK. Whereas the UK's position is that this occurred on 1 October 2015, when the EU acceded to the Convention on its member states' behalf (*paragraph 5, Schedule 5, Private International Law (Implementation of Agreements) Act 2020*), the EU Commission instead maintains that the UK only became a member following its accession in its own right on 1 January 2021 (*EU Commission's Notice to Stakeholders dated 27 August 2020, section 3.3*). There is therefore a risk that an EU member state court may not apply the Hague Convention if the relevant jurisdiction agreement was entered into prior to 1 January 2021.

WHAT YOU CAN DO TO LIMIT THE RISKS

To avoid the risk of falling outside the scope of the Hague Convention, it may be useful to:

- Restate any exclusive jurisdiction clauses entered into prior to 1 January 2021, to ensure that EU member state courts apply the Hague Convention.
- Seek legal advice in relation to contracts entered into with a counterparty located in an EFTA state.
- Consider redrafting your dispute resolution clauses.

HOW SHOULD YOU NOW DRAFT YOUR DISPUTE RESOLUTION CLAUSES?

Given that there is a real risk that non-exclusive and asymmetric clauses fall outside the scope of the Hague Convention and will instead be determined by the national laws of the relevant country, which may entail an uncertain result, delays, and higher legal costs, it seems prudent for parties to:

- Ensure that any new dispute resolution clause is drafted as an exclusive jurisdiction clause that falls within the scope of the Hague Convention.
- Review, and if necessary amend, dispute resolution clauses that have already been entered into, to ensure that they constitute exclusive jurisdiction clauses falling within the scope of the Hague Convention (if this is feasible

in practice and if the loss of the flexibility offered by non-exclusive and asymmetric clauses is commercially acceptable).

- Consider whether recourse to arbitration or alternative dispute resolution mechanisms, such as mediation, may be a possible alternative and if so, amend the dispute resolution clause accordingly. The New York Convention, which governs the recognition and enforcement of arbitral awards, continues to apply to the UK and the EU member states.