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FOREIGN FORUM SELECTION CLAUSES: LIMITATIONS ON ENFORCEABILITY

A well-drafted forum selection clause can provide companies and individuals, especially those dealing in an international market, with certainty about the location of litigation arising out of a contractual relationship. While these clauses sometime identify a neutral jurisdiction, frequently the choice of the location is offered in negotiation by "outside" entities to obtain access to a foreign market where the native participants may not contract internationally if they believe they could be sued in a jurisdiction other than the one of their choosing. As part of this process, the "outside" entity must perform a cost–benefit analysis based on the foreign jurisdiction's then current legal structure to determine if the forum is an acceptable venue for any future litigation. However, jurisdictions can and do (sometimes frequently) suffer political change and, as a result, changes in official attitudes toward foreign investment. If such a change occurs, it is vital for a contracting entity to understand the revisions to the legal system of the venued jurisdiction. It is equally important to know whether or not these revisions could serve as justification to invalidate an existing forum selections clause.

This *Commentary* discusses the limited circumstances when a litigant can challenge a contractual forum selection clause if, based upon post-contracting events, the negotiated venue is no longer a viable jurisdiction for litigation.

BACKGROUND: GENERAL ENFORCEABILITY OF FOREIGN FORUM SELECTION CLAUSES

The seminal case addressing the general validity of foreign forum selection clauses is *The Bremen v. Zapata Off-Shore Co.* (407 U.S. 1 (1972)). In *The Bremen,* the contract contained a forum selection clause that venued in London any dispute arising out of a shipping contract between a Houston-based corporation and a German corporation for the transport of equipment from Louisiana to Italy. During transport, the equipment was damaged in a storm, and the shipping company's vessel took port in Florida to make repairs. As a result of the delay, a dispute arose between the parties, and the equipment owner filed suit in the United States District Court

in Florida. The shipping company, in response, sought to enforce the London forum selection clause.

Ultimately, the U.S. Supreme Court, siding with the shipping company and honoring the strength of a negotiated contract, held that a court should enforce a forum clause unless the objecting party can "clearly show that enforcement would be unreasonable and unjust, or that the clause was invalid for such reasons as fraud or overreaching." The Court also reasoned that mere inconvenience for one party is not sufficient to make this showing. Rather, it is "incumbent on the party seeking to escape his contract to show that trial in the contractual forum will be so gravely difficult and inconvenient that he will for all practical purposes be deprived of his day in court." *Id.* at 17-18.

The Bremen v. Zapata set the initial standard requiring that, to invalidate a forum selection clause, the enforcement of the clause must deprive a litigant of its day in court. It was several years, however, before a decision provided insight on the specific mechanics of successfully challenging a forum selection clause and the severity of the events necessary to meet the threshold established in *The Bremen v. Zapata*.

ENFORCEABILITY STANDARDS: THREE EXAMPLES

Although each case detailed below has its own unique factual setting and procedural history, the process of challenging a foreign forum selection clause essentially entails two steps. First, the challenging party must identify drastic and unexpected changes in the forum's legal process that occurred during the period between the contract date and the litigation. Second, that same party must show that, due to such changes, it will be deprived of its day in court.[1]

1 It is worth noting that some courts have held, based on the facts of those cases, that increased cost or difficulty, on their own, do not create enough of a burden. According to these courts, they do "not provide a 'sufficiently strong showing' that enforcement of a forum selection clause would be unreasonable or unjust." *Martinez v. Bloomberg*, 883 F.Supp.2d 511, 522 (S.D.N.Y. 2012) (citing *Phillips v. Audio Active, Ltd.*, 494 F.3d 378, 384 (2d Cir. 2007)).

Example One: *McDonnell Douglas Corp. v. Islamic Republic of Iran*, 758 F.2d 341 (8th Cir. 1985)

McDonnell Douglas entered into a contract with the Imperial Iranian Air Force in 1975. In 1979, before the contract was completed, the Imperial Government of Iran was overthrown by the Islamic Republic of Iran, leading to strained relations between the new government and the United States and ultimately a directive from the United States government to McDonnell Douglas that it could not ship material to Iran, under the contract or otherwise. Iran filed suit against McDonnell Douglas in Iran pursuant to the forum selection clause in the agreement, and McDonnell Douglas filed suit in the United States seeking declaratory judgment that its nonperformance was excused and that the contract was void. McDonnell Douglas also sought to invalidate the forum selection clause.

The Eighth Circuit Court of Appeals determined that due to changed circumstances in the chosen forum, there was a "'compelling and countervailing reason' why the forum clause should not be enforced." 758 F.2d at 345 (citing *The Bremen*, 407 U.S. at 12). The court reviewed the conditions in Iran, stating:

> [W]e take judicial notice of the recent escalation of the war between Iran and Iraq, the bombing of Tehran by the Iraqi Air Force, Iraq's threat to shoot down all commercial planes over Iran, and the suspension of flights to Iran, by several commercial airlines, which would make it gravely difficult, inconvenient and dangerous for McDonnell Douglas to litigate its dispute with Iran in the Islamic Court of the First Instance in Tehran. We thus take judicial notice that litigation of the dispute in the courts of Iran would, at the present time, be so gravely difficult and inconvenient that McDonnell Douglas would for all practicable purposes be deprived of its day in court.

Id. at 346. Accordingly, based in large part on the severe and drastic change in the political climate in Iran and the relationship with America, the court held that that the forum selection clause was no longer enforceable.

Example Two: *Rice Corp. v. Grain Bd. of Iraq*, No. 2:06-cv-01516., 2009 BL 232128, at 6 (E.D. Cal. Oct. 26, 2009)
Rice Corp. entered into an agreement with the Grain Board of Iraq to deliver rice to Iraq. The contract contained a forum selection clause requiring that all disputes be resolved in Iraq. Despite this requirement, when a dispute arose, Rice Corp. filed suit in the Eastern District of California. The Grain Board of Iraq moved to dismiss the dispute based upon the forum selection clause. Unlike *McDonnell Douglas* above, the court enforced the forum selection clause because Rice Corp. did not meet the requirements to invalidate the clause.

Specifically, the court determined that Rice Corp. had notice, prior to entering into the agreement, of certain difficulties in litigating in Iraq and that Rice Corp. "presumably should have known about these judicial features before it agreed to select Iraqi [sic] as the litigation forum in 2005." *Id.* at 6. Furthermore, the court held that any inconvenience and expense of foreign litigation was also foreseeable at the time of contracting. *Id.* Accordingly, the court determined that Rice Corp. was bound to the forum selection clause and granted the motion to dismiss. *Id.* at 6-7.

Example Three: *Bancroft Life & Casualty ICC, Ltd. v. FFD Resources II, LLC*, 884 F. Supp. 2d 535 (S.D. Tex. 2012)
Courts have also shown a reluctance to void a forum selection clause where the language of the agreement allows for change after the execution of the agreement (where the forum is not identified as a specific location but instead tied to the location of a party to the contract).

For example, in *Bancroft v. FFD Resources*, a contractual forum selection clause provided that disputes would be resolved in Bancroft's place of residence, which, at the time of contracting, was the British Virgin Islands but later changed to St. Lucia. *Id.* at 546. FFD claimed that the clause was unreasonable since, during the contractual period, the plaintiff had "unilaterally changed the forum from British Virgin Islands to St. Lucia … and [the defendant] had no notice of this change nor a meaningful opportunity to agree or to reject the new forum." *Id.* at 553. Further, St. Lucia did not recognize the right of a jury trial in civil cases, unlike the British Virgin Islands and the United States. *Id.* at 553-54. Despite these changes, the court noted that the lack of a jury trial would not render a forum inadequate and found that the defendant had not shown that "the St. Lucia forum will deprive them of their day in court." *Id.* at 559.

CONCLUSION

Companies or individuals may find it beneficial to include forum-selection clauses in foreign contracts, as these give the parties a sense of security and certainty about where any potential litigation may take place. However, there are risks associated with designating a forum by contract, and a party may find that the legal or political environment of the designated forum is markedly different at the time of litigation than at the time of contracting. In such situations, a party may be able to avoid the application of the forum-selection clause. U.S. courts, however, have thus far allowed this only where the changes to the forum were drastic and unexpected, were not contemplated by the terms of the agreement, and would have effectively deprived a party of its day in court. Contracting parties should therefore carefully consider the potential risks and rewards—both at the time of contracting and over the course of the contractual relationship.

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