On the Value of Choice of Forum and Choice of Law Clauses in Spain

A contract was held between two companies: a Spanish company and a foreign one. They agreed to refer any dispute concerning the contract to the courts of Barcelona (Spain), and chose Spanish law as applicable law. Later, the Spanish company decided to sue its counterparty in the United States. The foreign company believed that this behaviour amounts to a breach of contract, and that it results in extra costs (such as fees for local lawyers hired to raise the plea) that should be repaired. The question is, is she right?

The issue was raised for the first time in Spain in a ruling of the Supreme Court (Tribunal Supremo, TS) from February 23, 2007, to which I referred in a previous post . Actually, the main issue in the ruling was international lis pendens. However, the TS also told us that a choice of forum clause is of contractual nature, and that failure to comply with it implies economic consequences: the defaulting party may be sued and sentenced to pay compensation for the legal costs incurred by the counterparty, when forced to defend itself in courts other than those chosen. The elected courts have jurisdiction to decide on the breach of the choice of court agreement.

Recently, the TS ruled again on the issue (STS, from January 12, 2009: see here). The circumstances of the case are those described above. The foreign company sued the Spanish one for breach of contract; both the Court of First Instance (Juez de Primera Instancia) and the Court of Appeals (Audiencia Provincial) denied the claimant's right to compensation. The TS, however, decided otherwise and overturned their rulings.

The inconsistency between opinions is largely due to different understandings of the nature of choice of forum clauses. For the Court of First Instance and the Spanish company, the agreement to submit is not part of the contract, nor is it a contract; on the contrary, it is an agreement of adjective or procedural nature. Its breach (the non-submission of the parties to the elected Court) ends up in a restricted effect: depending on the willingness of the counterparty, the claim

before the non-chosen court will not be decided by this court. The law provides no other penalty for failure to comply with the clause.

The Court of Appeals followed the Court of First Instance opinion, noting that "the principle of contractual freedom does not work the same way in cases where only private interests are at stake, and in case of procedural covenants to submit to jurisdiction" , the latter having limitations of public-procedural order; "agreements of contractual contents (economic agreements) and procedural covenants to submit to jurisdiction cannot be assimilated"; "the pact to submit to a certain jurisdiction is a subsidiary one; it only comes into play when the contract has to be enforced or interpreted." The Court also said that there is no causal link between the breach of the covenant and the damages claimed by the foreign company in Spain: these damages being due for the proceedings before the Courts of Florida, they must be labelled as "costs of the proceedings" (legal costs); and only the Florida Court could determine the costs to be paid.

The claimant's (the foreign company) thesis, quoting Spanish and foreign academics, is the opposite: the choice of forum agreement should be treated like any other contractual clause. The plaintiff also recalled that the agreement was not only a choice of court one; the parties had also chosen Spanish law. Finally, the claimant argued the bad faith of the defendant: sole purpose of the claim (of several hundred million dollars) in Florida was to cause further injury and to intimidate.

The TS ruled in favour of the claimant. The Court expressly stated that "[the choice of forum agreement] is incorporated to the contractual relationship as one of the rules of conduct to be observed by the parties; it creates a duty (albeit an accessory one); failure to comply with it (…) must be judged in relation to the significance that such failure may have in the economy of the contract, as this Court has consistently maintained (…) that breaches determining the economic frustration of contract for one party are to be regarded as having substantial meaning (…)". The TS goes on saying that "(…) in the instant case, the choice of the applicable law and jurisdiction may have been crucial when deciding whether to establish the relationship. If so, they would have clear significance for the economy of the contract, given that Spanish law establishes a concrete contractual framework for the assessment of damages (for instance, it excludes punitive damages, which on the contrary may be awarded under the law of the United States of America);" " The conscious breach of the covenant, raising a

claim where the law of the U.S. was to applied (…) and asking for punitive damages , has created the counterparty the need for a defense, generating costs that go beyond the predictable expenses in the normal or the pathological development of the contractual relationship".

Finally, the TS denied that costs can only be imposed by the Court of Florida. In this regard, the TS said that neither the attorneys' fees nor other damages claimed by the plaintiff are considered "costs" in the U.S. The TS also added that even if they were to be deemed so, this would not have hindered the claim for damages for breach of contract: the only effect would have been the reduction of the amount that could be claimed. Hence the TS quashed the Court of Appeal ruling, without entering to determine whether the Spanish company acted in bad faith or with abuse of her right to litigate.