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### **Abstract**

***As the inflow of Foreign Direct Investment continues unabated in Nigeria, investors are increasingly adopting mechanisms to protect their investments against legal and regulatory risks. One of such methods being adopted in commercial transactions is the use of choice of law clauses. Whilst most investors are inclined to choose foreign laws to govern their contracts, it has become imperative to examine the enforceability of choice of law clauses in Nigeria in particular where the transaction is deemed to be illegal.***

### **Introduction**

Choice of law clauses are of critical importance to international transactions. As noted by the United States Supreme Court in the *Sherk*<sup>1</sup>, Choice of law provisions, along with forum selection clauses, are almost indispensable precondition(s) to the achievement of orderliness required in international business transactions. Thus, it is not unusual these days, for parties to an agreement to specify the law of a particular country they would want to govern their transaction. Such clauses in an agreement are known as choice of law clauses.

However, in spite of its general acceptability these days in international business transactions, problems do arise where choice of law clauses, although valid, may yet be unenforceable. A recent decision of a Federal Court in the Southern District of New York in *Lehman Brothers Comm. Corp v. Minmetals Int'l Nonferrous Metal Trading Co.* has again brought to the fore the proposition that choice of law clauses in commercial agreements are no longer to be seen as conclusive or absolute<sup>2</sup>. For such clauses to be effective, the courts over time have imposed certain limitations. One of such limitations requires the transaction to be legal before a specified choice of law clause can be enforceable. This requirement, which is the focus of this paper, formed the basis of the decision in the *Lehman case* and to an extent that of our Supreme Court in *Sonnar (Nig.) Ltd. V. Partenreedri M.S. Nordwind (owners of the M.V. Norwind)*<sup>3</sup>.

### **The Nordwind case.**

The facts of the Nordwind are as follows:

The Plaintiffs were Nigerian companies claiming damages for breach of contract arising from non delivery of par boiled long grain rice shipped to Lagos from Bangkok on board the M.V. Nordwind. The 1<sup>st</sup> Defendant, partenreedri M.S. Nordwind (owners of the M.V. Nordwind) carries on its business as shipowners in Germany. The 2<sup>nd</sup> Defendant, Barbridge Shipping Company is based in Liberia and it issued the Bill of Lading in this case. While the 3<sup>rd</sup> Defendant, Chaipayorn Rice Company Limited is based in Thailand and it sold and supplied the rice involved in this case. The Plaintiffs and Defendants entered into an agreement which was evidenced by a Bill of Lading, clause 3 of which provided:

***"Any dispute arising under this bill shall be decided in the country where the "Carrier" has his principal place of business and the law of such country shall apply except as provided else where herein"*** (emphasis mine).

In an application challenging the jurisdiction of the Federal High Court of Nigeria and the applicable law to govern the dispute, both that court and the Court of Appeal, gave effect to the choice of law clause based on the maxim *pacta sunt servanda*, that is, parties are bound by their contract. Dissatisfied with the judgement of the Court of Appeal, the Plaintiffs then appealed to the Supreme Court. At that court, the appeal was allowed on the basis that the transaction was more significantly connected to Nigeria, *a' fortiori*, Nigeria law ought to apply.

Said Oputa, J.S.C. in that case:

"What is the relevance of German law to a Liberian ship owner and a Nigerian Shipper? I see none. It is also conceded that when the intentions of the parties to a contract as to the law

governing the contract are expressed in words, this expressed intention is general and as a general rule determines the law of the contract. But to be effective, the choice of law must be **real, genuine, bonafide, legal, and reasonable. It should not be capricious and absurd.** Choosing German law to govern a contract between a Nigerian shipper and a Liberian ship owner is to my mind capricious and unreasonable. **Luckily, nowadays a clause of the proper law by the parties is not considered by the court as conclusive...** In this case, the rice was to be shipped from Thailand, the shippers are in Nigeria and the contract was to be performed in Nigeria by delivery in Lagos, Nigeria. The Bill of Lading was issued by a Liberian company. The whole transaction from beginning to end had little or nothing to do with Germany. Why then invoke German law as the proper law of the contract?" (Emphasis mine).

The above statement stands out as the most illuminating discuss of choice of law in contracts by Nigerian courts in that apart from adopting the earlier criteria by **Lord Wright in Vita Food Products Incorporation v. Unus Shipping Co. Ltd<sup>4</sup>**, it went on to set new categories for the recognition of an express choice of law. Thus, the requirement that a choice of law clause must be real, genuine, bonafide, legal and reasonable, not capricious and absurd are clearly novel categories and can easily be said to be the contribution of Nigerian courts on the issue of choice of law in International Commercial transactions<sup>5</sup>.

However, with utmost respect for the highly regarded jurist, **Oputa J.S.C.** in the Nordwind case, the statement that a choice of law clause must be **legal** before it can be effective or recognized appears unclear since the legality of the transaction to be performed under the contract was never in dispute. To that extent, that statement of **Oputa J.S.C.** must have been made **Obiter**. As regards the requirement of **legality** though, was **Oputa J.S.C.** referring to the validity of the choice of law clause itself or was he referring to the legality of the transaction to be performed under the contract?

The safer view, it would appear, is that the respected jurist must have been referring to the legality of the transaction to be performed under the contract. Support for this position can be found in the following statement of **Oputa J.S.C.** at page 543 of the said judgement:

"....Agreements which is neither contrary to law, nor fraudulently entered into, should be adhered to in every manner and details".

In effect what Oputa J.S.C. seem to be saying is that, where the transaction to be performed under the contract is contrary to law or illegal, the court will not give effect to the Agreement and invariably the choice of law clause. A similar situation was the basis of the decision in the **Lehman** where the court found that although the choice of law clause was valid, it was unenforceable because the transaction was illegal in the country of performance.

### The Lehman Case

The dispute in Lehman arose out of foreign exchange and swap trading transactions during the years 1992 – 1994 between **Lehman Brothers Commercial Corporation (LBCC) and its affiliates and HU Xiangdong (HU) an employee of Non-ferrous Metal Trading Company in China (Non-ferrous).**

During the relevant period, (1992 – 1994), (HU) an affiliate of Non-ferrous entered into several foreign exchange transactions on behalf of Non-ferrous. A dispute soon arose over certain payments which were due to LBCC under the several contracts between the parties. These payments, save for the first installment, were never made, thus resulting in LBCC bringing an action for breach of contract claims against Non-ferrous and its parent corporation.

On summary judgment, the court observed, that the contracts executed by the parties contained a clause designating New York law to govern their transactions. The court appeared to have no doubt that New York law was enforceable. Nevertheless, the court applying New York law found that the contracts were subject to potential unenforceability because their performance in China was illegal.

The illegality arose from the fact that during the relevant period 1992 – 1994, Chinese law required state owned enterprises such as Non-ferrous to obtain a license from the **State Administration Exchange Commission (SAEC)** before engaging in foreign exchange transactions. Because Non-ferrous did not obtain any such license, (HU's) foreign exchange transactions and swap trading were

illegal under Chinese law. The court thus held that a New York choice of law provision could not be used to circumvent the laws of a foreign country and was thus unenforceable.

## Conclusion

In sum, whilst in the Lehman, the illegality of the transaction was the main focus of the New York Court, in the Nordwind Oputa J.S.C. merely treated this point as *Obiter*. However, both decisions emphasize the point that for a choice of law clause to be enforceable the transaction must be legal in the country of performance. Where the transaction to be performed is illegal the choice of law clause would be unenforceable even if valid. This is based on the principle that the courts will not give effect to a choice of law clause if the intent is to circumvent the laws of a foreign country. Beyond this point however, the Nordwind went on to state new categories of limitations which must be met before a choice of law clause may be enforceable. These are the requirements of bona fide and reasonableness. It must be real, genuine, not capricious and absurd.

In the final analysis, it behooves parties to commercial contracts wishing to be bound by their designated choice of law clauses to ensure that all of these requirements are met, otherwise, as some lawyers have been known to say, [*pacta (will not be) sunt servanda*].

## Footnotes

1. 417 U.S. 506, 516 (1984)

2. See Dictum of Lord Atkin in R.V. International Trustee (1937) AC where choice of law clauses

were regarded as conclusive or absolute.

3. (1987) 4NWLR (pt.66) 520

4. (1939) A.C. 277

5. I.O. Omoruyi: The determination of applicable law in international contracts: A Nigerian approach, published in modern practice journal of finance and investment law, July/October, 2004 Vol. 8 No. 3-4 at page 468

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