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The "No Oral Modification" Conundrum and its implications to aircraft leasing and beyond

Introduction

A "no oral modification" clause (NOM clause) is as commonly found in a commercial aircraft lease agreement as in many other formal commercial agreements. As in the case that we will discuss below, it typically says that the "provisions of this Agreement shall not be varied otherwise than by an instrument in writing executed by or on behalf of [the parties]", and that "a right may be waived under this Agreement by an express waiver or variation in writing… and no act or course of conduct or negotiation on the part of such party or on its behalf shall in any way preclude it from exercising any such right or constitute a suspension or any variation of any such right." A recent New York court judgement brought to fore the question of whether an NOM clause effectively restricts the way in which the parties may consensually vary the contract. That question is not only interesting but is of much practical relevance as many airlines sought, and indeed may still be seeking, forbearance from their aircraft lessors during COVID-19 and its aftermath.

A recent New York decision

The facts of ***Frontier Airlines, Inc v AMCK Aviation Holdings Ir*** (decided 14 June 2024, 20 Civ 9713 (LLS)) may be briefly summarised. The lessor entered into a Framework Agreement with the airline in March 2020 (ie, soon after COVID-19 broker out), whereby the lessor committed to purchase from the airline six aircraft on the airline's orderbook with Airbus and then lease them back to the airline. (Such sale and leaseback (SLB) arrangement is one common way to finance aircraft deliveries.) Airbus was scheduled to deliver the first three aircraft in March 2020.

On the same day the Framework Agreement was entered into, the airline requested a short-term deferral of the rents of 15 aircraft previously leased from the lessor and a temporary return of the security deposits of those aircraft. In response, the lessor requested a deferral of the delivery of the first aircraft under the Framework Agreement, perhaps because the lessor hesitated to incur further investment when the airline was falling behind on rental payment. That would however require Airbus' consent to defer the delivery. Understanding that the airline needed time to persuade Airbus, the lessor's CEO agreed over the phone to defer rental payments on a month-to-month basis while the lessor and the airline were negotiating a formal rent deferral agreement.

Two months passed but the negotiation bore no fruit. The lessor gave notice to terminate the Framework Agreement by reason of a cross default of the non-payment of rents. Within the next three business days, the airline paid all outstanding rents, but the lessor nonetheless terminated the Framework Agreement and did not consummate the SLB arrangements for the remaining aircraft. The airline sourced alternative financing urgently on worse-off commercial terms. The airline sued for breach of the Framework Agreement.

Although the Framework Agreement contained the NOM clause mentioned above, the New York court found in the airline's favour on the ground that the lessor was bound by the oral waiver and did not give reasonable notice to the airline before retracting that waiver. (Impliedly, had the airline not paid up quickly, or had the lessor demanded the airline to pay up by a reasonably deadline, the decision might have been different.)

Whilst not cited in the New York judgement, the decision is in line with the well-known passage of

Cardozo J in a New York Court of Appeals judgment:

> "Those who make a contract, may unmake it. The clause which forbids a change, may be changed like any other. The prohibition of oral waiver, may itself be waived. 'Every such agreement is ended by the new one which contradicts it'… Whenever two men contract, no limitation self-imposed can destroy their power to contract again…" (***Beatty v Guggenheim Exploration Co*** (1919) 225 NY, 380, 387-388)

Such is the paradox presented by a NOM clause: are the parties free to restrict their freedom to agree otherwise? English law appears to diverge from New York law on this.

The English law position

The seminal English authority is the Supreme Court's decision in *MWB Business Exchange Centres Ltd v Rock Advertising Ltd* [2019] AC 119. In that case, the respondent occupied office space managed by the appellant. The respondent fell behind on its rent payments. It proposed a revised payment plan that involved deferring some payments to a later date. The credit controller of the appellant (whom the trial judge found to have ostensible authority to represent the appellant) agreed to this revised schedule during a telephone conversation. However, the original contract included a NOM clause. Despite the oral agreement, the appellant locked the respondent out of the premises for non-payment and sued for the arrears. The respondent counterclaimed for wrongful exclusion from the premises, arguing that the oral agreement to vary the payment schedule was binding.

The majority of the law lords disagreed with the respondent and allowed the appeal – the NOM clause was legally effective, and parties to a contract can bind themselves to a requirement that any variation must be in writing. Lord Sumption, delivering the majority view, observed:

> "Party autonomy operates up to the point when the contract was made, but thereafter only to the extent that the contract allows… The real offence against party autonomy is the suggestion that they cannot bind themselves as to the form of any variation, even if that is what they have agreed." (at 127)

He continues,

> "There are at least three reasons for including [NOM] clauses. The first is that it prevents attempts to undermine written agreements by informal means, a possibility which is open to abuse, for example in raising defences to summary judgment. Secondly, in circumstances where oral discussions can easily give rise to misunderstanding and crossed purposes, it avoids disputes not just about whether a variation was intended but also about its exact terms. Thirdly, a measure of formality in recording variations makes it easier for corporations to police internal rules restricting the authority to agree them. These are all legitimate commercial reasons for agreeing a [NOM clause]." (at 127-128)

Reconcilable?

Perhaps the apparent difference between New York law and English law here can be resolved to an extent by the common law principle of promissory estoppel: if one party to a contract promises the other that they will not enforce their full legal rights, and the other party relies on that promise, acts upon it and changed their position to their detriment, the party who made the promise is "estopped" from going back on it if it would be inequitable to do so, even though the promise is not supported by consideration (or, if you will, "money or money's worth"), which is normally required for a contract to be binding.

In *Frontier Airlines,* the word "estoppel" was not mentioned in the New York judgement although the principle was recognised under New York law so far as this author is aware. However, the presiding judge (Louis L Stanton, USDJ) put a lot of weight on the fact that, on the faith that the lessor had granted a month-to-month rental deferral, the airline exposed itself to great financial risks by negotiating with Airbus for the deferral of the next aircraft delivery. Indeed, the learned judge considered such detriment to constitute "consideration" paid by the airline:

> "That waiver was supported by consideration, as Frontier made a substantial sacrifice to achieve deferral with Airbus. It risked default on its single largest contract, which could have exposed the company to Chapter 11 bankruptcy proceedings and resulted in the loss of $250 million in PDPs [ie, predelivery payments that the airline paid towards the manufacture of 150 aircraft] … With each aircraft deferral, Frontier also lost repayment of $15 million [of PDP from Airbus], at a time when it was desperate for liquidity… In turn, AMCK received the benefit of delaying its payment of $51 million per aircraft [under the Framework Agreement] …" (20 Civ 9713 (LLS), p 21)

In *Rock Advertising,* Lord Sumption was likewise clear that an NOM clause is subject to the caveat of estoppel:

> "The enforcement of No Moral Modification clauses carries with it the risk that a party may act on the contract as varied, for example by performing it, and then find itself unable to enforce it. It will be recalled that both the Vienna Convention and the UNIDROIT model code qualify the principle that effect is given to No Oral Modification clauses, by stating that a party may be precluded by his conduct from relying on such a provision to the extent that the other party has relied (or reasonably relied) on that conduct. In some legal systems this result would follow from the concepts of contractual good faith or abuse of rights. In England, the safeguard against injustice lies in the various doctrines of estoppel." ([2019] AC 119, at 130)

No such estoppel existed in *Rock Advertising* though as the respondent merely offered a deferred payment plan on what they originally contacted to pay. In Lord Sumption's words,

"… the minimal steps taken by Rock Advertising were not enough to support any estoppel defences… the scope of estoppel cannot be so broad as to destroy the whole advantage of certainty for which the parties stipulated when they agreed upon terms including the No Oral Modification clause. At the very least, (i) there would have to be some words or conduct unequivocally representing that the variation was valid notwithstanding its informality; and (ii) something more would be required for this purpose than the informal promise itself…" (at 130-131)

Takeaway

What can we learn from the above decided cases? Whilst parties to an English law governed contract may take comfort from the fact that English court would be slow to infer that a subsequent oral agreement has overridden an NOM clause, it must not be taken for granted because of the possibility of an estoppel argument. Although it is hypothetical, this author would not be surprised should an English court come to the same conclusion as the New York court did, had the facts of *Frontier Airlines* happened in an English law setting. Much time, energy and legal fees would have been saved had the parties in *Frontier Airlines* reduced their telephone conversation into writing, even in a follow-up email if not a letter agreement. There are multiple ways to express it, but the lessor could have, for example, clarified in writing that the month-to-month rent deferral would end automatically if the parties do not agree upon a formal deferral agreement by a specified date for any reason, whereupon all outstanding amounts must be paid immediately, etc.

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