A CONTRACTUAL TERM SOLID AS A ROCK

In a review of a recent judgment of the United Kingdom Supreme Court, which overturned longstanding precedent on No Oral Modification clauses, partner **Ben Hobden** and associate **Spencer Vickers** of **Conyers Dill & Pearman** in the Cayman Islands find the decision will provide welcome certainty on contracts

NON-LAWYERS may be surprised to know that the omnipotence paradox is a commonly considered topic by law students. The paradox is expressed in the question: "Can an omnipotent being create a rock so heavy it could not lift it?" In law school, the question instead is: "Can two parties agree a term so enduring that they could not subsequently agree to deviate from that term?"

The United Kingdom's Supreme Court judgment of 16 May 2018, which will be of guidance to Cayman Islands courts, in the aptly named *Rock Advertising v MWB Business Exchange Centres* provides an answer to the question. The court was asked to consider whether a written contract which required modifications to be made in writing and signed by the parties was effective (referred to as the 'No Oral Modification' clause (NOM clause) in the judgment). A five-justice panel comprising **Lady Hale** as president, alongside **Lords Wilson**, **Sumption**, **Lloyd-Jones** and **Briggs**, sitting in the Supreme Court, upheld the effectiveness of NOM clauses, answering the paradox with a resounding and unanimous 'yes'.

As a result, parties varying their contractual arrangements should be careful to ensure that any subsequent agreement/variation meets any requirements of formality which were previously agreed. A failure to comply with an earlier agreed protocol in relation to variations may prevent a party from relying on the varied terms.

Common law

The Supreme Court's decision overturns a long line of jurisprudence which held that parties could orally vary a contract, even if that contract contained a NOM clause.

The earlier case law was based upon the fundamental principle of law that parties are free to contract with each other as they so choose, whether in writing or orally (subject to any requirements of formality required in special circumstances, for example in relation to land).

Before the Supreme Court's decision, NOM clauses have been treated by the courts as ineffective for the following reasons:

- a variation of an existing contract is itself a new contract;
- the common law imposes no requirements of form on the making of contracts. Accordingly parties may agree informally to dispense with an existing clause that makes requirements as to form; and
- if parties agree to a variation of an existing agreement informally, they must impliedly also be taken to have agreed to vary or waive the NOM clause (or other formality clause) in the original agreement.

This principle was well articulated in the 1919 judgment of Justice Cardozo in *Beatty v Guggenheim Exploration Co*, who said:

"Those who make a contract, may unmake it. The clause which forbids a change, may be changed like any other."

Rock Advertising v MWB Business Exchange Centres

Rock Advertising (Rock) entered into a written license agreement with **MWB Business Exchange Centres** (MWB) under which Rock received a license to occupy office space for a term of 12 months. The license agreement included a NOM clause.

Rock failed to pay the license fees to MWB as required, and approximately six months into the term had accumulated arrears of more than GBP 12,000. During telephone discussions, Rock and MWB agreed to a payment plan in relation to these arrears which allowed Rock to continue to occupy the office space and pay off the arrears at a lesser rate that was acceptable to Rock (oral agreement). Notwithstanding the oral agreement, a month later MWB terminated the license for failing to pay the full amount of the arrears and sued Rock for the arrears. Rock counterclaimed in damages for wrongful exclusion from the premises. The fate of the dispute turned on whether the NOM clause or the oral agreement was effective.

At first instance **Judge Moloney QC** in the Central London County Court decided in favour of MWB as the judge found that the oral agreement was ineffective due to the NOM clause.

In 2016, **Lady Justice Arden**, **Lord Justice Kitchin** and **Lord Justice McCombe**, sitting in the English Court of Appeal, overturned the decision and found that the oral agreement also amounted to an agreement to dispense with the NOM clause. The Court of Appeal then considered whether there was consideration between the parties under the oral agreement, finding that, although MWB would receive less under the oral agreement, there was an increased chance of payment and an increased likelihood that the property would not be left vacant for an extended period of time. The Court of Appeal found this was a practical benefit to MWB and was therefore sufficient as valid consideration.

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- UK Supreme Court

Accordingly, it considered that MWB was bound by the oral agreement and was not entitled to terminate the license when it did.

The United Kingdom Supreme Court was asked to consider two issues in relation to the effectiveness of the NOM clause:

- First, was the oral agreement valid?
- Second, was there valid consideration between the parties under the oral agreement?

In relation to the first issue, the Supreme Court found that the oral agreement was invalid as it was not made in writing as required by the NOM clause, stating that:

"What the parties to such a clause have agreed is not that oral variations are forbidden, but that they will be invalid. The mere fact of agreeing to an oral variation is not therefore a contravention of the [NOM] clause. It is simply the situation to which the clause applies."

In light of the court's decision on the first issue, it declined to rule on the second issue as to whether there was in fact valid consideration between the parties.

Conclusion

NOM clauses are intended to provide parties with certainty of their contractual terms. They guard against attempts to undermine written agreements by informal means and assist parties to avoid disputes about whether an oral variation has occurred and/or its exact terms. The clauses are particularly important for long-running contracts and large businesses where any agreed oral variations may be lost over the passage of time or simply with changes of personnel.

Given the common use of NOM clauses in commercial agreements, the Supreme Court's decision will be welcomed by the business community as it upholds the certainty of contracts. The judgment is also a reminder to businesses to ensure that any prior agreed contractual formalities are met when agreeing variations.

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