

Can contracts be orally modified?

STUART JORDAN* discusses the topic of verbal modifications to a contract and whether 'no oral modification' clauses are effective or can be amended.

MOST commercial contracts include a standard provision in terms that any amendment to the contract must be made in writing, and that any waiver of entitlement or disapplication of an obligation must be recorded formally and signed by authorised representatives – or it will not be valid.

This is a "no oral modification" provision and the reasoning behind it is particularly applicable to construction contracts. These contracts are not agreed and then put away in the drawer: in most projects, the contract terms are discussed every day, to reference correct and incorrect performance, to raise issues such as difficulties (or impossibility) in achieving strict performance, and to propose solutions. These are usually productive discussions but they introduce the danger (to both parties) of inadvertent change to the contract.

So, parties naturally want to make sure that doing B instead of doing A (as the contract required) is a good idea and that all consequences have been thought through, before that change is made binding, through a written contract amendment, signed by people authorised to make such changes.

But this raises an interesting logical question: can parties prohibit themselves from making an oral (or other informal) change to their contract, if they later decide to agree to such a change? The two opposing viewpoints on this question are both based on the principle of "freedom of contract".

One side says no: parties are free to agree anything they want to; and that includes agreeing to limit the way in which they will make later changes to their contract.

The other side says yes: parties are free to agree whatever they want, and in any manner that counts in law as an agreement. That includes amendments to their own

earlier contract. And if their amendment is made orally, then they have implicitly also amended the 'no oral modification' clause.

Courts internationally have struggled with this question; and it is important, for commercial certainty, that parties to construction contracts know whether these 'no oral modification' clauses will be effective.

A recent court decision on this comes from Singapore:

Charles Lim Teng Siang v Hong Choon Hau. Not a construction contract – this was a sale and purchase agreement for shares in a company, requiring completion by October 17, 2014. It included the following clause:

"[no] variation, supplement, deletion or replacement of or from this Agreement or any of its terms shall be effective unless made in writing and signed by or on behalf of each Party."

Additionally, the agreement provided that time was of the essence and that any delay by a party in exercising a right would not constitute a waiver of that right.

The sale didn't go through and the sellers eventually (after a four-year delay) brought an action against the buyers for damages arising from their failure to complete. Among the arguments raised in defence to that claim, the buyers said that the deal had been rescinded by mutual agreement in a phone call – and that the above 'no oral modification' clause did not apply to that later rescission.

This ended up in the Singapore Court of Appeal, which agreed with the buyers. They said that the clause applied only to a "variation, supplement, deletion or replacement of or from" the contract, which

did not cover rescission of it. I have to say that I'm not immediately seeing how an agreed rescission is not a variation or a "deletion..of" the contract although the wording of the clause is unusual.

Since the court's finding was based on the clause not covering the action of rescission, they didn't need to answer the above question of principle, but they did make some remarks "obiter" (that is, not material to the court's decision on the dispute) about that question:

They said that a 'no oral modification' clause does not prohibit a later oral modification but acts as a rebuttable presumption against oral modifications. In other words, the clause is effective unless and until the parties have shown by their words or actions, that they are amending it. In practice, that means showing clear evidence that the parties noted the prohibition on oral amendments, and agreed to change it. The conversation might be:

"Shall we do B instead of A?"

"Yes but you know we agreed no oral modifications?"

"Yes we did. Let's delete that too."

"OK."

We can all see the practical difficulty in providing evidence of this exchange but that doesn't change the principle.

This is different from the current English law approach, which is that parties are bound by such clauses and they cannot be disapplied orally, either by rebutting the presumption as above or by implication, simply because the parties have purported to change the contract orally.

Parties under English law contracts might, therefore, feel safer from the danger of inadvertent amendment, but they should continue to keep strong processes to manage communications in: Variations; non-conformance reports; requests for deviations; and notices. ■

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Jordan ... "no oral modification" provision is applicable to construction contracts.