

AIRCRAFT LEASING CONTRACTS IN THE PANDEMIC
ERA: NAVIGATING THE CHALLENGES OF
INVOKING *FORCE MAJEURE* BY APPLYING
HARDSHIP UNDER INTERNATIONAL COMMERCIAL
LAW

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Most aircrafts are acquired through leasing agreements where the financial burden is placed on the lessor through financing of heavy equipment in favor of the lessee. To ensure that lessees fulfil their obligation of payment, the leases often include “Hell or High-water” clauses that ensure payment by the lessee irrespective of any circumstantial change that might make it difficult for the lessee to pay. However, due to the pandemic, the airline industry is currently suffering from a severe cash crunch, and as a result, it is difficult for airline companies to honor their upcoming contractual obligations. In response, airline companies are considering invoking force majeure in these contracts to avoid liability for non-performance. However, considering the nature of such contracts and the legal principles adopted in Private International Air Law, taking such measures might pose several challenges. Therefore, this paper proposes the application of Hardship, codified in the UNIDROIT Principle of International Commercial Contracts, so that airlines can renegotiate their contracts with lessors and avoid liability for delayed or non-performance of their obligations, instead of completely avoiding their contractual obligation through the invocation of force majeure. Such action will provide breathing space for lessees while ensuring that their obligations towards lessors are maintained during the pandemic, thereby ensuring that lessors are financially safeguarded.

I. INTRODUCTION

The UNIDROIT Convention on the International Interests in Mobile Equipment (Cape Town Convention), along with its protocol on matters of Aircraft equipment, became effective in 2006, indicating significant development for the Airline Industry.¹ These treaties have

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led to the creation of an international legal standard for transactions involving aircraft equipment, substantially contributing to increased global connection through the model known as “one flight away.” However, the outbreak of COVID-19 has severely affected the operations of this industry.² Global lockdowns and international border controls have hampered the financial position of airline companies, thereby forcing them to reassess their obligations towards leasing contracts. Most commercial contracts provide a provision of *force majeure* remedy, which allows parties to excuse their liability for non-performance during an unforeseeable event that is beyond their control. However, the majority of Airlines acquire their aircrafts through leases that do not excuse payment based on absolute obligations under the “Hell or High-water” clause.³ Therefore, irrespective of any event, airline operators must fulfil their obligations by both paying for and taking delivery of the agreed aircrafts. However, due to the pandemic, airlines are in a state of quandary regarding their position as to the fulfillment of these absolute obligations. Are airlines still bound to fulfil these obligations when mere survival has become a financial battle?

This paper is an attempt to understand the impact of COVID-19 on the contractual obligation of aircraft operators. This paper begins by providing insight into the nature and regulation of aircraft lease contracts under international law as well as the rationale for such obligations contained within aircraft lease agreements. This paper then seeks to study whether *force majeure*, as interpreted under national and international jurisdiction, holds valid under these contracts. This paper is limited to aircraft leases, as the acquisition of aircrafts through other means may provide different remedies not discussed in this paper. The author has attempted to propose applying the *rebus sic stantibus* principle of Hardship, as provided under UNIDROIT’s International commercial law on aircraft acquisition contracts. This principle may provide temporary relief to airline operators while also striking a proper balance

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1. Convention on International Interests in Mobile Equipment, Nov. 16, 2001, 2307 U.N.T.S. 285 [hereinafter *Cape Town Convention*]; Protocol to the Convention on International Interests in Mobile Equipment on Matters Specific to Aircraft Equipment, Nov. 16, 2001, 2367 U.N.T.S. 517, [hereinafter *Aircraft Protocol to Cape Town Convention*].

2. Sakkakom Maneenop & Suntichai Kotcharin, *The Impacts of COVID-19 on the Global Airline Industry: An Event Study Approach*, 89 J. AIR. TRANSP. MANAG. 1, 1 (2020).

3. *Regional: COVID-19 as Force Majeure in Aviation Contracts. Comparative Analysis Across 10 Jurisdictions*, KINTELLAR (Mar. 26, 2020), <https://www.kintellar.com/insights/detail/1059/regional-covid-19-as-force-majeure-in-aviation-contracts-comparative-analysis-across-10-jurisdictions>.

between both contractual parties, allowing airline operations to re-negotiate and adjust their lease agreements.

II. GENERAL NATURE OF AIRCRAFT ACQUISITION CONTRACT

There has been exponential growth in the commercial aviation industry in recent years, which has required airlines to acquire more aircrafts through leasing contracts.⁴ Instead of leasing, airlines may also purchase aircrafts through their own, or another available credit resource. However, purchasing aircrafts is a capital-intensive task, and because the aviation business is constantly fluctuating, most airlines are inclined to lease aircrafts.⁵ Leasing provides airlines with several economic advantages, including the ability to grow and remain flexible.⁶ Therefore, in recent years, the majority of airlines choose to operate aircrafts through leasing contracts.⁷ The main spirit of a lease is the right to possess and use the leased asset in exchange for consideration. The Cape Town Convention defines a lease as “an agreement by which one person (the lessor) grants a right to possession or control of an object (with or without an option to purchase) to another person (the lessee) in return for a rental or other payment.”⁸

The International Accounting Standards Board has classified leases into finance and operating leases.⁹ The main difference between the two is that the former transfers the substantial risk and reward on the lessee by awarding them ownership of the leased aircraft once the lease is paid.¹⁰ In the case of the latter, no such transfer takes place and the lessee has the option to return the aircraft to the lessor.¹¹ Different kinds of lease contracts are generally tailor-made and designed on the

4. See Eva Endrizalova et al., *Operating Lease as a Specific Form of Airlines Outsourcing*, INTERNATIONAL SCIENTIFIC CONFERENCE BUSINESS LOGISTICS IN MODERN MANAGEMENT 641, 642-43 (Oct.12, 2018) (discussing the “growth in demand for air travel” and the purpose of acquiring aircrafts through leases, providing several advantages including several funding arrangements that create different kinds of ownership obligations).

5. Hortencia Jimenez, *Commercial Aircraft Leasing and its Booming Complexities* (May 2017) (unpublished MSc. Aviation Administration thesis, Middle Tennessee State University) (on file with Middle Tennessee State University), at 5-7.

6. LEASE EUROPE & ARTHUR ANDERSONS, *LEASING IN EUROPE* 53-54 (McGraw Hill Book Company 1992).

7. Jimenez, *supra* note 5, at 5.

8. *Cape Town Convention*, *supra* note 1, at art. 1(q).

9. IAS Plus, *IAS 17- Leases*, DELOITTE, <https://www.iasplus.com/en/standards/ias/ias17> (last visited Apr. 7, 2021).

10. *Id.*

11. *Id.*

basis of a model lease pattern that accommodates the interest of the parties.¹²

However, the nature of absolute contractual obligations under these contracts, specifically regarding performance, mostly remains the same irrespective of the type of the lease, thereby creating no significant difference in the nature of lessor-lessee relationship. Private International Air Law has attempted to harmonize a standard legal regime that can act as an authority to determine the nature of these contracts and guide the global aviation industry, which conducts business across borders.¹³

A. *Regulations Under Private International Air Law*

The Cape Town Convention and its aircraft protocol,¹⁴ along with the UNIDROIT Convention on International Financial Leasing,¹⁵ lay down a system of regulations that provide a standard of rules ranging from governing law of the contract to the nature of responsibility and obligations for the lessor and the lessee.

i. *Governing Law*

The governing law of aircraft acquisitions variegates across different contracts because each contract is drafted in a bespoke manner in order to accommodate the different interests of parties from different jurisdictions.¹⁶ Typically, these contracts are governed by either English common law or New York law, because both legal regimes are comprehensive with abundantly available precedents, which reduces

12. Donal Patrick Hanley, *Aircraft Operating Leasing: A Legal and Practical Analysis in the Context of Public and Private International Air Law* (2011) (unpublished Doctoral Thesis, Leiden University) (on file with Leiden University), at 8.

13. Donal Hanley, *Covid-19 and International Aircraft Financing Law*, 45 AIR & SPACE L. SPECIAL ISSUE 155, 156 (2020).

14. Jeffrey Wool, *The Next Generation of International Aviation Finance Law: An Overview of the Proposed UNIDROIT Convention on International Interests in Mobile Equipment as Applied to Aircraft Equipment*, 20 U. PA. J. INT'L ECON. L. 499, 499-500 (1999) (discussing the foremost international treaty in facilitating flexible aircraft acquisition for airlines either by purchase or lease agreements).

15. UNIDROIT Convention on International Financial Leasing, Ottawa, May 28, 1988 [hereinafter *Financial Leasing Convention*] The objective of this international covenant is to provide a framework of unified guidelines to regulate lessor and lessee responsibility in cross border leasing agreements.

16. Roy Goode, Commentary, *Convention on International Interests in Mobile Equipment and Protocol thereto on Matters Specific to Aircraft Equipment: Official Commentary*, UNIDROIT 175-180 (2002).

uncertainty regarding each parties' position and contractual obligations.¹⁷

The Aircraft Protocol to the Cape Town Convention allows the parties that have ratified, accepted, and acceded to the Protocol to choose any governing law of their preference, ranging from *lex situs* to *lex loci contractus*, to regulate the relationship of the parties in the contract.¹⁸ To avoid *renvoi*, the parties can also choose International Contract Law, which may include UNIDROIT Principles of International Commercial Contracts.¹⁹ In addition, it is imperative to note that as per the Cape Town Convention standards, there is also an option to settle an issue in conformity with the General Principles of Laws in the absence of specific governing law.²⁰ This ensures that, under these Conventions, the parties have the freedom to choose any governing law regulating their contractual relationship which may range from domestic law to International Law of Contract.

ii. Default and Remedies

The Cape Town Convention and the Convention of International Financial leasing provide several remedies in cases of default that interact with existing domestic remedies available under the governing law selected by the parties in the agreement.²¹ The remedies available to the lessor against the lessee in cases of default under the Cape Town Convention and the Aircraft Protocol include repossession of the aircraft by physical transfer of the aircraft and remarketing it either by selling or leasing, recovering, or collecting any profit from the lessee from the use of the aircraft object.²² The Convention on Financial Leasing further ensures that the lessor has the power to recover unpaid rents, interest, and damages from the lessee in cases of non-performance of lease payment.²³ The remedies available to the lessor against the lessee under these Conventions and treaties ensure the financial

17. DONALD H. BUNKER, INTERNATIONAL AIRCRAFT FINANCING 173–74 (International Air Transport Association, 2d ed.2015).

18. *Aircraft Protocol to Cape Town Convention*, *supra* note 1, at art. 8.

19. Hanley, *supra* note 12, at 181-82.

20. *Cape Town Convention*, *supra* note 1, at art. 5(2).

21. These remedies clarify the parties' position, which coexists once the treaties have been ratified by the state of the parties involved in the Aircraft acquisition contract. *Cape Town Convention*, *supra* note 1, at art. 11

22. *Cape Town Convention*, *supra* note 1, at art. 8; *Aircraft Protocol to Cape Town Convention*, *supra* note 1, at art. 9.

23. *Financial Leasing Convention*, *supra* note 15, at art. 13(1).

security of the creditor (i.e. the lessor) by making payment from the lessee obligatory for any default.²⁴

B. *Standard Contract Clauses in Aircraft Lease Agreements*

Acquisitions of aircrafts by airlines under leasing agreements typically involve three parties, irrespective of the nature of the lease: a lessor, a lessee, and a supplier. The lessee enters into a supply agreement with the supplier to select the equipment that the lessor pays in the supply agreement. After that, the lessee, in exchange for the payment made by the lessor to the supplier for the equipment, enters into a lease agreement to pay off their lease in a rental arrangement, thereby enjoying the right to use the equipment.²⁵ Due to this peculiar nature of the Aircraft leasing agreement, there are certain standard clauses contained within the agreements, such as the “Hell or High-water” clause. The purpose of incorporating such a clause is to impose an absolute obligation on the lessee, irrespective of the circumstance, to pay the rent or lease to the lessor.²⁶

The purpose of these absolute contractual obligations, along with remedies for default available under international law, are to ensure protection of the lessor against failure of performance by the lessee. The lessee, under aircraft finance lease agreements and even in cases of default, has to pay the lease and is liable regardless of any problem the lessee is suffering from. Because the COVID-19 pandemic has caused complete disruption of the business activities of airlines currently leasing aircrafts,²⁷ it is pertinent to evaluate the necessary legal remedy available for airline lessees to help them circumvent “Hell or High-water” clauses and therefore, momentarily overcome lease payments, while simultaneously ensuring that airlines avoid damages for default.

24. Wool, *supra* note 14, at 524.

25. *Financial Leasing Convention*, *supra* note 15, at art. 1 & art. 2.

26. See Hanley, *supra* note 12, at 63-4 (explaining how the duty to pay the lease becomes unconditional for the lessee. It does not consider any unforeseen circumstance that might affect the airline’s ability to pay the lease. This contract clause gives an upper edge to the lessor over the lessee and obligates the lessee to honor his payment obligations. The necessity to bind the lessee with an obligation to pay is there to ensure liquidity for the lessor to repay the debt to the supplier for the aircraft that is being financed).

27. OECD Policy Response to Coronavirus (Covid-19), *Covid-19 and the Aviation Industry: Impact and Policy Responses*, OECD (Oct. 15, 2020), <https://www.oecd.org/coronavirus/policy-responses/covid-19-and-the-aviation-industry-impact-and-policy-responses-26d521c1/>.

III. IMPACT OF CORONAVIRUS ON THE AIRLINE INDUSTRY

As a result of harsh measures adopted across the globe to stop the progression of the Coronavirus, the world economy has been severely affected.²⁸ For example, after the World Health Organization declared the pandemic on March 11, 2021, the immediate response around the world was to close borders and restrict travel.²⁹ The aviation industry has come to a near halt, reporting a 73.7 percent drop in global air traffic in April 2020, compared to the previous year.³⁰ Airlines have suffered huge losses due to the reduction in passenger movement, which is estimated to have fallen by eighty-nine percent globally in the second quarter of 2020.³¹

Restriction on air travel, combined with flight cancellations and reduction in passenger movement, has forced airlines to ground their fleets, significantly affecting their liquidity. For example, Lufthansa, one of biggest European airline carriers, is expected to lose 500 million euro each month, thereby forcing the airline to reduce its fleet from 760 aircrafts to 610 aircrafts.³² This is not an isolated incident, as the International Airline Group reported a loss of 1,365 million euro in the second quarter of 2020.³³ Despite these losses, airlines still have additional costs and various other unavoidable fixed charges related to maintaining the aircraft's airworthiness. These expenses add a significant revenue burden on the airlines as they have to continue to pay

28. Gita Gopinath, *The Great Lockdown: Worst Economic Downturn Since the Great Depression*, IMF BLOG (Apr. 14, 2020), <https://blogs.imf.org/2020/04/14/the-great-lockdown-worst-economic-downturn-since-the-great-depression/>.

29. World Health Organization, *Director-General's opening remarks at the media briefing on COVID-19*, WHO (Mar. 11, 2020), www.who.int/director-general/speeches/detail/who-director-general-s-opening-remarks-at-the-media-briefing-on-covid-19-11-march-2020; Rahman MK, Gazi MAI, Bhuiyan MA and Rahaman M, *Effect of Covid-19 pandemic on tourist travel risk and management perceptions*, 16(9) PLOS ONE 1, 2-3 (2021), <https://doi.org/10.1371/journal.pone.0256486>.

30. Ian Petchenik, *Scrapping along the Bottom: April Air Traffic Statistics*, FLIGHTRADAR24 (May 1, 2020), <https://www.flightradar24.com/blog/scrapping-along-the-bottom-april-air-traffic-statistics/>.

31. IATA Economics, *Airline Financial Monitor*, IATA (Sept. 18, 2020), www.iata.org/en/iata-repository/publications/economic-reports/airlines-financial-monitor-august-2020.

32. *Pandemic Bill Heavier in Lufthansa*, DW (Sept. 21, 2020), www.dw.com/tr/lufthansada-pandemi-faturas%C4%B1-a%C4%9F%C4%B1rla%C5%9Ft%C4%B1/a-55006511.

33. Serap Zuvun & Onur Can Ucarer, *The Aircraft Financing Market after COVID-19*, INT'L B. ASS'N (2020), www.ibanet.org/article/2cb405cf-621a-4791-809f-748f09b0402d.

aircraft engineers, airline crew, and airport parking charges in order to satisfy the requirements of the Aircraft Approved Maintenance programme.³⁴ Airlines have started to mitigate this cash burn through various measures including reductions in aircraft crew and salary. For instance, British Airlines laid off around 12,000 employees in order to cut expenses during the pandemic.³⁵ It is estimated that in the second half of 2020, airline companies will burn through \$77 billion in cash.³⁶ Several other airlines have also decided to reduce their fleets and delay both lease payments and aircraft deliveries.³⁷

While it is clear that the pandemic has caused strenuous financial difficulty for airline companies, taking measures such as delaying lease payments may negatively impact the relationship between airlines and their lessors, because of the various absolute contractual obligations contained in the leasing agreements. Therefore, it is important to reevaluate these contractual obligations in light of the damage caused by the pandemic, in order to maintain the lessor/lessee relationship and ensure survival of the entire aviation industry until normal business operations resume.

IV. INVOKING *FORCE MAJEURE* IN AIRCRAFT LEASING CONTRACT

Due to financial losses suffered by the airline industry, airline industries are looking for a potential respite to survive and avoid liability for default on their leases. One such respite is the possibility of using *Force Majeure* to circumvent lease payments and therefore minimize the cash burden until pandemic related restrictions cease. However, because these lease agreements are enclosed with absolute obligations like the “Hell or High-water” clause, it is questionable whether airlines can invoke *Force Majeure* to excuse their performance. Furthermore, in an aircraft leasing agreement, the probability of a contract possessing a

34. Henry Kikoyo, *Liability Management for Airlines Following Complete Shut Down of Operations or Aircraft Groundings in the Wake of Coronavirus (COVID-19)*, BROWNRUDNICK (Mar. 26, 2020), <https://brownrudnick.com/alert/liability-management-for-airlines-following-complete-shut-down-of-operations-or-aircraft-groundings-in-the-wake-of-coronavirus-covid-19/>.

35. *How much did the Corona hit which airline company?*, DW (July 8, 2020), www.dw.com/tr/korona-hangi-havayolu-%C5%9Firketini-ne-kadar-vurdu/g-54488779.

36. IATA Economics, *Airline industry Will Continue to Burn Through Cash Until 2022*, IATA, (Oct. 9, 2020), <https://www.iata.org/en/iata-repository/publications/economic-reports/airline-industry-will-continue-to-burn-through-cash-until-2022>.

37. *Airlines Financial Reporting Implications of Covid-19*, KPMG (Apr. 2020), <https://assets.kpmg/content/dam/kpmg/xx/pdf/2020/04/airlines-financial-reporting-implications-of-covid-19.pdf>.

force majeure clause is very low.³⁸ However, if the clause is present, its scope of application must be explicitly interpreted to include a pandemic, which may prove difficult based on prior interpretations finding that pandemics are not *Force Majeure* events in the context of the aviation industry.³⁹

A. *The Principle of Force Majeure Under International Commercial Law*

The *force majeure* principle is incorporated under different international treaties guiding commercial contracts, including the United Nations Convention on Contracts for the International Sale of Goods (CISG) and the UNIDROIT Principle of International Commercial Contract (UPICC).⁴⁰ Because the CISG Convention does not generally apply to the sale of aircraft contracts,⁴¹ the best way to understand the principle of *force majeure* is to analyze its scope under UPICC and various other domestic law systems.

The literal translation of the word *force majeure* is “superior force.”⁴² According to article 7.1.7 of UPICC, the relief provided under *force majeure* excuses a party from performing contractual obligations after the occurrence of a certain unforeseeable event that is beyond the control of the parties.⁴³ The rationale behind this remedy is that such unforeseen events make it impossible for the parties to uphold the contract temporarily or permanently.⁴⁴ It also includes events that might occur after contract formation, such as floods, droughts, earthquakes, and acts of terrorism.⁴⁵ The ultimate consequence of such a remedy is the removal of liability for damages from non-performance, as well as

38. Gates Aviation Ltd., *Covid-19 Impact on Aviation Contract*, LEXOLOGY (Feb. 18, 2021), <https://www.lexology.com/library/detail.aspx?g=559fe59f-c1ef-4a92-b09e-fbc11c0e3b06>.

39. Leo Fattorini et al., *Covid-19: Where to Next for Airlines and Their Investors?*, BIRD & BIRD (Mar. 2020), <https://www.twobirds.com/en/news/articles/2020/global/covid19-where-to-next-for-airlines-and-their-investors>.

40. International Institute for the Unification of Private Law (UNIDROIT 2016) Principles of International Commercial Contracts [hereinafter *UPICC*]; United Nations Convention on Contracts for the International Sale of Goods, Apr. 11, 1980, 1489 *U.N.T.S.* 3, 19 *I.L.M.* 668 [hereinafter *CISG*].

41. John P. McMahon, *Applying for Managers and Counsel: Applying the CISG*, IICL, (May 2010), <https://iicl.law.pace.edu/cisg/page/guide-managers-and-counsel-applying-cisg>.

42. Klaus Peter Berger & Daniel Behn, *Force Majeure and Hardship in the Age of Corona: A Historical and Comparative Study*, 6 *MCGILL J. DISP. RESOL.* 77, 90 (2019-2020).

43. *UPICC*, *supra* note 40, at art. 7.1.7.

44. Berger & Behn, *supra* note 42, at 90.

45. *Principle No. V.I.3- Force Majeure*, TRANS-LEX, <https://www.trans-lex.org/944000>, (last visited Apr. 20, 2021).

the prevention of such performance.⁴⁶ Therefore, *force majeure* also affects the right of the other party to enforce its obligatory advantage, which may be monetary or not, depending on the terms of the contract.

Under English common law, this doctrine is not governed by any express legislation and instead, its application depends on the inclusion of the *force majeure* clause by the parties in a commercial contract.⁴⁷ Such clause must be construed restrictively and contain a list of unforeseen events that arise without the interference of the parties, which will qualify as the *force majeure* event and allow the party to invoke relief.⁴⁸ While the application of *force majeure* in civil law jurisdictions is similar to that of common law systems, the contractual provisions in civil law systems must describe the exact conditions required for an event to be qualified as *force majeure*.⁴⁹

B. *Pandemic as a Force Majeure Event*

While the scope of a *force majeure* remedy depends on the unforeseeable event, the guidelines provided under international law, and the practice prevalent in common and civil law systems, there is no particular condition that may explicitly qualify a pandemic as a *force majeure* event.⁵⁰ The common practice adopted by courts is to interpret it strictly and literally. For example, in 2005, the China International Economic and Trade Arbitration Commission failed to consider the SARS outbreak a *force majeure* event, thereby not allowing the parties to excuse themselves for non-performance.⁵¹ The majority opinion appears to be that unless there is specific mention of the epidemic, disease, and quarantine in the *force majeure* clause, the pandemic will not be applicable.⁵²

Restrictive measures taken by nations, such as lockdowns, border closures, travel restrictions, and quarantines, in order to control the

46. UPICC, *supra* note 40, at art. 7.1.7.

47. *Force Majeure/ Hardship clauses and frustration in English Law contract amid Covid-19*, NORTON ROSE FULBRIGHT (Apr. 2020), <https://www.nortonrosefulbright.com/en/knowledge/publications/b54cf723/force-majeure-hardship-clauses-and-frustration-in-english-law-contracts-amid-covid-19#section3>.

48. *Great Elephant Corp. v. Trafigura Bebeer BV* [2013] EWCA Civ 907 [25].

49. International Chamber of Commerce, *ICC Force Majeure And Hardship Clauses 2020: Introductory Note and Commentary*, ICC (June 2020), <https://iccwbo.org/content/uploads/sites/3/2020/07/icc-forcemajeure-introductory-note.pdf>.

50. Berger and Behn, *supra* note 42, at 80.

51. *People Republic of China v. Netherlands* [2005] CIETAC (IICL, 2005) <<https://iicl.law.pace.edu/cisg/case/china-march-5-2005-translation-available>> accessed 20 April 2021.

52. Brian W. Ledebuhr, *COVID-19, “Force Majeure” Clauses and Contractual Nonperformance*, XI NAT'L. L. REV. (2021).

spread of COVID-19, has caused varying levels of economic disruptions to both international and domestic supply chains.⁵³ However, even if there is a shift in the financial stability of one of the contractual parties, courts are unlikely to accept invocation of a *force majeure* clause.⁵⁴ Under English common law, the Commercial Court has opined that it is not considered a *force majeure* event when changes in market circumstances affect a party's ability to fulfill its contractual obligations.⁵⁵ In determining whether a government measure is a *force majeure* event because it restricts a party's ability to fulfill its contractual obligations, the law requires careful assessment of both the exact reference in the contract, and the specific government measure that impacts fulfillment of contractual obligations.⁵⁶

However, to provide economic relief, various national governments have proposed issuing a certificate to consider the pandemic a *force majeure* occurrence, which may provide relief depending on the conditions included in such certificate. For example, the China Council for the Promotion of International Trade issued approximately 1600 such certificates.⁵⁷ Furthermore, Bulgaria, Kazakhstan, Slovakia, Turkey, Ukraine, and Uzbekistan have issued various legislative amendments and notifications.⁵⁸

C. *Legal Effects of the "Hell or High-water" Clause on the Force Majeure Remedy*

While the adoption of these certificates may constitute a symbolic identification of the COVID-19 pandemic as an unforeseeable *force majeure* event, the legal consequence of these certificates is still undecided, especially in international forums, contracts, and lease payments involving parties from multiple countries. It is an accepted principle of law that a contract must be read as a whole, and courts have applied

53. OECD Policy Responses to Coronavirus (COVID-19), *The territorial impact of COVID-19: Managing the Crisis across levels of government*, OECD (Nov. 10, 2020), <https://www.oecd.org/coronavirus/policy-responses/the-territorial-impact-of-covid-19-managing-the-crisis-across-levels-of-government-d3e314e1/>.

54. *Northern Indiana Public Service Co. v. Carbon County Coal Co.*, 799 F.2d 265, 275 (7th Cir. 1986).

55. *Tandrin Aviation v. Aero Toy Store* [2010] EWHC 40 (Comm).

56. *Force Majeure in Aviation Contract*, WINSTON & STRAWN LLP (Apr. 2020), <https://www.winston.com/en/thought-leadership/force-majeure-in-aviation-contracts.html>.

57. Elodie Fortin, *The Impact of Coronavirus (COVID-19) on Aviation Finance*, LEXISNEXIS (Mar. 30, 2020), [https://www.lexisnexis.co.uk/blog/covid-19/the-impact-of-coronavirus-\(covid-19\)-on-aviation-finance](https://www.lexisnexis.co.uk/blog/covid-19/the-impact-of-coronavirus-(covid-19)-on-aviation-finance).

58. KINSELLAR, *supra* note 3.

this principle when rejecting the *Force Majeure* remedy.⁵⁹ The rigidity of “Hell or High-water” clause is visible in the case *General Electric Capital Corp. v. FPL Services Corp.*, where despite the loss caused to equipment by Hurricane Sandy, the court upheld a contractual clause mandating lessee payments.⁶⁰ Applied to aircraft leasing agreements, the court in *ACG Acquisition XX LLC v. Olympic Airlines SA* determined that the “Hell or High-water” clause absolutely binds the lessee, even after the lessor failed to provide an aircraft in airworthy condition.⁶¹ These cases demonstrate that irrespective of the circumstance, the “Hell of High-water” clause bars lessees from invoking the *force majeure* remedy and forces the lessee to bear all risk in an agreement.

In the case of *Celestial Aviation Trading 71 Ltd. v. Paramount Airways Private Ltd.*, the English High court held that regardless of the defense available to the lessee, its obligation to pay the lessor may not be exempted.⁶² This demonstrates the prevalent judicial opinion, that the *Force Majeure* remedy is not a viable legal option for airline companies. While the restrictive measures taken by governments to fight the pandemic may appear to be an unforeseeable event that qualifies as a *force majeure* event, especially considering express contractual clauses or government issued certificates, the spirit of the “Hell or High-water” clause ensures payment to the lessor without any space for default by the lessee without liability for damages. Even though airlines have suffered massive financial losses due to the pandemic, it is likely that airlines still cannot invoke *force majeure* in any circumstance to excuse non-performance. However, because the purpose of such absolute obligation is to ensure protection of the lessor, the general principle of the Hardship Doctrine may be an alternative legal remedy that allows the lessee to re-negotiate the terms of the contract and delay payment, instead of totally terminating all payment obligations. This will ensure that the lessor is paid and the lessee may avoid damages and receive relief from the immediate financial burden of payment.

59. *Golsen v. ONG Western Inc.*, 756 P.2d 1209, 1210-14 (Okla. 1988) (rejecting the defendants *force majeure* defense because the contract contained an absolute obligation of a take-or-pay provision, which may not be overridden by *force majeure* remedy).

60. *General Electric Capital Corp. v. FPL Services Corp.*, 986 F. Supp 2d 1029, 1036 (N.D. Iowa, 2013).

61. *ACG Acquisition XX LLC v. Olympic Airlines SA* [2012] EWHC 1070 (Comm).

62. *Celestial Aviation Trading 71 Ltd. v. Paramount Airways Private Ltd.*, [2009] EWHC 3142 (Comm) [7].

V. THE ALTERNATIVE REMEDY: THE HARDSHIP DOCTRINE UNDER INTERNATIONAL COMMERCIAL CODE

The formation of a contract is based on the fundamental principle of *pacta sunt servanda*, originating from principles of good faith and equity, which upholds the sanctity of a contract and ensures its continued enforceability.⁶³ While the enforcement of a contract depends upon the circumstances present at the time entering the contract, often, circumstances change that render enforcement of the contract impossible, and as a result, parties may defend under the principle of fundamental change in circumstances, known as *rebus sic stantibus*.⁶⁴ The *rebus sic stantibus* principle considers the circumstantial changes that necessitate amendments to the contract in order to accommodate new circumstances.⁶⁵ The requirements identified by courts that dictates the application of this principle, include:

1. the radical alteration of the state of affairs changing the position of the parties;
2. the imbalance created that hampers performance of the contract;
3. such alteration is unforeseeable at the time the contract was entered, despite exercising due diligence;
4. the principle is applied only in the absence of any other remedy, including the nonexistence of a contractual clause remedy.⁶⁶

The purpose of this principle is to rectify the imbalance between the parties by taking measures preserving the idea of good faith, and continuing the enforceability of the contract under new circumstances. In various legal jurisdictions, this principle has been referred to as a soft legal instrument, referred to as the Hardship Doctrine under the General Principles of Law in domestic and international forums.⁶⁷ The basis of this doctrine is the modern approach toward the *lex mercatoria*

63. *Principle No. VIII.1- Hardship: Requirements*, TRANS-LEX, <https://www.trans-lex.org/951000>, (last visited Apr. 15, 2021).

64. Berger & Behn, *supra* note 42, at 82.

65. *Id.*

66. Osborne Clarke, *The Rebus Sic Stantibus Clause in the Presence of Covid-19*, OSBORNE CLARKE (Mar. 25, 2020), <https://www.osborneclarke.com/insights/rebus-sic-stantibus-clause-presence-covid-19/>.

67. Giacomo Marchisio, *Rebus Sic Stantibus: A Comparative Analysis for International Arbitration*, SSRN 1-2 (July 12, 2012), <https://ssrn.com/abstract=2103641>.

principle, which identifies the duty to re-negotiate as a need to synchronize the terms of the contract with the change in circumstances.⁶⁸

The UNIDROIT Principle of International Commercial Contracts defines a Hardship event in article 6.2.2 as one that “fundamentally alters the equilibrium of the contract either because the cost of a party’s performance has increased or because the value of the performance a party receives has diminished.”⁶⁹ This definition is supplemented by the same requirement under *rebus sic stantibus*, that the change in equilibrium is caused by an unforeseeable event after the entering of the contract which is beyond the control of the parties and could not be accounted for at the time the contract was entered, by the party whose position has been altered.⁷⁰ Article 6.2.3 provides the tools for curing the hardship event, which includes renegotiation and adaptation of the contract so that it remains valid.⁷¹ The request for renegotiation does not eliminate performance by the disadvantaged party. If the renegotiations fail, the parties have the option to go to court, which may terminate the contract or make changes to restore the equilibrium.⁷²

The disadvantaged party has the right to request renegotiation of the contract when it becomes economically challenging to uphold the terms of the contract, thereby distorting the equilibrium.⁷³ This ensures that an economic tangibility of the contract, or the financial position of the parties and any changes thereof, may also qualify as a Hardship event, depending on the satisfaction of all the legal requirements of the

68. *Principle No. IV.6.7- Duty to Renegotiate*, TRANS-LEX, <https://www.trans-lex.org/935000> (last visited Apr. 15, 2021).

69. *UPICC*, *supra* note 40, at art. 6.2.2.

70. Joern Rimke, *Force Majeure and Hardship: Application in International Trade Practice with Specific Regard to the CISG and the UNIDROIT Principles of International Contracts*, PACE REV. OF CISG 197, 219 (2001).

71. *UPICC*, *supra* note 40, at Art. 6.2.3; Ndubuisi Augustine Nwafor, *Comparative and Critical Analysis of the Doctrine of Exemption/Frustration/Force Majeure Under the United Nations Convention on the Contract for International Sale of Goods, English Law and UNIDROIT Principles* (Mar. 6, 2015) (unpublished PhD thesis, University of Stirling) (on file with University of Stirling).

72. *UPICC*, *supra* note 40, at Art. 6.2.3.

73. *Scafo Int'l BV v. Lorraine Tubes s.a.s.*, [Cass.] [Court of Cassation], June 19, 2009, Case No. C.07.0289.N, <http://www.unilex.info/case.cfm?pid=2&do=case&id=1456&step=FullText>. The case tackles the result of an unexpected steel price fluctuation which severely interrupted the contractual equilibrium. The Supreme Court determined that the facts at hand amounted to hardship under article 79(1) of the CISG and referred to the UNIDROIT Principles of International Commercial Contracts to allow renegotiation of the price.

doctrine.⁷⁴ The characteristic feature of Hardship is the difficulty in continuing specific performance of the contract despite the excessive impact of the change of circumstances, so if the contract can adapt to this change by modification, then performance can be maintained.⁷⁵ While COVID-19 has caused severe economic harm to the market that makes it difficult for all stakeholders to survive, the Hardship doctrine can allow parties to modify their contracts according to the circumstances in order to survive until the pandemic ends.

A. *Application of Hardship Over Force Majeure in Aircraft Leasing Agreement*

Force majeure is clearly not a possible solution to circumvent the rigid “Hell or High-water” clause, due to the nature of aircraft leasing agreements. Because the spirit of these agreements are to ensure performance, even if there is a contractual provision or government measure allowing application of *force majeure*, the contractual provision or government measure will likely be inapplicable to the lease payments.

However, considering the nature of the Hardship doctrine, the COVID-19 pandemic may classify as a Hardship event for the airline industry. The purpose of applying *force majeure* to a contract is to excuse non-performance and avoid damage liabilities. However, Hardship allows re-negotiation of the contract terms, which can ensure continued maintenance of the contract, on revised terms. The occurrence of the COVID-19 pandemic is an unforeseeable event that the aviation industry could not have anticipated during the formation of their contracts. Furthermore, the economic difficulties suffered by the airline industry because of the pandemic have shifted the equilibrium in aircraft leasing agreements, forcing the airlines into a clearly disadvantageous position. Therefore, allowing the airlines the ability to request renegotiation of lease payments will restore the balance of obligations in the lease agreement. This will ensure that there is no exemption from performance by the lessee, uphold the essence of the “Hell or High-water” clause, and provide immediate relief for the airlines.

B. *Legally Invoking Hardship in Aircraft Leasing Agreements*

While there may not be an express legal clause in an aircraft leasing agreement that explicitly classifies a pandemic as a Hardship event, Hardship is a General Principle of Law, as codified in UPICC, which

74. Nwafor, *supra* note 71, at 186-87.

75. Berger & Behn, *supra* note 42, at 115.

is considered a soft legal instrument.⁷⁶ Because the Cape Town Convention and the Convention on Financial leasing allow parties to choose UPICC along with General Principles of Law to govern their aircraft contracts, Hardship may be applicable in the case of a pandemic to resolve conflicts between parties.⁷⁷

Even when there is no express accounting mechanism in the contract, parties also have the discretion to choose UPICC to resolve any dispute.⁷⁸ Application of UPICC in a contract will allow the parties to use the Hardship Principle to resolve a dispute.⁷⁹ In the absence of any specific reference to Hardship in the contract, the parties have wide discretion to adopt an ad-hoc mechanism recognizing *rebus sic stantibus* as part of the contract, making the general principle of Hardship applicable in a situation where there is change of circumstance altering the position of the parties.⁸⁰ In contracts where the reference has been made to the domestic law as the governing law of the contract, the parties also have the choice of applying the General Principles of Law in resolving the dispute, which UPICC shall guide.⁸¹ This demonstrates that the modern legal interpretation of International Commercial Law allows the remedy of Hardship to apply to aircraft leasing agreements.

VI. CONCLUSION

COVID-19, in combination with various government measures and the financial burden of maintaining existing aircraft agreements, has economically devastated the airline industry. Airlines are exploring every possible remedy to reduce their burden, which includes the avoidance of lease payments for aircrafts acquired through leasing agreements.

While the aviation industry is slowly recovering, the fear of multiple waves still persists, and the prospects of recovery do not absolve the airline industry's financial problems. In order to support continued operations, passenger airlines have remodeled their aircrafts into cargo flights to raise liquidity, and various governments have provided

76. Henry D. Gabriel, *The Use of Soft Law in the Creation of Legal Norms in International Commercial Law: How Successful Has It Been?*, 40 MICH. J. INT'L L. 413, 418-19 (2019).

77. *Cape Town Convention*, *supra* note 1, at art. 5(2); Wool, *supra* note 14, at 499-500.

78. Award 116, International Arbitration Court of the Chamber of the Commerce and Industry of the Russian Federation (Jan. 20, 1997).

79. Arbitral Award, Centro de Arbitraje de Mexico (Nov. 30, 2006), <http://www.unilex.info/case.cfm?id=1149>.

80. Marchisio, *supra* note 67, at 2-3.

81. Ministry of Defense and Support for the Armed Forces of the Islamic Republic of Iran v. Cubic Defense Systems, Inc., 7365/FMS, (ICC Int'l Ct. Arb. 1997), <http://www.unilex.info/principles/case/653>.

financial aid to the airline industry.⁸² However, these measures do not fully resolve the cumbersome burden that airlines are subject to as a result of liability from lease agreements which cannot be derogated from, irrespective of the circumstance. The Hardship doctrine may be the only way for airlines to re-negotiate their agreements while maintaining continued enforcement of leasing contracts during the pandemic.

Applying the Hardship doctrine to aircraft leasing agreements is a more viable legal solution for the airline industry, as compared to *force majeure*. The doctrine of Hardship can also help circumvent the “Hell or High-water” clause, because it is based on the principle of ensuring payment by re-negotiation, thereby upholding absolute contractual obligations and ensuring financial security for the lessor. This doctrine can be invoked by a contractual provision, or by following the modern interpretation of International Commercial Law.

82. OECD Policy Response to Coronavirus (Covid-19), *supra* note 27.