

## RESPONSE FORM

### DISCUSSION PAPER ON THIRD PARTY RIGHTS IN CONTRACT

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Faculty of Advocates

**Address:**  
Advocates Library  
Parliament Square  
Edinburgh  
EH1 1RF

**Email address:**

## Summary of Proposals

### Impact assessment

1. Do consultees know of any information or statistical data, or have any comments on any potential economic impacts of either the current law relating to the third party rights or any proposed reform of that law?

(Paragraph 1.29)

#### Comments on Proposal 1

We have no such information or comments.

### Company groups

2. Are there other situations involving company groups beyond those identified in paragraphs 3.4-3.19 in which third party rights might be of use to contracting parties?

(Paragraph 3.19)

#### Comments on Proposal 2

We are unaware of any other situations in which third party rights might be of use to contracting parties.

### Construction projects and collateral warranties

3. Do consultees agree that collateral warranties are currently relied on rather than third party rights in Scots law? If so, is this problematic in practical terms? Would a modern set of rules on third party rights be utilised in place of collateral warranties should such rules be introduced?

(Paragraph 3.28)

#### Comments on Proposal 3

Our understanding is that collateral warranties are invariably used in practice, in preference to reliance on third party rights. The logistical difficulties are self-evident, though their utility was emphasised by Lord Drummond Young in *Scottish Widows Services Ltd v Harmon/CDM Facades Ltd* 2010 SLT 1102. Though based on no more than a reasonable expectation, we would imagine that those involved in the construction industry (both as participants and as advisors) would welcome a modern set of rules on third party rights if they could then dispense with invariable reliance on collateral warranties.

## **Community of interest cases**

4. Do consultees agree that, while parties to “community of interest” transactions should continue to be free to make use of third party rights law, there is no need to make special provision for such cases in any reform of the law?

(Paragraph 3.47)

### **Comments on Proposal 4**

We agree, for the reasons outlined in paragraphs 3.37 – 3.47.

## **Concepts and terminology**

5. Should any legislation on third party rights that may follow from this Discussion Paper and any subsequent Report be expressed in terms of rights or benefits or both?

(Paragraph 4.6)

### **Comments on Proposal 5**

We suggest that clarity is best served by expression in terms of ‘rights’ alone. The Hohfeldian analysis outlined in the discussion paper allows for a sufficiently wide characterisation of that term without the need to use terms such as ‘benefits’ or ‘immunities’ as well.

6. Do consultees agree with the suggested terminology for the parties and for the right, and that these might be suitable for use in any legislation on third party rights in Scots law? Would these terms be easily understood in practice? Are there better alternatives?

(Paragraph 4.13)

### **Comments on Proposal 6**

We agree with the suggested terminology.

7. Do consultees agree it is preferable for any legislation dealing with third party rights to avoid as far as possible any explicit juristic characterisation of the right?

(Paragraph 4.14)

### **Comments on Proposal 7**

Yes. Any attempt to characterise the right would undoubtedly create more problems than it

would solve.

8. Is it a correct perception that a requirement that third party rights be constituted in formal writing (ie subscribed by the grantor(s)) is undesirable in the interests of maintaining flexibility?

(Paragraph 4.15)

#### **Comments on Proposal 8**

We see no good reason to insist on formal writing being required for the creation of third party rights.

9. Should any legislation on third party rights make clear that formal writing is not required for their constitution?

(Paragraph 4.15)

#### **Comments on Proposal 9**

Given the potential application of the 1995 Act, we agree that any legislation on third party rights should make it clear that formal writing is not required.

10. Is it useful in the interests of legislative economy to draw analogies as may be appropriate with other legal institutions such as the unilateral promise (eg to define without elaborating the remedies available to the third party)?

(Paragraph 4.18)

#### **Comments on Proposal 10**

We agree that a reformed third party right should be placed, so far as possible, within existing categories in the law of obligations rather than being a 'stand alone' right. Our common law recognises the enforceability of unilateral promises and it makes sense to make use of that concept by way of analogy. There is therefore no need to prescribe the remedies available to the third party.

11. Should there be any general or more specific provision to the effect that a third party right may be conditional upon some performance by the third party or some other uncertain future event?

(Paragraph 4.20)

**Comments on Proposal 11**

It follows from the preceding answer that we see no need to enact a specific provision in relation to conditionality. That characteristic already flows from the general law of obligations and any attempt to innovate in this specific area may only succeed in falling foul of the law of unintended consequences.

**Identification and intention**

12. Do consultees agree that the third party must be identified by or identifiable from the contract, in particular as a member of a particular class of persons or as a person fulfilling or meeting conditions laid down in the contract?

(Paragraph 5.11)

**Comments on Proposal 12**

Yes. Allowing rights to other third parties takes matters beyond the idea of a contract as an agreement between the parties.

13. Do consultees agree that a right in favour of a third party who is not in existence at the time that the right is set up should continue to be valid and enforceable by any such third party which subsequently comes into existence?

(Paragraph 5.11)

**Comments on Proposal 13**

Yes. We are not aware of any particular difficulties with this rule.

14. Should it be provided for the avoidance of doubt that when a third party right is drawn in favour of a class, a person who was in existence at the time the relevant contract is formed, but was not then a member of the intended class, may become so upon joining the class if the contracting parties so intended?

(Paragraph 5.11)

**Comments on Proposal 14**

Yes.

15. Subject to the over-arching requirement that the existence of any third party's right must depend upon the contracting parties' intention, should the identification or

identifiability of the third party come from the contract only, or should it be possible to refer to extra-contractual evidence by which a third party can be identified?

(Paragraph 5.15)

**Comments on Proposal 15**

Identification or identifiability should come from the contract only. Extra-contractual evidence is relevant to the question of whether a person falls within a class defined in the contract, but to say that the definition itself might be found elsewhere is to leave matters insufficiently certain.

16. If so, what kinds of evidence might be allowed?

(Paragraph 5.15)

**Comments on Proposal 16**

Superseded.

17. Do consultees agree that the current rule in Scots law, that the intention of contracting parties to create a right by their contract for an identified or identifiable third party can be express or implied, should be continued?

(Paragraph 5.21)

**Comments on Proposal 17**

Yes, as being consistent with the general approach to interpretation of contract.

18. Do consultees agree that it should be expressly provided that an exclusion or limitation of the third party's liability to one or more of the contracting parties can be an example of a third party right?

(Paragraph 5.25)

**Comments on Proposal 18**

Yes. We see no reason not to, and agree that the prospect of avoiding disputes about whether or not exclusions of liability can be cast as rights or benefits is attractive.

**Irrevocability**

*NB Respondents may wish to note the discussion in paragraph 6.3 of some of the terms which are used in the questions in this section*

19. Do consultees agree that any requirement that a third party right cannot be constituted in a contract unless the right has first been made irrevocable by the contracting parties should be abolished?

(Paragraph 6.6)

**Comments on Proposal 19**

We consider that irrevocability of the third party's right to sue on the contract should be a question to be determined by the contracting parties as a matter of contractual intention. We see no conceptual difficulty in parties A and B agreeing that C shall have a right to sue on a contract which A and B are entitled to revoke, for example where a landlord and a tenant agree that a third party shall be entitled to reside on the premises so long as the tenancy exists. However, we also consider that the separate question of whether the third party should be entitled to sue on the contract at all ought also to be determined by the intention of the parties. Where the contracting parties agree a term in favour of a third party but take no step to intimate that to him, we consider that they should remain free to revoke that term absent intimation or its equivalent and that they should not be regarded as having committed themselves to allowing the third party to sue. Where on the other hand, the parties agree expressly or by implication that the third party's right to sue on the contract should be irrevocable without intimation, we see no conceptual reason why the law should not give effect to it. However, in approaching the question of whether there is a right to sue at all, as opposed to the revocability of the right conferred, we favour the present position whereby the conception of a term in favour of a third party does not of itself confer a right to sue on him and that intimation or its equivalent should be regarded as the necessary step conferring the right to sue unless the parties agree that that step should not be required.

20. Do consultees agree that it should be specifically provided that where a contract provides for a third party right while reserving the entitlement of the contracting parties to vary or cancel the right, that entitlement may only be defeated by (i) the fulfilment of any conditions for the third party's entitlement to enforce the right before any variation or cancellation is completed, or (ii) the operation of personal bar against the contracting parties' exercise of their entitlements?

(Paragraph 6.9)

**Comments on Proposal 20**

Yes.

21. Do consultees agree that an express contractual statement that a third party right conferred by the contract is irrevocable should be given effect, at least if delivered, intimated or otherwise communicated to the third party?

**Comments on Proposal 21**

Yes. We also consider that such a statement should be given effect absent intimation if the parties so agree: see the comments on Proposal 19. Otherwise their common intention would be defeated.

22. Do consultees agree that, where a contract sets up a third party right without any provision for an entitlement of the contracting parties to vary or cancel the right, either:
- (i) the fulfilment of any conditions for the third party's entitlement to enforce the right will prevent any variation or cancellation by the contracting parties; or
  - (ii) representations of irrevocability or unmodifiability made to the third party by the contracting parties (or any one of them?) and detrimentally relied upon by the third party will lead to the operation of a personal bar against any attempt by the contracting parties to revoke or modify the third party's right?

(Paragraph 6.17)

**Comments on Proposal 22**

We consider that unless and until the contracting parties communicate the existence of the contract to the third party, they should be free to revoke it unless they have agreed that the third party should be entitled to sue absent intimation. That accords with the principle of freedom of contract. Prior to intimation the third party will have no knowledge of the existence of the bargain and cannot be said to be prejudiced by its revocation. Where both contracting parties agree to communicate the existence of the contract to the third party, we consider that the third party's right should thereafter be treated as irrevocable if the contract contains no provision for modification and that if the conditions are fulfilled for the enforcement of the right, the contracting parties should not be entitled to defeat that right. Where the contractual right is expressed without a right to the contracting parties to modify it, we do not see that representations by one contracting party about its unmodifiability are relevant because these could not affect the modifiability of the underlying right in the absence of consent of the other contracting party. The situation would be different if the underlying contractual right was expressed as subject to modification. In that case, representations made as to its unmodifiability by both contracting parties should operate as a bar against revocation or modification if detrimentally relied on by the third party.

23. Do consultees agree that a post-contract promise to the third party by the contracting parties that a third party right conferred by the contract is irrevocable or unmodifiable should be given effect if the steps needed for the constitution of an enforceable promise have been met by the contracting parties?

(Paragraph 6.18)



**Comments on Proposal 23**

Yes.

24. Do consultees agree that where a contract provides for a third party right without any provision about an entitlement of the contracting parties to vary or cancel the right, there will be no such entitlement if the term conferring the right upon the third party has been delivered or intimated to that party?

(Paragraph 6.21)

**Comments on Proposal 24**

Yes, provided intimation was made with the consent of both parties.

25. Do consultees further agree that the contracting parties may at the time of the delivery or intimation mentioned in the previous question reserve an entitlement to vary or cancel the third party's right?

(Paragraph 6.21)

**Comments on Proposal 25**

Yes.

26. Do consultees also agree that any purported acceptance of the right by the third party should not by itself have the effect of making the right irrevocable or unmodifiable?

(Paragraph 6.21)

**Comments on Proposal 26**

Yes.

27. Should registration of a contract conferring a third party right, whether for preservation only or also for execution, make that right irrevocable or unmodifiable unless the contract expressly provides the contracting parties with an entitlement to vary or cancel the right?

(Paragraph 6.23)

**Comments on Proposal 27**

Yes.

28. Should the third party's detrimental reliance (perhaps defined along the lines found in sections 1(3) and (4) of the Requirements of Writing (Scotland) Act 1995), based upon informal knowledge of its right and known to and acquiesced in by the contracting parties, make a third party right irrevocable or unmodifiable?

(Paragraph 6.27)

**Comments on Proposal 28**

Yes. We see no reason why the law of personal bar should not apply to both the question of whether the contracting parties intend to confer the right to sue and the qualified or unqualified nature of the right itself.

29. In addition, should third party reliance that is reasonably foreseeable by the contracting parties (although they had no actual knowledge of it at the time it happened) have the same effect?

(Paragraph 6.27)

**Comments on Proposal 29**

On the assumption that the reliance was based on knowledge of the contract communicated with the consent of both parties, yes.

30. Do consultees agree that a third party right should not become irrevocable simply because the third party has informally acquired knowledge of the existence of the right?

(Paragraph 6.30)

**Comments on Proposal 30**

Yes.

31. Should the third party's death prior to any cancellation or variation of the contract containing its right have the effect of making the right irrevocable or unmodifiable so that it becomes enforceable by the deceased's executors?

(Paragraph 6.31)

**Comments on Proposal 31**

We consider that this is a question of construction of the right intended to be conferred. If it was personal to the deceased, then his death should bring it to an end but not otherwise.

32. Should there be some provision about the effects of assignation in relation to making a third party right irrevocable or unmodifiable? If so, which direction should that provision take on the matter?

(Paragraph 6.37)

**Comments on Proposal 32**

No.

33. In relation to making a third party right irrevocable or unmodifiable, should there be some provision about the effect of the third party declaring a trust over its right? If so, which direction should that provision take, and, in particular, should it take account of the identity of the trust beneficiary?

(Paragraph 6.38)

**Comments on Proposal 33**

No. We consider that the rights of the contracting parties to revoke or modify the right should not be affected by a declaration of trust by the third party.

34. Do consultees agree that there is no need in the present exercise to deal with competing claims between the third party and the contracting parties, and that these should be left as matters for the interpretation of the contract and/or the application of other relevant rules of law such as donation?

(Paragraph 6.43)

**Comments on Proposal 34**

Yes, we agree.

**Renunciation or rejection of its right by the third party**

35. Would a statutory mechanism allowing third parties to renounce rights conferred in their favour be useful?

(Paragraph 7.8)

**Comments on Proposal 35**

Yes. Such a statutory mechanism would be useful, particularly in light of the concern that Scots law is not entirely clear on the matter.

36. Should it be provided that such renunciation of a third party right may be express or implied from the third party's conduct?

(Paragraph 7.8)

**Comments on Proposal 36**

We agree that provision to this effect should be made, again in the interests of clarity and certainty.

37. Is it necessary to make any provision to protect the contracting parties against unfair exercise of the third party's power to renounce the right, for example to require the return of any benefit already conferred and reimbursement of expenses incurred by the contracting parties?

(Paragraph 7.8)

**Comments on Proposal 37**

In our view, it is unnecessary to make such provision. The appropriate legal principle is that the third party cannot be forced to receive, or to continue to receive, a benefit that it does not wish to have. Accordingly, renunciation by the third party should not be conditional upon the third party returning any benefit already conferred or reimbursing expenses to the contracting parties.

In circumstances in which the third party has given to the contracting parties the impression of willingness to receive the benefit, it would be possible to impose liability upon the third party, following renunciation, to return any benefits received and to reimburse expenses incurred by the contracting parties. In practice, the framing of appropriate statutory provisions to achieve that result is likely to be an extremely complex task and we do not consider such provisions to be necessary or desirable. Contracting parties who choose to confer benefits on a third party simply run the risk that the third party will renounce its right.

38. Should it be made possible to renounce a right in part if it is divisible?

(Paragraph 7.8)

**Comments on Proposal 38**

Yes, we see no objection in principle to that approach.

### **Remedies available to the third party**

39. Should it be provided that third parties have at their disposal all remedies which are appropriate to the enforcement of their right? If not, how (if at all) should the issue of remedies be addressed in any legislation on third party rights?

(Paragraph 7.13)

#### **Comments on Proposal 39**

In our view, it is desirable in the interests of clarity that such provision should be made.

40. Would it be useful to make clear in legislation the availability of (i) a damages claim; (ii) a right to a cure in appropriate cases, possibly as an aspect of specific implement; (iii) a right to rescind for material breach?

(Paragraph 7.13)

#### **Comments on Proposal 40**

While arguably unnecessary because of the scope of the general provision as to the third party's remedies (see question 39 above), specific provision that these particular remedies are available would, in our view, be appropriate.

41. Should third parties be entitled to exercise the remedy of rectification in relation to the contract under which rights are claimed?

(Paragraph 7.14)

#### **Comments on Proposal 41**

Yes, subject to the proviso that the third party's right to seek rectification must relate either to the failure by the contracting parties to express their common intention to confer third party rights or to such terms of the document as relate to such rights. The third party can have an interest in rectification only in respect of provisions, or the absence of intended provisions, as to third party rights.

### **Defences**

42. Are specific provisions required regarding the enforceability of third party rights arising from contracts which fail as a result of invalidity, illegality, or frustration?

(Paragraph 7.19)

### **Comments on Proposal 42**

In our view, it would be undesirable to leave these important matters to be dealt with under the general principles of the law of obligations and remedies. Accordingly, we consider that specific statutory provisions are appropriate.

43. Would a specific provision, to the effect that compensation under the Compensation Act 1592 arising from or in connection with the contract and relevant to the third party's right under the same contract could be used in extinction of the third party's claim if liquid, be appropriate and useful?

(Paragraph 7.24)

### **Comments on Proposal 43**

Yes. In our view, it is appropriate that this point is made clear in the legislation.

### **Prescription**

44. Should a specific provision be inserted into paragraph 1 of Schedule 1 to the Prescription and Limitation (Scotland) Act 1973 to make clear that the short negative prescription applies to third party rights arising from a contract?

(Paragraph 7.26)

### **Comments on Proposal 44**

Yes. In our view certainty on this point is desirable.

### **Liability of one contracting party if the other defaults on the contract**

45. If one of the contracting parties defaults on the contract so that the other contracting party is unable to perform to the third party as required by the latter's right under the contract, should the third party have a remedy against the initially defaulting party?

(Paragraph 7.27)

### **Comments on Proposal 45**

In our view the rights of the third party in the sort of example given at paragraph 7.27 of the Discussion Paper should be approached as one of the proper construction of the contract. No doubt the proper construction in many (perhaps most) cases would yield the result discussed at paragraph 7.27. In our view, however, there should not be any fixed rule which has the effect of preventing the contracting parties, A and B, agreeing that in the event of a default by A in A's obligation to B, which has the effect that B is in default of an obligation owed to a third party, that A shall not be liable to the third party (or rendering such an

agreement unenforceable). In our view such a rule would amount to an unwarranted interference with A and B's freedom of contract.

### **Contracting out of liabilities to third parties**

46. Do consultees agree that no express provision is needed to deal with the possibility that contracting parties may exclude or limit a liability to third parties (such as damages) that would otherwise arise?

(Paragraph 7.30)

#### **Comments on Proposal 46**

Yes, we agree that no such express provision is needed. Having said that, we can see no harm in there being such a provision in order to put the matter beyond any possible doubt.

### **Other points arising from the 1999 Act**

47. Do consultees agree that it should be clear on the face of any legislation arising from this Discussion Paper that the third party can enforce only its own rights under the contract?

(Paragraph 7.33)

#### **Comments on Proposal 47**

Yes, we agree that this should be made clear on the face of any legislation.

48. Would an equivalent to section 4(1) of the 1999 Act serve any useful purpose in Scotland?

(Paragraph 7.34)

#### **Comments on Proposal 48**

Yes. While we agree that such a section may not be strictly necessary, in our view certainty is desirable and it would be better to insert an equivalent section to put the matter beyond doubt.

49. Do consultees agree that the third party need not involve any of the contracting parties in its action beyond the one from whom it seeks a remedy?

(Paragraph 7.35)

#### **Comments on Proposal 49**

Yes, we agree.

50. Do consultees agree that there is no need in Scots law for a provision equivalent to section 5 of the 1999 Act?

(Paragraph 7.38)

#### **Comments on Proposal 50**

Yes, we agree. In addition to the reasons set out in paragraph 7.38, we would mention that (as pointed out in the commentary to the DCFR) it is unlikely that contracting parties would expressly provide for a situation in which there might be double liability, and it is unlikely such a liability would be implied. However, if the contracting parties were to make such express provision, or were such an agreement capable of being implied, in our view the effect of that express or implied agreement should not be interfered with by the legislature.

#### **Relationship with specific rules**

51. (a) Do consultees agree that, in principle, the general reforms proposed in this Discussion Paper should be without prejudice to the specific third party rights under the current law (for example, in the areas listed in paragraphs 8.3 and 8.4)?
- (b) Do consultees consider that any of the specific third party rights should be amended in the light of the general reforms which are proposed? Would it be desirable to provide that those reforms should not extend to employment contracts relating to employees, workers and agency workers?

(Paragraph 8.6)

#### **Comments on Proposal 51**

- (a) Yes, we agree. Unless the impact of the proposed general reforms upon the specific rights under the current law were to be considered in great detail, it seems to us that there must be a considerable risk of undesirable unintended consequences if general reforms were to be applied across the board.
- (b) We do not consider that amendment of specific third party rights should be made in the light of the general reforms proposed at this stage. Rather we consider that the proposed reforms and the work which has gone into the Discussion Paper would inform consideration of the specific third party rights if and when the particular areas of law in which they reside are reviewed.
- We consider that it would be desirable to provide that the general reforms proposed should not extend to employment contracts relating to employees, workers and agency workers.



## **Methods of reform**

52. (a) Are there advantages in having a comprehensive statutory statement of the law on third party rights?
- (b) Alternatively, should any legislation seek only to amend the common law so far as is necessary to achieve the desired reforms?

(Paragraph 9.17)

### **Comments on Proposal 52**

We take these questions together. In our view the problem of the unintended consequence should be avoided, in so far as it is possible to do so. It seems to us that the better way to avoid that problem is to make a comprehensive statutory statement of the law on third party rights. That is the principal advantage we see in such a statement. Certainty, or at least relative certainty, is desirable. We are in favour of a comprehensive statutory statement.

### **General Comments**

Thank you for taking the time to respond to this Discussion Paper. Your comments are appreciated and will be taken into consideration when preparing a report containing our final recommendations.