



THE LAW SOCIETY
of SCOTLAND
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Consultation Response

Discussion Paper (157) on Third Party Rights in Contract

The Law Society of Scotland's response
June 2014

Introduction

The Law Society of Scotland aims to lead and support a successful and respected Scottish legal profession. Not only do we act in the interest of solicitor members but we also have a clear responsibility to work in the public interest. That is why we actively engage and seek to assist in the legislative and public policy decision making processes.

To help us do this, we use our various Society committees which are made up of solicitors and non-solicitors and ensure we benefit from knowledge and expertise from both within and outwith the solicitor profession.

The Society's Obligations Law Sub-committee welcomes the opportunity to consider and respond to the Scottish Law Commission Discussion Paper (157) on Third Party Rights in Contract. The Committee has the following responses to put forward in response to the questions as set out in the discussion paper.

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?

We are not in a position to respond to this question.

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?

We would suggest that confidentiality undertakings and contractual warranties may be situations where it would be of use to allow the use of third party rights in company group situations.

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?

Collateral warranty agreements are common in practice. In practical terms, we believe all points noted in paragraphs 3.20 to 3.28 create problems and costs for parties concerned. The experience noted in England & Wales shows that there is value in developing such rules. However, uptake in use may take some time and there is likely to remain a preference for written collateral warranty terms particularly in bank financed transactions.

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?

Concepts and terminology

Yes, we agree.

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?

It would appear that the terminology of rights is more appropriate. If a benefit is conferred there must be an intention to create a right to such benefit.

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?

Yes, we agree.

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?

Yes, we agree.

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

Yes.

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

Yes, we agree this should be made clear.

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)?

Yes, we agree that it would be useful to draw such analogies.

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?

We do not consider there to be a real need to include such a statement given the general law of obligations. However, if correctly framed, such provision could, we suggest, provide useful guidance.

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?

Yes, we agree

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?

Yes, we agree.

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?

We would not consider such provision necessary but again, we suggest it may provide useful clarification if correctly framed.

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?

In the interest of certainty, it would be preferable to identify the third party from the terms of the contract only.

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

No Comments.

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?

Yes, we agree.

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?

Yes, we agree.

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?

We agree but, subject to safeguards in next following answers.

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?

Yes, we agree, subject to our response to question 25.

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?

Yes, we agree.

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?**

We agree, but there must be additional safeguards as per answer 25.

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?

Yes, we agree.

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?

Yes, we agree.

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?

See DCFR II 9:303 (3):

(3) Even if the right or benefit conferred is by virtue of the contract revocable or subject to modification, the right to revoke or modify is lost if the parties have, or the party having the right to revoke or modify has, led the third party to believe that it is not revocable or subject to modification and if the third party has reasonably acted in reliance on it.

Such limitation on reserved entitlement should be embodied in legislation and be not excludable.

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?

We agree that acceptance by the third party should not by itself make the right irrevocable, see for example our response to question 37.

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?

Yes, we agree with this proposal.

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?

Yes, on basis that "known to and acquiesced in" amounts to "led .to believe" as in DCFR II 9:303 (3) see our response to question 25.

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?

Not unless that facts show that the third party had been "led..... .. to believe" (DCFR)

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?

Yes, we agree.

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?

No. We note that Paragraph 6.31 refers to the position under Swiss law, but it is not clearly made out why the Swiss have taken this approach and further information on this would be welcomed.

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?

We would suggest that there appears to be no obvious reason why an otherwise assignable right should be modified by mere fact of assignation. The assignee takes tantum et tale. Intimation alters the identity of the person conduct towards whom might raise personal bar. This appears to us to be right and proper.

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?

Trust should make no difference. Nor should, we suggest, identity. In the case or trust the issue of personal bar stays where it was.

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?

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?

We consider that yes it would be useful.

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

Yes though we think that caution should be the watch word in relation to any implied renunciation. The example given in Paragraph 7.6 is clear and we think any implied renunciation should need to be clear from the actions.

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?

Yes. It would appear unfair to the contracting parties to expend sums to benefit the Third Party for the Third Party to subsequently renounce. On balance we consider that the sums recovered ought to be restricted to the expenses/out of pocket costs.

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

Yes where applicable.

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?

Yes though it appears to us that this is the existing law.

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?**

Yes clarity on this would be welcomed.

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

Yes on the same basis as the Law Reform (Miscellaneous Provisions) Act 1985.

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?

No. We agree with the view expressed in the Stair Memorial Encyclopaedia that if the underlying obligation is frustrated then the third party right falls.

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?

No. We do not consider it necessary or appropriate. The rules on compensation have operated for some considerable time and we do not feel that there should be specific provision in relation to Third Party rights.

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?

We do not consider there to be uncertainty on this but it may be useful to put the matter beyond doubt.

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?

Logically yes.

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?

Yes, we do not consider this necessary.

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?

Yes, we agree.

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

No. In our view this would not serve any purpose.

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?

Yes. It would remain open to any Defender to bring in the other contracting party as a Third Party to Court proceedings if appropriate.

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

Yes, we agree.

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?

(a) Yes

(b) No. We consider that this should not apply to employment law at all.

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?

We would prefer a comprehensive, codified statement of the law of Third Party rights. This will clarify, revise and re-state the law which will provide clarity for businesses, contracting parties and beneficiaries.



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