OFFICIAL REPORT
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Delegated Powers and Law Reform Committee

Tuesday 21 March 2017

Session 5

The Scottish Parliament
Pàrlamaid na h-Alba

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DELEGATED POWERS AND LAW REFORM COMMITTEE
10th Meeting 2017, Session 5

CONVENER

*John Scott (Ayr) (Con)

DEPUTY CONVENER

*Stuart McMillan (Greenock and Inverclyde) (SNP)

COMMITTEE MEMBERS

*Alison Harris (Central Scotland) (Con)
*Monica Lennon (Central Scotland) (Lab)
David Torrance (Kirkcaldy) (SNP)

*attended

THE FOLLOWING ALSO PARTICIPATED:

George Adam (Paisley) (SNP) (Committee Substitute)
Ross Anderson (Faculty of Advocates)
Professor Hugh Beale (University of Warwick)
Karen Fountain (Brodies LLP)
Jonathan Gaskell (DLA Piper)
John MacLeod (University of Glasgow)
Karen Manning (Burness Paull)
Kenneth Rose (CMS Cameron McKenna LLP)
Paul Wheelhouse (Minister for Business, Innovation and Energy)

CLERK TO THE COMMITTEE

Euan Donald

LOCATION

The Adam Smith Room (CR5)

Scottish Parliament

Delegated Powers and Law Reform Committee

Tuesday 21 March 2017

[The Convener opened the meeting at 10:02]

Bankruptcy (Scotland) Act 2016 (Subordinate Legislation)

Bankruptcy and Protected Trust Deeds (Miscellaneous Amendments) (Scotland) Regulations 2017 [Draft]

The Convener (John Scott): Good morning, everyone, and welcome to the 10th meeting in 2017 of the Delegated Powers and Law Reform Committee. I welcome George Adam to the committee today in place of David Torrance, who has sent his apologies.

Item 1 relates to the Bankruptcy (Scotland) Act 2016. We will consider in the first instance the draft Bankruptcy and Protected Trust Deeds (Miscellaneous Amendments) (Scotland) Regulations 2017. Members will recall that the committee considered the technical merits of the instrument at its meeting on 28 February 2017. The committee has also been designated as the lead committee for the instrument and today we are invited to consider its policy merits.

The instrument amends minor drafting errors in the Bankruptcy (Scotland) Regulations 2016 (SSI 2016/397) and the Protected Trust Deeds (Forms) (Scotland) Regulations 2016 (SSI 2016/398) that our committee identified in November 2016. At that time, the Scottish Government agreed to correct the errors at the next legislative opportunity. Today we are invited to consider this amending instrument.

We welcome Paul Wheelhouse, who is the Minister for Business, Innovation and Energy—good morning, minister. We also welcome Graham Fisher, who is head of branch 1 of the constitutional and civil law division of the Scottish Government legal directorate, and Carol Kirk, who is policy review team leader at the Accountant in Bankruptcy.

I invite the minister to make an opening statement.

The Minister for Business, Innovation and Energy (Paul Wheelhouse): Thank you, convener, and good morning, everyone.

The regulations that are before the committee today fulfil a commitment that I made to the committee at its meeting on 1 November last year, when I undertook to bring forward regulations that would amend drafting errors that had been identified in bankruptcy regulations that had been put before the committee. The drafting errors included missing words and incorrect referencing in the Bankruptcy (Scotland) Regulations 2016 and the Protected Trust Deeds (Forms) (Scotland) Regulations 2016, which were part of an exercise to consolidate legislation following the Bankruptcy (Scotland) Act 2016.

Those measures came into force on 30 November last year, and the committee might recall that I fully acknowledged the errors at the time. As a temporary mitigation, we took steps to clarify the errors, where appropriate, to ensure that the legislation was clear for those who would use it, which included annotating the available forms on the Accountant in Bankruptcy's website with the correct information.

However, it is important to put right the errors formally at this time. The regulations that are before the committee therefore fix the errors to ensure that the regulations are accurate. In addition, we have taken the opportunity, as I indicated in my letter to the committee, to amend other minor points that stakeholders had raised during the committee's scrutiny. I thank the committee for taking the time to consider the Scottish statutory instrument that is before it this morning. We are, of course, happy to take questions.

The Convener: Thank you. As members have no questions, we move to agenda item 2, which is a debate on the motion recommending approval of the regulations. I remind the Government officials that they cannot participate in the formal debate on the motion. In accordance with rule 10.6.3 of standing orders, the debate on the motion can last no longer than 90 minutes. I invite the minister to move motion S5M-04390.

Motion moved,

That the Delegated Powers and Law Reform Committee recommends that the Bankruptcy and Protected Trust Deeds (Miscellaneous Amendments) (Scotland) Regulations 2017 [draft] be approved.—*[Paul Wheelhouse]*

The Convener: As committee members have no points to make, I thank the Scottish Government for addressing its commitment to correct the errors so promptly. I am sure that the minister had a personal influence on that.

Paul Wheelhouse: I thank the team. We are sorry that the errors happened in the first place, but we are glad to have fixed them early.

The Convener: We are very grateful for that consideration. I invite you formally to respond to the debate, or the lack of it.

Paul Wheelhouse: Thank you, convener. I thank the committee for its attention.

The Convener: The question is, that motion S5M-04390 be agreed to.

Motion agreed to.

The Convener: I thank the minister and his officials for attending the meeting. I suspend the meeting briefly to allow them to leave and others to take their seats.

10:08

Meeting suspended.

10:09

On resuming—

Contract (Third Party Rights) (Scotland) Bill: Stage 1

The Convener: Agenda item 3 is our second oral evidence session on the Contract (Third Party Rights) (Scotland) Bill at stage 1. We welcome our first panel: Ross Anderson, who is from the Faculty of Advocates, and John MacLeod, who is a lecturer in commercial law at the University of Glasgow and is representing the Law Society of Scotland today.

I invite questions from members—and I will ask the first question myself. As you know, the Scottish rules on third-party rights are currently based on the common law. The bill team and the Scottish Law Commission have argued that case law is unlikely to develop quickly enough to deal with the problems in the law that have been identified, and that statutory rules are needed. Do you agree?

Ross Anderson (Faculty of Advocates): Let me begin to answer that. The short answer is yes, we agree. The reason is that the existing authority on the subject is a House of Lords decision from 1920, which makes development of the law very difficult unless a litigant is willing and able to take matters to the equivalent of the House of Lords today, which is the United Kingdom Supreme Court.

The Convener: Do you have anything to add to that, Mr MacLeod?

John MacLeod (University of Glasgow): Not a great deal—merely that, as the Scottish Law Commission suggested in its report, there has been a tendency to choose English law as a way of getting round the problems or to choose other workarounds. In so far as parties continue to do that, the core law relating to third-party rights is not being used. Therefore there will be very little opportunity for litigation, even were there parties with deep enough pockets to deal with the matter. I do not see any prospect of a Supreme Court case on these issues.

The Convener: Great—thank you. Our next group of questions is from Alison Harris.

Alison Harris (Central Scotland) (Con): Good morning. One of the main criticisms of relying on the common law is that there is uncertainty about the scope of the law. Do you agree with that criticism? To what extent do you think that the law needs to be clarified in legislation?

Ross Anderson: In short, I agree with that criticism. There is a lack of clarity on a number of levels. The first difficulty is a lack of clarity as to

what the law actually is. There is difficulty in interpreting what the existing case law requires in practice. The committee will be aware of the Scottish Law Commission's report, in which it sets out one of the difficulties: the conflation of ideas between creating a right and rendering it irrevocable. In practice, that causes innumerable difficulties.

There is a lack of clarity in understanding what the law is, and there is therefore a lack of clarity in providing solutions in practice.

Alison Harris: Noting that the bill seeks to provide greater clarity, do you think that its provisions are clear, and do they resolve some of the uncertainty associated with the current law?

Ross Anderson: In broad terms, yes. At this juncture it might be most useful if, on the points of detail, I simply refer to some of the written comments that the Faculty of Advocates has made on particular points of detail in response to the committee's consultation. In broad terms, we welcome the bill, and we think that it is a positive development. We think that, as a matter of policy and of achieving its aims, it is successful.

John MacLeod: I largely echo those comments. When it comes to accessibility of the law, there is value in the rules being set out in statute, because statutory material is often much easier to handle compared with the present position, where we have to read a case from the 1920s and think about how a writer from the 17th century was commented on in that case. That is not accessible. You can see that in the doubts that have been expressed in the major texts that practitioners rely on in this area.

In section 1, the bill deals very clearly with the core issue of the requirement that a right be irrevocable in order to be created. That is a massive step forward. I agree that there are some points of detail where the signalling within the bill might make the rules a little bit more accessible but, on the whole, it represents a vast step forward in terms of clarity and accessibility.

The Convener: It is also a vast step forward in terms of uncertainty. Are there any other areas of uncertainty that you or Mr Anderson would like to discuss so that they are in the *Official Report*?

10:15

John MacLeod: In relation to the current law?

The Convener: Yes.

John MacLeod: The main issue, to my mind, is twofold—as Dr Anderson said, two things are tied together. First, there is the question of whether a right needs to be irrevocable, and thus fixed and unchangeable, in order to be created. That causes problems at the outset, because people are not sure what they need to do in order to create third-party rights. There is also the potential of problems being caused later, when people wonder whether it is possible to vary a right and they have questions about what steps to follow to change it. It is clear that things would be much better were the bill to become law.

The Convener: Okay; thank you very much. We move to the next group of questions.

Stuart McMillan (Greenock and Inverclyde) (SNP): On the point about a right being irrevocable, section 2 abolishes the irrevocability rule such that contracts that grant third-party rights can be "cancelled or modified". Given what you said a few moments ago, do you support the abolition of that rule?

John MacLeod: Yes. It is important to bear in mind that the ability to revoke rights is restricted; there are protections for the third parties later in the bill. However, as a matter of general law in Scotland, outside the third-party context, I can for instance make a unilateral promise to you that is binding. At that point you have a right. However, it is also possible for me to make that promise in such terms as to make it subject to revocation or modification in certain circumstances.

The bill moves the law of third-party rights to bring it in line with the law that generally applies to voluntarily created rights. To my mind, it improves the consistency and coherence of the law.

Ross Anderson: I agree with everything that has been said. Also, although the rule of irrevocability in relation to constitution of a third-party right is abolished by section 2, the bill will not prevent parties from creating irrevocable rights, if that is what they choose to do. The bill removes the tie of creation to irrevocability, which was the problem with the law. It addresses the problem without going too far.

Stuart McMillan: Do you think that the bill could be strengthened in that regard, or are you content with what it states?

Ross Anderson: On that point, we are content with what the bill states.

Stuart McMillan: Okay. The provisions in the bill set out in general terms the default position. The contracting parties are free to make express provisions to the contrary. Do you agree with that approach?

Ross Anderson: We do, yes. The whole law of third-party rights, to use that general expression, is fundamentally based on party autonomy. The bill provides a framework for the parties to use, and it is for the parties to decide whether to use it. There is no obligation to use the framework, but in so far

as the framework is engaged, it is for the parties to formulate the rights that they wish to create.

John MacLeod: I would add to that only that it is important to bear in mind that you cannot impose a third-party obligation using the bill. Anything that the third party gets is in some sense a windfall. All that the contracting parties can do is give the third party something that it did not have before. Therefore, we are pretty relaxed about the contracting parties being able to restrict that. Provided that the terms of potential modification are clear at the outset, we do not see problems with the power of modification. At the end of the whole process, whatever happens, the third party will be no worse off than it was in the first place.

Stuart McMillan: Sections 4 to 6 stop the contracting parties modifying or cancelling a third-party right. Do those sections provide the right balance between the rights of contracting parties to change their mind and the rights of third parties?

Ross Anderson: Yes—in short, they do. To a large extent, those provisions mirror the existing law, which is contained in section 1 of the Requirements of Writing (Scotland) Act 1995, in relation to situations in which reliance has been placed on rights that have been granted but which have not complied with formalities. Therefore, there is an element of continuity in the provisions. In addition, in any event, and going back to the general principle of party autonomy, as I have already indicated, the parties are free to contract out of the provisions themselves. As far as we are concerned, we are content that the correct balance has been struck.

The Convener: Excellent. Many thanks. That is very clear, and I am grateful to you for that. We move to the next group of questions.

Monica Lennon (Central Scotland) (Lab): The policy memorandum states that the bill will promote the greater use of Scots law, but I understand that people will remain free to use English law if they wish or if they prefer. Based on your experience, will the bill promote greater use of Scots law?

John MacLeod: I think so; yes, in short. It is always difficult to predict the future, and my colleagues from the solicitors profession who will give evidence next will probably be able to comment more specifically on any changes in practice that they envisage in their sectors.

The brief that I have from the Law Society of Scotland is to talk in general terms. However, we can look at, for instance, the Legal Writings (Counterparts and Delivery) (Scotland) Act 2015, which clarified a point of law on which it could have been argued that the law was what the act provided anyway. However, the evidence that the Law Society of Scotland has received is that there has been an increase in usage, just as a result of placing the law on a clear statutory basis. It would increase solicitors' confidence in advising clients if they were to use Scots law, because they would be able to find all the rules in an easily accessible place.

Also, the lack of flexibility that the irrevocability rule was perceived as creating—and probably did create—meant that some parties had a strong incentive not to use Scots law because of that problem, or not to use the most efficient and simple technique in Scots law. Taking those barriers away makes it easier for people to contract using Scots law, therefore one would expect there to be an increase in the use of Scots law.

Monica Lennon: I ask Ross Anderson the same question, and also whether he can think of circumstances in which it would be preferable to use English law rather than the bill, if it comes forward.

Ross Anderson: I will address the initial question first, and then I will come back to that supplementary point. I agree with what is being said. The general principle in relation to choice of law is party autonomy and freedom of choice. The parties are free to choose English law in the same way that, ultimately, they are free to choose German law, French law or the law of New York state or of anywhere else. If they have an arbitration clause, they can choose a non-state law.

The key point in relation to the bill has been not so much to try to attract other people from around the world to choose Scots law as it has been to ensure that, for those who wish to use Scots law because they are businesses that are based here and their contracts will be performed here, Scots law provides the tools within itself to allow them to achieve what they wish to achieve without, in an artificial sense, having to use some foreign law—whether that is English law or any other law.

The other point that it is important to make is that, whereas sophisticated parties who have the benefit of sophisticated advice—perhaps from some of the lawyers sitting behind me in the public gallery—will always be able to come up with some sort of workaround to any lacuna in the law, those who do not have the benefit of such advice are in a difficult position at the moment because the law is so unclear. One of the great advantages of the bill is that it sets out, in modern language, what the law actually is.

Forgive me, was your supplementary question in relation to English law asking for particular examples?

Monica Lennon: Yes, I wanted to identify the circumstances in which people who were trying to access law would use English law instead of Scots law.

Ross Anderson: If the bill is passed in substantially the form that it is in, the incentive to use English law simply to deal with the difficulties with third-party rights will disappear. There may be other reasons why parties choose English law: a particular project might be UK-wide and, at the end of the day, England is bigger than Scotland; or we may not be aware of reasons to do with the requirements of a funder or something else. However, in so far as the sole incentive at the moment for choosing English law in a practical situation is a desire to ensure that one has enforceable third-party rights, one of the beneficial effects of the bill will be to remove that incentive.

Monica Lennon: You mentioned workarounds, particularly in the context of people who can perhaps afford more sophisticated advice. Will there continue to be a reliance on workarounds, or is it realistic to think that we will see a shift away from that?

Ross Anderson: As John MacLeod said, it is difficult to predict the future. To some extent, where parties involved in, let us say, construction projects, are used to taking collateral warranties, there is a standard document and a practice that has grown up around using them, and they may continue to use them for some time. However, if there are additional transaction costs and inconvenience from having to sign those additional documents, one would expect rational economic operators to change their practice. Based on anecdotal evidence from colleagues in the legal profession, it is fair to say that such parties would envisage making use of the bill to avoid some of those workarounds.

Beyond that, it is difficult to say much. You will hear later from Professor Beale, from the University of Warwick, who undertook some research in England after the Contracts (Rights of Third Parties) Act 1999 was introduced there, to see what the lag time was for practice altering to reflect the remedies that were the substantive content of that act.

Monica Lennon: It sounds as if you agree with the Scottish Law Commission that third-party rights are preferable to collateral warranties. Can you explain the problems with collateral warranties? Is it the cost?

Ross Anderson: That is one of the difficulties. Wherever one has extra documents to sign at different times, particularly where the signatory of that document may have come into existence some years after the initial project documents were concluded, it may be difficult to get people to sign up to them, as there may not be a huge monetary incentive to do so. It is to do with the general transaction costs and inconvenience. That is the easiest way to explain it, and I think that the same would be true of other sectors that use different workarounds. Wherever you need an additional document or an additional step, there is a cost.

The Convener: Mr MacLeod, is that a view that you would share?

John MacLeod: Yes, it is better to do something directly than indirectly.

The Convener: I note that the Scottish Law Commission has indicated that the bill will make it easier for business to avoid what it calls the “black hole of non-liability”, which currently reduces protection for company groups. Do you agree with that?

John MacLeod: Yes, absolutely. Would you like me to talk about what the black hole is?

The Convener: Yes, please expand on that.

John MacLeod: An example might be a construction project where one company within a group concludes a contract with contractors to do works for properties held by a number of other companies within that group. Unless you use collateral warranties or some other device to set up additional contractual rights, the issue is that, if the contractors do not do their job properly and breach their contract, the contractual right is held by the head company—the first company that concluded the contract—but the losses will be suffered by different legal persons, that is, by other companies within that group.

There is therefore a mismatch, if you like, between the person suffering the loss and the person with the right to enforce. Typically, when you are suing for breach of contract, you seek damages that reflect the loss that you yourself have suffered, rather than the losses that someone else has suffered.

10:30

The term “black hole” refers to the loss going somewhere that is not covered by the contractual right. If you used the new, shiny, exciting third-party rights in the bill, you would, at the outset, create rights in favour of all the companies in the group with respect to their relevant properties. That would enable them to enforce a claim for breach of contract and thus to recover the full damages. That is how it would work. The Scottish Law Commission is right that the bill would make things much easier in that regard.

The Convener: The proposed approach would be progress.

John MacLeod: Yes. You could do some of that already if you were willing to use the jus quaesitum tertio, but people will—we hope—be more willing to use the new approach because, once you take away an automatic irrevocability rule, you can create those rights but still leave it open to the initially instructing company to modify the contract with the contractor if that is appropriate. You will get the best of both worlds: the right to cover the damages and flexibility between the constructor and the head company in the group.

The Convener: One of the things that we are seeking to establish is whether the bill as it is drafted strikes the right balance, so we are, I suppose, seeking your endorsement that we have managed to achieve that. Have we struck the right balance?

John MacLeod: Yes. As Dr Anderson said, this all ultimately comes back to party autonomy. Almost every section is subject to the parties' agreement, so ultimately it will be for the parties themselves to strike the balance, which is appropriate. If we believe in an economy that is driven by freely negotiated contracts, the parties' balance is the right balance unless we have reason to doubt that in a specific situation. We are dealing with the general law, rather than consumer or labour law, so there is no reason to fiddle with the balance between the parties.

The Convener: Dr Anderson, do you wish to add anything or are you happy?

Ross Anderson: I do not have much to add. I endorse the balance that the bill seeks to strike. The only caveat to black-hole liability—which, believe you me, is as unpleasant in practice as it sounds—is that third-party rights will not solve all liability issues. There will be situations in which the parties have not envisaged something that will happen subsequently. The classic example is where one of the parties—a bank, for example—is restructured, whether voluntarily or involuntarily, and the contract, when it was concluded in year 1, may not have made provision for that particular eventuality in which a completely different party comes to hold the contractual rights.

However, the bill cannot achieve everything. In so far as there is a problem with black-hole liability in relation to third-party rights, the bill will go some way towards solving that.

The Convener: Notwithstanding what you have just said, we are here to try to make the bill as good as it possibly can be. If you have suggestions for improvements, we would be pleased to hear from you now in that regard—or subsequently, if you have an elegant improvement to make to the bill, as we will amend it at stage 2.

Ross Anderson: We are very grateful for that opportunity. To be clear, however, I am not seeking in what I have just said to criticise the bill in any way. Notwithstanding what the bill can achieve under the law of third-party rights, the point about black-hole liability is that it is not just about third-party rights; there are other situations that the bill could never address without opening up wider areas of the law with which it is not concerned.

Again, I simply emphasise that the bill strikes the right balance in seeking to address the particular problem of third-party rights.

The Convener: Mr MacLeod, are you content?

John MacLeod: What was said is correct. The other types of black-hole situations are beyond the scope of the bill, and the bill would be spoiled if it sought to deal with them. I believe that Professor MacQueen stated in evidence that the Scottish Law Commission is considering the broader issues as part of another project, so you would be best advised to wait for the commission to report on that matter, and to deal with it once it has been properly considered.

The Convener: That is very helpful; thank you very much.

George Adam (Paisley) (SNP): The Scottish Law Commission report refers to the new rules having the biggest impact in the construction industry—you have already given a couple of examples—and the oil and gas, financial services, information technology and pension sectors. Are there any other sectors or industries where the legislation could be important?

John MacLeod: I do not have specific data to hand; I could seek it from the Law Society if you wish.

This is general contract law so, in principle, it could be useful at any time where we have two parties agreeing and a third party that they want to be able to enforce. That could potentially happen in certain agricultural contexts, if we have a contractor and an estate, and a tenant farmer. The commission gave the main examples where we tend to have a complex relationship, with multiparty contracts.

George Adam: Is that why construction is such an easy example? I ask just to get it right in my own head. There are so many subcontractors and other people involved.

John MacLeod: Absolutely—and similarly with finance contracts, there are lots of parties with slightly different sets of interest; lots of different legal persons are used. We could have that in any number of contexts; what matters is to get the general principles correct.

George Adam: Could the bill benefit individuals as well? I know that I am asking you to look in a crystal ball, but there could be cases where individuals could benefit.

John MacLeod: The example that the Scottish Law Commission gave about pensions seems to be the core example. It gave another example, if I recall correctly, about a caregiver procuring services for somebody who is mentally impaired and does not have active capacity. That example is off the top of my head, but there are a couple of other examples of situations where one person needs to contract on behalf of another—those are the most obvious that come to mind.

Ross Anderson: I do not have much to add. For presentational purposes, one talks about the particular problems that arise in particular sectors. The construction industry is a good example to use, because it is relatively easy to explain the different contractual matrices. In broad terms, the bill applies to all persons natural and legal, in whatever context they are entering into contracts. It would apply equally to a construction contract as it would to a domestic arrangement in which people were buying a house that was being funded by a third party, which is another of the examples in the commission's report.

In my experience of practising before the courts, it is very often individuals who have not had the benefit of detailed or sophisticated advice who have assumed that it is quite easy to confer a third-party right and, perhaps to their cost, have found that they have not complied with the detail of Lord Dunedin's speech in the case that is referred to in the commission's report. For those ordinary citizens, there is a benefit to this bill in recording what the law is in simple and modern language.

George Adam: Thank you.

The Convener: Given that it is impossible to envisage every situation to which the bill might apply, it is important that we establish the general principles. If I have understood you correctly, I am, I hope, reassured that you believe that we have managed to do that in the bill as proposed.

Ross Anderson: That is correct.

The Convener: Thank you. I have a couple more questions, including one about arbitration. Do you have any comments on section 9, which allows arbitration agreements between contracting parties to operate in respect of third-party rights?

Ross Anderson: That was a matter about which our faculty response made some comments, which were more about drafting details than they were about major points of principle. The issues that arise can be somewhat complex to explain, but I am happy to do so.

The particular drafting issue that arises is in section 9(3). Rather than give the committee a long explanation of why it arose, I will simply observe that paragraph 38 of the explanatory notes points out correctly that the provision in section 9(3) is designed to deal with a particular situation where the third party does not have a substantive right under the contract but might otherwise have a procedural right to invoke the arbitration agreement. The drafting point is very short and relates to the use of the term "third-party right" in section 9(3)(c). We referred to that in our written evidence, which is available to the committee for more detailed deliberations.

More broadly, if we stand back from the detail and look at the policy and what section 9(3) seeks to achieve, the approach is broadly consistent with the international trend in relation to moving away from privity for the purposes of arbitration. It confers the option to a third party who wishes and needs to enforce a third-party right; that party thereby becomes a party to the arbitration agreement and can enforce it. Similarly, if that party enforces the arbitration agreement or seeks to sue the party who is due to render performance, the arbitration agreement can be invoked against the third party. Again, that is consistent with the international trend. Indeed, it is consistent with the Arbitration (Scotland) Act 2010, which the Scottish Parliament passed in accordance with the general international trend.

Again, subject to the small drafting point in relation to section 9(3)(c), to which we referred in our written evidence to the committee, we are broadly in favour of the approach that has been taken to the arbitration provision.

The Convener: Thank you. Do you wish to add anything, Mr MacLeod?

John MacLeod: I have nothing to add.

The Convener: Fine. Finally, I have a question on the speed of law reform. From the evidence that we have received, it seems that some of the problems in the Scots law of third-party rights have been in existence since at least the second world war and possibly before then. On that basis, do you think that there is an argument—or would you adhere to the view—that the pace of law reform in this area has been a little too slow?

John MacLeod: We have to be careful to strike a balance between trying to go faster and ensuring that we get it right. It is true that law reform in these areas has been slow, but it is also true that although the position is suboptimal, the defects in law have not crippled the Scottish economy. I therefore think that it is better for those involved in law reform to take their time and ensure that they have thought carefully about the full implications of what they are doing, so that we do not end up

having to return to the matter in 10 or 20 years' time. That is particularly the case for areas of law that deal with big general principles, where there is value in stability as well as in modernity. We should therefore be careful about criticising those involved in law reform for being too slow, because that is liable to make them rush and we could end up doing something twice, quite slowly, instead of taking a long time but getting it right.

The Convener: Thank you. What is your view, Mr Anderson?

Ross Anderson: I broadly agree with what Mr MacLeod said. In preparation for coming to the committee, I looked at some passages in *Hansard* on the passage of the 1999 act in England, and it was interesting to note that one of the justifications for the legislation that the Government gave at that juncture was that it was to bring English law into line with what was perceived to be Scots law. The point about law reform more generally though, which John MacLeod touched on, is that it is important to get it right rather than reform for the sake of reform.

10:45

The other interesting contemporary circumstance is that, in the past 10 to 20 years, there has been considerable international development—that is to say, collaborative work on international benchmark instruments—which has allowed bodies such as the Scottish Law Commission to consider particular aspects of Scottish contract law in quite a focused way and see how we measure up.

I observe that, in so far as the Parliament is considering reforming the law, it is not alone in that regard. One can look, for example, to France, where the famous wee red book, the "Code civil", which has been in force for 200 years, had one of its most fundamental reforms in October. All that reform was in contract law. Scots law is not alone in considering such matters right now.

The faculty broadly welcomes the fact that the Parliament is now seriously considering the good work that the Scottish Law Commission has done on those focused areas. We encourage the Parliament and the committee in that consideration.

Stuart McMillan: Are you aware of any other countries that are considering the SLC's recommendations to the Parliament and whether to adopt the measures that are being introduced in Scotland?

Ross Anderson: The UNIDROIT principles of international commercial contracts are one of the standard benchmark instruments—UNIDROIT is an international body for the unification of private law and is based in Rome. The last edition of the commentary on the third-party rights principles made interesting reference to the reforms that were proposed. At that stage, the reference was to the discussion paper that the Scottish Law Commission had produced.

We are fortunate that the quality of the work that the commission has done in recent years is such that it is internationally recognised. Whether the bill will influence developments elsewhere is difficult to say. There are always local differences of approach to the formulation of legislation. The continental approach is normally to have much shorter, concise provisions, for example. However, the development that one sees in the Scottish Law Commission's work and the bill is a more collaborative one of developing measures in tandem with international consensus.

The Convener: Gentlemen, thank you for your evidence and for placing the bill in the context of Napoleonic law and other law in your final comments. We are grateful to you both for taking the trouble to come through to the Parliament and we wish you a safe journey home. If, on your way home or subsequently, anything occurs to you that you wish to add, please feel free to let us know. In the meantime, I express our grateful thanks for your help.

I suspend the meeting briefly to allow the witnesses to leave.

10:48

Meeting suspended.

10:50

On resuming—

The Convener: The next panel of witnesses to provide evidence on the Contract (Third Party Rights) (Scotland) Bill are representatives of legal firms. I welcome Kenneth Rose, a partner at CMS Cameron McKenna LLP; Karen Fountain, a partner at Brodies LLP; Jonathan Gaskell, a legal director at DLA Piper; and Karen Manning, a senior associate at Burness Paull.

My first question is about alternative approaches and putting the common law on a statutory footing. The bill team and the Scottish Law Commission have indicated that case law is unlikely to develop quickly enough to deal with the problems that have been identified with the law and that statutory rules are needed. Do you agree with that statement?

Karen Fountain (Brodies LLP): I agree that that is unlikely. When we advise a client, we cannot recommend that they take a course of action that will only become certain if they follow it through to the Supreme Court. That is not a

credible proposition. If we are trying to achieve, with confidence, a third-party right with some flexibility in it, which is where we have a problem with the current law, we tend to use a workaround. With a workaround, in the event of a dispute, there will not be case law on third-party rights; there will be case law on something else. Therefore, case law will simply not develop.

Jonathan Gaskell (DLA Piper): Lawyers tend to be quite risk-averse creatures and we do not like to advise clients in areas of law that are not particularly certain. There is no recent case law in this particular area of common law, so there is a lot of uncertainty. Institutions and businesses do not like uncertainty and that is one of the reasons why there is no reliance—in general terms and certainly not in construction, which is my sector—on third-party rights under the common law. For that reason, the bill is a good thing: it codifies the existing law and gives certainty. Businesses and individuals who work in industry like certainty.

The Convener: Excellent. Does everyone share that view?

Kenneth Rose (CMS Cameron McKenna LLP): The challenge for Scots law as a whole is that, with a common-law system, we are very dependent on people having an inclination to take a case to court and pursuing that case right up to the Supreme Court, as Karen Fountain touched on. Given the size of our jurisdiction, there are challenges in how quickly that process can move the law. I speak as a corporate commercial lawyer, rather than one who specialises in construction, and a lot of the relationships are governed by extraneous English law—even in Scotland, between two Scottish parties. That is nothing to do with third-party rights as such, but it means that there is even less potential for case law and common law to develop the law.

Approaching the issue through a legislative process, which would be a step change, seems to be a logical way of doing things, bearing in mind that it is almost 100 years since the previous step towards change in third-party rights.

Karen Manning (Burness Paull): I whole-heartedly agree with everything that has been said. I am also a construction expert and I have never come across the use of the JQT principle to confer third-party rights on a person. Although my experience is specific to construction, I am pretty confident that that position is not unusual for lawyers in Scotland today. It seems to be generally accepted that JQT is not fit for purpose.

The Convener: Thank you. That is clear and conclusive, which is welcome.

Alison Harris: My questions are similar to the ones that I asked the witnesses from the Law Society and the Faculty of Advocates. You touched on common law, but I want to clarify something. One of the main criticisms of relying on common law is that it creates uncertainty about the scope of the law. Do you, as legal practitioners, agree with that criticism, and to what extent do you think that the position needs to be clarified in the legislation?

Karen Fountain: If we are talking about third-party rights specifically, the answer is yes. The case law got itself into a bit of confusion in the 1920s, and there has not been a throughput of cases looking at the issue to resolve that. Had there been, we might not be in this position, and the law in this area might have reintegrated itself into the general conceptual stream of contract law. However, that has not happened and it has got itself into a bit of a dead end. The way to take it out most quickly and certainly would be to put it on a statutory footing. That seems to be the way that people have gone in other jurisdictions.

The legislation helpfully codifies the law and takes it back to the basic principle that people should be able to enter into whichever contractual and promissory rights they want to enter into, as long as they write it down. The bill is effectively taking us back to the Ronseal moment: the contract should do what it says on the tin. At the moment, you cannot be confident that that is the case, and you need to be confident. If it is important enough to draft the contract, it is important enough to be confident that that will work. There is a general practice of workaround, which is not helpful, because if you try to achieve something indirectly, rather than simply writing down that "X, Y and Z will be the case," there will usually be additional ramifications that you do not necessarily want. One way of dealing with third-party rights in the types of contracts that I deal with is to interpose a trust for the benefit of third parties, but that is not always exactly what you want to achieve. It brings in fiduciary entitlements that you might not wish to be there, and it muddies some of the conflict positions. It is much better to take it back to the original, basic principles of party autonomy.

Alison Harris: Does everyone agree? I see that the other witnesses are nodding.

Given that the bill seeks to provide greater clarity, do you think that its provisions are clear and that they resolve some of the uncertainty associated with the current law?

Jonathan Gaskell: Yes.

Karen Manning: Yes.

Kenneth Rose: Yes.

Alison Harris: Thank you.

The Convener: That is the collective view. If there is anything that the witnesses would like to

discuss, now is the opportunity, otherwise I will take it that you are all happy with that.

Kenneth Rose: You have to be careful with the expectations of any legal reform. You need to guide it through a sensible mid-course. The bill represents a step change. You are doing something quite fundamental, but that is not a reason not to make the change or to explore the reactions. When the 1999 act came in in England, people did not know quite how they would react to it—I know that the committee is to hear evidence on that. You have to take a decision and choose a sensible mid-course that is not overly complex, although that is always in the eye of the beholder. What looks relatively simple to us lawyers can appear quite complex to people who are not lawyers, but to me the bill looks like a sensible course to take. It is relatively straightforward, compared with what we have at the moment.

Stuart McMillan: The provisions in the bill set out the default position in general terms, and contracting parties are free to make express provisions to the contrary. Do you agree with that approach?

Jonathan Gaskell: I completely agree with that position. It is important that we do not undermine the essential freedom of parties to contract in such manner as they would like, provided that they are not doing it in an illegal way. An example that I raised in the Scottish Law Commission paper was the ability to raise defences, so that the counterparty that is being sued by the third party can raise any defence that it has against the other party to the contract, provided that it is relevant to the claim by the third party. The point that I made was that, as far as collateral warranties are concerned, certainly in the construction industry, that would not be sufficient. You would generally want the ability to exclude any commercial issues between the contracting parties, in so far as a third-party claim is concerned.

Such commercial issues would generally be relevant to a claim by a third party, but because market practice is to exclude them—certainly in relation to collateral warranties—you would want to do something similar on third-party rights, so you would need that basic reservation to do as you saw fit in the contract, provided that it was sensible and not illegal. I therefore agree entirely with the approach in the bill.

11:00

Karen Fountain: I agree. In our initial submissions, we said that it is quite important that there is an ability to contract out of the right to rely provisions, as regards amendments. I often deal with very long-term contracts that might run for 10 or 12 years, and the parties' ability to make on-going finessing changes as they go along is very important.

For some types of clause, it is just not viable for the parties to grant a third-party right where they cannot then amend the agreement if someone has relied on it. It could give rise to difficult questions—for example, "What is reliance?" If the provision is something like an exclusion of liability or an indemnity, a difficult question arises, which is, "At what point did you rely?" Would it be at the point when someone did the thing and it went wrong, or at the point when the claim arose? It is too uncertain. In those situations, you would often want to provide in the contract that any amendments would simply require the consent of one person, who perhaps represents a constituency, and that the others would have to go with that. As long as it is clear on the face of it that that is the position, people should be able to contract on that basis.

Karen Manning: I too agree that the bill provides a good balance between flexibility on the one hand and certainty on the other. Party autonomy is key, and there should be an ability to contract out of that flexibility to alter third-party rights—for example, under sections 4 to 6—if the commercial circumstances require that.

Stuart McMillan: Section 2 of the bill abolishes the irrevocability rule so that contracts granting third-party rights can be cancelled or modified. Do you support the abolition of that rule?

Kenneth Rose: Yes—I cannot speak for everyone, but I support its abolition. The approach that was taken in the 1920 Carmichael case was unfortunate. It may well have applied to the equities of that particular case, but the long-term effect was to create—contrary to what some of my colleagues have said—an inflexibility that has prevented or hindered the use of the JQT principle. Anything that makes the approach more flexible and goes back to the basic principle of two or more parties contracting with each other and voluntarily agreeing a set of obligations and rights would make our legal system more attractive and more user-friendly for individual parties.

Stuart McMillan: Sections 4 to 6 of the bill prevent the contracting parties from modifying or cancelling a third-party right. Do those sections provide the right balance between the rights of contracting parties to change their mind and the rights of third parties?

Karen Fountain: The legislation provides scope for contracting parties to contract out of those reliance provisions, provided that that is made clear to the third party, and that will ultimately give sufficient flexibility. It will likely mean the development of standard form clauses that indicate which bits of the legislation will apply and

which bits will be contracted out of, which should give everyone the certainty that they are getting the mix that they want.

The Convener: I declare that I have an interest.

John MacLeod touched on aspects of agricultural law earlier. Given that you are in front of us, I ask you to say how the bill might have a bearing on agricultural law. As I said, we want to make the best law possible, and agricultural law has been the area in which this Parliament has fallen short. Karen Fountain talked about 10 to 12-year contracts, but in agricultural law many contracts go on for generations. Do you have any comments to make on that?

Karen Fountain: I speak from a position of having no expertise in agricultural law, but, as the owner of a field, some interest. [*Laughter*.] I would say that the bill takes the concept of contract law back to its roots in the expression of intent and agreement. That is a helpful tool, and it should be a helpful tool across any industry. It is helpful to have the ability to write down what one wants to happen, and to have it happen without having to comply with a particular technical requirement that we might not naturally assume would be required.

In any industry where there is a tendency to disaggregate relationships and subcontract—we see that happening in agriculture; there is a lot of agribusiness and a lot of subcontracting on farms between different service providers—there seems to be a bit of a natural home for multiparty relationships, so the bill could be a useful tool in that regard.

The Convener: Thank you. Does anyone else want to venture into that area of law?

Jonathan Gaskell: Sorry, convener. We all have our areas of expertise and it is difficult to step outside them.

The Convener: I understand that perfectly. Thank you. Let us move on.

Monica Lennon: Thank you. We have talked a bit about the practical problems with the current law. The witnesses heard me ask the previous panel about the proposition in the policy memorandum that

"The Bill will promote the use of Scots law".

You all seem on board with that; there seems to be a united approach. As legal practitioners, are you confident that you and your colleagues will use the law? Can you think of a situation with a client in which you would continue to use English law or other workarounds?

Kenneth Rose: May I comment first, given that I touched on the issue earlier? There is a specific point about this particular reform, but there is also the mood music around Scots law. Legal systems are in competition with one another. The position has moved on—I think that your previous panel touched on the issue—so Scots law has to win the right to be relevant to a particular agreement or situation. That is particularly the case with contractual law. We can choose English law, Delaware law, New York law and all the rest of it; there is a lot of choice, particularly in more significant commercial relationships.

The mood music is not just important in relation to specific reform—the Legal Writings (Counterparts and Delivery) (Scotland) Act 2015 has been discussed, and there are other reforms to do with requirements of writing, electronic signatures and so on. The mood music around moving the legal system forward is very important in the context of presenting Scots law as a modern form of law that people will readily use.

I would be a brave lawyer if I sat here and said that the reason for using Scots law is that we want more work for Scottish lawyers. That is not really the point. The point is that we want contracting parties in a jurisdiction to be comfortable using the natural law of that jurisdiction. There are general advantages to doing so. If we consider the advantage of using Scots law versus English law, which is the most obvious example, we find that—I would say this—the accessibility of Scots law is much greater and the cost is much less. If we encourage—not necessarily intentionally, but de facto, by not having a modern legal system that is responsive to change—the mindset that we need to default to another legal system, whether it is English law, New York law or anything else, that is the mindset that people will have.

There is a longer-term aspect to this. This is a step change in one particular area, but other changes need to be made on a progressive basis in order to present Scots law in a modern and progressive way.

Monica Lennon: How do you encourage people to behave in that way and go in the direction that you have set out?

Kenneth Rose: We practitioners need to be helped by a legislature and a reform process for Scots law that support that sort of thing. If it looks like the legal system that we are representing is behind the times, that is more difficult.

I have a bit more perspective in some respects. Some have said this half-jokingly, but it is true that, before the 1999 act, people in England compared Scots law quite favourably with English law because we had the jus quaesitum tertio principle. However, that advantage was probably more than levelled out by what happened to English law in 1999.

It is a question of reacting to change and bringing law forward in a sensible manner and in

steps to help larger commercial parties, which is probably my particular focus. I should say that everyone is affected, but the issue is more relevant at the level that I have highlighted, because for those parties the choice is easier to make and it is easier for them to say that they will use English law or that they will take their disputes to the English courts, or to some form of international arbitration or whatever. There is a need to present Scots law as a viable alternative in such situations and to ensure that it is not just locked into the non-commercial situations to which it might be more immediately relevant.

Monica Lennon: Perhaps I can open the discussion up to the rest of the panel.

Karen Fountain: I agree with Mr Rose. Having practised in England until relatively recently—I have now come back here—I can tell you that if something had a Scottish dimension it would inexorably find its way to my desk in the same way that Irish questions would inexorably find their way to my Irish colleagues. People would often come to me and say, "If this gets done under Scots law, will it work or will it be a problem?" With more multijurisdictional situations, you could say, "Yes, it's fine. There are some differences, but it will come out in broadly the same place." With that approach, you are able to take the decision on which law should be applied on the basis of more rational questions such as, "Where do I want to enforce?" or, "Where is the natural locus?", instead of saying, "That would be fine, but we need to do this little bit here, and that bit's not going to work", which artificially skews the decision.

Karen Manning: I do not think that we in the construction industry have as much of an issue in that respect. It seems to be generally accepted that if the construction project is in Scotland, the law will be that of Scotland, even without the third-party rights legislation, and that is probably because we have very established workarounds for collateral warranties. I therefore do not think that the issue is as relevant to the construction and engineering industries.

Monica Lennon: I will pick up on that point. If the position is very established and people are very much wedded to collateral warranties in the construction sector, will it be difficult to get clients to move from that?

Karen Manning: I think that it will be a challenge. I work on quite a lot of English projects, and I know that the 1999 third-party rights legislation is not used very often. Indeed, such rights are not used as often as collateral warranties are.

Our sector has had numerous discussions about why that is, and a number of issues have emerged. There are, for example, issues south of the border with the 1999 act, and I am glad to see that the bill is different in some respects. That is positive. In general, any change is difficult, and when you have such an established approach in which the standard position or market norm is to have a suite of collateral warranties, which create third-party rights, it is very difficult to say, "We don't need those now. We'll just have this statute instead." It will be a challenge, but I do not think that it will be impossible, and I whole-heartedly support the bill.

It will be key to raise awareness about the legislation, if it is passed. We need to get construction parties comfortable with using something that might look different, but which essentially creates the same protections, and to make them aware of that.

11:15

Monica Lennon: I do not want to put words in anyone's mouth, but is it your view that, broadly speaking, legal practitioners will make use of the legislation and that, over time, there will be a reduced reliance on workarounds?

Jonathan Gaskell: That is right. If you consider the experience of England—Professor Hugh Beale will talk about this in due course—you will note that it took quite a long time for practitioners and parties to take up the 1999 act. I do a lot of work in England, too. I am English qualified as well as Scots qualified. I find that the 1999 act is becoming much more prevalent and is being used a lot more for certain types of third parties, for example purchasers and tenants in the context of a construction project.

The issue around the use of third-party rights in England comes from their use with funders, who typically want to be able to step into a building contract or appointment if the project becomes distressed. Because third-party rights only confer rights, a contractor or consultant will also want the funder in effect to take over the payment obligations under the contract. It is not easy to do that using third-party rights. Funders are very nervous about using third-party rights at all.

I have been involved in large shopping centre projects, where there are dozens of tenants, and there might be about 10 people involved in the construction project. We end up with dozens and dozens of collateral warranties, which are an administrative nightmare for solicitors. They are a management distraction, they incur unnecessary legal costs and their use is bad for the environment.

The use of third-party rights in the context of this area of legislation is to be applauded and promoted. Speaking as a practitioner, if the bill

were to be passed in Parliament, I would have no hesitation in recommending to clients that it should be used wherever it could be.

Monica Lennon: What could be done to speed things up if the bill is enacted? Will it be down to you to be strong advocates for it?

Jonathan Gaskell: I think that it will be. It has to be practitioners who take it on board and recommend its use to clients. Practitioners have to be in the driving seat. As Karen Manning mentioned, it is incumbent on us to raise the profile of the legislation, if the bill is passed, and to bring it to people's attention and recommend its use. We have to be in the driving seat.

Monica Lennon: That is helpful.

I return to a point that we raised last week with the Scottish Law Commission, and which the convener raised earlier—about the "black hole of non-liability", which sounds rather scary. The Scottish Law Commission indicated that the bill would make it easier for businesses to avoid that "black hole of non-liability", which reduces protection for company groups. Do you agree with that position?

Kenneth Rose: That is a big point. I do not know whether it should be called a "black hole", but the whole idea of recognising that people often contract on a group basis, although not all the group companies are necessarily parties to the agreement, is a big one. Something that is more efficient in allowing individual group companies rights under such agreements is a good thing commercially. It will help to simplify agreements rather than making them more complex, although there are workarounds, using agency agreements and other routes.

Speaking as a corporate practitioner, I emphasise that many of the contracts that are entered into are not just binary between supplier and recipient of supplies; they can very much involve group contracting. New companies may come into a group, they may be formed from scratch, they may be acquired or they may be disposed of. Anything that is flexible and acknowledges that other companies in the group can enforce rights in certain circumstances, as negotiated between the parties, is a good thing.

Karen Fountain: Yes, I agree. As the Faculty of Advocates said, the legislation will not necessarily resolve every problem—it will resolve only those that we are able to anticipate and legislate for—but there is a current category of obvious problems with group arrangements that it will at least enable us to work with.

Monica Lennon: While I have you all here, I have a final question. In looking at this piece of work, I think that one of the challenges is that it is difficult to quantify the extent to which all that we have spoken about is a problem and who it affects. However, given that we have here people who work in construction and in the finance sector, I would like to ask what impact the "black hole of non-liability" has on your clients.

Karen Manning: We have the very established workaround of collateral warranties, which covers the "black hole" issue. Where there are collateral warranties, there is not as much of a problem. However, the bill will certainly be welcome in instances where there may be provision for collateral warranties to be granted but they do not materialise, which is relatively common.

Monica Lennon: Thank you.

Alison Harris: The Scottish Law Commission has indicated that the bill will benefit the financial services sector—for example, in relation to pensions and insurance contracts. Do you agree with that view? Are there other areas of financial services that might also benefit?

Karen Fountain: Financial products and financial services arrangements are often quite complicated. There tend to be multiple parties in them. Even for the internal mechanisms of organisations, the third-party right is a useful additional flexibility. For customer-facing products, we often have a position in which a party who enters into a financial arrangement does so in part with a view to benefiting their successors, their family and so on. Having something that we can use over and above the trust mechanism, which is a common workaround, is helpful, so I think that the bill will benefit the sector.

Kenneth Rose: The financial services sector has a lot of different aspects to it. Many of those that I come across are not customer facing but are industry-to-industry ones. At the moment, many of the commercial relationships in the financial services industry are not governed by Scots law—even those between different Scottish entities. Therefore, anything that makes the Scottish legal system appear more flexible and more modern will mean that it is more likely to be used. What the direct benefit of that is probably goes back to the question of the forum for any disputes and access to resolution. Clearly, it is easier if parties use a local system rather than one from somewhere else. It is not a very binary change: that one suggested change will not make a massive amount of difference, but it is part of what we might call a journey and a process.

Alison Harris: Thank you.

The Convener: If everyone is happy with that, we will move on to George Adam, who has questions on the bill's benefits for individuals.

George Adam: I asked this question of the previous panel as well. I know that most of you are in construction. We have mentioned all the sectors that the bill could benefit. How do you see it benefiting individuals?

Karen Fountain: Probably the biggest benefit is that it takes the law back to the concept that, if we want to write down that someone will benefit a third party in a particular way, we can do that without having to go through conceptual loopholes as to whether that is irrevocable or not. It should reinstate the concept of party autonomy. If we look at the situation of private individuals, we can see that private contracts are often put together without the benefit of a lawyer or with limited advice; they may be family arrangements. People can have more confidence that what they have written down will work, which has to be a good thing.

Jonathan Gaskell: Anything that sets out the law in clear terms that individuals and businesses can understand is to be applauded. As we have said, the bill strikes the right balance between protecting the rights of individuals and protecting the rights of counterparties. It is good that it is clear and easily understandable, which is the ideal position to achieve.

George Adam: I have a totally random supplementary question. Mr Rose, you have mentioned New York law twice, and it was also mentioned by the previous panel. Is there a particular reason why you mentioned it?

Kenneth Rose: I do not have the statistics, but I suspect that New York law is one of the most widely used legal systems in the world. New York law and English law are the two most recognised international commercial legal systems—they are not really international, but they are used internationally for large funding commercial contracts and arrangements. I would not overemphasise the use of New York law in the context of Scotland, but it is used. It is very much more relevant to international situations, where there might not be a natural legal system, so a system must be picked from among a number of systems. The New York system is the most obvious US system and it is probably the centre of legal activity in the US, which is why I picked it as an example. New York and English law are probably the two most obvious examples in that category. Scots law is not in that category—it is occasionally used internationally but, for a variety of reasons, it is not seen in the same way as those other jurisdictions.

The Convener: I have a question on arbitration. The previous panel had specific comments on section 9, which allows arbitration agreements between contracting parties to operate in respect of third-party rights. Do you have any specific comments on arbitration and in particular section 9?

Karen Fountain: It is a good idea. Ultimately, if you introduce a third party into a contract, you do not want to introduce a possibility for different dispute resolution mechanisms. When something goes wrong, it often goes wrong in a complicated way. Potentially, the parties to the contract, as well as the third party, will be involved in a dispute. You do not want to have different forums for dealing with that. If you have chosen arbitration, you really want to know that you can pull everything into the same arbitration, for confidentiality, cost and case management reasons.

The Convener: Is that view shared universally by the witnesses?

Karen Manning: Yes.

Jonathan Gaskell: Yes.

Kenneth Rose: Yes.

The Convener: Finally, I have a question on the speed of law reform. From the evidence that we have received, it seems that some problems in Scots law relating to third-party rights have been in existence since the second world war. On that basis, is there an argument that the pace of law reform in this area has been too slow? You have heard the question before, so what do you think?

Kenneth Rose: As with a lot of things, expectations are changed. People now expect the law to change. As someone said earlier, most lawyers are very conservative in many ways. We do not necessarily want change, which means that things are less predictable. However, expectations have changed. A common-law system based on case law will progress slowly in certain areas if there are not many cases in those areas. That is part of the reason for the slow progress on what is a very finite point of law. However, I do not think that the Scots legal system as a whole should beat itself up about its lack of reform. The right way to address the issue is for the Law Commission to look at it and to develop modern legislation along the lines that it has done. That seems to me to be the right thing to do.

Karen Fountain: I agree that the bare bones of the system are fine. Over time, friction points periodically emerge where things have either not moved fast enough or moved too fast in the wrong direction. Addressing those in a measured way is probably the best approach. It is best done in the round, with careful consideration. I agree with Kenneth Rose that choosing the right legal system is a competitive business, so it is important to keep an eye on what everybody else is doing.

That is a question that we are asked. If an international organisation is coming to Scotland and replicating its business model, it will get out all

its old contracts, whether they were written under New York law, English law or French law, and ask, "Can we be confident that we can do exactly the same thing?" That is what they want to do, because they are replicating their business model. You want to look at what people can do elsewhere and make sure that you are allowing people the right tools to do those things.

The Convener: Excellent. If there is nothing further that anyone wishes to add, I thank Kenneth Rose, Karen Fountain, Jonathan Gaskell and Karen Manning for giving of their time to give evidence to the committee today. We are grateful to you for doing so. As I said previously, if anything occurs to you subsequently, please let us know, and we will be very grateful for any further views or advice that you can give us. I wish you a safe journey home on this snowy day, and thank you for coming to help us today.

11:31

Meeting suspended.

11:33

On resuming—

The Convener: The final witness today is Professor Hugh Beale from the University of Warwick. He reviewed the effectiveness of the equivalent legislation in England and Wales and therefore brings an interesting perspective to today's evidence.

Professor Beale, welcome to the Scottish Parliament. Thank you very much for taking the trouble to come and talk to us. I will begin by questioning you, and after that we will move to other committee members. Will you explain the background to the 1999 act and the reasons why it was introduced in England and Wales?

Professor Hugh Beale (University of Warwick): Thank you very much, convener. It is an honour to be invited to talk to the committee.

In England, we had no jus quaesitum tertio, which meant that someone could not acquire rights under a contract to which they were not a party. Sometimes, there were simple cases in which people did not realise that there was a problem. That goes back to the question that we just had about the benefit to individuals.

The committee might have heard of an English case called Beswick v Beswick. It was a simple case in which a man who owned a coal business wanted to retire and sell it to his nephew. The nephew could not afford to pay cash, so the agreement was that he would pay his uncle the princely sum of £6 and 10 shillings a week for the rest of the uncle's life and, thereafter, £5 a week to his widowed aunt. However, after the uncle's death, the nephew stopped paying and it was held that the widow had acquired no rights under the contract because she was not a party to it.

I suspect that the answer might have been different in Scots law, because it might have been arguable that the widow had some kind of right. However, that illustrates how people got into difficulties because they simply did not realise that there was a problem. In that case, the House of Lords was able to find a solution. Although the aunt had no rights, she was the administratrix of her late husband's estate and, in her capacity as administratrix, she was able to get an order of specific performance—the English equivalent of an order of specific implement—against her nephew that ordered him to pay her £5 a week in her other capacity as the widow. It all ended happily ever after, except that they had to go to the House of Lords to achieve that. That is the sort of situation that arose.

So far, we have been talking mainly about contracts that are made between sophisticated parties with legal advice, in relation to which English law developed many workarounds to achieve third-party rights. However, that involved a lot of difficulty in many cases, and the devices were not always reliable. There was therefore a long-term move to get our law changed. Back in 1937, the Law Reform Committee recommended that the doctrine of privity of contract should be abolished, and I believe that legislation was beginning to go through Parliament when the second world war broke out, and nothing was done thereafter.

For many years, judges in particular called on Parliament to do something. At one stage, they even threatened to do something themselves if Parliament would not get on with it. However, as members will know, the matter was referred to the Law Commission, and the 1999 act was an attempt to address a long-standing complaint that English law was seriously defective—much more defective than Scots law is at the moment.

The Convener: Are you saying that the problem was identified before the second world war and that it took until 1999 to resolve it?

Professor Beale: That is correct, convener. It is embarrassing, but that is what happened.

The Convener: Thank you for those introductory comments. If no one else wants to ask Professor Beale about that, I invite Mr Adam to ask his question on the impact of the 1999 act.

George Adam: Professor Beale, in 2010, you carried out a review of the operation of the 1999 act. How did you do that? What did you go through and what were your conclusions?

Professor Beale: I am afraid that the review was very informal, because it is difficult to establish what use is being made of legislation—I think that Jill Clark made that point to the committee last week. It is difficult to put figures to anything, because that would require an enormous survey of every law firm to find out how many clients had ever asked for contracts that were to benefit third parties and so on. Although that could in theory be done, it would be extremely time consuming and costly, and it might run into problems with client confidentiality.

All that I did—at the request of my colleague Andrew Burrows, who was the law commissioner responsible for producing the report for the Law Commission and seeing the legislation through—was a 10-year review of the act, and it seemed sensible to try to find out the extent to which it was being used. I contacted people with whom I had had dealings when I was at the commission and asked for their opinions, and I got a certain amount of useful information. Nevertheless, the process was difficult.

Let me start with construction law. The committee has been told about the use of collateral warranties and the problem of the black hole of non-liability. When I looked at the standard forms of building contract—we have the Joint Contracts Tribunal standard forms of building contract, which are equivalent to the Scottish forms—I found that they are being redrafted so that there is provision for the client to demand either that the contractor give collateral warranties, which you have discussed, or that the contractor agree that third-party rights will come into existence.

That is on paper, but we do not know how often the collateral warranty approach is used and how often the third-party rights approach is used, or whether parties sometimes go for both at the same time, which would be theoretically possible. It is quite hard to establish how often the third-party rights approach is used in practice in construction, but I am told that it is very much used in other areas.

I will give the committee a couple of examples. One of the big problems has been protecting third parties from potential liability in tort. For example, if there was a contract between company A and company B, and if company B was afraid that its individual officers or its employees might be sued by company A if something went wrong and it therefore wanted to exclude the liability of those officers or employees, it was possible to do that through rather elaborate schemes that used agency or circles of indemnities. However, it is now easy and—I am told—common simply to provide in contract that one party shall have no right of action against named individuals.

Another context in which very much the same sort of thing happens is where contracts are made, in effect, on behalf of a group of companies. For example, someone might contract for services to be provided and want to protect the different groups in the companies that are providing the services through the work being subcontracted out to them. That confers a negative benefit of protection on a third party but, equally, it might be preferred to confer positive benefits. For example, indemnities might be offered to officers or employees of a company or to other members of the same group of companies, which is all much easier to do now. I am told that that is done fairly regularly, but I am afraid that I cannot give the committee chapter and verse on that, because my inquiries were simply answered by, "We do this regularly."

George Adam: You referred to the use in some cases of both collateral warranties and third-party rights. Is that peculiar to the construction sector?

Professor Beale: I think that collateral warranties are most used in the construction sector, but I suspect that they are being used in other fields as well, such as the oil and gas sector, which the committee discussed last week. There is the problem of multiple actors in that industry, but I am afraid that I cannot say whether collateral warranties were or are used because of that. However, I am pretty sure that third-party rights are being used in that sector when a contract is subject to English law.

George Adam: I got the distinct impression earlier from Karen Manning, who spoke for the construction sector, that it works around things by using collateral warranties. At last week's meeting, I asked whether the big corporate legal firms will just continue with their workarounds.

Professor Beale: I am sure that they will. As one of the earlier witnesses said, lawyers tend to be rather conservative and stick with the things that they know. Some clients are rather conservative, too, and like the piece of paper that they have always had. However, I have discovered that more and more standard forms are allowing third-party rights as an alternative to collateral warranties. I suspect that that would not be happening if there was no take-up, which means that some people are using third-party rights. However, we have no litigation on that and it is difficult to establish figures.

I have no idea whether collateral warranties and third-party rights are being used at the same time, but I suspect that that might be the case. The forms provide for one or the other, and I imagine that using one or the other is more usual.

George Adam: Thank you.

Monica Lennon: Good morning, Professor Beale. I am interested in what you have said so far. The Scottish Law Commission's report indicates that there have been few cases on the 1999 act and that there has been a lot of academic criticism of the act. Will you expand on the reasons for the lack of case law and the academic criticism and on why lawyers are excluding application of the act from commercial contracts?

11:45

Professor Beale: The criticism of the act is that it ignores the doctrine of consideration, which you in Scotland are fortunate never to have been cursed with. In English law, there are two reasons for saying that somebody who is not a party to a contract cannot sue on it. One is the argument that, if there is a contract between A and B where A promises that they will do something for C, the promise is made to B, so why should C be able to sue on it? The other reason is that, for there to be a contract in English law, there has to be some kind of exchange—in other words, B has to provide something in exchange for what A promises. Normally, it is B who provides that, not C, who is the third party.

Most of the academic criticism has been that the reforms ignore the problem of consideration. I have to say that many of us do not agree with that criticism, because there is always a contract for good consideration between A and B. If the parties intended to confer rights on C, the fact that C is not providing any consideration seems irrelevant. In any event, that would not arise under Scots law, because it has no doctrine of consideration. Be grateful for that; I would not preserve that doctrine if it were my world.

Monica Lennon: It is useful to get that clarity. In last week's meeting, which you might have listened to or read about in our *Official Report*, the Scottish Law Commission indicated that use of the 1999 act has increased only slowly. Do you agree?

Professor Beale: There has not been much litigation on the act. There have been a number of cases but, as Professor MacQueen said last week, it is hard to know whether that is because everything is so clear that there is no problem or whether everybody is so scared of the act that they do not want to litigate over it. My impression is that there have been no major problems so far and that people are coming round to using the act.

There are examples from IT. I am told that it is common for an IT contract to be made between the IT provider and one company in a group, but the service is to be provided to all the other companies in the group. I have not seen any litigation arising from such a situation, which makes me hope that it is all relatively clear.

Of course, a problem arises only if something goes seriously wrong with a contract. It might just be that, by good fortune, nothing has yet gone wrong. I am not aware of any major problems being thrown up by litigation and I am not aware of any other major problems with the act.

Monica Lennon: We raised with the two previous panels the point that the policy memorandum expresses hope that there will be a shift to using Scots law. We have heard from a number of legal practitioners today. Are you confident that such a shift will happen in time or do you think that there will still be a reliance on and a preference for using English law, other law or collateral warranties?

Professor Beale: I have certainly heard that English law is sometimes being used when it would be more natural to use Scots law, simply because of the third-party rights issue, but that is only anecdotal evidence and I do not know how frequently that is happening. It seems to me that it can only help the position of Scots law if it is kept up to date. I am not a Scots lawyer, but my reading of the Scottish Law Commission's discussion paper and report is that there are quite serious problems at the moment—particularly problems of uncertainty. It can do no harm—it can only do good—to get rid of them. The bill seems to do a very good job of that.

Monica Lennon: That is helpful. Thank you.

Alison Harris: Good morning, Professor Beale. Can any general lessons be learned from the implementation of the 1999 act and are there any ways in which the Scottish legal establishment can ensure that the uptake of the new rules happens more quickly than seems to have occurred in England and Wales?

Professor Beale: I find that hard to answer. It is a good question but it is difficult to answer, because one does not really know whether the uptake has been slow or what one might expect.

I was told immediately after the act was passed that its only effect would be that people would go through their bank of standard forms and include a clause in every one that said, "The Contracts (Rights of Third Parties) Act 1999 shall not apply." Most standard-form contracts still contain such a clause but go on to say, "except for the following provisions," when they want to create third-party rights.

It is interesting that people are making the position absolutely clear by excluding the operation of the act but with specific rights in favour of third parties. When, after 10 years, I

found that that was beginning to happen, I was relatively relieved.

I am not sure that 10 years is a long time for uptake by practitioners, for the reasons that were given earlier. Having found a device that works, practitioners tend to stick with it even if it is inconvenient. There is no doubt that the collateral warranty in construction is inconvenient for all the reasons that other witnesses explained, such as the fact that one may have to chase around after the event to issue collateral warranties to new purchasers or tenants of the building, whereas that could all be done at once. Forgive me, but I am not sure that 10 years—or even longer now—demonstrates a slow uptake. Uptake is gradual.

You asked what the Government could do to encourage uptake. In England, the need to educate legal practitioners was perhaps greater than the need will be in Scotland, because the legal community in Scotland is much smaller and probably more cohesive. I imagine that everybody knows what is going on, whereas that is not always true in England and Wales.

Alison Harris: What is your general view of the bill? Based on your experience of the 1999 act, do you think that the bill will improve the law on third-party rights in Scotland?

Professor Beale: The bill is definitely an improvement and I support it whole-heartedly. The only slight point that I noted as I read it on the train coming up yesterday was that, in some places, it is more sophisticated than I would have made it, but English lawyers are rather crude compared with Scots lawyers. For example, some of the provisions about when the right remains revocable even though the parties did not say that it would be form a neatly graduated system. We have a simpler system that says that, once the right has been accepted, it cannot be changed unless a provision in the contract allows that.

We have adopted a cruder system, but there is nothing wrong with having a sophisticated system, provided that it is clear and understood. By and large, the bill is pretty clear. I am sure that everybody can make slight tweaks of improvement, but it is a good bill.

Alison Harris: That is good. Are there any areas in which the 1999 act provides a better solution to the problem of third-party rights than the bill does? Alternatively, are there any areas in which the bill is an improvement on the 1999 act?

Professor Beale: That is difficult to answer. Despite the differences in wording, the differences in substance are small. Just occasionally, I prefer the English wording because it is a bit clearer.

The principal example is in the opening provision, in section 1(1)(a) of the bill, which states:

> "A person who is not a party to a contract acquires a third-party right under it where—
>
> (a) the contract contains an undertaking that one or more of the contracting parties will do, or not do, something for the person's benefit".

I gather from the explanatory notes that that is meant to be read as saying that the contract—in most cases, the document—will indicate that something is for the benefit of the person, but I am not quite clear whether one might say that a provision does in fact benefit somebody, although they are not mentioned in the contract. It is that level of minor wording that I am talking about. Otherwise, the bill does an excellent job.

I see no major differences from the law that applies in England, although there are one or two differences. For example, in England we have prevented a third party from relying on the Unfair Contract Terms Act 1977. If party A promised the third party that it would take reasonable care and then limited its liability for having done bad work to repairing or replacing the work, that might fall within section 16(1)(b) of the 1977 act—I think that that is the section that applies to Scotland, though I am never quite sure of my numbers. In England, we simply said that such a term cannot be challenged by a third party.

It is six of one and half a dozen of the other. My initial reaction is that I prefer the English solution, but it is arguable either way and I do not care to second guess what Professor MacQueen and his colleagues have recommended. They are very good lawyers and I have no reason to doubt their judgment.

Alison Harris: Thank you. I appreciate your answers.

The Convener: Notwithstanding your deference to Professor MacQueen, which we share, since we are endeavouring to make absolutely the best law that we can, and given your review of the 1999 act and some of the shortcomings that you have acknowledged and pointed out, are there any errors that you foresee us making? We want to produce the best possible bill.

Professor Beale: No, I certainly would not say that there are any mistakes. There are one or two places where I think that the drafting could be clarified a little, but that is very much at the level of detailed drafting. I think that it would be better to feed in suggestions in writing later on, if I may.

The Convener: Would you?

Professor Beale: It is just a question of how easy it is for somebody to read the act and understand what it is saying. That is always a

problem in legislation. I am sure that you are aware of the Consumer Rights Act 2015; it was supposed to make the law much more accessible to consumers, but I find it very hard to read. It is not an easy task.

The Convener: We will leave the Consumer Rights Act 2015 to one side for the moment. We would, nonetheless, be grateful if you were to correspond with us on any area where you think that we could benefit from your experience and wisdom.

Stuart McMillan: Do you agree with the general policy in the bill that the rules should normally be default in nature, so that they can be contracted out of?

Professor Beale: Yes, I do. It is important that the rules should be default rules in both directions, so that on one hand the parties should be able to reserve the right to vary or even cancel the third party's rights, but on the other hand they should be able to create rights that cannot be cancelled. Although I do not have any concrete examples from real life, there might be situations where the third party needs to know from the outset that a right is totally irrevocable and unvariable, so that it can plan its own affairs. For example, if it is to have a right under an insurance policy taken out by another company in the group, it should not have to worry about whether it has relied on it; it should simply be able to say, "That is irrevocable; that is fine." It is very important that there should be default rules in both directions.

12:00

Of course, it is just possible that sometimes a contract involving third-party rights might be made in favour of a consumer. Then, of course, the unfair terms in consumer contract legislation—now part of the Consumer Rights Act 2015—would cut in. A clause that seemed to be unfair, in allowing the third party to have their rights taken away, could be challenged.

My only concern is that the clauses that allow a party to vary the third-party rights might not always be understood by someone who is not a consumer but who is rather consumer-like, that is, the very small business. That is part of a much broader problem, which you could not possibly tackle in this bill, about the need to protect very small businesses. I still believe that we need legislation to protect very small businesses from unfair terms, as the joint report of the English commission and the Scottish Law Commission recommended back in 2005. Such legislation does not exist at the moment. However, that is a much more general problem; the answer to your question is that it is absolutely right that the rules should be only default rules.

Stuart McMillan: On a point of clarification, you said that the very small business is not a consumer but is "consumer-like". I am not a lawyer, so will you explain that?

Professor Beale: Let me give an example. We have had quite a lot of problems in England—and I believe also north of the border—with corner shops making contracts, for example to lease a photocopier so that customers can go to the shop to make photocopies. Some terms of those leases have been very harsh. However, because small businesses are not technically consumers and the contracts are technically for the purposes of the business, they are not protected by the unfair terms directive or the legislation that implements it. However, they have no better understanding of what they are doing and no greater bargaining power, as it were, than an individual consumer has. That is what I mean by "consumer-like"—they are so small that, in effect, they do not have any expertise and they are probably making relatively low-value contracts; they are not able to take legal advice each time, as the cost is disproportionate. I hope that that is clear enough.

Stuart McMillan: It is. Thank you for that.

Sections 4 to 6 prevent the contracting parties from modifying or cancelling a third-party right. Based on your experience of the operation of the legislation in England and Wales, do those sections provide the right balance between the rights of contracting parties to change their minds and the rights of third parties?

Professor Beale: Yes, I think that they achieve a very sophisticated balance. This is the area where our provision is a bit cruder—it is possibly easier to understand but it is not as sophisticated. Whether you care to be sophisticated, or clearer but cruder, is a matter of judgment. That was one of the areas that I put pencil marks against during my train journey, but by the time I got to Carlisle I realised that there was nothing wrong with the bill—it was just that my approach is slightly different. I support those sections.

Stuart McMillan: Have you had discussions with other legal professors about the Scottish bill, to gauge whether they feel that the bill is positive?

Professor Beale: I am afraid that I have to declare an interest. I spent last night having dinner and staying with Professor MacQueen, so I have been thoroughly briefed. [*Laughter*.] I have not heard recently from any professor other than him.

Stuart McMillan: No problem; thank you very much.

George Adam: Did Professor MacQueen give you the money for your pencil eraser? [*Laughter*.]

The Convener: We will assume that you have had the bill fully explained to you in that regard.

In your answer a moment ago to Stuart McMillan, you spoke about the need to protect small businesses following the 2005 joint review. Would such provision fit more elegantly into another piece of legislation, or should it be a stand-alone piece of legislation? Given that you have generously undertaken to correspond with us about the improvements that we might make, will you add a note on why that issue should be addressed, from a small business perspective? In the meantime, will you say why the matter needs to be addressed?

Professor Beale: It is simply that, whenever there are default rules that can be varied by the parties, and there is a situation where a contract appears to confer a benefit on the third party but is subject to a variation section, there is always a danger that the third party will observe the good bits and not be aware of the sections that cut down its rights. That danger exists for small businesses in particular, because they are not likely—or are less likely than larger businesses—to read and understand the contracts that they are signing. That is part of a more general problem; it is not a problem that could be addressed in the bill.

That was the only concern that I wanted to express in response to Mr McMillan's question, because he was asking me whether I thought that it was correct that there should be default rights. My response is that I absolutely think that there should be default rights, but I hope that contracts will be drafted in such a way as to make clear to the third party when their rights are subject to variation. As I said, that is a bigger question; it is not a matter that could be sensibly dealt with in the bill. It would be possible to say, "Every section allowing variation should be prominent", or something along those lines, but it would be rather odd to try to do that in this bill alone.

The Convener: I was not suggesting that. Nonetheless, thank you for your considered view on the issue.

We will move on to arbitration. What is your view on section 9, which allows arbitration agreements between contracting parties to operate in respect of third-party rights?

Professor Beale: I am afraid that I must apologise to the committee, because I do not have any information about the application of section 9. I am not aware that it would give rise to problems. It seems to be a perfectly sensible arrangement. However, as I am sure that you know, it was all drafted after the Scottish Law Commission had produced its report. I was a little bit involved—I was a consultant of sorts—at the report stage, but I was not involved in the discussion of arbitration and I do not have any information about its use. I am not aware of any problems, but that is as far as I can go.

The Convener: The final question is about the speed of law reform. Your answer to my initial question rather gave away the game, in that you think that reform has been a little too slow. Do you have anything further to add in that regard? How should we proceed from here?

Professor Beale: It is time to put this bill through Parliament. Doing so would give you a much more creditable record than we have in England. We started work in this area in 1937 but did not achieve anything until 1999. Arguably, it is true that Scotland has had problems since 1920 but, in reality, the problems have emerged only much more recently. That it has taken a few years to get things done is nothing to be ashamed of, but now is the time to bring Scots law up to date.

We have, to some extent, copied the Scottish approach; maybe you are now going to follow us. However, in doing that, you would be very much following a model that has been adopted in many jurisdictions, in one form or another. The bill is an excellent proposal and I support it whole-heartedly.

The Convener: Thank you very much for those supportive comments. We are hugely indebted to you for coming today to give us evidence on the topic. I wish you a safe journey home.

Professor Beale: It has been a privilege and a pleasure.

The Convener: We look forward to receiving your further reflections on what we have discussed—and, indeed, reflections on any other matters that we have not discussed and that would enhance our scrutiny of the bill.

I suspend the meeting briefly to allow Professor Beale and others to leave.

12:10

Meeting suspended.

12:13

On resuming—

Instruments subject to Negative Procedure

The Convener: Item 4 is consideration of instruments subject to the negative procedure. No points have been raised by our legal advisers on the following six instruments.

Non-Domestic Rates (District Heating Relief) (Scotland) Regulations 2017 (SSI 2017/61)

Protection of Seals (Designation of Haul-Out Sites) (Scotland) Amendment Order 2017 (SSI 2017/63)

Representation of the People (Absent Voting at Local Government Elections) (Scotland) Amendment Regulations 2017 (SSI 2017/64)

Local Governance (Scotland) Act 2004 (Remuneration) Amendment Regulations 2017 (SSI 2017/66)

First-tier Tribunal for Scotland Housing and Property Chamber (Procedure) Amendment Regulations 2017 (SSI 2017/68)

First-tier Tribunal for Scotland Tax Chamber (Procedure) Regulations 2017 (SSI 2017/69)

The Convener: Is the committee content with the instruments?

Members *indicated agreement.*

The Convener: Excellent. We now move into private session.

12:15

Meeting continued in private until 12:28.

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