OFFICIAL REPORT
AITHISG OIFIGEIL

Delegated Powers and Law Reform Committee

Tuesday 28 March 2017

Session 5

The Scottish Parliament
Pàrlamaid na h-Alba

Tuesday 28 March 2017

CONTENTS

Col.

DECISION ON TAKING BUSINESS IN PRIVATE 1
INSTRUMENTS SUBJECT TO AFFIRMATIVE PROCEDURE 2
Roads (Scotland) Act 1984 (Environmental Impact Assessment) Regulations 2017 [Draft] 2
Transport and Works (Scotland) Act 2007 (Environmental Impact Assessment) Regulations 2017 [Draft] 2
INSTRUMENTS SUBJECT TO NEGATIVE PROCEDURE 3
Non-Domestic Rates (Transitional Relief) (Scotland) Regulations 2017 (SSI 2017/85) 3
Transport and Works (Scotland) Act 2007 (Applications and Objections Procedure) Amendment Rules 2017 (SSI 2017/74) 4
Little Loch Broom Scallops Several Fishery Order 2017 (SSI 2017/77) 4
Valuation Appeal Committee (Procedure in Appeals under the Valuation Acts) (Scotland) Amendment Regulations 2017 (SSI 2017/78) 4
Road Traffic (Permitted Parking Area and Special Parking Area) (Angus Council) Designation Order 2017 (SSI 2017/79) 4
Parking Attendants (Wearing of Uniforms) (Angus Council Parking Area) Regulations 2017 (SSI 2017/80) 4
Road Traffic (Parking Adjudicators) (Angus Council) Regulations 2017 (SSI 2017/81) 4
Road Traffic (Permitted Parking Area and Special Parking Area) (Stirling Council) Designation Order 2017 (SSI 2017/82) 4
Parking Attendants (Wearing of Uniforms) (Stirling Council Parking Area) Regulations 2017 (SSI 2017/83) 4
Road Traffic (Parking Adjudicators) (Stirling Council) Regulations 2017 (SSI 2017/84) 4
CONTRACT (THIRD PARTY RIGHTS) (SCOTLAND) BILL: STAGE 1 5

DELEGATED POWERS AND LAW REFORM COMMITTEE
11th 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:

David Christie (Robert Gordon University)
Craig Connal QC (Pinsent Masons)
James Rust (Morton Fraser)
David Wedderburn (Royal Incorporation of Architects in Scotland)

CLERK TO THE COMMITTEE

Euan Donald

LOCATION

The Adam Smith Room (CR5)

Scottish Parliament

Delegated Powers and Law Reform Committee

Tuesday 28 March 2017

[The Convener opened the meeting at 10:30]

Decision on Taking Business in Private

The Convener (John Scott): Good morning, everyone, and welcome to the 11th meeting in 2017 of the Delegated Powers and Law Reform Committee. Agenda item 1 is a decision on taking business in private. Does the committee agree to take in private item 5, which is consideration of the Child Poverty (Scotland) Bill?

Members *indicated agreement.*

Instruments subject to Affirmative Procedure

10:31

The Convener: Agenda item 2 is consideration of the following two affirmative instruments.

Roads (Scotland) Act 1984 (Environmental Impact Assessment) Regulations 2017 [Draft]

Transport and Works (Scotland) Act 2007 (Environmental Impact Assessment) Regulations 2017 [Draft]

The Convener: Both instruments were initially laid before Parliament, in draft, on 8 March 2017. Subsequent to that, the committee's legal advisers identified some drafting inconsistencies and minor errors in both of the instruments. Accordingly, they were withdrawn by the Scottish Government, and relaid on 23 March 2017 with the errors identified having been corrected.

No points have been raised by our legal advisers on the relaid instruments. Is the committee content with them?

Members *indicated agreement.*

Instruments subject to Negative Procedure

Non-Domestic Rates (Transitional Relief) (Scotland) Regulations 2017 (SSI 2017/85)

10:32

The Convener: Agenda item 3 is consideration of instruments that are subject to the negative procedure.

The regulations reduce the amount payable as non-domestic rates for certain properties for 2017-18. The regulations were laid before Parliament on 16 March and come into force on 1 April 2017. They do not respect the requirement contained in section 28(2) of the Interpretation and Legislative Reform (Scotland) Act 2010 that at least 28 days should elapse between the laying of an instrument that is subject to the negative procedure and the coming into force of that instrument.

Accordingly, does the committee agree to draw the regulations to the attention of the Parliament under reporting ground (j), that the instrument fails to comply with the requirements of section 28(2) of the Interpretation and Legislative Reform (Scotland) Act 2010?

Members *indicated agreement.*

The Convener: Does the committee also agree to find the failure to comply with section 28 to be acceptable in the circumstances as outlined in correspondence from the Scottish Government, published as part of our papers for this meeting?

Members *indicated agreement.*

The Convener: No points have been raised by our legal advisers on the following nine instruments.

Transport and Works (Scotland) Act 2007 (Applications and Objections Procedure) Amendment Rules 2017 (SSI 2017/74)

Little Loch Broom Scallops Several Fishery Order 2017 (SSI 2017/77)

Valuation Appeal Committee (Procedure in Appeals under the Valuation Acts) (Scotland) Amendment Regulations 2017 (SSI 2017/78)

Road Traffic (Permitted Parking Area and Special Parking Area) (Angus Council) Designation Order 2017 (SSI 2017/79)

Parking Attendants (Wearing of Uniforms) (Angus Council Parking Area) Regulations 2017 (SSI 2017/80)

Road Traffic (Parking Adjudicators) (Angus Council) Regulations 2017 (SSI 2017/81)

Road Traffic (Permitted Parking Area and Special Parking Area) (Stirling Council) Designation Order 2017 (SSI 2017/82)

Parking Attendants (Wearing of Uniforms) (Stirling Council Parking Area) Regulations 2017 (SSI 2017/83)

Road Traffic (Parking Adjudicators) (Stirling Council) Regulations 2017 (SSI 2017/84)

The Convener: Is the committee content with the instruments?

Members *indicated agreement.*

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

10:35

The Convener: Agenda item 4 is our third day of consideration of oral evidence on the Contract (Third Party Rights) (Scotland) Bill. Today we are delighted to welcome James Rust, who is a partner at Morton Fraser specialising in agricultural law.

I have the first question for Mr Rust, which is about whether there is a need for a statutory approach. 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 in the law and that statutory rules are needed. Will you outline your views on the need for statutory rules for third-party rights?

James Rust (Morton Fraser): Yes, and I will be brief. It is necessary to ensure that the law changes in an appropriate way. I am a practitioner rather than an academic lawyer in any sense, and I had to remind myself of the difficulties with the jus quaesitum tertio position, because it has become a backwater in the approach of practitioners to contract law. There are one or two specialist areas that deal with it a lot but, otherwise, it has fallen into a state of disuse because of its difficulties and uncertainty and therefore legislation is a good idea.

The Convener: Excellent. I turn now to default rules. The provisions in the bill set out the default position and contracting parties are free to make express provisions to the contrary. Will you outline to the committee to what extent you agree with that approach and why?

James Rust: I agree with the approach. It is important to give as much flexibility as possible to contracting parties to adjust and come to their own basis of understanding and so the introduction of a default position is good because it allows the necessary flexibility that parties may be seeking.

The Convener: Thank you very much.

Alison Harris (Central Scotland) (Con): Good morning. As you will be aware, there are a range of third parties in the agriculture sector—such as spouses—who benefit financially from partnership agreements that are used to run farms but who are not party to the agreements. Will you explain in more detail what kinds of third-party rights exist in the agriculture sector? What are the most important examples?

James Rust: I will try. I have given that some thought. The agriculture sector is a business sector like any other. It is typified by contracts between A and B—it is not often that you come across a C in such contracts, in whatever context that might be. That might be possible where farmland is owned by an individual, the farm is worked by a partnership and there is a contract farming arrangement that hangs off that. Consequently, we see some situations in which there are three parties with different rights attaching to them. However, more typically, it is a matter of a relationship between A and B and therefore there is no particular issue that I have come across that would mean that the change in the law would have a significant impact on farming.

Your comment about spouses who are not engaged in the partnership but who are involved in the farming enterprise is interesting. To that extent, there may well be some impact on family law situations—there have been some particularly difficult cases involving such situations.

The Convener: Before we go any further, I should declare an interest in the matter, being a farmer myself. I apologise to the committee for not having declared an interest earlier in the proceedings. Do you have any further questions, Alison?

Alison Harris: Yes, I would like to look at the impact of the current law. One of the main criticisms of the common law on third-party rights is that its scope is uncertain and another is that the irrevocability rule makes it difficult to amend or cancel third-party rights. What is your view of those general criticisms and what is the impact of those problems, if any, on the agriculture sector?

James Rust: Those problems make the law almost unworkable, because it does not give any opportunity for flexibility if circumstances change before a third party has an entitlement to operate the right that may be granted. That largely explains why it is an area that is ripe for legislative change.

Alison Harris: Thank you.

The Convener: It is potentially a problem in a growing area of the agriculture sector. You mentioned contractors and other parties in and around agricultural law. Can you expand on that point in relation to agricultural contractors and the use of contract farming instead of tenancies?

James Rust: Yes. I do not want to stray into agricultural holdings, which is a topic in itself, but the law on agricultural holdings is in a constant state of flux and uncertainty and therefore, convener, you are correct in your presumption that other forms of farming have become more popular as an alternative to agricultural holdings per se. Consequently, there are a number of contracting arrangements that can be entered into between

the farmer, landowner and a contractor or a partner for a particular season, to farm the land and get a profit off it. The agriculture sector has a number of different arrangements for working the land beyond the traditional landlord and tenant approach of agricultural holdings.

The Convener: Yes. The more one thinks about it the more areas there are, such as seasonal lets and grass-park lets.

James Rust: Yes, grass-park lets are very popular, but they have a seasonal aspect, so investment in the land is pretty minimal unless a landlord chooses to invest for whatever reason. There are several different contracts that allow the land to be worked by someone other than the landowner.

The Convener: Indeed. Is there a limit on the number of third—or perhaps you would call them fourth—parties? I am thinking of a situation in which someone who has taken a seasonal let has contracted someone to, for example, put fertiliser on that land via an arrangement that has absolutely nothing to do with the person who let the land.

10:45

James Rust: In that example, the connection between the landowner and the fertiliser spreader is quite detached. Equally, the landowner would want to know whether fertiliser is to be spread. Commonly, that would have been a matter for discussion between the landowner and the grazier, and a basis for the commercial arrangement arising from that would have been reached, with either the grazier being on a softer rent to account for the investment that he was putting into the land or the landowner making a contribution.

The Convener: Thank you. I think that we have exhausted that line of questioning.

Monica Lennon (Central Scotland) (Lab): Good morning. Unlike the convener, I do not have any specialist knowledge of agriculture or fertiliser. Nevertheless, I will ask my question.

In previous evidence sessions, the committee has heard that in many sectors—including construction, for example—legal workarounds seem to be used to get around the problems in the current law on third-party rights. Are there any workarounds that are used in the agriculture sector to grant rights to third parties? If so, what are they and what benefits and disadvantages do they offer?

James Rust: I have given that some thought—indeed, I have racked my brains—and I can honestly say that I have not come across any such workarounds that are particularly relevant to agriculture. For example, there is no standard collateral warranty that we pull out of the drawer every time that we deal with some form of new tenancy arrangement or contract arrangement. In the old days, when limited partnership agreements were much more popular than they are now, there would occasionally be a back letter of some sort, but it was usually just between the parties—in other words, there was not necessarily a third-party involvement.

Clearly, some of the bigger farming operations might well be involved in significant construction contracts. I am aware that construction has a number of collateral warranty approaches to subcontracting and that sort of thing, and, to that extent, farmers might become involved in such warranty arrangements. However, I have not been able to think of any such workarounds that are particular to agriculture and the practice of that.

Monica Lennon: That is helpful—it is a clear answer. In previous evidence sessions, we have heard that, in areas such as the construction sector, where collateral warranties are quite commonly used, clients and practitioners might be quite wedded to that approach, and we wondered to what extent the new law might be used.

The Scottish Law Commission has indicated that the bill will make it easier for businesses to avoid what it calls the black hole of non-liability, which currently reduces protection for company groups. Do you agree and, if so, will you explain what the impact of the change will be in relation to agriculture?

James Rust: I agree with that as a proposition, because I understand it. I do not think that it will have a particular resonance in agriculture, because we do not tend to operate with group companies. There are one or two substantial operations with two or three linked companies that might find themselves in that situation, but most farming operations are pretty straightforward. They are either individuals or they are partnerships although, occasionally, there might be a limited company and I suppose that you might have a trading company as a sub-company of the limited company, such as a farm shop or something of that order. You can see that there might be a relevance in those circumstances. However, for the vast majority of agriculture businesses, it is not an issue.

David Torrance (Kirkcaldy) (SNP): The bill seeks to provide greater clarity. Are the provisions in the bill clear and will they resolve some of the uncertainty that is associated with the current law?

James Rust: Yes—the bill is clear and it will resolve uncertainty. It will be interesting to see how practitioners receive it, because they have got used to the state of uncertainty and have factored

that into their practices. The bill will provide an opportunity for significant rethinking of their approaches. It will take a little time to get people to move away from something with which they feel familiar and a regime with which they are comfortable, albeit one that has its difficulties, to something new. One hopes, however, that the advantages will be perceived fairly quickly.

David Torrance: Can you give examples from the agriculture sector?

James Rust: Again, I gave that some thought, but I am afraid that I cannot think of anything that would have me rushing to the act and saying that I am going to change my styles here, there and everywhere. We are constantly reviewing and updating things, and we will have the bill as enacted in front of us when we examine our standard-form offer and standard-form leases to see whether we want to stick any reference to it into them. The act will apply across the board, in any event. The common law is to be done away with, so we will be in a new regime, come what may.

David Torrance: Will the bill improve the law on agriculture? If so, how?

James Rust: It will do so in the sense that agriculture is a commercial operation and the bill clarifies an area of law that affects commercial contracts, so there will be benefits to be had in particular circumstances. The answer is yes, in the right circumstances.

Stuart McMillan (Greenock and Inverclyde) (SNP): You said that

"the bill is clear and it will resolve uncertainty."

That being the case, could the costs of entering into contracts be cheaper in the future?

James Rust: The legislation will not have a material effect on cost because many more factors bear on cost than simply the change in the law that the bill proposes. If the legislation reduces the side documentation that is introduced in some circumstances—I come back to the construction industry as an example—through necessary rights being built into contracts, that might speed things up, which may reduce costs, because so much cost is incurred simply in the time that is taken to get things done. I hope that simplifying the process will take some cost out of the procedure.

The Convener: There has been a suggestion that the new legislation might not be taken up in other sectors. Will parties in the agricultural sector use the new rules in the bill or is there a risk that they will continue to use existing legal structures, such as they are, to set up third-party rights?

James Rust: That is a risk that I have probably touched on already. It might, therefore, not be a bad thing to have some fairly clear direction from academics and, possibly, the Law Society of Scotland on the positive applications of the bill and its benefits. As practitioners, we are always hugely busy and it is a constant challenge to open our minds to something new, such as the bill. Therefore, the more encouragement we can get that there is benefit to it and that it is not just more legislation for legislation's sake, the better.

The Convener: Thank you very much.

Mr McMillan—over to you.

Stuart McMillan: On the latter point about the benefits of the bill, obviously much, but not all, of the focus has been on the sectors that will certainly benefit from the bill. Earlier, you touched on the point that many contracts are between two individuals, notwithstanding the odd contract with the larger agricultural providers. Will the bill benefit individuals as well as businesses? If so, can you provide more detail about those benefits?

James Rust: I think that every business has an individual behind it. To that extent, there will be benefit to individuals to be had from the bill. In the agriculture industry, there are many businesses, great and small—some of them are sole-trader businesses. One would hope that there will, through a process of evolution, be increasing utilisation of the third-party provisions in the bill, which will allow individuals to benefit. I am sorry—it is crystal-ball stuff, really.

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

James Rust: Yes. Those rights have been thought through reasonably carefully and sections 4 to 6 strike the right balance. One of the difficulties with the law as it is at present is its lack of flexibility. Those sections will introduce the necessary balance.

Stuart McMillan: Will you comment on section 9, which allows arbitration agreements between contracting parties to operate in respect of third-party rights? What impact will the new rules on arbitration have on the agricultural sector?

James Rust: The introduction of an arbitration section is sensible, and I think that it is right to extend it to third parties, as it does. Section 9 also integrates quite neatly with the existing legislation; it will all work quite well. Disputes are not unknown in agriculture, and there are various ways in which those disputes can be settled. Arbitration is one, mediation is another and the Scottish Land Court is another, for disputes between landlords and tenants. Various routes can be taken in disputes in

the agricultural context. The section 9 proposals will simply enhance the current arbitration arrangements.

The Convener: This is probably an unfair question. You have mentioned that agriculture is not unknown for its disputes and for not fulfilling European convention on human rights requirements. Parliament has spent much time considering ECHR compliance and fairness. Are the arbitration proposals in the bill ECHR compliant as regards fairness?

James Rust: Yes—I would say that they are. Nothing I read in the bill is unfair or unreasonable for anybody. I am well aware of the sensitivities of the situation, but I think that it is correct to allow a third-party locus within an arbitration procedure. That is only right—not to do it might well lead to greater difficulty.

11:00

The Convener: Our final question will come from Monica Lennon.

Monica Lennon: In our other sessions we have been taking cognisance of the speed of law reform. We have heard from witnesses that some of the problems in the Scots law of third-party rights have been around since at least the second world war, so has the pace of law reform been too slow?

James Rust: That must be the case, in the sense that changes to Scots law always played second fiddle to United Kingdom legislative change when we had to work through Westminster, which was a well-known set of circumstances. A lot of very good legislative change has been spoken about in the Scottish Law Commission, but there was no parliamentary time to deal with it. Since we have had the Scottish Parliament, the dam has burst and we have got on with it. Practitioners have, in the past, just got on with the job of life and made do with the law with all its imperfections. We are catching up with this particular imperfection.

My personal view is that it would not be fair to characterise the issue in the bill as one that has been particularly noteworthy for being slow to change; rather it is part of a wider problem that we are in the process of dealing with.

Monica Lennon: The Scottish Law Commission has set you the aim to increase use of Scots law. The Contracts (Rights of Third Parties) Act 1999, which applies to England and Wales, is being relied on in Scotland. If we get this right and get an act in Scotland that is fit for purpose, will there be less use of other forms of law?

James Rust: I am absolutely sure that that will be the case. I am sure that people will, when we provide our own solution to the issue, as we will do with the bill, turn to it. My only caveat—I come back to this point—is that people are familiar with what they know. If what they know works, albeit that it is English legislation, they will need to be educated that a new act exists and persuaded about the intention that they utilise it rather than an English act.

The Convener: Does anyone have final questions?

Stuart McMillan: When the bill is enacted and its provisions are in operation, if there is the perception—and the reality—that it could save money and time for legal firms, will that be one of the main drivers for legal firms to use it, as opposed to doing what they currently do?

James Rust: Yes. If the legislation eases the process, people will obviously want to make use of it. Once that is recognised, the benefit of cost savings should ensue.

Sometimes the driver is not just cost—utility, practicality and speed of process also all have a bearing. You have to look at the situation in a slightly broader sense.

The Convener: I thank James Rust for his evidence. If, in the dark hours of the night, or subsequently, you or any of your colleagues at Morton Fraser—or any other law firms that deal in agricultural law—having reflected on the issue and your evidence, decide that you can tell us anything else that would help us to produce the best bill that we can, I would be pleased to hear from you. In the meantime, thank you for your help.

I suspend the meeting to allow for a change of witnesses.

11:04

Meeting suspended.

11:06

On resuming—

The Convener: It is my great pleasure to welcome our next witness to provide evidence on the Contract (Third Party Rights) (Scotland) Bill. David Wedderburn is a forensic architect representing the Royal Incorporation of Architects in Scotland.

The first question is on whether there is a need for a statutory approach. The bill team and the Scottish Law Commission have indicated that case law is unlikely to develop quickly enough to deal with the problems identified in the law, and that statutory rules are needed. What is your view on whether there is a need for statutory rules for third-party rights?

David Wedderburn (Royal Incorporation of Architects in Scotland): We feel that there is a need for such rules because, with the common-law approach, first of all the law is uncertain. The development of the law is also uncertain because it depends on which cases come before the courts and how the courts deal with them.

I notice that you have referred to the construction industry. The problem there is that the approach to third-party rights has been through a lot of separate contracts, or collateral warranties. The kind of people who need those assurances, because they are exposed, either because they have lent money or are occupying properties constructed and designed under other contracts, and are liable for the maintenance or are buying properties for investment, need certainty because they are hazarding quite a lot of money, both capital and expenditure. At the moment, therefore, even though there is the common-law right, both Scotland and England tend to use collateral warranties.

Another driver is that a lot of third parties that want third-party rights have headquarters in London and tend to have English solutions. I was in practice until about five or 10 years ago and, even in England, notwithstanding the Contracts (Rights of Third Parties) Act 1999, institutions were still using collateral warranties. It will take a lot of persuading for them to move over.

As well as being a representative of the RIAS I am on the drafting committee of the Scottish Building Contract Committee. That committee has actually drafted third-party rights into standard-form building contracts with the assistance of Professor Hector MacQueen. They have not been used very much and are a bit cumbersome, because of the problem of irrevocability. There is a requirement to lodge the rights in books of council and session or some other kind of delivery, to make them enforceable. The new law will assist in getting rid of some of the cumbersome aspects of the present attempts to use third-party rights.

The Convener: We have heard a little about the 1999 act in England, and that there has not been a huge uptake of what that offers to contracting parties. Do you have any comments on that?

David Wedderburn: I am not an English lawyer and I do not have extensive experience of operations in England, but we have been involved in projects that included English developers. They still think in terms of using collateral warranties rather than third-party rights.

The Convener: Is that even now?

David Wedderburn: That is even now.

The Convener: It is almost 20 years since the 1999 act came into force.

David Wedderburn: Yes. Commercial law moves slowly.

The Convener: That is certainly consistent with what we have been hearing from others.

The provisions in the bill set out the default position. Contracting parties are free to make express provisions to the contrary. To what extent do you agree with that approach, and why?

David Wedderburn: We at the RIAS agree with that approach, because we want to have those third-party rights established clearly and to have non-applicability as an exception to the rule. There are benefits to architects in having all their legal obligations set up under the one document. Anything that makes it uncertain that those rights have been established will encourage other third parties to insist upon extra contractual arrangements. Anything that can establish all those third-party rights under the architect's appointment would be to the benefit of everyone.

The Convener: Thank you. That is clear cut.

Alison Harris: Good morning. In your written evidence, you explained that third-party rights are needed in commercial developments to protect the position of funders, purchasers and tenants. Will you expand on why third-party rights are so important to commercial developments? Are there other areas of construction where third-party rights are important?

David Wedderburn: The rights in relation to funders, purchasers and tenants are important. The funder is extending a large amount of money as a loan to somebody, and the only security is the property. That security is damaged if the property is defective in any manner. Therefore, funders need recourse against those that they think may have caused the damage to the property.

Funders have special kinds of third-party rights. In addition to having recourse in relation to defects, they also usually insist on what are called step-in rights, which mean that if the contractor or the developer goes bust, for example, the funders can step in, take over the construction from the developer and finish it so that, again, they protect their investment.

Purchasers need to know what they are buying. The problem with buildings is the latent defects. It is often not patently obvious that there is a problem with a building, and a forward purchaser can purchase what they think is a perfectly good building, then find that there are loads of defects.

Normally, commercial tenants are let on a full repairing and insuring lease. Therefore, if there is something wrong with the building, they are liable, so they need to protect their position.

11:15

Alison Harris: Are there any other areas of construction involving third-party rights that you can think of?

David Wedderburn: Those are the main ones. The other area is what I would call the Panatown type of situation. It is quite common for developers to have a group arrangement, whereby they transfer the ownership of their property to one member of the group company, while another member of the group company enters into the contracts to have them built. That is a situation of contract with no loss and somebody suffering a loss with no contract. That is an ideal situation for having third-party rights, so that that person would be protected.

The Convener: We will now explore the subject of collateral warranties.

Monica Lennon: Good morning, Mr Wedderburn. I have had a look at your written evidence, in which you explain that the uncertainty in the current law means that parties in the construction sector normally use collateral warranties, and I listened to your earlier comments—you touched on that in your first response to the convener. Is it simply that commercial lawyers are creatures of habit? Is that what is going on?

David Wedderburn: Lenders and banks in particular like to have a piece of paper with which they can show that they can pursue or raise an action. It will be an educational task, once the bill becomes an act, to persuade them that they can point to provisions in the contract that they can rely on.

Monica Lennon: It sounds like the use of collateral warranties is very well established, in the light of the uncertainty around the common law. In your evidence, however, it appears that collateral warranties are quite difficult to arrange logistically. It is perhaps not an easy option. Will you explain what some of the practical problems are?

David Wedderburn: I have been in circumstances where one of the parties to a deal that was about to be signed was on holiday in a cottage in the far north, so we had to dash off to the Highlands. We had to send two solicitors up there to stand at his door until he signed the document and then take it back so that we could do the deal the next day. Those things can happen.

Monica Lennon: Is that a typical example? Are there others?

David Wedderburn: No, that one was unusual. Usually, we manage to get everyone lined up and all together, and everyone signs, but it is like herding cats sometimes.

Monica Lennon: In your written evidence, you indicate a technical problem with collateral warranties: that sometimes the rights and benefits in the warranty are not aligned with the initial contract terms. Will you expand on that point?

David Wedderburn: Yes, that is a problem. Collateral warranties are independent legal documents, and they can be drafted in any way that parties like. The danger comes if people take them off the shelf from one development and apply them to another. The advantage with the third-party rights approach is that those rights are aligned with the contract, as they are written into it. With a separate document, however, the parties could enter into all sorts of things that do not align with the underlying contract.

Monica Lennon: Other witnesses have made similar points to yours and have said that, in the short term, collateral warranties, rather than the new rules, will probably still be used for some time. Do you agree with that view? You have touched on the need for education. How do you go about educating practitioners?

David Wedderburn: The first thing that we will be doing as an incorporation is to issue practice notes to members, alerting them to when the bill becomes an act. Of course, the problem is that developers often approach their architect when they are thinking about a development, so that is the point at which these approaches should be brought to their attention. However, if they go to a bank for funding, the bank will go to its own lawyers and will not involve anyone in the development team. That is where lawyers need to be educated, too.

Monica Lennon: How will the banking sector address that issue?

David Wedderburn: I am not sure. That is not my area of expertise.

Monica Lennon: Thank you.

The Convener: We now move to Alison Harris, who has questions on another subject.

Alison Harris: The Scottish Law Commission has indicated that the bill will make it easier for businesses to avoid what it calls the “black hole of non-liability”, which currently reduces protection for company groups. Do you agree? If so, what will be the impact of that change on the construction sector?

David Wedderburn: I touched on that in relation to the Panatown type of situation, in which one member of the group contracts to get the thing built and, as soon as it is finished, it is passed on to another part of the group that holds all the property. A number of parties, including the House of Lords, have used fancy footwork to try to bridge the gap in the present law, but the creation of

third-party rights is a nicer legal approach that allows all the members of the group to benefit from the original contract.

Alison Harris: So it is cleaner.

David Wedderburn: Yes.

The Convener: Over to you, Mr McMillan.

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

David Wedderburn: Yes, I think so. As I have indicated before with regard to the kind of people in the construction industry who are looking for warranties, the important thing is to make sure that the underlying contract cannot change under people's feet; they must be able to rely on it. The provisions that make it quite clear when things can be cancelled—and, indeed, those that still allow them to rely on the underlying contract, even though it might have subsequently changed—are very useful for those in the construction industry who rely on third-party rights.

Stuart McMillan: In the discussions that we have had this morning and in previous evidence sessions, much but not all of the focus has been on the various business sectors that will benefit from the bill. Will the bill benefit individuals as well as businesses? If so, can you provide further examples of, or more detail about, those who you think will benefit?

David Wedderburn: My main experience with third parties is with organisations such as companies and business partnerships. However, they are all made up of individuals. To the extent that a lot of our members are sole traders and, therefore, individuals, they will benefit from having less paperwork and from having third-party rights established right at the beginning with their appointment. At the moment, what often happens is that, towards the end of a job and after an individual has already entered into their appointment, somebody will come along and say, "By the way, you need to sign this great sheaf of collateral warranties." Hopefully, such a situation will be less likely to occur.

Stuart McMillan: Given that collateral warranties have been used for some time and, as Monica Lennon suggested, lawyers are creatures of habit, will those protections continue to be used, even though they are an expensive route for legal practice? When the bill is passed—in whatever shape or form—will that be a cheaper method than collateral warranties?

David Wedderburn: It will certainly be cheaper, although given the scale of some of the large commercial operations, the percentage of saving will be quite small. However, more important, there will be less hassle doing it this way because it is neater and causes less disruption to the parties involved.

Stuart McMillan: I have a final question. Earlier, you gave the example of two solicitors being sent up to the Highlands to stand at the door, but was that before the Scottish Parliament passed the Legal Writings (Counterparts and Delivery) (Scotland) Act 2015?

David Wedderburn: Yes, it was years ago.

Stuart McMillan: Thank you very much.

David Torrance: My question is on arbitration and the impact on the construction sector. In your written evidence, you explain that it is currently difficult for third parties to join in arbitrations dealing with collateral warranties and that section 9 of the bill will make it easier for multiparty arbitrations to take place. Could you expand on that point and explain the advantages of multiparty arbitrations in the construction sector?

David Wedderburn: Over the past few years, arbitration has been a varying thing in the construction industry. When I was first practising as an architect back in the 1970s, the standard form had the default of arbitration. However, that fell into disrepute because arbitration relied on articles of 1695—or sometime around then—so it was rather antiquated and could go on and on. In later years, there was a move towards court proceedings but, since the Arbitration (Scotland) Act 2010, the Scottish Building Contract Committee, which is the major drafter of Scottish building contracts, has moved back to arbitration as the default position for dispute resolution. Therefore it is very likely that any underlying contracts will have arbitration as the means of dispute resolution. That creates problems for third parties, who are not party to the underlying construction contract, being involved in any arbitration. That is why we welcome the approach in the Contract (Third Party Rights) (Scotland) Bill, which will allow third parties to join in any such proceedings.

There is a further point, which I just thought of this morning. I have not thought it fully through, but as you may be aware, construction contracts are subject to the Housing Grants, Construction and Regeneration Act 1996, which gives a right to adjudication on disputes. We are already in an interesting position regarding the interaction between the two acts, but that interaction needs to be borne in mind in respect of the bill.

David Torrance: On the speed of law reform, from the evidence that we have received, it seems that some of the problems in third-party rights in

Scots law are of long standing. Do you think that law reform has been too slow?

David Wedderburn: No. It is good to see it happening and the fact that we have a Scottish Parliament has allowed many issues that have lain unresolved for a long time to be addressed. I welcome that. It is interesting that, when the third-party issue was addressed in England in 1999, the legislators were coming from a different position, as they had privity of contract and therefore no third-party rights to begin with. I am glad that we are now legislating so that we have a proper statutory basis for Scottish third-party rights.

The Convener: Excellent. If there are no more questions for Mr Wedderburn, it is my pleasant duty to thank him for taking the time to come and give us the benefit of his advice. As I have said to other witnesses, Mr Wedderburn, if matters occur to you following the meeting that you think would be of benefit to us in making good, or better, law that you have not managed to convey to us today, please do so subsequently, should you wish. In the meantime, thank you very much for your help today.

11:30

Meeting suspended.

11:33

On resuming—

The Convener: The final witnesses today are Craig Connal QC, who is a partner at Pinsent Masons, and David Christie, who is a senior lecturer in law at Robert Gordon University. I welcome both of you, and thank you for joining us.

My first question is on moving third-party rights from common law to 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 identified in the law, and that statutory rules are needed. Can you outline your own views on the need for statutory rules for third-party rights?

Craig Connal QC (Pinsent Masons): I thank the committee for its courtesy in allowing me to rearrange my appointment to appear at last week's meeting so that I could attend my colleague's funeral—in Ayr, as it happens. It is very much appreciated.

I will let Mr Christie chip in in a second, but my view is that this is quite a tricky balance for the Parliament to maintain. Although the common law is, in a sense, cumbersome, it has the advantage that it develops over time as things change and different types of case emerge. Third-party rights would not have been discussed in the context of collateral warranties 20 years ago; they would have been discussed in the context of title conditions on people's houses, which is where they were largely to be found. The common law shifts along in a slightly cumbersome way. Of course, as soon as you put legislation in place you are faced with detailed statutory provisions that may or may not all turn out to be ideal. I suspect that I am rather more ambivalent about the pros and cons of legislating, although I acknowledge that the revocability point that the Law Commission identified, which I realise is another question, is not easily resolved by case law.

David Christie (Robert Gordon University): I set out some of the reasons for my position in my paper for the committee, but it might be helpful if I briefly summarise them. On the broad policy, the codification of the common law in this situation is probably necessary if there is a recognised need to have third-party rights. The general consensus seems to be that there is a benefit in having third-party rights. In the construction sector, where a value is put on pragmatism and flexibility, at least having the option of third-party rights would be useful.

Perhaps slightly poetically, I called the position of third-party rights in Scots law a "death spiral" because no cases are coming before the courts to help to clarify the existing law. In the absence of clarity in the existing law, nobody is using third-party rights, which means that no cases are coming before the courts to clarify it and so nothing is happening with third-party rights. If codification occurs, as has happened in England and Wales, there is the possibility—I would not necessarily put it any higher than that at the moment—of a virtuous cycle whereby use of third-party rights increases, it becomes perpetuating to the extent that the more people use it, the more it becomes accepted and the more useful it is. That is not to say that collateral warranties in the construction context, which is what I am most knowledgeable about, would go away, but there may be changes in the extent to which they are emphasised and used.

The Convener: Thank you. We will get you to explain the term "primordial soup", which is in your submission, later in your evidence. In the meantime, I ask Monica Lennon to take up the uncertainties about the scope of the law.

Monica Lennon: One of the main criticisms of the common law is that its scope is uncertain. Do you agree with that criticism and, if so, why? Will you give us some examples of the extent to which the law needs to be clarified in legislation?

David Christie: Partly, there is a general perception of lack of clarity, which, as I said, is self-perpetuating. I think that you have heard about irrevocability as the particular issue, and the

lack of clarity around exactly how third-party rights are constituted in a way that can be binding. The danger with third-party rights is that if there is uncertainty as to constitution, there is always the risk, if you are entering a contract, that some third party might crawl out of the woodwork and raise a claim against you. That makes third-party rights quite scary, because there is a lot of uncertainty about where a claim might come from. As a result, parties will simply exclude third-party rights from contracts altogether, so that there are never any questions about it. The inherent uncertainty is the real problem here. The Law Commission has plotted a route through how you could interpret the law in one way, but that probably requires more work, and the need to argue these cases before court in order to achieve that. The best way to short-circuit the problem, if we think that third-party rights are a good idea, which I think they probably are, is to codify them in legislation—essentially, we reboot the common law.

I was thinking on the train down that it is a bit like what happens when someone has a technical problem with their computer. Often, they just continue to use it and find a way to get along with the problem. That is in some ways like collateral warranties in the construction industry—it is not necessarily easy but it does the job. What we really need is for somebody to upgrade the system and get rid of the problem altogether. At least that would give a choice about how to keep going.

Monica Lennon: Is the proposed upgrade a step in the right direction?

David Christie: Yes.

Monica Lennon: Given that the bill seeks to provide greater clarity, are its provisions clear enough and do they resolve some of the uncertainty linked to the current law?

David Christie: I have reflected on the supplementary evidence given by the Faculty of Advocates, which was interesting. That picked out a number of difficulties with the bill; or, rather, not necessarily difficulties but areas where it is inelegant. Certainly, there are sections that are very wordy.

The conceptual difficulty is that with third-party rights there is a distinction between the right and where that right comes from. A contract contains rights, and the way that we work out what those rights are is by reading the contract. With third-party rights, the rights have to come from somewhere. In the bill, that is what is termed the "undertaking".

The interpretation of the undertaking gives us the scope and the parameters of the third-party right. The bill is trying to take account of that duality, because so much of what it is doing seems to be facilitating the intention of the parties in giving the third-party right. I do not know whether I am making sense now.

Monica Lennon: I am just about with you. Does Mr Connal want to add to that?

Craig Connal: It is interesting. It probably goes back to the point that I made at the outset. Taking revocability as an example, if the law says that the right must be irrevocable to work, that is pretty clear. Whether it is a good rule or a bad rule, it is clear and everybody knows the rule. It did not cause any problem in the previous regime for third-party rights in relation to titles, because it was always in the title deeds, so it was there.

As soon as we say that we want to change the rule, we then get into some of the provisions in the bill, which are probably quite well designed to create a lot of dispute: take for example sections 4 to 6, which have been commented on by other contributors and which I know we will come to later.

As soon as we take away the simple position, we find ourselves possibly having to create quite a complicated answer in order to cope with the issue that we are addressing. I was trying to think of another issue about clarity, because I realised that this question might arise. Mr Christie will tell me that I am attacking the coherence of the law, but the one that occurred to me was that, if we want to make things very simple, we just say that third-party rights can only be created expressly; if we want them we write them down, they are in the contract and everybody can look them up and see what they are. We do not allow the rights to be implied, because as soon as we allow that, we open up a whole range of questions such as, if they are not there in express terms, under what circumstances they can be implied. There are degrees of certainty. Mr Christie pointed out to me this morning that if we remove "implied" then we create a different position to that in other areas of the law. It is quite an interesting trade-off between clarity and progress.

Monica Lennon: Sticking with the approach in the bill, Professor Hugh Beale and the Law Society have touched on the complexity of sections 4 to 6. Do you share some of those concerns?

Craig Connal: Absolutely. I make it clear to the members of this committee that I am a contentious lawyer—I deal with problems—although for the purposes of giving this evidence I have spoken to people who work in other areas, such as drafting documents, so I may be able to assist on some of those points as well. However, when I see sections that talk about "reliance" and "to a material extent" I wonder what that means and think to myself that we can litigate over that.

Monica Lennon: Does that mean that the language is too woolly?

11:45

Craig Connal: The bill covers a lot of areas in which it would be difficult to find a simple fix, but it provides quite a complex fix. That may not matter if there are not many cases, but it creates a number of areas of complexity. I am not a parliamentary draftsperson, so I am afraid that I have not come here with a nice, neat, one-sentence solution, but there is something to be said for wondering whether the provisions in the bill are too complicated.

David Christie: On the point about implied rights—which Mr Connal and I have discussed previously—the Scottish Law Commission has considered whether rights should be allowed by implication, because that is different from the approach that is taken in some other jurisdictions. I do not have a particular view either way, but I made the point to Mr Connal that the legislation treats third-party rights partly by interpreting them essentially as if they were other provisions of a contract that just happened to give the rights to a third party. To allow implied rights therefore brings them within the broad sphere of how we interpret contractual provisions, which involves looking at the words in their surrounding circumstances—Mr Connal knows all this—and working out what the parties' intention was.

Monica Lennon: I am not so sure—he is shaking his head.

David Christie: If you start to differentiate third-party rights from the broader sphere of contract interpretation, you may find yourself in difficulties, because you are not allowed to use the broader suite of rules to understand how the third-party rights work. If you do not have access to that broader suite of rules, it is harder to work out what the meaning of the rules and the third-party rights terms are, which increases the uncertainty.

Monica Lennon: I might pick that up again in some later questions—I will digest it first.

Craig Connal: I am sorry—the secret that we are not letting out is that Mr Christie and I used to work in the same office, so we know each other from long ago, hence some of the discussion.

Monica Lennon: We like to bring people together in this committee.

The Convener: Professor Beale implied—if my memory serves me correctly—that the English legislation is more straightforward and clear-cut, and indeed almost binary. Do you believe that the bill does not provide sufficient clarity? Do you agree with the response from the Faculty of Advocates, which you may or may not have seen—

Craig Connal: I confess that I have seen only sections of the faculty's response. I dipped into Professor Beale's evidence, but I regret that I did not have time to read it all.

Although I am qualified in England too, I am not sure that I can offer a definitive view as to whether the 1999 act and the bill are the same, when one compares them precisely, or whether there are material differences.

David Christie: As I am not a practitioner, I would not want to hazard a view, especially on the interpretation of specific provisions. However, I looked at the faculty's further response and thought that it seemed to be an elegant way of dealing with the matter. From a pragmatic point of view, if the people in the Faculty of Advocates, who are the ones who will argue about the legislation, are already picking up issues in the drafting, we should probably take that into account.

A possible issue with sections 4 to 6 is that they are aimed at addressing specific problems that exist in the current common law. It is almost as if a problem has been identified and the bill presents a drafting fix to sort that problem out, whereas the Faculty of Advocates is taking a more holistic approach to all the issues.

The Convener: We should move on—to a question from me, it appears, on default rules. The policy memorandum states:

> "the provisions in the Bill set out ... the default position. Contracting parties are free to make express provisions to the contrary."

To what extent do you agree with that approach, and why? You may already have touched on that subject, but you might like to put on record some further views on the issue.

Craig Connal: The phrase "party autonomy" is usually used to describe the general principle that, as far as possible, parties should be free to put into a contract what they want to, and the other party to the contract should be free to accept or reject that, leading to a conclusion, and those provisions ought not to be restricted in any unnecessary way. That is the general principle that is widely applied, and which should apply in the bill. The answer is, therefore, that party autonomy is provided for.

David Christie: I agree with that. It is important that parties have the choice, and I think that this legislation helps give them a choice where they might not have a full range of choices just now, compared with other jurisdictions. That said, I certainly foresee situations in which collateral warranties would still be highly useful, even if this

bill were to be passed. It might take out of the frame some of the more basic situations where collateral warranties are used and allow you to focus your efforts on more complex situations. However, that is a matter of choice, and this will help give flexibility in what are relatively complex contractual situations.

The Convener: Thank you very much. I call Alison Harris.

Alison Harris: Section 2 abolishes the irrevocability rule to allow contracts that grant third-party rights to be cancelled or modified. Do you support the rule's abolition? If so, why?

Craig Connal: I think that I will defer to Mr Christie on this issue. I will say, though, that this would not have been an issue in many of the situations in which third-party rights might have been envisaged in the past. I come back to the title deed example that I cited earlier: if something is included in a title deed, it is in the deed, and the issue of the deed itself being revoked or changed just does not arise. If the construction industry, for example, wanted a more nuanced ability to shift and change, that is not provided for under current common law, and the position can be changed only through statute.

David Christie: There is a benefit in allowing the parties to agree on and construct third-party rights that suit their particular situation, and if that limits or restricts the extent to which you have to hit certain pre-set criteria, that can be only a good thing.

I am slightly conscious of the fact that most of the evidence that you will have heard will have come from lawyers involved in setting up collateral warranties and such arrangements, and we need to reflect on the extent to which the beneficiaries of third-party rights and of collateral warranties will often be those buying property and construction sets, the funders and so on. Obviously, they have an interest in certainty, and an important issue is the extent to which there is certainty with regard to the third-party right that they get.

There is therefore a balance to be struck between revocability and the ability of funders and the beneficiaries of third-party rights to rely upon those rights. That is what the bill sets out to achieve, and perhaps the wording that we have been discussing is fiddly because it is trying to strike that balance between flexibility in constitution and certainty in execution.

The Convener: I will be the first to admit that I am not a lawyer, but how might renunciation impact on the situation that you have just set out? Would it have an impact at all? I am aware that the issue was raised in the Faculty of Advocates evidence, but is it relevant or not to irrevocability? If not, please just say so.

David Christie: I think that we would all like to confess to not being lawyers, if the option was open to us.

I have no particular view on renunciation, apart from within the general framework of not being able to force someone to have a right that they do not want. However, I have not really engaged any further than that with the reasoning of the Faculty of Advocates.

Craig Connal: I must confess that I have not engaged at all with the faculty's reasoning. One of the complications is, I think, that the bill is dealing with the granting of rights alone, as that is what the previous law dealt with, and in many of the situations that arise in practice, there might be an attempt to impose obligations. For example, one of your previous witnesses talked about documents going beyond simply saying, "You have the right to do X". Of course, as soon as you go there, you find yourself in much more complicated territory. If all that we are talking about is simply the granting of a right, the person to whom the right is given can say, "No, thank you. I give it up." That is reasonably straightforward.

The Convener: Thank you very much. We now move to Mr McMillan's questions.

Stuart McMillan: Some of this has already been touched on. 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?

Craig Connal: I will not reiterate the general comments about the nature of some of these points. To make an educated guess, I suspect that, if you need provisions of this kind, a fair attempt has been made to create a balance between the right of the original contracting parties to say no and the right of the person who has received the option to insist on it in certain circumstances, which are specified.

In a sense, that rather elaborate answer to your simple question gives a clue as to why the provisions are quite complicated.

David Christie: I would not add much beyond what Mr Connal has just said and what I have said already. The issue partly concerns the conceptual difficulty of separating out the underlying instrument that creates the right and the right itself. I do not feel qualified to look at the drafting for dealing with that, but the Faculty of Advocates has had a good think about it, and it might be a matter for further reflection.

Stuart McMillan: The policy memorandum states that the bill

"will promote the use of Scots law".

Based on your experience, do you think that that is correct?

Craig Connal: I think that there is a prospect of it. Other witnesses have spoken about what you might call the London weighting—in other words, the fact that many transactions are dealt with by people who have originally been advised by lawyers in London and so on. Therefore, there is a natural inclination to assume that nothing outside London matters.

The bill is bound to help. As other witnesses have said, it is worth remembering that the English changed their law partly because they thought that the Scots law was better than the rigid privity of contract rules that the English had, while the Scots had third-party rights, albeit with some difficulties.

I suspect that the reality is that, as with all changes, these changes may come out and people will prick up their ears. They may well have forgotten jus quaesitum tertio, which they learned when they were at university, because they have not seen it since. When there is a new act, people will ask what it does and they may well then consider whether they can use it and whether it advantages their clients. On balance, the answer is that there is a reasonable prospect of some greater use of Scots law.

David Christie: I agree, based on the literature that I have looked at and on my own experiences. I do not necessarily think that the bill represents a radical change that will cause an explosion in its use but, in itself, it closes a gap between Scots law and its main competitor, English law, and aligns Scots law more closely with broader European law. It is also useful as a way of demonstrating—along with the legislation on counterparts to which Mr McMillan referred earlier—that Scots law is moving forward and of recognising where there are relevant areas, with the ability to start sorting out those issues.

Stuart McMillan: Indeed—I was going to refer back to the Legal Writings (Counterparts and Delivery) (Scotland) Bill, which went through this committee. The minister who introduced the bill highlighted numerous times that it was about trying to modernise Scots law. As we have heard this morning regarding the Scottish Law Commission bills that have come to the Scottish Parliament, it is about modernising Scots law and making it more competitive internationally.

Craig Connal: To stick with the construction example, if we have a project in this jurisdiction, the logic of putting anything in with the law of another jurisdiction is silly. As the committee is probably aware from other evidence, the classic example is the North Sea. Contracting has been conducted largely, although not entirely, under Scottish jurisdiction, and yet the suites of contracts into which the industry has entered have been dominated largely—almost by default—by English law provisions. In fact, a lot of the disputes disappear elsewhere. There is now an opportunity at least to edge something forward in that respect.

12:00

David Christie: The construction industry often uses standard forms of contract, and the main suites use English law, albeit that the Joint Contracts Tribunal has a version with a kilt on. If Scots law was aligned more closely, it would be easier to tweak the standard forms to apply it, and less consequential drafting would be needed. If there were other good reasons—logistics and so on—why Scottish jurisdiction might be preferred, closer alignment would make it easier to use the standard forms, and Scots law would therefore be more appealing.

Stuart McMillan: We have heard evidence today on the workarounds. When the bill passes through the parliamentary process and becomes an act, an education process will be necessary. I accept that this is a crystal-ball exercise, but how much effort do you think would need to go into such a process to encourage practitioners to consider the effects of the bill in relation to future contracts?

Craig Connal: My guess—for which I have no evidence—is that something would need to be done after the initial activity. Assuming that the bill becomes an act, the royal assent date will be announced and people will prick up their ears and think about it. However, a year later everybody will have forgotten about it unless there is some effort among the professional organisations to reiterate the new scheme.

With regard to the reality of the workarounds—the collateral warranties—I had a long chat with a colleague of mine who does little else but draft construction contracts. He told me that the drafting will still need to be done exactly as it is now: one will still need to work out who is to get the right, who is to give the right, what the terms of the right are and whether there is any additional material. However, the bill could enable people to avoid the paper chase, as my colleague puts it, as it may be possible to put everything in one contract that is provisioned to grant rights in favour of various parties, rather than having a number of collateral warranties.

In a recent contract, we had 120 collateral warranties, because each of the specialist participants in the building process had to grant warranties in favour of each of the parties—tenants, funders and so on—who had an interest. Each of those warranties requires another piece of paper. Some people like to have their own little

piece of paper, as we have heard, but I suspect that, in principle, it is always a good idea to avoid a paper chase. The professional bodies can take up the mantle after the Parliament has given them the opportunity, as a bit of consistent education will be required.

David Christie: With regard to the education process, the ideas that go into third-party rights, to the extent that collateral warranties are used in construction contracts, show that the thinking is already there. The bill will not introduce a whole range of foreign terms to the industry. People understand what collateral warranties do, and that third-party rights can do some of the same things. They will also understand third-party rights if they have had experience of operating in England and Wales, as most of the large, complex construction companies that engage in the large projects that require collateral warranties will have had. There will be some familiarity with Scots law, because we have all studied jus quaesitum tertio at university. The bill is a reminder and is bringing the process up to date, rather than introducing a brand-new concept that we will all have to get our heads around.

Stuart McMillan: The SLC indicated that the bill will make it easier for businesses to avoid what it calls the "black hole of non-liability", which currently reduces protection for company groups. Do you agree with that view? If so, can you outline your reasons?

Craig Connal: I am a bit cynical about the prospects, to be frank, speaking as a contentious lawyer. The black-hole cases tend to arise because somebody has not thought the matter through. Things have happened and, as the previous witness—Mr Wedderburn—said, it turns out that the loss is in one place, but the right is in another and the two are not matching up. Of course, if someone has not thought about the issue, it does not matter what the bill provides because they will not have written it in. If they have thought about it in advance, there is already a suite of mechanisms for dealing with it and the bill will just add another one.

There are not that many black-hole cases. The witness from the RIAS said that the courts sometimes use what he described as fancy footwork to get round them, because the courts do not like the idea of a black hole—it is abhorrent. If there is a loss caused by somebody's failure, why should that fall into a black hole as opposed to landing on the appropriate person? Footwork can be done and I am not convinced that the bill will make much difference to those relatively rare cases in which a black hole arises.

David Christie: Similarly, there might be scope to pick off some of those if we have a third-party rights act. In its submission, the SLC used the example of a group of companies, in which it might be possible to construe the third-party right quite widely to cover companies in the group. However, the overall problem with the black holes defies a simple solution. The number of dissertations that I see on the masters course in construction law that look at the issue and try to solve it testifies to that. I was glad to see that the SLC is looking at ways to progress that, and I wait with interest to see that progress.

The Convener: That was quite long on analysis, in terms of defining the problem. Do you have any solutions, particularly from an academic perspective, given the benefit of advice that you have had from many students as well?

David Christie: No. It is not something that I have yet dared to grapple with. Conceptually, it opens up a gap between various classifications of law—between contract law, the law of delict and things like that. I am aware that there is a gap that might be interesting, but I would want to delve deep into the literature to come to any view. In that particular area, the prospect is too daunting. I have decided to go for some other areas at the moment.

The thought of an interesting point of law reminds me of a colleague of Mr Connal and former colleague of mine, who said that if you go to the doctor and are told that you have an interesting condition, that is the worst possible diagnosis that you can hear. Having an interesting problem, such as the transferred loss of black holes, is not a great thing. I look forward to other people taking forward some work on that; I will keep an eye out for that and think about it in the future.

The Convener: It is currently in the "too difficult" box, then. Thank you very much. We will now go into yet more detail about collateral warranties, if you have any information left to give us.

Monica Lennon: We like to hear about collateral warranties. Sticking with construction, the sector is diverse. There are very large companies, as we touched on earlier, some of which are headquartered in London. Can you give us some examples of how collateral warranties are used, bearing in mind that there is a range of players within the sector?

David Christie: The growth of collateral warranties was a response not to the gap in relation to third-party rights, but to a change or evolution in the law of delict in the late 1980s and early 1990s—the extent to which people who were not parties to a contract could recover for pure economic loss, which is the loss caused by defect rather than physical damage.

That is a complicated area in itself, but suffice to say for the present purposes that there are a

number of reasons why we have collateral warranties as a way of giving parties control over their liability. Such warranties will be used by parties almost as a comfort that there is a route to recover losses, for which recovery might otherwise be cut off through the insolvency of other parties or for a host of other reasons.

The funders and insurers—the people who have a financial stake—are generally the driver for having those warranties because it is a way to control the finances. Craig Connal might have more to add.

Craig Connal: I have had some discussion with my colleagues, who have pointed out that, in past eras, if someone wanted a building built they went to a builder who did the building. However, in the more complex times in which we now live, in many cases, the person who you think is the builder will be little more than a manager who will organise under his umbrella a raft of highly specialised people, dealing with electrical equipment, heating and so on. Therefore, the real expertise lies not in the hands of the builder, with whom you have a contract, but with those very specialist contractors. Part of the reason for the rise of the collateral warranty is that it enables those who want to know who to blame and who to recover from to go direct to the party who is responsible for the particular defect—it is usually something very technical, not something simple like bricks and mortar. I suspect that that is why there has been a tendency towards having lots of people with legal obligations.

David Christie: In terms of the interests of the funders, step-in rights are often used in collateral warranties, which is where the funder can take on control over the contractor. That has been identified in the literature in England as a gap in the legislation, because it would mean transferring not just a benefit, but to some extent an obligation. Having said that, the discussion in England suggests that that gap can be filled by drafting the contracts appropriately, rather than by requiring a fix in the legislation, and that it would occur only in complex commercial situations where it is worth putting in the resources to ensure that the provisions are appropriately contained within the contract.

Monica Lennon: It strikes me that, in those very complex commercial examples, the collateral warranty is a bit like a comfort blanket that people will not want to let go too easily. How will the investors—those who are putting in the big money—be persuaded over time to detach from that comfort blanket?

David Christie: It is interesting that you use the metaphor of the comfort blanket, because I was about to use it myself. A possible gap is opening up in England—I would say no more than that. When Mr Connal referred to chasing after collateral warranties, my face was darkening at the memory of having to do that when I was in practice. The logistical problems of collateral warranties are well known; you will have heard of them many times, and we have all had experience of chasing after collateral warranties.

From case law in England and Scotland, issues have emerged about enforcing parties' obligations to provide collateral warranties. There was the case of Liberty Mercian v Cuddy Civil Engineering in England and a case involving Kier Construction in Scotland in which the court had to make an order to force a party to produce the warranty. It can be difficult to procure the collateral warranties. Those decisions that have come in the past couple of years have brought the problem to light.

A number of decisions have been surprising in respect of the interpretation of collateral warranties; for example, in the Parkwood case, it was held that the Housing Grants, Construction and Regeneration Act 1996 applied to collateral warranties. Some commentators have remarked that perhaps there is some shaking of the faith in collateral warranties as—to mix metaphors—the foundation of the comfort blanket. As third-party rights become established—Professor Beale's research has confirmed that they are becoming more recognised in England—it might be that we will have the opposite of the death spiral, which is the virtuous cycle, in which people think that collateral warranties are not as much of a security blanket as they had hoped, so they start to think about whether third-party rights can be used instead.

The Joint Contracts Tribunal has produced, as part of its standard form, a schedule that sets out detailed provisions for third-party rights, so there is support from one of the standard forms. I am conscious that I am going on a bit. The standard forms are drafted by commercial bodies, which would not go to the time and effort of pulling together those documents if there was no demand for them or if they offered no benefit.

12:15

As I mentioned in my submission, the NEC3 suite also uses a standard form contract. It might have a schedule too—I could not find that when I was looking for it, but nevertheless there is provision in the other standard forms for third-party rights. Those bodies are looking to sell their standard forms to parties to use in their construction projects, so they must think that it is worthwhile to include third-party rights. There is a growing baseline of support in England for third-party rights, which will help parties that operate in both England and Scotland to be more

comfortable with those rights as a way of protecting their interests.

Monica Lennon: Why is that shift happening in England and Wales now, some 18 years after the 1999 act came into force?

David Christie: There are three possible factors that contribute to the growing zeitgeist. Sometimes one is not quite sure how legal reforms emerge—they need to fill a gap, for a start. After 2007, the general growth in litigation and arguments may have involved people using points to promote cases that they may not have used in previous years.

Monica Lennon: What is the significance of 2007?

David Christie: The financial crash in 2007 led to a significant downturn in the construction industry, and it may be—I cannot recall the statistics just now—that certain arguments were run as a means of promoting a dispute where they might not have been run in the past. That may have put more stress on the legal system's rules, which have now allowed certain points to be taken. The more those points are taken, the more people think, "Maybe there is something in that argument—let's try it."

Craig Connal: It will be a slow burn—nothing will change overnight. People are accustomed to working in the way that they have been doing. My guess is that it will take an example of a third-party right in a construction contract being successfully relied on, either in what could be described as a public dispute or in a dispute that happens behind the scenes under one of the dispute resolution procedures for the construction industry. The news will spread that contractor X successfully used remedy Y, and somebody else will think, "Oh—that sounds as if it might save us some paperwork."

Monica Lennon: If the bill is enacted and people continue to rely on collateral warranties, should we be troubled by that? We have heard mixed reports about collateral warranties. They are a bit of a safety net and a comfort blanket as they are familiar, but I am picturing a sea of paperwork and difficult transactions. To what extent would it be a problem if people continued to turn to warranties?

Craig Connal: It would be difficult to describe that as a problem—the issue is just a little bit of unnecessary paperwork. People still have to do all the negotiation detail—it is only in the last bit of the process that there is a difference between putting down the terms in a contract, and creating a series of different contracts and then persuading all the parties to agree to give them. I am not sure that I would necessarily describe it as a problem, but if one option requires more admin than is necessary, it is better to remove it.

The Convener: Mr Connal, do you agree with your colleague Mr Christie that collateral warranties are "a sub-optimal solution", as he colourfully describes them in his submission?

Craig Connal: They can be a suboptimal solution in some straightforward circumstances. I am conscious that we are talking about replacing a general principle of law, rather than creating an ideal structure for contract X. I suspect that a fair number of what we are calling collateral warranties, as if they were all the same, contain much more detailed provisions that will not be replicated in the new process, and I imagine that those warranties will continue. For example, Mr Christie referred to step-in rights. It may be quite difficult to structure things to create all the different obligations and rights that would then flow.

David Christie: I agree with that interpretation of my remarks. On the coexistence of third-party rights and collateral warranties, I am not aware of a particular unhappiness with the 1999 act in England, where collateral warranties and third-party rights are used. I do not think there is a suggestion that that legislation is not of some use, although it may be of only limited use. There are some indications that it may be of growing use, although that is not altogether clear, because it is difficult to get hold of detail.

The Convener: The position that we seek, notwithstanding your reservations, is that the bill will represent progress, rather than the alternative to progress.

David Christie: Yes. My opening point was that people should have options. Third-party rights are recognised in Scots law today, but not as usefully as they could be for people who are involved in construction projects. Clarification of the law is a good idea because that will provide parties in construction contracts with another option in respect of how they go about protecting their interests, and with options that are available in other jurisdictions.

The Convener: I am not sure that there is much left to say about that.

Finally, I turn to arbitration. What are your comments on section 9 of the bill, which provides for arbitration agreements between contracting parties to operate in respect of third-party rights? The Faculty of Advocates was less than flattering about the section.

Craig Connal: Mr Christie and I had a lengthy—one and a half minutes—conversation about this before we started our evidence. I suspect that my answer depends on what the point of the provision is. If the idea is, in a general sense, that all disputes that may arise from a contract should be handled in the same type of way, the logic of

saying that the third party should also deploy arbitration is compelling.

Many disputes might involve construction contracts, which do not generally have arbitration as their first port of call. Such contracts use what is called adjudication as a dispute resolution mechanism. They have other dispute resolution mechanisms—in particular, a thing called expert determination, which is simply an agreement to refer a particular matter to a skilled person whose decision will be binding. There may be other dispute resolution mechanisms within a contract. If the logic that drives that provision is that third parties should use the same suite of options, I would have expected a wider provision than one that focuses just on arbitration because it happened to be a statutory scheme that recently came into force.

Arbitration was the dispute resolution mechanism of choice for construction when I was a lad, but it is now not much used in construction. It is almost always adjudication that is used, either with a contractual set of provisions or with an overlay by statute, which Mr Christie mentioned earlier.

I see the logic of everybody using the same system, but I was a little surprised to see that it is restricted to arbitration. I think that if the logic is that the third party should use the same mechanism, all the mechanisms should be available.

The Convener: If the logic of the bill is to offer more choice, it stands to reason that it would be reasonable to offer more choice. Would the bill do that with dispute resolution?

David Christie: It is interesting that Mr Connal and I were considering the same question independently. I left the topic of arbitration for my train journey down here. A colleague who is expert in arbitration had a look at the bill and did not have much on which to fault the drafting on arbitration, but I was interested in it and reflected on the difference, in this context, between arbitration and alternative—that is, non-court—dispute resolution.

There is a particular issue with construction adjudication. In England and Wales, there was a decision that the statutory scheme was held not to apply by default to third-party rights, but there would be nothing to prevent that being included by contract, if the parties agreed to it. Adjudication is intensive: it lasts 28 days, so bringing in a third party adds an extra layer of complexity. That might be a policy reason not to include adjudication in the bill. However, there might be reasons why adjudication and other alternative dispute resolution might be brought in as options.

I was not able to satisfy myself that there is a good reason not to include adjudication in the bill, but at the same time I was not able to work out exactly how we could do it. The only reason why arbitration is to some extent different is that there is a role for the state in enforcement of arbitration awards that does not necessarily exist in other forms of dispute resolution, which are purely contractual. There is also a possible issue in that the borderlines between arbitration and forms of alternative dispute resolution are not altogether clear in law; the definitions are not necessarily fixed.

There is scope to consider introducing other forms of dispute resolution. For the reasons that Mr Connal outlined, there would be sense in reflecting on that.

The Convener: Thanks. That is helpful and allows us to take the matter up with subsequent witnesses.

Stuart McMillan: Two sessions ago, Parliament updated legislation on arbitration. Notwithstanding earlier questions and comments about updating Scots law to make it more competitive, could one of the reasons why the bill's focus is on arbitration—as opposed to a wider suite of options—be to allow the updated legislation to be the focus for dispute resolution? I do not know what the thinking is, which is why I am posing the question.

Craig Connal: I am not sure, to be honest. I suspect that arbitration is in the bill because the reform that you mentioned moved arbitration out of a collection of case-law led material and some very old statutory provisions to a single suite of all-encompassing statutory controls. Therefore, it is in everybody's mind that we need to ensure that nothing in the bill cuts across or fails to fit with that relatively recent legislation.

My question is whether there is a broader point to the provision. Is it the intention that third parties, in exercising their rights, should do so in accordance with the suite of provisions that other parties to the contract would exercise? I confess that I have not studied the matter in sufficient detail to know the answer. It just seems to me to be a question that might be worth pondering before anything is finalised.

David Christie: There is no reason not to include arbitration in the way that it is included in the bill; the question is more whether the principle ought to be adopted more broadly, as Mr Connal said. The interest in aligning arbitration in Scotland with arbitration in other jurisdictions is useful and, from what my colleague said, seems to have been achieved in the basic drafting, notwithstanding the comments of the Faculty of Advocates, which I have not gone into in detail.

Craig Connal: Parliament, the Scottish Government and a range of other bodies are

currently actively promoting arbitration in Scotland as a dispute resolution mechanism. It may be that parties had in mind that anything that could be done to assist that would be useful.

Monica Lennon: We have spoken a lot about the speed of law reform in this area and we heard that some problems with third-party rights in Scots law have been around since the second world war, at least. What are your reflections on that? Is that a fair assessment? Has reform been too slow? I invite final comments on that.

12:30

Craig Connal: The difficulty with law reform lies in achieving agreement on what the reform should be. You will often find, to be blunt, that one party's real problem is another party's real advantage. There may be very conflicting views on whether there should be a change in the law. Other changes might attract a wide range of views. I suspect that one of the real challenges in any law reform is to achieve consensus.

It is probably a legitimate criticism that no one has quite cracked how to move swiftly to make change in an ideal way where there is pretty broad consensus that there should be change. Other witnesses have spoken about the situation in that respect being better now than it was, which must undoubtedly be correct. The Parliament has been working to find ways of making such things easier and swifter, which is a good thing, although I am not sure that we are quite there yet.

I was instancing to Mr Christie an example in which I found an error in a piece of Scots law involving time limits. It was clearly an error—there was no dubiety about that. I raised the matter with the Scottish Law Commission, which said, "We can't deal with it. It's not in our programme of activities at the moment. Sorry." The commission then told us that we would need to take up the matter with a division in the Scottish Government, with which I then communicated. I never heard any more about it, and that was the end of it. It so happens that the issue is now being dealt with by the Law Commission in a process to deal with the law of prescription more generally. The commission has tagged the matter on at the end, because it can now do that.

I suspect that other people spot things that could be done faster. We are probably all constantly thinking about ways to achieve that.

Monica Lennon: Now that the matter is on the radar and there is a commitment to reform, what, in general terms, are the expectations within the legal profession? We have spoken about limitations and challenges. Ultimately, it is about improving the situation. Are people in the profession optimistic? Do they take a close interest in how the policy develops?

Craig Connal: I suspect that the matter is not on most people's radar at all—it is too esoteric a topic. In the world of the legal profession now, people are becoming increasingly devoted to working in little boxes; they do personal injury cases, or construction cases or whatever. If whatever is going on is not sitting in their box, they are probably not putting their heads up.

I am perhaps an exception in that I am old enough to come from an era when most of us did everything. Some of the bar is the same and academia as a whole is the same, because there is usually someone in academia studying a particular area, but it can be difficult to raise interest in anything that is not landing on people's desks every day of the week.

David Christie: Monica Lennon's first question was on the speed of law reform generally.

As I mentioned earlier, collateral warranties became a thing only in the early 1990s, and legislation in England followed in 1999, with the position in Scotland following that. In England, which has been a testing ground for third-party rights, practice has not necessarily changed, which demonstrates that there was not a burning issue that needed to be resolved.

In order for law reform to be successful, it has to fill a gap. Clear identification of a gap and urgency in fixing it are probably necessary. It is interesting to compare the impact of the 1999 act with the impact of the Housing Grants, Construction and Regeneration Act 1996, which introduced adjudication, among other things. The provisions in the 1996 act are mandatory, so the legislation is of a very different character, but it took off immediately and has had a massive impact on construction law. However, I do not think that one would suggest, as a way of promoting them, that third-party rights should become mandatory. Not only was the 1996 act mandatory, but it captured a moment in the zeitgeist; people were ready for the change and there was a lot of industry consultation and publicity around it.

The reform in the bill is more technocratic. It is necessary, for the reasons that I have outlined, but people are not crying out on the streets of Aberdeen, Glasgow or Edinburgh for a particular solution. I will leave it there.

Monica Lennon: That is very helpful.

The Convener: Thank you very much, gentlemen—Mr Christie and Mr Connal—for taking the time to come along and give us your elegant thoughts on these matters. We are very much in your debt, as we are in the debt of other witnesses. As I have said to other witnesses,

please let us know if any other matters occur to you on reflection—perhaps in your discussion on the train back home, or subsequently. We would be grateful for your further considerations.

12:35

Meeting continued in private until 12:49.

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