

Director of Legal Services :
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BRIEFING

CONTRACTS (RIGHTS OF THIRD PARTIES) ACT 1999

Purpose of Act

1. The purpose of the Act is to enable third parties who are not parties to a contract to be able to enforce its terms against a person who is a party to that contract. It therefore makes a change to the normal rule of privity of contract that a contract cannot be enforced by a person who is not a party to it. The Act however, will not enable such action to be brought against anyone other than the parties to the contract.
2. The Council enters into many contracts which are designed to benefit persons who are not parties to those contracts:-
 - In a contract for the repair of housing a **tenant** will benefit from the improvement of their dwelling.
 - In a social services care contract a **service user/ client** will benefit from the provision of care.

It would therefore be possible under the 1999 Act to confer on a tenant or a social services client the right to enforce the contract that is being made for their benefit.

Commencement

3. The Act came into force on **11 November 1999**. However it will only apply automatically to contracts entered into on or after **11 May 2000**. However the parties to a contract may in a contract entered into on or after **11 November 1999** expressly provide for the Act to apply.

Third Party Rights

4. A person who is not a party to the contract is termed a third party. It is possible to give a third party rights in a contract to which that person is not a party. This can be done if:-
 - (A) **The contract expressly so provides.** Therefore if the parties to a contract expressly agree that a third party may enforce specific terms then that third party can enforce those terms.

Alternatively:-

- (B) The contract purports to **confer a benefit on the third party** (unless on the proper construction of the contract the parties did not intend the term to be so enforceable). Therefore if in a contract one party agreed to

pay a sum of money to a person who is not a party to the contract then that third party could enforce that term against a person giving that promise.

Identification of Third Party

5. The third party who is being given the right to enforce the contract must be either identified in the contract as a member of a class or answering a particular description. The third party need not be in existence when the contract is entered into. Therefore a third party could be named as:- a freeholder, a council tenant, a successor in title, an adjoining occupier or a sub-contractor.
6. What is fundamentally novel is that the third party does not need to provide any value/promise in return for being able to enforce his rights.

Action

7. It is therefore necessary to take a view with every contract as to whether the intention is to apply the 1999 Act or not. There is no prohibition on deciding that the 1999 Act is not to apply. A drafting solution to **contract out** of the 1999 Act is as follows in a contract between an Employer and a Contractor:-

"The Employer and the Contractor agree that the Contracts (Rights of Third Parties) Act 1999 shall not apply to this Agreement. Therefore any person who is not a party to this Agreement cannot enforce any term of it in their own right."

8. It is equally possible to **contract in** only to certain clauses and in respect of certain persons. A drafting solution could be as follows:-

"The Employer and the Contractor agree that the Contracts (Rights of Third Parties) Act 1999 shall apply to this Agreement only insofar as the following persons namely [insert names of persons] shall be entitled to enforce Clauses [identify number] of this Agreement against the Contractor subject to the provisions of the remainder of this Agreement. No other person shall be entitled to enforce any term of it in their own right."

Nature of Third Party Rights

9. A third party can only enforce a term of the Contract subject to the other relevant terms of the contract. Therefore if there is a timescale within which to bring claims, or if there are exclusion clauses they will apply. The third party has the same remedies as if they had been a party to the contract e.g. damages, injunction, specific performance.

Variation/Rescission

10. Once a third party has a right to enforce a term of the contract, the parties to the contract cannot rescind or vary it to either extinguish or alter the third party's entitlement if either:-

- A. The third party has communicated his assent to the term to the person giving the promise;
- B. The person giving the promise is aware that the third party has relied on the term; or
- C. The party giving the promise can reasonably be expected to have foreseen that the third party would rely on the term and the third party has in fact relied on it.

11. Therefore if it is decided to apply the 1999 Act to the contract care must be given as to whether an express variation clause to the terms of the contract should be included. One drafting solution would be as follows in a contract between a Developer and a Contractor:-

"The Developer and the Contractor agree that they may by written agreement at any time vary any of the terms of this Agreement or rescind this Agreement without the consent of [insert the names of the relevant third parties]."

Defences

12. The person giving the promise will still have the same defences that they would have had against a party to the contract against any claim made by the third party. The contract however can cut down on such defences.

Double Jeopardy

13. If a contract is enforceable by a third party and a party to the contract has recovered from another party:-

- A. the third party's loss; or
- B. their expense of making good to the third party the other party's default;

then if the third party brings proceedings then a Court or Arbitrator has to reduce the amount of any award to the third party to the extent it thinks appropriate to take account of the sum recovered.

Exceptions

14. There are a limited number of exceptions to the application of the 1999 Act. It does not apply to certain types of banking

documents, employment contracts and contracts for the carriage of goods.

Arbitration and Adjudication

15. It will be possible for a third party to enforce an arbitration agreement in their own right. It is unlikely that a third party will be able to pursue a claim for adjudication under Section 108 of the Housing Grants, Construction & Regeneration Act 1996.

Novation

16. The 1999 Act will not supersede Novation Agreements, as only a Novation Agreement can transfer the obligations of a contracting party.

Collateral Warranties

17. If a third party who would otherwise have required a collateral warranty is identified in the main contract (e.g. works contract/consultancy) as a party having a right to enforce its terms, it may be possible to dispense with a collateral warranty if the main contract is carefully drafted. It is however likely that funders will continue for some time still to require that collateral warranties are executed.

Relevant Considerations

18. Before granting rights to third parties in a contract it is important to consider:-

- Whether any **goodwill** which is necessary to make a contract workable could be lost if the party who the Council is contracting with then has to be directly answerable to a number of other parties including the Council.

- Whether it is necessary to give a third party **the right to enforce all the terms** of the contract or only certain terms, consider also what remedies the third party should secure.
- If a third party is to be able to enforce a contract they will need to have **access to/a copy of the contract**.
- Whilst the Act clearly provides that the 1999 Act does not affect any right of a person to whom a promise is made in a contract to enforce any term of the contract, it is likely in practice that if a settlement is made with one or more third parties for breach of a particular term then the person to whom the promise is made, e.g. the Council, may not be able to secure any better outcome itself.
- If a contractor is tendering for a contract in which a third party is identified then that could result in a higher tender being submitted.

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