

How the Contract (Rights of Third Parties) Ordinance (Cap. 623) will impact construction contracts

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Structure of Presentation

1. Introduction to common construction contracts
2. Effect of the Contract (Rights of Third Parties) Ordinance (Cap. 623)
3. Third parties in a construction project
4. Whether construction contracts take into account third party rights
5. Suggested clauses



**What are the common
types of construction
contracts used?**



Common Standard Forms

Domestic

- HKIA/HKIS/HKICM Standard Form of Building Contracts (2006)
- NEC3 Contracts

International

- FIDIC Contracts



Standard Form of Building Contracts

- Jointly published by the HKIA, HKIS and HKICM in 2005
- Full name is:

“Agreement and Schedule of Conditions of Building Contract (Standard Form of Building Contract) for use in Hong Kong, Private Edition (With or Without Quantities)”

NEC3 Contracts

- Stands for *New Engineering Contract* – 3rd edition
- Promote values of teamwork, flexibility and fairness
- NEC3 shall be used by the Government in all public work projects shortly
- Adjudication





FIDIC Contracts

- Stands for *Federation Internationale Des Ingenieurs-Conseils*
- English for the *International Federation of Consulting Engineers*
- Founded in 1913
- Aim was to draft and publish a standard form of contract for international civil engineering projects

FIDIC Contracts

- FIDIC offers a range of standard forms, made up of different books, known as “FIDIC’s Rainbow”
- Caters for different projects and stakeholders





What is the Contract (Rights of Third Parties) Ordinance (Cap. 623) and how will it affect us?



The Contracts (Rights of Third Parties) Ordinance (Cap. 623)

New legislation

- Effective from 1 January 2016
- Enacted to reform the common law doctrine of privity of contract
- Similar legislation enacted in England & Wales, Australia, New Zealand & Singapore
- It will apply to all construction contracts



The Contracts (Rights of Third Parties) Ordinance (Cap. 623)

Third party rights under statute

- Under section 4 of the Ordinance, a third party may enforce the term of a contract under two circumstances:
 - Where it expressly provides so; or
 - Where the term purports to confer a benefit on the third party, if on a proper construction, it is intended to be enforceable by a third party



The Contracts (Rights of Third Parties) Ordinance (Cap. 623)

Opting out

- However, section 4(3) allows parties to contract out of the Ordinance by express provision:

“Subsection (1)(b) does not apply if, on a proper construction of the contract, the term is not intended to be enforceable by the third party”



Who are the affected third parties?



Parties under the HK Standard Form

Main Contractual Parties

- Employer / Client / Developer
- Contractor

Non-exhaustive

Non-Contractual / Third Parties*

- Supplier
- Sub-contractors



Are they entitled to claim third party rights under the Ordinance?



How has the construction industry tackled such third party rights?

Collateral Warranties

- Traditionally, the construction industry has relied on collateral warranties
- Essentially, a secondary contract that confers third party rights





Collateral Warranties

Examples:

- *Principal covenant*: the third party warrants that they have complied with their terms of their sub-contract/appointment
- *Copyright*: the contractor is free to use any design documents the third party prepares
- *Step-in rights*: the contractor is entitled to ‘step into the shoes’ of the third party, if problems arise



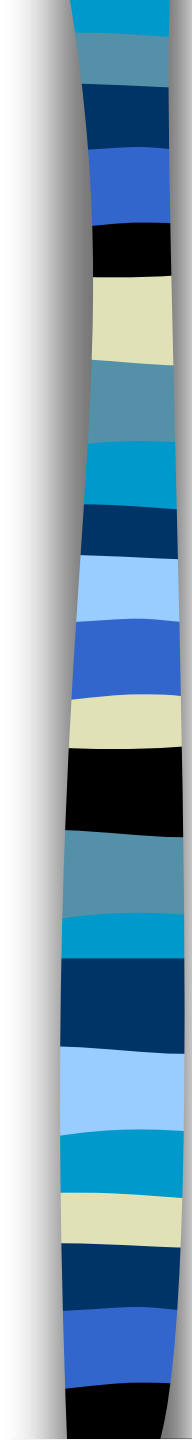
Effect on Arbitration Clauses

- Arbitration clauses are common in construction contracts
- Whether arbitration clauses can be enforced by a third party is still unclear



Potential Problems if Third Parties can Enforce Arbitration Clauses

- First, multiple separate arbitrations will be created
- Second, practical issues, who can appoint the arbitrators?
- Therefore, may need to redraft the standard arbitration clauses



**Should we opt-out of the
Ordinance? If so, how?**



The Construction Industry's View on the New Ordinance

- Industry has expressed reservations about the new Ordinance
- There are already tried-and-tested methods for benefitting third parties
- Highly likely to opt out
- Continue to use collateral warranties



Suggested Clauses

- One suggested opt-out clause is:

“The provisions of the Contracts (Rights of Third Parties) Ordinance (Cap. 623) of the laws of Hong Kong are hereby expressly excluded from this [Agreement] and/or any other documents issued pursuant thereto, save and except for [the name of that third party] who may enforce [the clause number] of the [Agreement].”



Suggested Clauses

- Another suggested opt-out clause is:

"[Subject to the form of the conditions set out in clause [] of this Agreement], [name of third party] shall be entitled to enforce the benefits conferred on [it/him] by clause [] of this Agreement [and for that purpose shall be entitled to the benefit of clause [] of this Agreement [i.e. jurisdiction and/or arbitration clauses] but otherwise no party other than the parties to this Agreement [or their respective assigns] or persons becoming party to this Agreement by novation shall have any right to enforce any terms of this Agreement."



Suggested Clauses (for opt-out arbitration clauses)

- “No party other than the parties to this Agreement [and their respective assigns] or persons becoming a party to this Agreement by novation shall have to enforce any terms of this Agreement”



Q&A

PLEASE NOTE

The law and procedure on this subject are very specialised. This article is a general explanation for your reference only and should not be relied on as legal advice for any specific case. If legal advice is needed, please contact our solicitors.

請注意

本題目之法律及程序十分專門。此文章只屬一般性之解釋，供你參考，而不應被依賴為關於任何特定事件之法律意見。如需法律意見，請與我所律師聯絡。

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