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**THREE MAY NOT BE A CROWD - WHO IS IN THE DRIVER'S SEAT UNDER  
SECTION 9 OF THE CONTRACT (THIRD PARTY RIGHTS) ACT 2017**

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**I. BACKGROUND**

To be in line with other jurisdictions<sup>1</sup> and to address the gaps in current Scots Law relating to third parties' contractual rights (*just quaesitum tertio*),<sup>2</sup> the Contract (Third Party Rights) Act (the Act hereinafter) is introduced to codify third-party common law rights (*jus quaesitum tertio*) in Scotland. According to the Scottish Law Commission (hereinafter the SLC), the rigidity of current Scots law lies in the irrevocable nature of *just quaesitum tertio* in relation to third-party rights<sup>3</sup> and the consequential "significant barriers" inhibiting the use of third-party rights in practice.<sup>4</sup> The Commission holds the view that the element of certainty would be brought into Scots Law when issues such as: transformation from common law rules to statutes, prescription, remedies available to third parties in the case of breach<sup>5</sup> and the relationship between defences rules and third-party rights,<sup>6</sup> are addressed. By removing legal uncertainty caused by the *ad hoc* development of common law, the Act suggests the abolishment of the irrevocability rule, the clarifications of the remedies available to third parties, the confirmation of the defences rules allowing the parties to avoid obligations towards third parties, and the alignment with the contractual prescription rule and procedural access to arbitration.<sup>7</sup>

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<sup>1</sup> *SLC Report on Third-Party Rights in Contract*, paras 7.18 and 7.33, the jurisdictions mentioned as further comparative evidence included Singapore (s 9 of the Contracts (Rights of Third Parties) Act (Act 39 of 2001)), Cayman Islands (s 11 of the Contracts (Rights of Third Parties) Law 2014) and Hong Kong (s 12 of the Contracts (Rights of Third Parties) Ordinance (c 623, 2015))

<sup>2</sup> William McBryde, *The Law of Contract in Scotland*, (3<sup>rd</sup> edn Thomson & W Green Edinburgh) 10-17-10-24

<sup>3</sup> *SLC Report* (n 1) 1.6, 2.18-2.24

<sup>4</sup> *Ibid.* paras. 5.1-5.3

<sup>5</sup> *Ibid.* 2.49 and 7.12

<sup>6</sup> *Ibid.* 2.49 and 7.15

<sup>7</sup> Angus Evan, *SPICE Briefing Contract (Third Party Rights) (Scotland) Bill*, 6

Procedurally, section 9 of the Act allows a third-party to access the arbitration proceeding agreed as the dispute resolution mechanism between the parties. Regarding the procedural right to arbitration, the SLC holds the view that the current failure to address third-party rights in the Arbitration (Scotland) Act 2010 (the AA hereinafter) has left a third-party who is offered a substantive right by the parties to a contract but fails to satisfy the requirement of privity without a procedural entitlement<sup>8</sup> to join an arbitration or invoke an arbitration agreement between the parties to resolve disputes. Consequently, the Act recommends that ‘contracting parties may provide for disputes with third parties on whom they intend to confer an enforceable benefit (a third-party right) to be also subject to arbitration.’<sup>9</sup> Section 9 enables the third-party who has been conferred with the benefit of undertaking by the parties to the contract defined in section 1 of the Act the right to access arbitration proceedings if they want to avoid the courts. The Act also ‘allows them to do so through arbitration clauses.’<sup>10</sup> Nevertheless, allowing a third-party to exercise or invoke the right to arbitration and transforming himself from a person without privity to an arbitration agreement to a third-party taking part in arbitration proceedings may prompt concerns. The SLC correctly pointed out that third-party right would work very well ‘if the contracting parties are content that the matter ... should be determined by arbitration’,<sup>11</sup> nevertheless, due to privity, it would not work well if ‘the third-party makes the move which is opposed by one or more of the contracting parties.’<sup>12</sup> In the case of the latter, ‘the third-party will be confronted with the currently insuperable difficulty that it is not party to the arbitration agreement.’<sup>13</sup>

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<sup>8</sup> *SLC Report* (n 1) 7.29

<sup>9</sup> *SLC Report* (n 1) 7.33 and Contract (Third Party Rights) (Scotland) Act, s 9(1)

<sup>10</sup> Delegated Powers and Law Reform Committee 14 March 2017, Column 20 (per Hector MacQueen)

<sup>11</sup> *SLC Report* (n 1) 7.29

<sup>12</sup> *Ibid.*

<sup>13</sup> *Ibid.*

In the SLC's effort to make provision for a third-party to access arbitration proceedings through a third-party substantive right, it overwrites the essence of privity in arbitration and rules out the possibility of the parties who may have changed their mind about arbitration. During the Parliamentary evidence, Dundas was critical of the confusion between substantive rights and the procedural rights in the drafting language.<sup>14</sup> However, the Minister for Community Safety and Legal Affairs<sup>15</sup> remained unconvinced of the existence of such a confusion and claimed "a misunderstanding"<sup>16</sup> whereas the team leader's willingness to consider an amendment led to the removal of section 10 in the second reading.<sup>17</sup>

This research sets out to examine whether section 9 of the Act interacts well with domestic and international arbitration practice on privity. The main considerations of this research are the issues of nature of undertaking, privity in arbitration practice and the possible impact on the finality of the Scottish awards internationally. The current research will examine the above issues from the interactions between the Act, the AA and The Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (hereinafter the New York Convention). The research will start with a brief introduction of the purpose of the Act. It will be followed by a detailed discussion on the issue of privity, definition of party, timing of agreeing on arbitration agreement, definition of arbitration agreement and joint liability will be examined. Further examination into the right to justice will be carried out from the

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<sup>14</sup> Delegated Powers and Law Reform Committee, 18 April Column 7; Similar concerns were also raised by the English Law Commission which firstly reject the inclusion of arbitration provision but later decided to include it in s 8 of the Act. Similar concerns were also expressed by Robert Merkin, Arbitration Law (Informa Law Library) 17.49

<sup>15</sup> Annabelle Ewing

<sup>16</sup> Delegated Powers and Law Reform Committee, 25 April column 12, Annabelle Ewing, Minister for Community Safety and Legal Affairs; Catriona Marshall, solicitor, Scottish Government legal directorate; and Jill Clark, Bill team leader, civil law reform unit, Scottish Government 25 April

<sup>17</sup> *Ibid.* column 12, Annabelle Ewing, Minister for Community Safety and Legal Affairs; Catriona Marshall, solicitor, Scottish Government legal directorate; and Jill Clark, Bill team leader, civil law reform unit, Scottish Government 25 April

perspectives of the third-party and party respectively. The research will be concluded with suggestions on how section 9 of the Act would interact better with the AA.

## **II. FROM SUBSTANTIVE RIGHT TO PROCEDURAL RIGHT**

### **A. Codification Of Substantive Rights - *Jus Quaesitum Tertio***

Prior to the Act, subject to conditions, a third-party right can be conferred under common law rule of *jus quaesitum tertio* which has existed for many years in Scotland.<sup>18</sup> Third-party's right is conferred through the parties' undertaking which is the one intended by the parties to or not to perform some acts for the third-party's benefit.<sup>19</sup> However, McBride pointed out that the current development and practice of such a right have to be determined by the "construction of the contract"<sup>20</sup> in the cases where the ambiguity occurs. Consequently, the court may deny a third-party the benefit of suing the parties for breach of contract, despite the parties' intention. The Act was introduced to remedy the issues mentioned above by strengthening third-party rights.

The Act is intended to be right based as it expressed no intention to impose reciprocal duty on a third-party.<sup>21</sup> The codification of the rule of *jus quaesitum tertio* sees the creation of a third-party's statutory independent right to both substantive and procedural claims but with a more implicit language. For instance, the wording "in his own right" used in the English version is replaced with "a third-party right" throughout section 1 of the Act for the creation of the right

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<sup>18</sup> Evan, (n 7) 4; it is worth noting that the Scottish Act is to codify the third-party right whereas the English version is to create the third-party right.

<sup>19</sup> For instance, s 1(1) prescribes "acquires a third-party right", s 1(2) defines such right to enforce or invoke the undertaking is "a third-party right", s 1(3) requires possible identification of the person to be conferred the 'third-party right', furthermore, under s 1(4), a party who is not in existence or does not fall into description at the time of the contract was constituted may still acquire "a third-party right."

<sup>20</sup> McBryde (n 2) 10-24

<sup>21</sup> Contract (Third Party Rights) (Scotland) Act, ss 1 and 2

to enforce the undertaking.<sup>22</sup> The provision also prescribes both positive undertaking in the form of doing something for the person's benefit<sup>23</sup> and negative undertaking<sup>24</sup> in the form of refraining from doing something for the person.

Apart from codification, section 3(1) of the Act also intends to remove the current irrevocability in *jus quaesitum tertio*.<sup>25</sup> The draftsmen intend to mitigate the harshness of common law of *jus quaesitum tertio* by offering the party or the parties to the contract the freedom to revoke or modify the undertaking. This freedom corresponds with section 2(4)(a) of the Act on cancellation and modification. On the same token, such freedom is also recognised in section 3(2) which actively allows the party or the parties to the contract to declare non-possibility of cancellation and modification in a third-party right. However, the irrevocability is subject to the reliance exception discussed in the later section.

Agreeing with the view that current practice of third-party rights was 'real or potential issues for arbitration',<sup>26</sup> the justification of the inclusion of section 9 of the Act is introduced by the SLC. Such a justification is further agreed by practitioners<sup>27</sup> who prefer the use of the same dispute resolution forum when an arbitration agreement is embedded in the main contract which offers a third-party the right to a substantive claim. Modelled on section 8 of the

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<sup>22</sup> *Ibid.* s 1(2); Section 1 of the Act used "a third-party right" throughout the provision to create his right to enforce the undertaking<sup>22</sup> that one or more of the contracting parties will or will not perform some acts for the third-party's benefit which was intended by the parties. For instance, section 1(1) prescribes the condition of the acquirement of "a third-party right", section 1(2) defines such right to enforce or invoke the undertaking is "a third-party right", and identification of the third-party or ascertainment of a non-existing third-party is prescribed in sections 1(3) and 1(4) respectively.

<sup>23</sup> Contract (Third Party Rights) (Scotland) Act, s1(1)(a) and s 2(5)

<sup>24</sup> Contract (Third Party Rights) (Scotland) Act, s1(1)(b) and s 2(6)(a)-(b)

<sup>25</sup> *Carmichael v Carmichael 's Executrix* 1920 SC (HL) 195

<sup>26</sup> Delegated Powers and Law Reform Committee, 14 March (n 10) column 20

<sup>27</sup> Delegated Powers and Law Reform Committee, 21 March, column 28, Karen Fountain, Karen Manning, Jonathan Gaskell and Kenneth Rose. Although Craig Connal view share such a view, he highlighted the fact that arbitration is usually not the first port of call in disputes involving modern construction contracts. (28 March Column 34)

English Contracts (Rights of Third Parties) Act 1999<sup>28</sup> which was viewed by the SLC as the English solution working out the third-party right subject to arbitral enforcement,<sup>29</sup> the SLC followed suit and included the arbitration agreements and jurisdiction agreements in section 9 of the Act. Further aided by section 9 on arbitration, both provisions create a transformation of third-party's substantive right into a potential joint duty or independent procedural right. However, such a preference was questioned by the concerns over privity and the rarity of arbitration practice where 'third parties suddenly appear, acquire rights under a contract and therefore acquire rights to arbitration or obligation to arbitrate.'<sup>30</sup>

## B. Creation Of The Procedural Right - Privity In Arbitration

Section 9 offers a third-party the procedural right to arbitration. To do so, privity which is viewed as the core element of jurisdiction in arbitration<sup>31</sup> has to be removed to allow the third-party to enforce or invoke the right.<sup>32</sup> Allowing a third-party who is not a party to the original arbitration agreement to be engaged in arbitration raises the issues of: privity, jurisdiction, definition of party, timing of agreeing on arbitration agreement, definition of arbitration agreement and joint liability. All these concerns require a further detailed examination from the interaction between the Act and the AA. In this section, the examination will focus on the definition of "party" and "third-party", the nature of a third-

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<sup>28</sup> Although the English Law Commission (hereinafter the ELC) pointed out that the rationale of the 1999 Act is to be in line with Scots Law. The ELC also expressed the negative view prior to the inclusion of s 8 of the Act. See generally, The Law Commission (LAW Com 242), Privity of Contract: Contracts for the Benefit of Third Parties, Item 1 of the Sixth Programme of the Law Reform: The Law of Contract (1996), <[http://www.lawcom.gov.uk/wp-content/uploads/2017/02/lc242\\_privity-of-contract-contracts-for-the-benefit-of-third-parties.pdf](http://www.lawcom.gov.uk/wp-content/uploads/2017/02/lc242_privity-of-contract-contracts-for-the-benefit-of-third-parties.pdf)>

<sup>29</sup> Delegated Powers and Law Reform Committee, 14 March 2017, Column 20 (n 10), per MacQueen

<sup>30</sup> Delegated Powers and Law Reform Committee, 18 April Column 6 (n 14), per Dundas.

<sup>31</sup> It was described as "physical power" by Justice Holmes in *McDonald v Mabee*, 243 US 90, 91 (1915) or "legitimate authority" in Evan Tsen Lee, 'The Dubious Concept of Jurisdiction' (2003) 54 Hastings LJ 1613, 1620. Lord Justice Kerr, 'Arbitration and the Courts - the UNCITRAL Model Law' (1984) 50 *Arbitration* 3, 15, where avoiding "waste of time and costs" was mentioned.

<sup>32</sup> Merkin, (n 14) 17.1, though, he also highlighted the changes brought in by the Contracts (Rights of Third Parties) Act 1999 (c 31) in his discussion on *Northern Regional Health Authority v Derek Crouch Construction Co Ltd*. [1984] 2 All ER 175

party's right to arbitration ( based on a right or obligation), the effects of subsequent addition or withdrawal of arbitration, the interaction between the interpretation of arbitration agreement and the conferring of the third-party right under s 9(3), the action required by the third-party in the submission of dispute to arbitration under s 9(4) and how the Act would work with the international framework which is still dominated by privity.<sup>33</sup>

### 1. Section 9 In General

According to section 9, providing that there is an arbitration agreement between the parties' contract<sup>34</sup> which provides an undertaking benefitting a third-party, the third-party would have the right and /or duty retrospectively to submit the dispute to arbitration or apply to the court to sist (suspension of the legal proceedings) or suspend the court proceedings as if he were a party to the arbitration agreement.<sup>35</sup> This overwrites the concept of privity of arbitration agreement and endeavours to place the third-party on the same level as the parties by deeming him as a party to the arbitration agreement under s 9(1). Under this section, the third-party is allowed to exercise his third-party rights to enter into an arbitration to claim substantive rights based on the undertaking.<sup>36</sup> To allow the third-party to resolve disputes over a third-party substantive right arising from the undertaking of the contract between the parties, two conditions must be fulfilled before a third-party can exercise such a right; namely, there is a dispute concerning an undertaking in favour of the third-party and arbitration is specified as the means of dispute resolution.<sup>37</sup>

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<sup>33</sup> Bin Cheng, *General Principles of Law as Applied by International Courts and Tribunals* (2006) Cambridge University Press 262; Zheng Sophia Tang, *Jurisdiction and Arbitration Agreements in International Commercial Law* (Routledge 2014) 1-3.

<sup>34</sup> Explanatory Notes, para 36

<sup>35</sup> *Ibid*, para 37

<sup>36</sup> Contract (Third Party Rights) (Scotland) Act, s 1(1)(a)

<sup>37</sup> Contract (Third Party Rights) (Scotland) Act, s 9(2)(a) and (b)



Beyond section 9(1), sections 9(2) and (3) provide two legal bases for arbitrating the disputes involving third-party rights. Section 9(2) provides a mechanism based on contractual claims whereas the settlement of non-contractual claims is provided in section 9(3). Section 9(2) applies to a dispute concerning a substantive third-party right arising from the main contract which requires contractual disputes, including disputes about the right in the third-party's favour, to be submitted to arbitration. According to the Explanatory Notes,<sup>38</sup> this provision intends to cover most cases, such as those arising from the situations where the third-party has a right to be indemnified by a contracting party against claims for which the third-party is found liable. Under this provision, the third-party must submit the dispute to arbitration if he wishes to pursue it. This is an imposition of duty on the third-party. Section 9(2) also provides a third-party the defence power to apply to the court for a sist to enforce the arbitration agreement against the main parties if a contracting party raises a court action against the third-party. However, section 9(2) offers the third-party not only a right to enforce or invoke the arbitration agreement but also a duty to resolve disputes by arbitration.

Section 9(3) provides a third-party an independent right to pursue non-contractual disputes related to the main contract, e.g. a delict brought by or against a party to an arbitration agreement, where a third-party is conferred with the similar right to enforce the arbitration agreement or seek a sist from the court. According to the provision, based on the independent and non-contractual right, the third-party has the right to exercise his option (but not the obligation) of submitting the dispute to arbitration or seeking a sist in respect of a court action raised against it.<sup>39</sup>

### C. Confusion Between Substantive And Procedural Rights

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<sup>38</sup> Explanatory Notes, para 37.

<sup>39</sup> Evan, (n7) 11

In terms of substantive rights, there are positive undertakings in the form of doing something for the person's benefit<sup>40</sup> and negative undertakings<sup>41</sup> in the form of refraining from doing something for the person. Dundas was critical of the confusion between substantive rights and the procedural rights in the drafting language.<sup>42</sup> He proposed the drafting changes made by the Faculty of Advocates to be considered.<sup>43</sup> However, the Minister Ewing remained unconvinced of the existence of such a confusion. She held the view that it was 'a misunderstanding on the part of those who have a problem with the drafting – they might not have understood the way in which section 9 sits in the Bill and its interrelationship with other sections, ...'<sup>44</sup> while the Clark, the Bill team leader acknowledge their willingness 'to consider an amendment'.<sup>45</sup> In its second reading, though leaving section 10 out of the Bill, the draftsmen maintained their position on section 9 of the Bill in terms of third parties' access to procedural right to arbitration through the substantive right. The main amendments are carried in section 9(4) and (4A) of the Act where the draftsmen removed the ill-drafted section 9(4A) and further tightened up section 9(4) with a more concise provision which now reads: 'For the purpose of subsection (3)(d)(i), the person who has the third-party right is to be regarded as having submitted the dispute to arbitration if the person has done whatever a party to the agreement would need to do in order to submit the dispute to arbitration.' They also further inserted section 9(4A) which is a succinct version of the removed section 10(2) about the issue of renouncement. It reads: 'A person is not to be regarded as having renounced a third-party right to enforce or otherwise invoke an undertaking to resolve a dispute by arbitration by bringing legal proceedings in relation to the dispute.'

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<sup>40</sup> Contract (Third Party Rights) (Scotland) Act, s 1(1)(a) and s 2(5)

<sup>41</sup> Contract (Third Party Rights) (Scotland) Act, s1(1)(b) and s 2(6)(a)-(b)

<sup>42</sup> Delegated Powers and Law Reform Committee, 18 April, column 7 (n 14)

<sup>43</sup> *Ibid.* column 7

<sup>44</sup> Delegated Powers and Law Reform Committee 25 April, column 12 (n 16)

<sup>45</sup> *Ibid.* column 12

### **III. ISSUE OF PRIVITY IN ARBITRATION AGREEMENT – SHOULD A THIRD-PARTY BE A PARTY FOR THE PURPOSE OF THE ACT?**

#### **A. Privity in international arbitration framework**

The AA is promulgated to modernise the Scottish arbitration law and to attract the users of international arbitration to Scotland.<sup>46</sup> To bridge Scotland with the international arbitration, the enforceability of the Scottish awards cannot be a Pyrrhic victory.<sup>47</sup> The Contract (Third Party Rights) Act gives a third-party the substantive right<sup>48</sup> to access to the procedural right to arbitration by regarding the third-party as a party to the arbitration agreement.<sup>49</sup> This would prompt the question whether section 9 fulfils the conditions required for international practice of the recognition or enforcement of arbitral awards under the framework of the Convention on the Recognition and Enforcement of Foreign Arbitral Awards 1958 (hereinafter the New York Convention) which currently dominates the enforceability of convention awards.

The combined readings of section 9 of the Act and the AA raises concerns of the potential unenforceability of awards made in Scotland due to the potential lack of support in other national laws.<sup>50</sup> Such a caution is warranted as an arbitration agreement between the parties is

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<sup>46</sup> Luca Radicati Di Brozolo, 'International arbitration and domestic law' in Giuditta Cordero-Moss (ed) *International Commercial Arbitration: Different Forms and their Features* (Cambridge University Press 2013) 40, 47 where the author has indicated that jurisdictions have started modernisation of their arbitration laws in order to become arbitration-attractive seats.

<sup>47</sup> A. Belohlavek, 'The Legal Nature of International Commercial Arbitration and the Effects of Conflicts Between Legal Cultures' (2011) 2 *Law of Ukraine* 27.

<sup>48</sup> Contract (Third Party Rights) (Scotland) Act, s 1(1)

<sup>49</sup> *Ibid.* section 9(1)

<sup>50</sup> Tang, (n 33), 224.

based on privity which is carried throughout the international framework<sup>51</sup> and the AA. The dominating role played by privity is evident in the current international framework of enforcement as Articles, II, IV and V of the Convention stipulates. For instance, Article II(2) of the Convention requires the arbitration agreement to be signed by the parties;<sup>52</sup> a copy of the arbitration agreement mentioned in Article II(2) of the Convention is required as evidence for the application of recognition and enforcement of foreign awards;<sup>53</sup> All these are provided to satisfy the requirement of jurisdictional element before the effects of the tribunal's power can reach the parties to the arbitration agreement.<sup>54</sup> The recognition or enforcement of an award may be refused if a lack of jurisdiction is apparent<sup>55</sup> or the agreement referred to in Article II is not valid under the law applicable to the parties.<sup>56</sup> Furthermore, the issue of privity may be examined by the enforcing court under Article V(2)(b) of the New York Convention which allows the enforcing court exercise its discretion to set aside an award on the ground of breach of public policy which imposes the requirement of privity.<sup>57</sup> A strict application of the principle of privity by the enforcing court would rule out the participation of a third-party and have a direct impact on jurisdictional issues when the parties arrive at the point of setting aside, recognition or enforcement of arbitral awards.

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<sup>51</sup> Margaret L. Moses, *The Principles and Practice of International Commercial Arbitration* (Cambridge University Press 2008) 17; Henry P de Vries, 'International Commercial Arbitration: A Contractual Substitute for National Courts' (1982) 57 *Tulane Law Review* 42.

<sup>52</sup> The New York Convention, Article II (2) reads: '2. The term "agreement in writing" shall include an arbitral clause in a contract or an arbitration agreement, signed by the parties or contained in an exchange of letters or telegrams.'

<sup>53</sup> *Ibid.* Article IV(1)(b)

<sup>54</sup> Maria Hook, 'Arbitration Agreements and Anational Law: A Question of Intent?' (2011) 28 *Journal of International Arbitration* 175.

<sup>55</sup> Fraser Davidson, Hew, R. Dundas, David Bartos, *Arbitration (Scotland) Act 2010* (W. Green 2010) 18-19.

<sup>56</sup> The New York Convention, Article V(1)(a) reads: '(a) The parties to the agreement referred to in article II were, under the law applicable to them, under some incapacity, or the said agreement is not valid under the law to which the parties have subjected it or, failing any indication thereon, under the law of the country where the award was made.'

<sup>57</sup> Horatia Muir Watt, '"Party Autonomy" in international contracts: from the makings of a myth to the requirements of global governance' (2010) 6 *European Review of Contract Law* 250, 254.

Placing the family holiday example<sup>58</sup> discussed in the Policy Memorandum within the international framework, a third-party may find it difficult to enforce the award in his favour in a country which upholds the principle of privity or expressly disallows third-party rights in engaging in the parties' arbitration. Similarly, a party may find himself fighting against jurisdictional issue in a foreign court over the enforcement against the third-party. Under these circumstances, the finality of the Scottish awards may be called into question on the ground of the tribunal's lack of jurisdiction over the third-party. After all, as both Lew<sup>59</sup> and Paulsson<sup>60</sup> pointed out that the contractual nature of arbitration is facilitated and regulated by the national legal framework which requires a mutually acceptable agreement that complies with the legal requirements between the parties. As a result, international parties will have to exercise an extreme caution in their choice of Scotland as the place of arbitration. As a result, the Scottish Government's intention to attract international arbitration to Scotland or indeed parties' attempts to enforce the Scottish arbitral awards in the signatory countries to the New York Convention may be affected. To avoid this, it is first essential to examine the definition of "party" and "third-party" in order to clarify the jurisdictional issues.

#### 1. Can a third-party be a party?

Section 9(1) of the Act provides that, in relation to a dispute to which section 9(2) or (3) applies, the person who is conferred with the third-party right is to be regarded as a party to the arbitration agreement. Similar to its English counterpart, the language suggests that once the third-party invoke or enforce the arbitration agreement, through sections 1 and 9, this third-party will be viewed as a party to the arbitration.

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<sup>58</sup> The example argued that the Act will be able to allow the family members to sue the tour operator directly, rather than through the member who is a signing party to the package holiday contract.

<sup>59</sup> Julian DM Lew, 'Arbitration Agreements: Form and Character' in Petar Sarcevic (ed), *Essays on International Commercial Arbitration* (Graham & Trotman 1989) 51, 52

<sup>60</sup> Jan Paulsson, *The Idea of Arbitration* (Oxford University Press 2013), 1-2

However, this may go against a strict interpretation of the requirement of parties' direct consent which is still currently in place of the arbitration system.<sup>61</sup> The references to "parties", "between parties" or "parties otherwise agree" can be observed throughout the Act and the Scottish Arbitration Rules (the Rules hereinafter). For instance, all default rules in the Rules make room for parties to the arbitration agreement to modify or disapply the default rules while "between parties" can be noticed in section 1(b) on the founding principles, section 2(1)(b) on the definition of arbitration, section 8 on mandatory rules, section 19 on the binding effects of award between the parties, and section 31(2) of the AA. All these indicate that privity in the parties' consent is an essential feature of the Scottish arbitration law. Based on this, privity clearly takes a pro-dominate role in the AA. The Policy Memorandum further expressly stated that 'the arbitration agreement between the parties is fundamental to arbitration.'<sup>62</sup> At this juncture, s 9 of the Act will have to be drawn into discussion on whether the requirement of mutual consent in an arbitration agreement would prohibit a third-party to exercise his right under section 9 of the Act and the AA.

First of all, it is important to highlight that the AA has always been based on privity. According to privity, a third-party's right to enter into arbitration between other parties is currently not considered. This is because arbitration is argued for its contractual character that originates in the parties' arbitration agreement. Such a voluntary nature in arbitration agreement was succinctly asserted by Kellor who stated:

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<sup>61</sup> George A. Bermann, 'The "Gateway" Problem in International Commercial Arbitration' (2012) 37 *The Yale Journal of International Law* 1, 2, where the author argued: 'its use is predicated on the consent of the parties'

<sup>62</sup> Policy Memorandum accompanied the Arbitration (Scotland) Act 2010, para 69; Jonatan Mance, 'Arbitration: a Law unto itself?' (2016) 32 *Arbitration International* 223, 224; Hiro N Aragaki, 'Does Rigorously Enforcing Arbitration Agreements Promote "Autonomy"?' (2016) 91 *Indiana Law Journal* 1143, 1146; Thomas E Carbonneau, 'The Exercise of Contract Freedom in the Making of Arbitration Agreements' (2003) 36 *Vanderbilt Journal of Transnational Law* 1189, 1195

Arbitration is wholly voluntary in character. The contract of which the arbitration clause in a part is a voluntary agreement. No law requires the parties to make such a contract, nor does it give one party power to impose it on another. When such an arbitration agreement is made part of the principal contract, the parties voluntarily forgo established rights in favour of what they deem to be the greater advantages of arbitration.<sup>63</sup>

Based on privity and the voluntary nature of arbitration, party autonomy is well recognised in the international instruments and arbitration rules, such as the UNCITRAL Model Law,<sup>64</sup> the UNCITRAL Arbitration Rules, the ICC Arbitration Rules, The LCIA Arbitration Rules and other authorities. For instance, Lew stated: '[t]he agreement to submit disputes to arbitration is governed by two intertwining principles: party autonomy and the contractual nature of the agreement.'<sup>65</sup> In Scotland, party autonomy is set as one of the founding principles provided in section 1 of the AA.<sup>66</sup> However, the effect of an arbitration agreement affects only the parties who are directly involved in the agreement.

The SLC Report on the Act argued against the significant importance of the direct consent in arbitration. In the report, The SLC relies heavily on Steingruber<sup>67</sup> and Brekoulakis who invoked the concept of 'third-party beneficiaries of rights under a contract' to 'address multi-

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<sup>63</sup> F Kellor, *Arbitration in Action*, quoted by P Stone, 'Paradox in the theory of commercial arbitration' (1966) *Arb J* 156, 156 and J Lew, *Applicable Laws in International Commercial Arbitration* (1978) 55

<sup>64</sup> Norbert Horn, 'The arbitration agreement in light of case law of the UNCITRAL Model Law (Arts 7 and 8) (2005) 8 *International Arbitration Law Review* 146; Gerold Herrmann, 'Introductory Note on the UNCITRAL Model Law on International Commercial Arbitration' (1985) 1 *Uniform Law Review* 285, 291-293.

<sup>65</sup> Lew (n 59) 51; Mia Louise Livingstone, 'Party Autonomy in International Commercial Arbitration: Popular Fallacy or Proven Fact' (2008) 25 *Journal of International Arbitration* 529, 530.

<sup>66</sup> Joanna Dingwall, 'International Arbitration in Scotland: A Bold New Future' (2010) 13 *International Arbitration Review* 138, 140.

<sup>67</sup> A M Steingruber, *Consent in International Arbitration* (OUP 2012) Chapter 9

party, and indeed multi-contract relations in international arbitration’,<sup>68</sup> where Brekoulakis further argued for third-party’s “automatic entitlement” to enforce the arbitration agreement once his third-party substantive right is established.<sup>69</sup>

Following this, in order to link the Act with the existing Arbitration (Scotland) Act 2010, section 9(5) provides the definitions of arbitration agreement and dispute by referring to sections 2 and 4 of the AA.<sup>70</sup> However, a direct application of section 9 of the Act would require a wider interpretation of “party” provided in the AA. This is because the wording of “third-party” used in the AA means any parties apart from the direct parties to the arbitration agreement. This is rather different from the one provided in the Act which deems the third party as a party. Hence, it is necessary to examine the issues of definitions of “third-party” and “party” and whether a third-party can be a party under both the AA and the Act.

2. *Does “third-party” mean the same thing in both the AA and the Act? - A clarification and a wider definition is required*

According to section 2(1) of the AA, “party” means a party to an arbitration without other further qualification. If one takes international arbitration consensus into consideration, “party” is the person who has positively waived his right to resolve dispute in courts and

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<sup>68</sup> SLC Report (n 1) 7.9; Ibid, paras 9.26-9.28 The SLC also cited the example of “string contracts”, discussed in F Davidson, *Arbitration* (2<sup>nd</sup> ed, 2012), para 13.08.

<sup>69</sup> S Brekoulakis, *Third Parties in International Commercial Arbitration* (2010), paras 2.143-2.163; Stavros L. Brekoulakis, ‘Parties in International Arbitration: Consent v Commercial Reality’ in Stavros L. Brekoulakis, Julian D.M. Lew et al (eds) *The Evolution and Future of International Arbitration* (Kluwer Law International 2016) Chapter 8, paras 8.35-8.43. The SLC also relied on the English proposition on the third –party being bound by the agreement and constrained to pursue arbitration, US practice of estoppel, French and Chilean court judgements. paras 7.12-7.13

<sup>70</sup> Explanatory Notes accompanied the Arbitration (Scotland) Act 2010, para 39



opted for arbitration as the dispute resolution mechanism.<sup>71</sup> The term “party” can be seen in the AA and the Rules in relation to parties’ exercise of their autonomy in deciding the matters related to arbitration proceedings. For instance, section 6 of the AA mentioned “the parties” to an arbitration agreement in the determination of the law governing arbitration agreement and s 9 sets out the parties’ power in modifying or applying default rules.

Meanwhile, the reference to a “third-party” in the AA and the Rules means any person who is not the direct parties to the arbitration agreement, but for some reason is involved in arbitration proceedings. For instance, the issue of the lack of tribunal’s jurisdiction over a person who is not the party to the arbitration agreement discussed in sections 12(3) or 20(2)(b) and (3)(c) of the AA in an enforcement of a Scottish or international award respectively as well as rule 67 in the case of challenge of an award on the issue of substantive jurisdiction. “Third-party” is also highlighted in rule 26(2) which requires the tribunal and the parties to take reasonable steps to prevent unauthorised disclosure of confidential information defined in rule 26(1) by any “third-party” involved in the conduct of the arbitration.

The different meanings of parties and third-party in both the Act and the AA prompted the SLC to search the Explanatory Notes to the AA for a possible wider definition of “party”. It found no further clarification whether a third-party can be deemed as a “party to an arbitration” defined in section 2 of the AA.<sup>72</sup> Despite the SLC’s acknowledgement that no comment was offered on this issue, it positively assumed that the term “party” ‘must be wider in scope than “parties to the arbitration agreement” because the AA elsewhere refers to the possibility of parties to the arbitration being persons claiming “through or under a party to the

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<sup>71</sup> Henry P de Vries, 'International Commercial Arbitration: A Contractual Substitute for National Courts' (1982) 57 *Tulane Law Review* 42, 43; Margaret L. Moses, *The Principles and Practice of International Commercial Arbitration* (Cambridge University Press 2008) 17.

<sup>72</sup> Arbitration (Scotland) Act 2010, s 2.

arbitration agreement”.<sup>73</sup> Therefore, the SLC held the view that ‘the 2010 Act thus deliberately leaves open the possibility that persons not privy to the arbitration agreement might nonetheless become parties to the arbitration under the agreement.’<sup>74</sup> Once the link between the AA and the Act was created, the discussion above would be able to create a platform which clearly demonstrated that privity is no longer an essential element in a third-party’s access to arbitration according to sections 1 and 9 of the Act. The SLC was able to use its idea of “party claim under the right” as its justification to bring a third-party into the arbitration proceedings.

Nevertheless, the researcher is of the view that amendments to the definition of party in section 2 of the AA will provide opportunity for the applications of s 31(2) of the Act and s 9 of the Act. Currently, section 31(2) reads: ‘[t]his Act applies in relation to arbitrations and disputes between three or more parties as it applies in relation to arbitrations and disputes between two parties (with references to both parties being read in such cases as references to all the parties).’ However, this provision refers to multi-party arbitration provided in rule 40 of the Rules where all parties’ consent is required. However, an amendment to section 2 of the AA linked to the Act will afford the legal basis for third-party’s right to arbitration under s 9 of the Act.

Over and above, the definition of “party” is significantly linked to rule 1 of the Rules. It is commonly accepted that a party to an arbitration agreement can give the other party notice submitting a dispute to arbitration in accordance with the agreement. Access to arbitration

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<sup>73</sup> Arbitration (Scotland) Act 2010, ss 10 and 11. See also Rule 1 of the Scottish Arbitration Rules. It reads: “An arbitration begins when a party to an arbitration agreement (or any person claiming through or under such a party) gives the other party notice submitting a dispute to arbitration in accordance with the agreement.” For discussion of the equivalent phrase in s 82(2) of the Arbitration Act 1996 (England & Wales) see T Molloy QC and T Graham, “Arbitration of trust and estate disputes” (2012) 18(4) *Trusts and Trustees* 279, 282-286.

<sup>74</sup> *SLC Report* (n 1) 7.24

proceeding would only work if the third-party is clearly defined in both instruments as “party” to satisfy the requirement of privity. If a third-party is confronted with the ‘currently insuperable difficulty’<sup>75</sup> of privity, it would have no legal entitlement to commence arbitration under rule 1 of the Scottish Arbitration Rules. However, it is also worth noting that the initiation of the arbitration process can also be carried out by ‘any person claiming through or under such a party’ who is the direct party to the arbitration agreement. The claim through or under such a party is thought to be the claim of a substantive right. Linking such an interpretation with s 1 of the Act, a third-party who has been conferred would have the right to the arbitration process where he was not a party to it.

To eliminate any possible confusion between “party” and “third-party” arising from the Act and the AA, the researcher urges the draftsmen to consider to propose an amendment to widen the definition of “party” given in s 2 of the AA to include a cross-reference to sections 1 and 9 of the Act, by adding wording such as “party means a party to arbitration, including a third-party defined in Contract (Third Party Rights) (Scotland) Act”. Furthermore, an amendment to the term of “third-party” mentioned in rule 26(2) should also be addressed as third-party in this rule can mean lawyers, witnesses or expert witnesses. Similarly, in the provision related to appointment referees, the use of “third-party” indicates a third-party who is delegated with the power to appoint the arbitrators and has the legal status of assuming the role of a party.<sup>76</sup> Such an amendment will allow the third-party to assume the role of a party to the contract and avoid the difficulties arising from the debates over consent. Further amendment may also be required to be made to sections 1(1), 11, 8 and 13 of the AA for clarification purposes. Once a wider definition is provided, a third-party will not encounter “currently insuperable difficulty” but will be viewed as a party who would fulfil the

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<sup>75</sup> *Ibid.* 7.29

<sup>76</sup> The Scottish Arbitration Rules, Rule 24

jurisdictional requirement stipulated in Articles V(1)(a) and V(2)(b) of the NYC in those jurisdictions recognise a third-party right.

Unfortunately, at the time of writing, no such cross reference was made to the Act and the AA at the all stages of legislation. Instead, the Act sought a clarification within the Act itself and merely provided that: “For the purpose of subsection (3)(d)(i), the person who has the third-party right is to be regarded as having submitted the dispute to arbitration if the person has done whatever a party to the agreement would need to do in order to submit the dispute to arbitration.”

3. Party’s right – contractual / non-contractual right, future / retrospective right, dependent / independent right

Being a party to the arbitration agreement, the party has a contractual right to commence arbitration according to rule 1 of the Scottish Arbitration Rules. Before exercising such a right, the party concerned must prove that he is the party to the arbitration agreement to submit a present or future dispute to arbitration as discussed above. For a third-party to invoke his right to arbitration under section 9(2) of the Act, his identity must be named or established in the contract<sup>77</sup> to allow his procedural access to arbitration to claim his substantive contractual right defined in section 2 of the AA. For a present dispute, such fact is easier to be established, ‘there is no difficulty where contracting parties and a third-party are already in dispute about a third-party right said to arise from the contract’<sup>78</sup>. In the case of a

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<sup>77</sup> Contract (Third Party Rights) (Scotland) Act, s 1(3)

<sup>78</sup> *SLC Report* (n 1) 7.28

future dispute,<sup>79</sup> the Act offers the parties to name or provide sufficient information to establish the identity of the third parties<sup>80</sup> whom they wish to benefit from the conferred right under s 1 of the Act. In the case of a future dispute, difficulty may arise when one of the parties challenge the identity of the third-party who makes a claim to a substantive right under the contract or not or applies to the court for a sist. In the event of a successful challenge, the “third-party” is not party to the arbitration agreement via sections 1 and 9, consequently, it has no entitlement to commence arbitration according to rule 1 of the AA.

The other issue related to the Act is the types of dispute which are allowed to be submitted to arbitration. Section 2 of the AA defines the dispute as “contractual or not”. This opens the door for non-contractual disputes to be submitted to arbitration. As discussed, the submission of a contractual claim falls into the scope of section 9(2) of the Act, whereas the submission of a non-contractual dispute demands the application of section 9(3) of the Act which provides a third-party with an independent procedural right to arbitration for both present and future disputes.

It is also worth noting that, according to the Explanatory Notes, section 2 allows the third-party substantive right to be a future or conditional right but not a retrospective right. For instance, it stated that the undertaking referred in section 1(2) of the Act can be dependent upon the occurrence or non-occurrence of a future event as discussed. Equally, the third-party right can also be established, enforced, invoked once a condition is fulfilled. The background of this provision is linked to general Scottish contract law which allows the existence or

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<sup>79</sup> Arbitration (Scotland) Act 2010, s 2 provides the definition of a dispute as a present or future dispute.

<sup>80</sup> Contract (Third Party Rights) (Scotland) Act, s 1(3)

resolution<sup>81</sup> of a right to be suspended or pending upon the occurrence of an event which may or may not happen.<sup>82</sup>

A further issue which one has to consider is whether the conferring of a third-party right is to create a dependent right upon the original right-holder, and subsequently being transferred into an independent right when the third-party elects to exercise the right or a person comes into existence or answering the relevant description.<sup>83</sup> According to the SLC's interpretation of *Love v Amalgamated Society of Lithographic Printers of Great Britain and Ireland*,<sup>84</sup> the SLC seems to suggest that the third-party right comes into existence when it was given but such a right is only 'suspended until the condition is met.'<sup>85</sup> Once the condition is met the third-party should be able to exercise his right. Such an analysis seems to indicate that the SLC intends to offer an independent third-party right which may be an active right or a suspended or resolute right. If this is the case, it can be assumed that the SLC intends to create dual independent substantive rights for the parties and the third-party who can exercise their rights individually. However, the reading of proposed provisions seems to suggest otherwise. In the Act, the SLC proposes that, subject to sections 4, 5 and 6, the creation of third-party right can be cancelled or modified by the contracting parties.<sup>86</sup> If a cancellation or modification is allowed, a third-party's right is only a conditional independent right because it would be affected by the original right holder's power to modify or withdraw.

However, the answer may be different in terms of a third-party's procedural right. Due to the principle of separability which allows an arbitration agreement to be detached from a void

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<sup>81</sup> The SLC used resolute condition discussed in *Kelly v Cornhill Insurance Company Ltd* (1964) SC (HL) 46 to illustrate how a third party's right could be brought to an end at any time by permission being withdrawn.

<sup>82</sup> Explanatory Notes accompanied Contract (Third Party Rights) (Scotland) Act, para 14

<sup>83</sup> *Ibid.* para 12

<sup>84</sup> (1912) SC 1078

<sup>85</sup> Explanatory Notes accompanied Contract (Third Party Rights) (Scotland) Act, para 15

<sup>86</sup> Contract (Third Party Rights) (Scotland) Act, ss 3(1) and (2)

main contract.<sup>87</sup> Unless the third-party right is cancelled by the original right-holder, a third-party would be required to exercise his independent procedural right to apply for a sist or have access to arbitration<sup>88</sup> in order to pursue a substantive contractual claim against one of the parties or respond to the claim against him brought by one of the parties. Furthermore, a third-party can always exercise his independent right to pursue a settlement of a non-contractual dispute in arbitration or court.<sup>89</sup>

#### 4. A third-party's duty or right to arbitration?

Although it appears that a third-party is offered a right to arbitration, it is worthwhile highlighting that a third-party's right to pursue arbitration is in fact both a right and corresponding duty to engage in arbitration according to the language of section 9(2) of the Act and the Explanatory Notes. In the event of a contractual dispute, a third-party's corresponding duty lies in the only choice available to him to respond to a claim against him through arbitration. At the same time, the SLC adopted the "third-party right to arbitrate" by offering a third-party active /defending right to seek a sist if a court action was brought against him when the main contract contains an arbitration agreement. In contrast to the prescribed method of dispute resolution for contractual disputes, section 9(3) of the Act was encouraged by Brekoulakis' view on the "benefit conditional on arbitral enforcement" where a third-party is not imposed upon the duty to arbitration, where he argued that '[t]his effectively means that if, but only if, the third-party beneficiary chooses to exercise the substantive benefit offered to it, it will be bound by the arbitration clause contained in the

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<sup>87</sup> Arbitration (Scotland) Act 2010, s 5

<sup>88</sup> Contract (Third Party Rights) (Scotland) Act, s 9(2)

<sup>89</sup> Contract (Third Party Rights) (Scotland) Act, s 9(3)

main contract.<sup>90</sup> Consequently, a third-party is given the choice to pursue a non-contractual claim in court or arbitration under section 9(3).<sup>91</sup> Section 9(3) is designed to deal with the situation where the third-party does not have a substantive right under the contract but might otherwise have a procedural right to invoke the arbitration agreement.<sup>92</sup> It was pointed out that the purpose of this section is broadly in line with international trend in relation to moving away from privity for the purposes of arbitration.<sup>93</sup>

#### 5. Forcing the parties to return to arbitration?

For any dispute arising from a non-contractual dispute but related to the main contract, section 9(3) of the Act provides the third-party with an independent right to resolve the disputes by arbitration. The draftsmen used the term ‘a right created outwith the bounds of the contract’.<sup>94</sup> For example, the third-party is given an ‘option’<sup>95</sup> to choose whether to submit the dispute to arbitration or not; such as a delictual dispute arose from the construction contract. It is important to point out that this is a right, not an obligation imposed upon the third-party. Apart from the two conditions listed in section 9(2), a third-party has the right to enforce or otherwise invoke the agreement in relation to the matter under dispute, moreover, the third-party has already submitted the dispute to arbitration or sought to sist the legal proceedings by asking the courts to decline the jurisdiction based on the existence of an arbitration agreement. A third-party with the right can also be presumed to have exercised the

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<sup>90</sup> Brekoulakis (n 69) paras 8.33-8.34; W. Park, ‘Non-signatories and International Contracts: An Arbitrator’s Dilemma’ in Permanent Court of Arbitration (ed), *Multiple Party Actions in International Arbitration* (OUP 2009), para. 1.51

<sup>91</sup> Brekoulakis (n 69) *Third Parties in International Commercial Arbitration*, para 2.165. See also paras 2.179-2.180, for a re-statement of this position on which “there is safe consensus”, para 2.178; *SLC Report* (n 1) 7.9-7.11

<sup>92</sup> Delegated Powers and Law Reform Committee 21 March (n 27) column 14, per John MacLeod

<sup>93</sup> *Ibid.*

<sup>94</sup> Explanatory Notes (n 85) para 38

<sup>95</sup> *Ibid.* The draftsmen stated that ‘gives the third party the option (but not the obligation) of submitting the dispute to arbitration or seeking a sist in respect of a court action raised against it.’



right under section 9(3)(d)(i) if he ‘has done whatever a party to the agreement would need to do in order to submit the dispute to arbitration.’<sup>96</sup>

Leaving privity aside, given such a choice, what a third-party will do is to bring a party or both parties to the forum of his choice. The SLC specifically pointed out that this entitlement is not an obligation but a choice.<sup>97</sup> Suppose the parties chose to elect their contractual right to resolve their contractual disputes by arbitration, under the proposed provision, the party or parties can still be brought back to the court to resolve non-contractual disputes by the third-party. Such an undesirable scenario can also occur in the situations where parties elect an amiable settlement and choose not to commence arbitration under rule 1 of the Rules or where the parties jointly denounced the arbitration agreement and choose court as the forum but being brought back to arbitration with the third-party.

#### **IV. DIFFICULTIES ARISING FROM THIRD-PARTY’S DENUNCIATION OF THE SUBSTANTIVE RIGHT**

During its first reading, the Act suggested that, though the parties can confer the third-party an undertaking, the third-party does not have to accept it. The third-party could denunciate the substantive right either expressly or impliedly according to section 10(1). Interestingly, section 10(2) of the Act stipulated that, with the existence of an arbitration agreement in the contract, third-party’s rights to arbitrate under section 9(2) and (3) remains. This provision seemed to be unnecessary as the autonomy of arbitration agreement would require the court to sist the court proceedings raised by the parties, includes a third-party who is deemed to be a party, to the agreement.

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<sup>96</sup> Contract (Third Party Rights) (Scotland) Act, s 9(4)(b)

<sup>97</sup> Evan (n 7) 11 The example given was a deliberate or negligent breach of a legal duty.

However, what if the parties did not seek a sist in the court proceedings raised by the third-party, does this indicate that the parties and third-party denounce the arbitration agreement? To operate section 10, the most important consideration is that the party to the legal proceedings has to make an application to the court<sup>98</sup> to enable the court to exercise its power to sist the proceedings.<sup>99</sup> The reading of the provisions seems to suggest that the parties are bound by the arbitration agreement whilst the third-party has a cherry-picking approach in terms of dispute resolution. However, a further issue may arise if the parties neither take any steps prescribed in the Act nor seek a sist in the court proceedings raised by the third-party. Does this indicate that both the parties and third-party denounce the arbitration agreement? If so, would the court be able to, on its own initiative, decline its jurisdiction and refer the parties back to arbitration as if the arbitration agreement was not renounced by actions? The researcher is of the view that the court should refer all parties to arbitration related to section 9(2) which is based on a duty, whereas the scope for parties' joint denunciation of arbitration may be available in the case of section 9(3) which is based on an option. Although the draftsmen had a second thought on section 10, they remained unchanged on the issue of renunciation by moving section 10(2) into section 9(4A) in the second reading which made its way through the final reading.<sup>100</sup>

## **V. ISSUES OF CONSENT, ORAL AND IMPLIED AGREEMENT?**

In relation to concerns over non-enforceability of the Scottish awards in the countries where a third-party procedural right is not allowed, one may suggest the removal of section 9 of the

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<sup>98</sup> Arbitration (Scotland) Act 2010, s 10(1)(b)

<sup>99</sup> Arbitration (Scotland) Act 2010, s 10(1)

<sup>100</sup> Delegated Powers and Law Reform Committee: Stage 2, 27 June 2017, Marshalled List of Amendments for Stage 2, Contract (Third Party Rights) (Scotland) Act

Act. Other suggestions include the requirement of a third-party's signature and parties' consent, however, they could only be sustained in the case of a present dispute and the third-party's awareness of the conferred right. For a future dispute or a third-party whose identity needs to be ascertained or who is unaware of the right may require further consideration. In any case, a third-party should not be compelled to sign the arbitration agreement as this would be breach the voluntary nature of arbitration and further impact upon the validity of the arbitration agreement.

These concerns can also be examined from the issues of written requirement and implied agreement. For the written requirement, Section 1 of the Act provides that the third-party right does not have to be in the written form. This is to underpin the general Scots contract law which recognises both written and verbal agreements.<sup>101</sup> That an undertaking can be expressed in writing in a contract or orally between the parties to the contract is also reflected in section 4 of the AA which allows oral arbitration agreements.

However, an oral arbitration agreement comes with its own set of problems at the stage of enforcement of NYC awards.<sup>102</sup> To enforce a NYC award in a signatory country to the New York Convention and in Scotland under section 21 of the AA or enforce a Scottish award in a New York Convention country, the original or a duly certified copy of arbitration agreement is required to be submitted as evidence when seeking enforcement.<sup>103</sup> In the case of an oral arbitration agreement, difficulties may arise from the burden of proof. Under these circumstance, the SLC may wish to consider to amend section 21 of the AA which currently

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<sup>101</sup> Hew R Dundas, 'The Arbitration (Scotland) Act 2010: Converting Revision into Reality' (2010) 76 *Arbitration* 2, 13.

<sup>102</sup> See generally about the difficulties with oral agreement raised in H Yu, 'Written Arbitration Agreements – What Written Arbitration Agreements?' (2013) 33 (1) *Civil Justice Quarterly* 68

<sup>103</sup> The New York Convention, Article IV

requires the original or a duly certified copy of the award as the key evidence to be produced to the Scottish courts by the winning party for enforcement.

It is worth noting that if other enactment or rule of law requires fulfilment of steps to create an enforceable obligation then this “necessary step” became essential to the creation of a third-party right. For instance, section 1(2) of the Requirements of Writing (Scotland) Act 1995, the fulfilment of writing requirements in the constitution of a contract or unilateral obligation for the creation, transfer, variation or extinction of an interest in land<sup>104</sup> or otherwise than by the operation of a court decree, enactment or rule of law,<sup>105</sup> a gratuitous unilateral obligation,<sup>106</sup> a trust whereby a person declares himself to be sole trustee of his own property or any property which he may acquire,<sup>107</sup> will, testamentary trust disposition and settlement or codicil.<sup>108</sup>

Section 2(3) of the Act allows both express and implied creation of the undertaking to give rise to a third-party right. However, difficulties may arise when the parties disagree over the contents of an implied undertaking. Further difficulties can also occur in the case where the parties or the parties to the main contract unintentionally created such an undertaking. This would create further issues in the interpretation of the validity of arbitration agreement. Hence, an express creation of the undertaking would provide legal certainty in the researcher’s view.

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<sup>104</sup> Requirements of Writing (Scotland) Act 1995, s 1(2)(a)(i)

<sup>105</sup> *Ibid.* s1(2)(b)

<sup>106</sup> *Ibid.* s 1(2)(a)(ii), except an obligation undertaken in the course of business

<sup>107</sup> *Ibid.* s 1(2)(a) (iii)

<sup>108</sup> *Ibid.* s 1(2)(c)

**VI. “RELIANCE” AND RIGHT TO JUSTICE - THIRD-PARTY’S  
KNOWLEDGE OF THE UNDERTAKING IS NOT A REQUIREMENT  
AND HIS RIGHT TO JUSTICE**

Section 2(4) of the Act does not require third-party’s knowledge of the creation of the undertaking. It highlights that a third-party does not need to be aware of the right existed in his benefit as the provision entitles the party to acquire a third-party right to enforce or invoke an undertaking even if ‘there has been no delivery, intimation or communication of the undertaking to the person.’<sup>109</sup> This provision is said to remove any doubt which might exist under the current law on *jus quaesitum tertio* as to whether the creation of a third-party right is dependent on the third-party’s awareness of the undertaking as the draftsmen do not view such an awareness or written requirement as ‘a necessary step’<sup>110</sup> for the creation of the right.<sup>111</sup> Following the above-discussion on reliance, one has to enquire how would a third-party exercise reliance if he is not aware of the undertaking conferred upon him.

This may transpire into the third-party’s loss of right / choice to arbitration. A third parties’ inability to exercise reliance<sup>112</sup> leads to his loss of right /choice to arbitration, consequently places him in a disadvantageous position. In the context of arbitration, under the section 2(4) of the Act, a third-party may be able to argue for the loss of access to arbitration due to the lack of knowledge of the right. To avoid this, the researcher calls for an express conferred undertaking. The third-party’s awareness of the right will allow space for the management of third-party right and dispute resolution under sections 3 and 4 of the Act. It is important to point out that revocation is not the main problem in the context of arbitration, but the lack of

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<sup>109</sup> Contract (Third Party Rights) (Scotland) Act, s 2(4)(b)

<sup>110</sup> Explanatory Notes (n 85) para 18

<sup>111</sup> Explanatory Notes (n 85) para 18

<sup>112</sup> Contract (Third Party Rights) (Scotland) Act, s 5(2) - (4)

opportunity of exercise reliance leads to the debates over access to third-party right or justice through the loss of his third-party right.

#### A. Third-Party's Inability To Exercise Reliance

In the cases where "reliance" has not been exercised by the third-party, the parties would have the contractual right to renounce arbitration. However, if the non-exercise of reliance is due to unawareness under s 2(4) of the Act, questions have to be raised such as whether the third-party's right to arbitration would be affected accordingly. Section 2(4) creates a situation where a third-party who may not be aware of the right conferred upon him. As discussed above, the lack of knowledge of the third-party right will prohibit him from acting or not acting in a required way to exercise the reliance exceptions to benefit from the third parties right and the procedural right to arbitration. While the third-party's right to arbitration proceeding may be partially or totally affected (modified or cancelled by the parties) before he becomes aware of the creation of a right, his right to national court under the European Convention of Human Rights (herein after the ECHR) will not be affected as the change of dispute resolution mechanism still leave the choice of national courts open to the third-party if he wishes to pursue his substantive right once he becomes aware of his right. Consequently, the right to justice is maintained under section 2(4) of the Act.

In relation to the right to justice under section 9(2) which require the third-party to resolve contractual disputes by means of arbitration which is specified by the parties who had already exercised the choice for the third-party. Under these circumstances, a third-party is not given the same privileges as those available to the parties at the time of making the choice of dispute resolution.

The SLC raised the possibility of third-party's consent by action<sup>113</sup> in the cases where a third-party seeks a sist in the Scottish court. In the SLC's very own words:

The third party cannot be bound to arbitrate (imposition of a duty); but if it chooses to invoke the arbitration clause in response to an action against it by a contracting party, then the third party by voluntary action becomes party to an arbitration agreement between itself and the contracting party or parties. In terms of article 6(1) ECHR, therefore, section 9(2)(b) of the draft Bill appears to be entirely acceptable, as also section 8(2) of the 1999 Act.<sup>114</sup>

The application for a sist is viewed by the SLC as a consent to arbitration by action, consequently, the third-party becomes a party to arbitration. Furthermore, a third-party's response to a dispute being raised against it is viewed by the SLC as a defence by action to be part of arbitration proceedings. By demanding a third-party to pursue dispute resolution by the parties' choice of arbitration, a question needs to be asked is whether section 9(2) breaches third-party's right to justice. In other words, whether the non-fulfilment of the prior consent requirement in arbitration would constitute a breach of Article 6(1) of the ECHR?

In relation to the right exercised under section 9(3) of the Act, a third-party's right to elect the choice of forum will ensure that the Act does not contradict the ECHR. If the third-party elects the court, his right to justice is maintained. If arbitration is elected, no right is breached because such a choice is made out of different dispute resolution mechanisms available to him as well as those arguments discussed in s 2(4) of the Act. For the parties who had already expressed their choice of arbitration, the third-party's choice of arbitration will not breach their right to justice because it was based on their own prior choice contained in the main

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<sup>113</sup> *SLC Report* (n 1) 7.58

<sup>114</sup> *Ibid.* 7.57

contract. For the parties who managed to change their mind over the dispute resolution mechanism, the situation will return to the one discussed under section 2(4) of the Act. Even for those parties who failed to exercise their right of revocation to cancel the third parties right would not provide the parties with a claim of breach of justice as the law does not protect such a failure.

#### B. Third-Party's Exercise Of Reliance And The Parties

The emphasis on party autonomy is removed by sections 4-6 which provide the third-party the defence against the parties' modification or cancellation of third-party right. These are said to be specific fix to problems that exist in the current common law without taking 'a more holistic approach to all issues.'<sup>115</sup> The lack of a holistic approach can also be observed in the combined effects of sections 4-6 and 9. Under the Act, the third-party has an independent right to pursue arbitration for both contractual and non-contractual disputes. Once the "reliance" exception is exercised, the parties is no longer entitled to modify or cancel the right, including right to arbitration. However, in the context of arbitration, the immediate issue is whether the parties' lost entitlement of modification or cancellation of the right would lead to coercion in the cases where the parties renounced arbitration as the dispute resolution mechanism. Supposing, the parties chose not to exercise this right or even mutually agree to renounce this right, there should be no reason to force both parties to re-enter into arbitration proceedings where the parties did not commence or actually wished to get out of arbitration. In other words, even with the parties' renunciation, would the parties be forced to return to arbitration and have their right to justice under Article 6(1) ECHR breached?

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<sup>115</sup> Delegated Powers and Law Reform Committee 28 March, column 24 (per David Christie)



To answer this question, it is essential to examine this issue from two perspectives. One is the parties' choice of arbitration as the dispute resolution mechanism and the other is the nature of initiation of arbitration. It is commonly agreed that parties' choice of arbitration does not constitute a breach of parties' right to justice under Article 6(1) of the ECHR.<sup>116</sup> This is because the parties were afforded the choices of arbitration and national courts before arbitration is chosen as the main method of dispute resolution. Furthermore, parties are also offered public hearings in the national courts at the later stages of challenge, recognition or enforcement of arbitral awards, if any.

Examination has to be carried out in terms of the question of whether the initiation of arbitration is a right or duty in order to answer the second question. On the face of it, the exceptions to the revocation of the third-party rights appears to overturn one's current understanding of privity and party autonomy underpinning arbitration agreements and may likely coerce the parties to enter into arbitration after they had changed their mind about their previous choice of dispute resolution mechanism. However, it is commonly accepted that an arbitration agreement imposes the parties' a duty to resolve their disputes by arbitration in the eyes of the courts.<sup>117</sup> Such a duty corresponds with the contractual right possessed by both parties to bind the other party to arbitration. In the cases where "reliance" has been exercised by a third-party, both parties would be required by the Act to honour their contractual duty based on their original arbitration agreement. Since this arbitration agreement is based on the parties' choice of forum available to them, hence, no breach of right to justice. Both the

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<sup>116</sup> See in general, J J Fawcett, *The Impact of Article 6(1) of the ECHR on Private International Law*, (2007) 56(1) ICLQ, 1

<sup>117</sup> *Sanderson & Son v Armour & Co* 1922 SC (HL) 118, 126

Explanatory Notes and the Briefing suggest that the premise of this entitlement is based on the contracting parties' mutual wishes to pursue the matter in arbitration and the legal consequences of a valid arbitration agreement in relation to a tribunal's jurisdiction.<sup>118</sup> Consequently, considering the legal effects of an arbitration agreement, the issue of coercion would never arise had the parties not wished to change the dispute resolution mechanism.

However, if the parties did wish to change their previous chosen dispute resolution mechanism following a third-party's "reliance" being exercised, the parties would be statutorily barred from exercising their contractual right to do so. This leads to concerns over coercion over the parties who are the creators of the contract; more directly, whether such coercion would have an impact on the right to justice under Article 6(1) of the ECHR.

## **VII. CONCLUSION – SUGGESTIONS OVER THE ROAD AHEAD**

It was correctly put that certainty with regard to the third-party right is essential to the success of the Act.<sup>119</sup> However, the transformation from substantive right to procedural right may create confusion. Leaving this aside, to achieve a full benefit of s 9 of the Act, ideally both the Scottish procedural and substantive laws are applied and the enforcement forum is in Scotland. However, the success of the Scottish arbitration should not limit itself within its own borders. Internationally, the finality of awards holds the key to the success of arbitration systems within different jurisdictions. To avoid the SLC's concerns over the third-parties' access to arbitration being opposed by one or more of the contracting parties,<sup>120</sup> ideally, it would be an idea to draw a clear distinction between procedural rights and substantive rights. As the Act has now passed the final reading before the Scottish Parliament, the draftsmen

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<sup>118</sup> Explanatory Notes (n 85) para 37 and Evan (n 7) 11

<sup>119</sup> Delegated Powers and Law Reform Committee 28 March (n 115) column 24

<sup>120</sup> *SLC Report* (n 1) 7.29

should now consider the amendments discussed in this paper to provide clarification on “parties” and “third-parties” as well as appropriate cross-reference between the AA, the Rules and the Act. It is also wise to consider the various difficulties and ambiguities which may arise from renunciation which is currently being provided in section 9(4) of the Act. Finally, in order to balance the contractual right against the right to justice, the possibility of coercion on the parties who have jointly abandoned arbitration as the means of dispute resolution to return to arbitration deserves a re-think.