



RPC

Collateral warranties v third party rights

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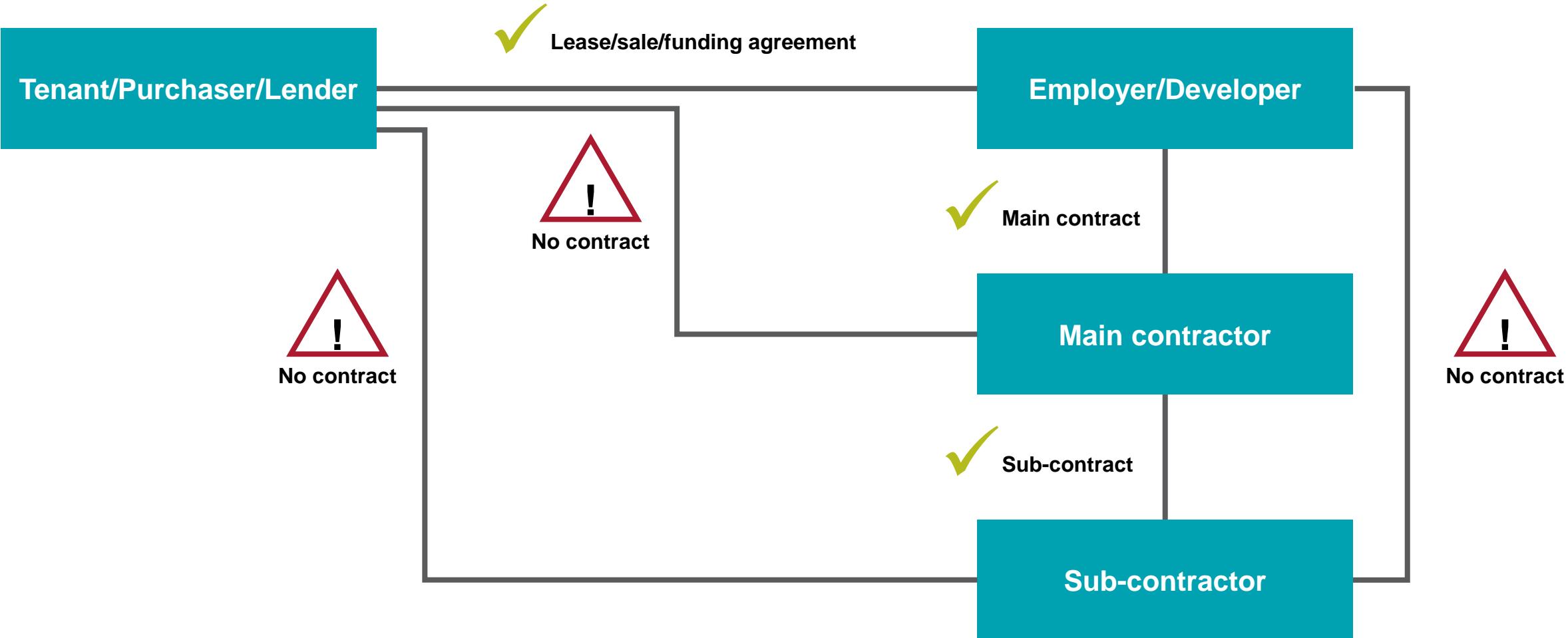
Introduction

- Collateral warranties
- Third party rights
- Which to use and when

Why do we need them?



On a construction project, this means



Collateral warranties

A contract under which a construction professional, contractor or sub-contractor promises to a third party (the "beneficiary") that it has complied with the requirements of its professional appointment, contract or sub-contract.



Collateral warranties

- Standard form v bespoke
- Common clauses:
 - Principal covenant
 - Step-in rights
 - Consideration
 - PI insurance
 - Liability period
 - Assignment



Collateral warranties

- Potential insurance issue:
“Any liability that arises in consequence of any assignment of a COLLATERAL WARRANTY OR DUTY OF CARE AGREEMENT to more than one party except in the case of a COLLATERAL WARRANTY OR DUTY OF CARE AGREEMENT given to a financier or funding party (not a purchaser or tenant) where a total of two assignments is permissible.”
- Exclusion 4.2 to the RICS Minimum Terms



Third party rights

- Who is a third party?
- Expressly grants a right to a third party so that they can enforce a contract (pursuant to the Contracts (Rights of Third Parties) Act 1999)



When do rights arise?

Right of third party to enforce contractual term

(1) Subject to the provisions of this Act, a person who is not a party to a contract (a “third party”) may in his own right enforce a term of the contract if -

(a) the contract expressly provides that he may, or

(b) subject to subsection (2), the term purports to confer a benefit on him.

The Act

- Modifying a contract
- Defences
- Original party's rights
- Double recovery

Collateral warranties

Pros

- Familiar
- Tried & tested
- Adjudication

Cons

- Time consuming
- Expensive
- Too late

Third party rights

Pros

- Quick
- Cheap

Cons

- Cannot impose an obligation
- Step-in rights could be more complicated
- Less familiar
- Insurance policies are less clear
- Who is given rights

Top tips: collateral warranties

GETTING A SIGNATURE

What is the penalty to the contractor/
sub-contractor if they do not sign? What
bargaining power do you have?
Delay payment?

INSURANCE

Professional indemnity policies usually
only cover collateral warranties if certain
conditions are met. Beware and ask the
contractor to check

EXECUTION

Execute it properly

STEP-IN RIGHTS

Who has them and when? Make sure the
order of priority is clear

Top tips: third party rights

HOW TO EFFECT

Make sure that the mechanism for granting rights and the parameters of who can be given rights is clear

INSURANCE

Professional indemnity policies are not always tailored to cover third party rights and may exclude them as an extended liability. Be aware and ask the contractor to check

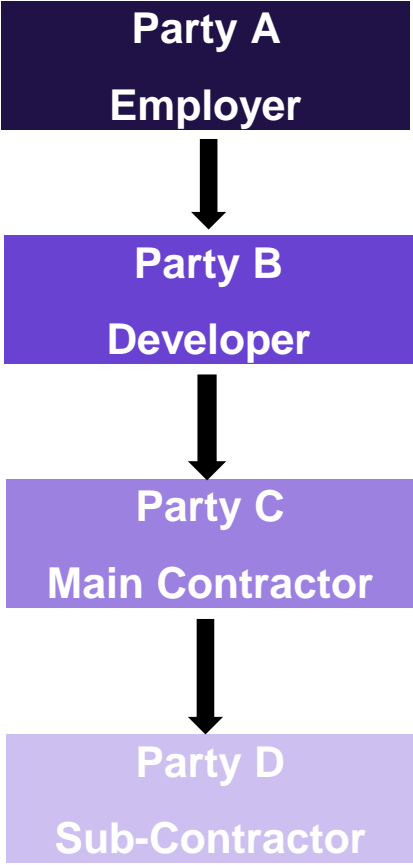
OBLIGATIONS

Be careful and check the drafting to ensure it is effective

BACK-TO-BACK

Ensure that the rights are back-to-back with the contract, to avoid making the rights unenforceable or inconsistent

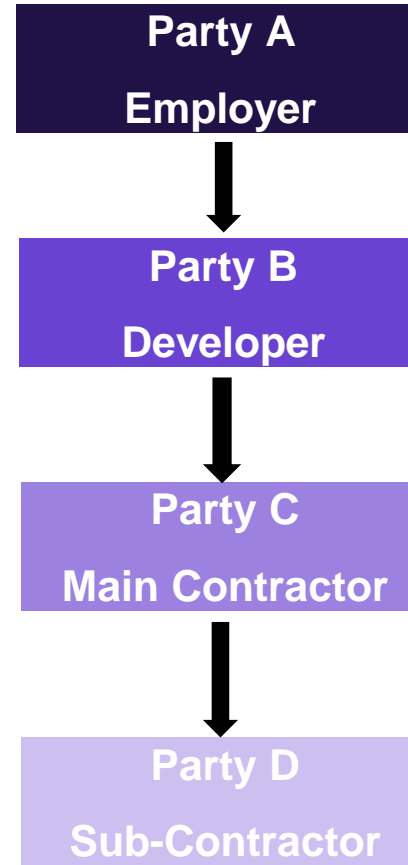
Examples: Third Party Rights



You can grant B Third Party Rights allowing it to seek to recover from D in the event D is negligent.

D has already agreed to grant Third Party Rights in its Appointment Contract.

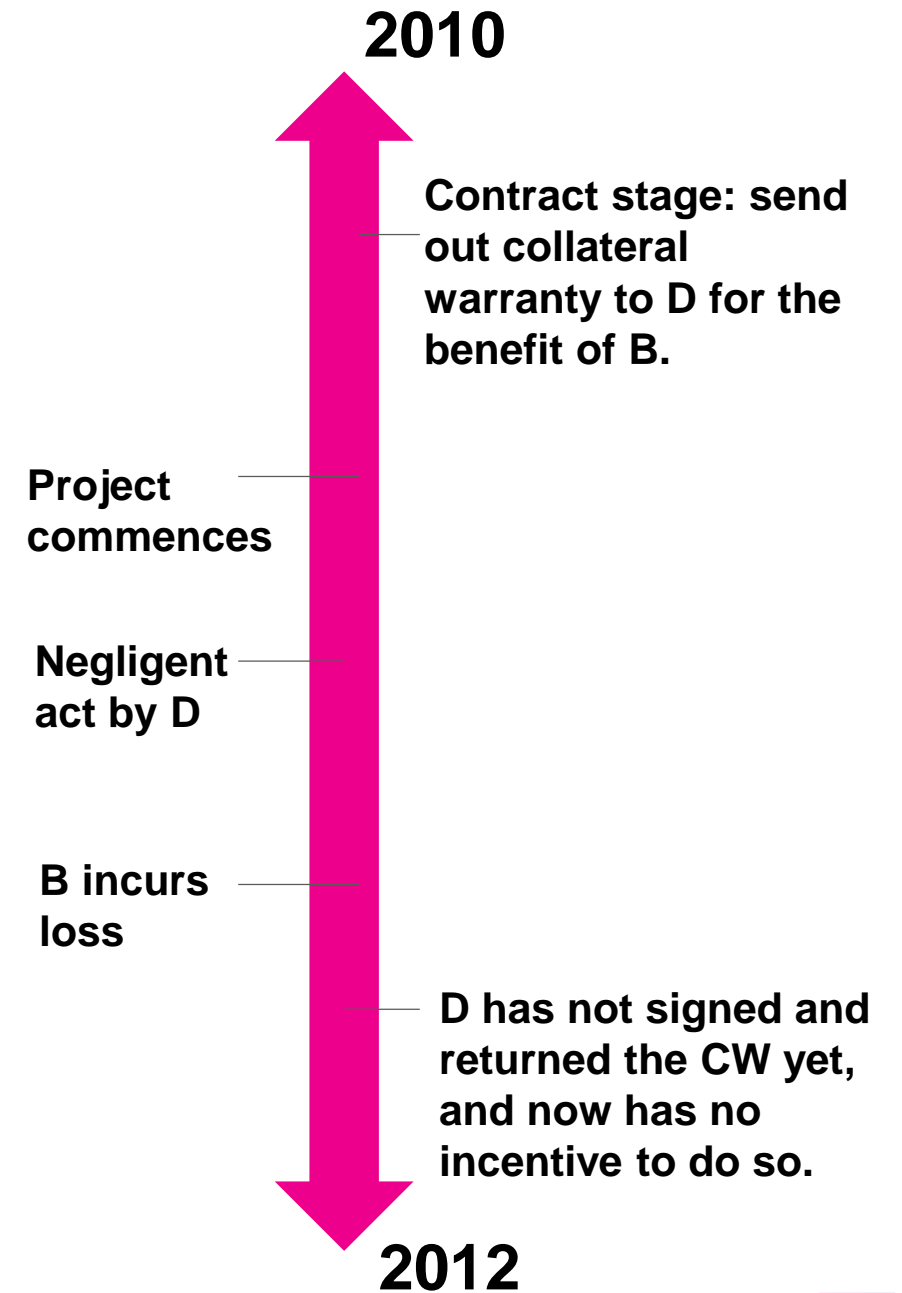
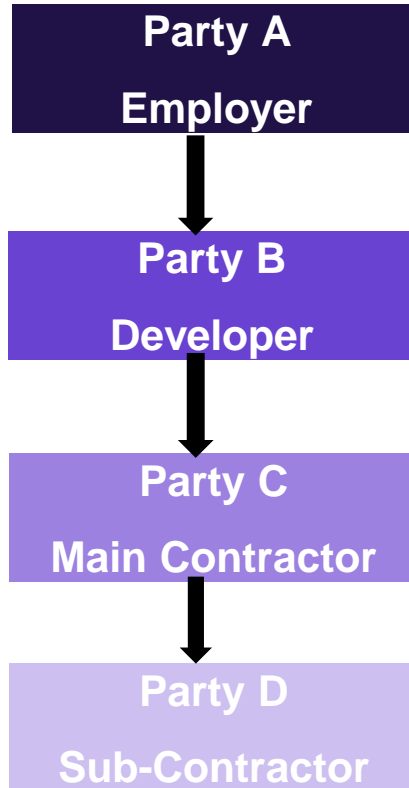
Examples: Collateral Warranties



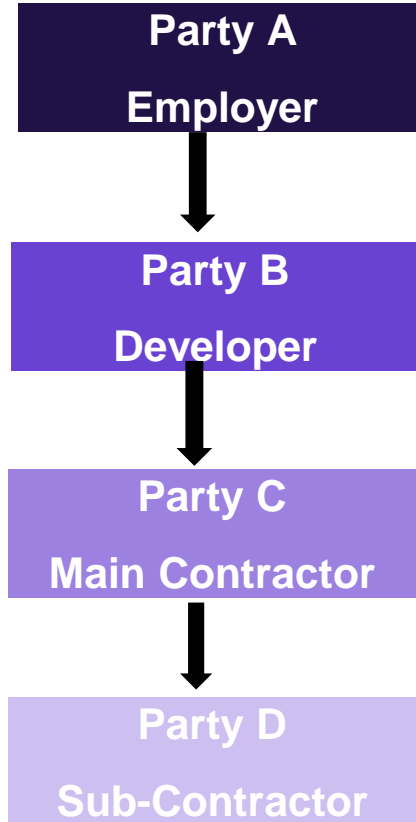
B seek a collateral warranty from D that D will comply with its obligations contained in its appointment.

Normally, parties would enter into negotiations into the terms of a collateral warranty, but if they are of unequal bargaining power, the sub-contractor will be forced to agree any terms

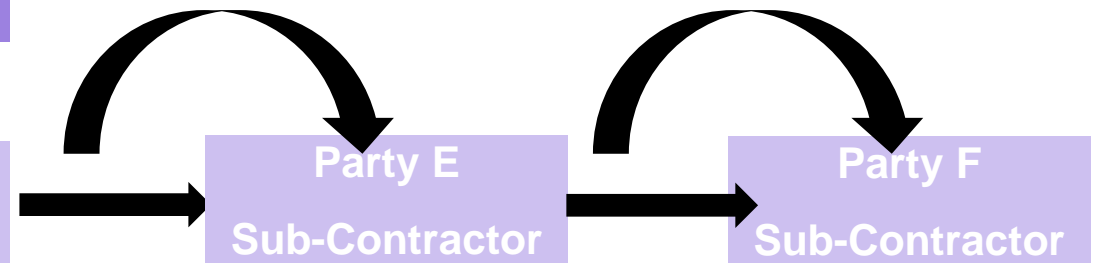
Examples: Collateral Warranties



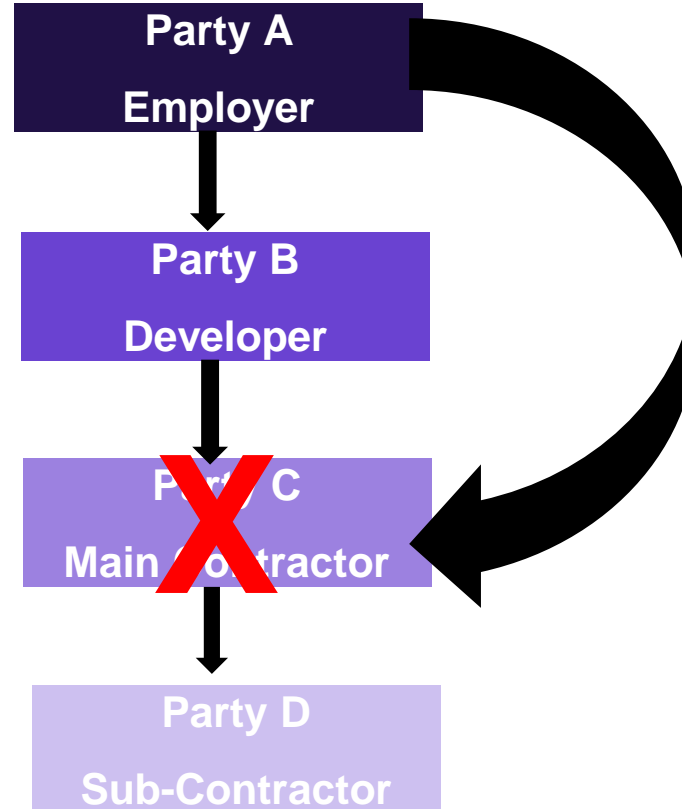
Examples: Collateral Warranties



D's collateral warranty may say that it can be assigned on, for example, three occasions. This will need to be checked against your PI policy's provisions.



Examples: Collateral Warranties



A collateral warranty can provide for "step-in" rights which will allow, in this instance, Party A to step into the shoes of Party C, should C become insolvent. In that scenario A can also accrue all rights previously bestowed upon C.

Q&A

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