

# 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* – 3<sup>rd</sup> 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



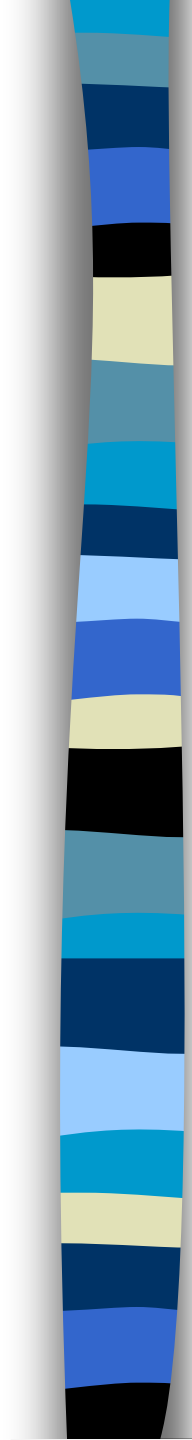
# Effect on Arbitration Clauses

- 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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