The Law Commission

Consultation Paper No. 121

Privity of Contract: Contracts for the Benefit of Third Parties

HMSO

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This consultation paper, completed on 23 October 1991, is circulated for comment and criticism only. It does not represent the final views of the Law Commission.

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Privity of Contract: Contracts for the Benefit of Third Parties

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PRIVITY OF CONTRACT: CONTRACTS FOR THE BENEFIT OF THIRD PARTIES

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PART I

INTRODUCTION

1.1 Although a contract or its performance can affect a third party,[1] the doctrine of privity means that, as a general rule, a contract cannot confer rights or impose obligations arising under it on any person except the parties to it.[2] There are several different aspects of the doctrine:

(i) a person cannot enforce rights under a contract to which he is not a party;

(ii) a person who is not party to a contract cannot have contractual liabilities imposed on him;

(iii) contractual remedies are designed to compensate parties to the contract, not third parties.

This paper is primarily concerned with the general rule that a person cannot enforce a right under a contract to which he

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1. As when C guarantees a debt owed by A to B and A pays, thus releasing C who thereby indirectly gains a benefit, or where the contract or its performance creates a property right in a third party.

2. Before Donoghue v. Stevenson [1932] A.C. 562, the privity doctrine was seen as precluding actions in tort by third parties arising from negligence by a party to a contract in carrying it out: Winterbottom v. Wright (1842) 10 M. & W. 109; 152 E.R. 402.

is not a party,[3] and references in it to the "third party rule" are to this.

1.2 Whilst it is self-evidently desirable that a complete stranger to a contract should not have contractual obligations forced upon him,[4] the general rule that a third party cannot acquire rights under a contract to which he is not privy has been much criticised. This criticism has come from academics,[5] law reform bodies (including the Law Revision Committee[6]) and the judiciary.[7] In 1967, in Beswick v. Beswick,[8] Lord Reid cited with approval the Law Revision Committee's proposals that when a contract by its express terms purports to confer a benefit directly on a third party, it shall be enforceable by the third party in his own name. While implying that the way forward was by legislation, he stated that the House of Lords might find it necessary to deal with the matter if there was a further long period of Parliamentary procrastination. In Swain v.

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3. Atiyah, An Introduction to the Law of Contract (4th ed., 1989), pp. 371-372.

4. We shall see that different considerations apply when P is taking the benefit of a contract to which he is not a party and D wishes to rely on defences in that contract. Here, although D purports to burden P, the latter is not a complete stranger. In seeking to take the benefit of a contract to which he is not privy, fairness dictates that he should, in principle, take the burden.

5. Corbin, (1930) 46 L.Q.R. 12; Furmston, (1960) 23 M.L.R. 373; Wylie, (1966) 17 N.I.L.Q. 351; Markesinis, (1987) 103 L.Q.R. 354; Flannigan, (1987) 103 L.Q.R. 564; Reynolds, (1989) 105 L.Q.R. 1; Kincaid, [1989] C.L.J. 243; Adams & Brownsword, (1990) 10 L.S. 12; Beyleveld & Brownsword, (1991) 54 M.L.R. 48.

6. (1937), Cmd. 5449. See para. 4.30 below.

7. See Part IV below for the details of these criticisms.

8. [1968] A.C. 58, 72.

Law Society,[9] Lord Diplock referred to the general non-recognition of third party rights as "an anachronistic shortcoming that has for many years been regarded as a reproach to English private law". In Woodar Investment Development Ltd. v. Wimpey Construction (U.K.) Ltd.,[10] Lord Salmon regarded the law concerning damages for loss suffered by third parties as most unsatisfactory and hoped that, unless it were altered by statute, the House of Lords would reconsider it.[11] Lord Scarman reminded the House that twelve years had passed since Lord Reid had called for a reconsideration of the rule in Beswick v. Beswick, and hoped that all the cases which "stand guard over this unjust rule" might be reviewed.[12]

1.3 The Law Commission first became interested in this subject after its creation in 1965. Item 1 of the First Programme of law reform was the codification of the law of contract. Item 3 included the topic of third party rights. A substantial amount of work was done on this topic in conjunction with work on consideration. At that time it was felt that reform of privity could not usefully be undertaken without reform of the doctrine of consideration. After the decision in 1973 to suspend work on the production of a contract code,[13] other contract projects have taken

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9. [1983] 1 A.C. 598, 611.

10. [1980] 1 W.L.R. 277.

11. At p. 291.

12. At p. 300. Lord Keith, at pp. 297-298, also associated himself with Lord Scarman's view.

13. 8th Annual Report 1972-1973, Law Com. No. 58, paras. 3-4.

priority.[14] More recently, our work on the rights of buyers of goods carried by sea,[15] involving a specific context of third parties being given rights of suit by statute, together with a more cautious judicial approach to the question of tort liability for economic loss, has suggested to us that the third party rule should be reconsidered. Meanwhile, the courts have decided cases without making a fundamental inroad into the privity doctrine, even assuming this to be a proper exercise of the judicial function.[16] It is our view that reform of the third party rule, which is concerned with who can enforce a contract, can be undertaken without reassessing the doctrine of consideration, which is concerned with which promises are legally enforceable. Our reasons are given in paragraphs 2.5-2.10 below. In these circumstances, we have taken the view that the time is ripe for a fundamental review of the third party rule.

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14. Exemption Clauses: Second Report by the two Commissions (1975), Law Com. No. 69; Scot. Law Com. No. 39 [see the Unfair Contract Terms Act 1977]; Report on Contribution (1977), Law Com. No. 79, [see the Civil Liability (Contribution) Act 1978]; Implied Terms in Contracts for the Supply of Goods (1979), Law Com. No. 95, [see the Supply of Goods and Services Act 1982]; Pecuniary Restitution on Breach of Contract (1983), Law Com. No. 121; Minors' Contracts (1984), Law Com. No. 134, [see the Minors' Contracts Act 1987]; The Parol Evidence Rule (1986), Law Com. No. 154; Implied Terms in Contracts for the Supply of Services (1986), Law Com. No. 156; Sale and Supply of Goods (1987), Law Com. No. 160, Scot. Law Com. No. 104; Firm Offers, Working Paper No. 60, (1975); Penalty Clauses and Forfeiture of Monies Paid, Working Paper No. 61, (1975); Contributory Negligence as a Defence in Contract, Working Paper No. 114, (1990).

15. Rights to Goods in Bulk, Working Paper No. 112 (1989); Rights of Suit in Respect of Carriage of Goods by Sea (1991), Law Com. No. 196; Scot. Law Com. No. 130.

16. Cf. Midland Silicones Ltd. v. Scruttons Ltd. [1962] A.C. 446, 467-468 per Viscount Simonds.

Arrangement of this Paper

1.4 Part II examines the meaning and development of the third party rule. Part III examines the principal exceptions to, and circumventions of, the rule. Part IV analyses the case for reform, including the main problems experienced in practice. Part V examines in detail the main issues involved in reform. Part VI summarises our provisional recommendations, on which comments and criticism are invited. An appendix outlines the law in some other jurisdictions, including several which have enacted statutory reforms of the third party rule.

Overview

1.5 By way of a brief overview, the reader may find it helpful to bear in mind the following points at the outset:

(i) We believe, as already indicated, that a reform of the third party rule can be undertaken without a review of the doctrine of consideration.

(ii) Although we canvass the possibility of a legislative reform which would, without more, allow third parties to sue on contracts to which they are not privy, our provisional conclusion is that reform of the third party rule will inevitably involve consideration of a number of complex ancillary, but nonetheless important, issues. It would not be right to undertake such reform without, at the same time, making clear through legislation the full implications for those issues of the method of reform that is selected. For that reason, and also because we consider the issues to be too significant to be left to the accident of resolution by the courts, we do not, as at present advised, support a

reform that did no more than simply to allow third parties a right of suit.[17]

(iii) The essence of our provisional proposals is to allow actions by third parties when to do so gives effect to the intentions of the contracting parties.[18] To this extent, they build on existing contractual doctrine and merely remove an obstacle which is apt to frustrate the wishes of the contracting parties.

1.6 In our study of this subject we have received valuable assistance from Professor M P Furmston, Professor of Law at the University of Bristol and Professor G H Treitel Q.C., Vinerian Professor of English Law at the University of Oxford, and we are most grateful to them for their advice and help. The views expressed in this Paper are, however, our own.

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17. See Part V below.

18. See para. 5.10 below.

PART II

THE MEANING AND DEVELOPMENT OF THE THIRD PARTY RULE

1. Meaning of the third party rule

2.1 Two of the central questions of policy in the law of contract are: (i) which promises are legally enforceable; and (ii) who can enforce them? The first question is associated with the doctrine of consideration; the second with the doctrine of privity, or at least that aspect of the privity rule which prevents a third party from suing on a contract to which he is not a party. In this part we examine the meaning and development of the third party rule and its relation with the doctrine of consideration. The question of what constitutes a contract for the benefit of a third party is also introduced in this Part[1] although it is discussed more fully in Part V.[2]

2.2 In Part I above we identified three strands to the doctrine of privity of contract. First, non-parties may not bring claims on a contract made for their benefit. Secondly, burdens may not be imposed on non-parties. Thirdly, remedies for breach of contract are designed to compensate losses suffered by the contracting parties rather those suffered by third parties. The first strand is the primary focus of our enquiry. The second strand has not attracted substantial criticism and rests on a sound policy. The third strand received little attention in the literature before Beswick

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1. See para. 2.17 below.

2. See para. 5.8 below.

v. Beswick.[3] We shall see that to reform only this strand of the doctrine would not necessarily suffice since even if the promisee could in principle recover the third party's loss, this may be impractical or the promisee may not wish to sue, even though at the time the contract was made, there was an intent irrevocably to benefit the third party.[4]

2.3 Within the first and second strands of the doctrine, there are four basic questions:[5]

(i) Can P sue on a contract to which he is not a party?[6]

(ii) Can D rely on defences based on a contract to which he is not a party?[7]

(iii) Can D rely on defences based on his own contract to which P is not a party?[8]

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3. [1968] A.C. 58.

4. See para. 4.29 below.

5. Adams & Brownsword, (1990) 10 L.S. 12, 15.

6. e.g. Beswick v. Beswick [1968] A.C. 58.

7. e.g. Elder, Dempster & Co. Ltd. v. Paterson, Zochonis & Co. Ltd. [1924] A.C. 522; New Zealand Shipping Co. Ltd. v. A.M. Satterthwaite & Co. Ltd. (The Eurymedon) [1975] A.C. 154; Norwich City Council v. Harvey [1989] 1 W.L.R. 828.

8. e.g. Pyrene Co. Ltd. v. Scindia Navigation Co. Ltd. [1954] 2 Q.B. 402; Morris v. C.W. Martin & Sons Ltd. [1966] 1 Q.B. 716.

(iv) Can P enforce his own contract against a third party?[9]

2.4 The first two questions relate to whether a third party can take the benefit of a contract to which he was not privy, whether by way of assertion or defence. The third and fourth questions relate to whether a third party can similarly be bound by a contract to which he was not privy. The third question needs to be covered as the policy issues which it raises are similar to those raised by the second; when P is suing in tort, there is little difference between D pointing to a term in a contract to which he (but not P) is privy, and D pointing to a term in a contract to which he is a stranger (but P is not). Although the focus of our enquiry will be on the first three questions, we will be inviting views on whether the fourth question requires investigation.[10] In general, the present law answers all of the above questions in the negative, although we shall see in Part III below that there are many exceptions whose existence casts doubt on the coherence of the general rule.

2. Privity and the rule that consideration must move from the promisee

2.5 We have said that privity and consideration involve separate issues of policy. However, when the Law Commission first examined the doctrine of privity the relationship between privity and the rule that consideration must move from the promisee caused particular difficulty. Are these principles different or are they in effect the same?

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9. e.g. Port Line Ltd. v. Ben Line Steamers Ltd. [1958] 2 Q.B. 146.

10. See paras. 4.33 and 5.36 below.

Although this question primarily arises out of the historical development of the English law of contract, it is not merely of historical or theoretical interest. If it is decided that as a matter of policy rights should be accorded to third parties, it is important that any reform to achieve this should not be capable of being imperilled by the argument that only those who provide consideration can enforce contracts, so that a third party who has not furnished consideration would remain unable to enforce those rights. Therefore, if there is to be reform, it would appear that it must be in such statutory terms as prevent the argument being raised that third parties who are strangers to the consideration cannot recover.

2.6 The balance of authority in fact supports the existence of two distinct rules of consideration and privity. In Dunlop Pneumatic Tyre Co. Ltd. v. Selfridge & Co. Ltd.,[11] Viscount Haldane L.C. said:

> "My Lords, in the law of England certain principles are fundamental. One is that only a person who is a party to a contract can sue on it... A second principle is that if a person with whom a contract not under seal has been made is to be able to enforce it consideration must have been given by him to the promisor or to some other person at the promisor's request."[12]

The Law Revision Committee took a similar view, giving the following example:

> "A, B, and C are all parties to a contract. A promises B and C to pay C £100 if B will do a certain piece of work desired by A. A declines to pay the £100 and C cannot

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11. [1915] A.C. 847.

12. At p. 853.

compel him to do so. C is a third party to the consideration but not to the contract."[13]

2.7 This approach has been criticised on the ground that a contract is not merely a promise but a promise supported by consideration, i.e. a bargain. If someone is not a party to the bargain, he is not a party to the contract.[14] In turn, this criticism has been said to be circular, since it "starts by assuming that only a person who supplies consideration can properly be treated as a party to the contract; it is then deduced ... that therefore C cannot be treated as a party to the contract because he supplies no consideration."[15] Whilst C may enforce a promise made to B and C even though the consideration was apparently provided only by B,[16] it has been argued that this does not represent an exception to the rule that consideration must move from the promisee. Where a promise is made to two or more persons jointly, it is made to them collectively, and, if the consideration is given on behalf of them all and thus moves from them all, it does not have to be furnished by them separately.[17]

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13. (1937), Cmd. 5449, para. 37. Atiyah has supported this differentiation, although he believes that C could indeed enforce the promise: Consideration in Contracts: A Fundamental Restatement" (1971), p. 40.

14. Furmston, (1960) 23 M.L.R. 373, 385; Ellinger, (1963) 26 M.L.R. 396; Wylie, (1966) 17 N.I.L.Q. 351; Samuels, (1968) 8 W.A.L.Rev. 378, 383; Flannigan, (1987) 103 L.Q.R. 564.

15. Atiyah, op. cit., p. 40.

16. Coulls v. Bagot's Executor & Trustee Co. Ltd. (1967) 40 A.L.J.R. 471.

17. Ibid., at p. 483 per Windeyer J.; Coote, [1978] C.L.J. 301; Kincaid, [1989] C.L.J. 243, 261. See also para. 3.33 below.

2.8 The Indian Contract Act 1872 departed from the rule that consideration must move from the promisee, although the preponderant view was that the English rule of privity applied to India.[18] Similarly, Kepong Prospecting Ltd. v. Schmidt,[19] supports the distinction between the two rules. A third party made a claim to enforce a contract under a Malaysian Ordinance, which was in all material respects the same as the Indian Contract Act, by which consideration need not move from the promisee. In rejecting the claim, the Privy Council advised:

> "It is true that section 2(d) of the [C]ontracts [O]rdinance gives a wider definition of `consideration' than that which applies in England particularly in that it enables consideration to move from another person than the promisee, but the appellant was unable to show how this affected the law as to enforcement of contracts by third parties ...".[20]

2.9 It is true that in the English cases the two rules have always led to the same result,[21] and that Tweddle v. Atkinson[22] and Dunlop Pneumatic Tyre Co. v. Selfridge & Co. Ltd.[23] were decided on the consideration point. Nevertheless, logically it would seem that two separate issues of policy are raised. The first, primarily associated with the privity doctrine, relates to who can

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18. Indian Law. Com. No. 13, p. 10.

19. [1968] A.C. 810.

20. Ibid at p. 826. See also Trident General Insurance Co. Ltd. v. McNiece Bros. Pty. Ltd. (1988) 62 A.L.J.R. 508, 511, 533, where Mason C.J., Wilson and Toohey JJ. said that the weight of authority favoured two distinct, albeit interrelated, principles.

21. Treitel, The Law of Contract, (8th ed., 1991), p. 527.

22. (1861) 1 B.& S. 393; 121 E.R. 762.

23. [1915] A.C. 847.

enforce a contract. The second, primarily associated with consideration, concerns the types of promises that can be enforced. Furthermore, to say that only a person who supplies consideration can properly be treated as a "party" to the contract fails to take account of contracts made by deed, under which the promisee is not required to furnish consideration.

2.10 For these reasons, we believe that the third party rule, i.e., that third parties cannot enforce contracts made for their benefit, can be reformed without prejudicing the rule that consideration must move from the promisee. To make this clear, rather than discussing the doctrine of privity or the rule that consideration must move from the promisee, in this paper we refer to the third party rule.

3. Development of the third party rule

2.11 It is generally agreed that the modern third party rule was established in 1861 in Tweddle v. Atkinson.[24] In Drive Yourself Hire Co. (London) Ltd. v. Strutt, Denning L.J. said:[25]

> "It is often said to be a fundamental principle of our law that only a person who is a party to a contract can sue on it. I wish to assert, as distinctly as I can, that the common law in its original setting knew no such principle. Indeed, it said quite the contrary. For the 200 years before 1861 it was settled law that, if a promise in a simple contract was made expressly for the benefit of a third person in such circumstances that it was intended to be enforceable by him, then the common

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24. (1861) 1 B. & S. 393; 121 E.R. 762; Treitel, op. cit., p. 529.

25. [1954] 1 Q.B. 250.

law would enforce the promise at his instance, although he was not a party to the contract".[26]

2.12 Denning L.J. cited several cases to support his view. In Dutton v. Poole,[27] a son promised his father that, in return for his father not cutting down a wood, he would pay £1000 to his sister. The father forbore from cutting down the wood, but the son did not pay. It was held that the sister could sue, on the ground that the consideration and promise to the father may well have extended to her on account of the tie of blood between them.[28] In Marchington v. Vernon,[29] Buller J. said that, independently of the rules prevailing in mercantile transactions,[30] if one person makes a promise to another for the benefit of a third, the third may maintain an action upon it. In Carnegie v. Waugh,[31] the tutors and curators of an infant, P, executed an agreement for a lease with D, for an annual rent to be paid to P. It was held that P could sue on the instrument, even though he

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26. At p. 272.

27. (1678) 2 Lev. 210; 83 E.R. 523. This decision was supported, obiter, by Lord Mansfield in Martyn v. Hind (1776) 2 Cowp. 437, 443; 98 E.R. 1174, 1177.

28. The report discloses disagreement in the King's Bench during the argument, on the grounds that the daughter was privy neither to the promise nor the consideration. Nevertheless, the decision was upheld in the Exchequer Chamber: Cowp. 294, 365; 83 E.R. 123.

29. (1787) 1 Bos. & P. 101 n. (c); 126 E.R. 801 n. (c). This case was described as "but a loose note at Nisi Prius" by counsel in the interesting case of Phillips v. Bateman (1812) 16 East 356, 371; 104 E.R. 1124, 1129, where D, in the face of a run on a banking house, promised to support the bank with £30,000, whereupon note holders stopped withdrawing their money. When the bank subsequently stopped paying out, D was held not liable to an action by individual holders of bank notes.

30. The case itself involved a bill of exchange.

was not a party to it. In addition, there is a respectable line of 16th and 17th century authority allowing an intended beneficiary a right of action.[32] These cases often involved the same factual setting, viz. the fathers of a potential bride and groom agreeing to pay a sum of money to the groom if he married, the bride's father subsequently reneging on the agreement. In several of these cases it was held that, not only could the groom sue to recover the amount promised, but that his father, the promisee, could not sue because he had no interest in performance.[33]

2.13 In spite of these cases favouring actions by third party beneficiaries, it would not be accurate to say that the third party rule was entirely a 19th century innovation. There were other 16th and 17th century cases where a third party was denied an action on the grounds that the promisee was the only person entitled to bring the action.[34] There were also cases where the reason why the third party could not sue was because he was a stranger to the consideration,

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31. (1823) 1 L.J. (O.S.) K.B. 89.

32. Simpson, A History of the Common Law of Contract (1975), pp. 477-478. See also Palmer, (1989) 33 Am. J. Leg. Hist. 3; Ibbetson in Barton (ed), Towards a General Law of Contract, 67, 96-99.

33. Lever v. Heys Moo. (K.B.) 550; 72 E.R. 751; also Levet v. Hawes Cro. Eliz. 619, 652; 78 E.R. 860, 891; Provender v. Wood Het. 30; 124 E.R. 318; Hadves v. Levit Het. 176; 124 E.R. 433. In the altogether different scenario in Rippon v. Norton Cro. Eliz. 849; 78 E.R. 1074, D promised P that his son would keep the peace against P and P's son. D's son thereafter assaulted P's son. P, alleging medical expenses and loss of the services of his son, failed in his action against D, even though he was the promisee. It was said that the son was the person who should have sued, which he later did successfully: Cro. Eliz. 881; 78 E.R. 1106.

34. Jordan v. Jordan (1594) Cro. Eliz. 369; 78 E.R. 616 (P gave a warrant to X to arrest D for an alleged debt. D promised X that, in return for not arresting him, he

i.e. he had given nothing in return for the promise.[35] These cases typically involved the following facts. X owed money to P. D would agree with X to pay P in return for X doing something for D, such as working or conveying a house. D would not pay, and P would sue D. P would lose because he had given nothing for D's promise.

2.14 Thus, by the mid-19th century there appeared to be no firm rule either way. The position was to be clarified in Tweddle v. Atkinson.[36] The facts involved an agreement by the fathers of a bride and groom to pay the groom a sum of money. When the bride's father failed to pay, the groom sued unsuccessfully. Wightman J. said that no stranger to the consideration could take advantage of a contract though made for his benefit. Crompton J. said that consideration must move from the promisee.[37]

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34. Continued
would pay the debt. P failed in his action, on the ground, inter alia, that the promise had been made to X); Taylor v. Foster (1600) Cro. Eliz. 776; 78 E.R. 1034 (D, in return for P marrying his daughter, agreed to pay to X an amount which P owed to X. It was held that P was the person to sue, being the promisee).

35. Bourne v. Mason (1669) 1 Ventr. 6; 86 E.R. 5; Crow v. Rogers (1724) 1 St. 592; 93 E.R. 719; Price v. Easton (1833) 4 B. & Ad. 433; 110 E.R. 518. Although in the former two cases, the reason why P failed was because he was a stranger to the consideration, Price v. Easton contains seeds of more modern doctrine: whereas Denman C.J. said that no consideration for the promise moved from P to D, Littledale J. said that there was no privity between P and D.

36. (1861) 1 B. & S. 393; 121 E.R. 762.

37. The earlier cases allowing children to be considered a party to their father's consideration were considered obsolete. Dutton v. Poole (1678) T. Raym. 302; 83 E.R. 156, being a decision of the Exchequer Chamber could not

2.15 The authority of Tweddle v. Atkinson was soon generally acknowledged. In Gandy v. Gandy,[38] Bowen L.J. said that, in spite of earlier cases to the contrary, Tweddle v. Atkinson had laid down "the true common law doctrine". In Dunlop Pneumatic Tyre Co. Ltd. v. Selfridge & Co. Ltd.,[39] the House of Lords accepted that it was a fundamental principle of English law that only a party to a contract who had provided consideration could sue on it.[40] Despite several attempts by Denning L.J. to allow rights of suit by third party beneficiaries,[41] the House of Lords reaffirmed the general rule in Midland Silicones Ltd. v. Scruttons Ltd.,[42] and rejected Denning L.J.'s attempts to relax the third party rule. Viscount Simonds said:

> "[H]eterodoxy, or, as some might say, heresy, is not the more attractive because it is dignified by the name of reform. ... If the principle of jus quaesitum tertio is to be introduced into our law, it must be done by Parliament after a due consideration of its merits and demerits."[43]

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37. Continued
be overruled by the Queen's Bench, but was nonetheless not followed.

38. (1885) 30 Ch.D. 57, 69.

39. [1915] A.C. 847.

40. The principle was reiterated by the Privy Council in Vandepitte v. Preferred Accident Insurance Corporation of New York [1933] A.C. 70.

41. Smith and Snipes Hall Farm Ltd. v. River Douglas Catchment Board [1949] 2 K.B. 500; White v. John Warwick & Co. Ltd. [1953] 1 W.L.R. 1285; Drive Yourself Hire Co. (London) Ltd. v. Strutt [1954] 1 Q.B. 250.

42. [1962] A.C. 446, Lord Denning dissenting.

43. At pp. 467-468.

2.16 Although the House of Lords in Beswick v. Beswick[44] and Woodar Investment Developments Ltd. v. Wimpey Construction (U.K.) Ltd.[45] strongly criticised the rule, it refrained (though without enthusiasm) from any judicial abrogation of it.[46] To conclude, therefore, the general rule remains that a third party cannot enforce a contract made for his benefit.

4. What is a contract for the benefit of a third party?

2.17 There is an important distinction between a contract for the benefit of a third party which is intended to give the third party enforceable rights and a contract which happens to benefit a third party without being intended to give him enforceable rights. It is important that reform should not go from the one extreme of disallowing in general all third party actions (even though the parties intend that the third party should have enforceable rights), to the opposite extreme of allowing third parties to sue on contracts with which they are only remotely connected.

2.18 There are several possible definitions of what constitutes a contract for the benefit of a third party.

(a) A contract in which the parties intend that the third party should receive a benefit and also

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44. [1968] A.C. 58.

45. [1980] 1 W.L.R. 277.

46. See para. 1.2 above.

intend to create a legal obligation enforceable by that third party.[47]

(b) A contract in which the parties intend that the third party should receive the benefit of the promised performance. [48]

(c) A contract on which a third party justifiably and reasonably relies.[49]

(d) A contract which confers a benefit on a third party. The only question would be whether in fact the third party benefited from the contract, regardless of the intentions of the contracting parties.

2.19 It will be seen later that our provisional view is that a third party should be able to sue on a contract made for his benefit where it is the intention of the contracting parties that he be given enforceable rights,[50] and that this formula will provide a workable solution applicable in all cases without opening the floodgates to third party actions. For instance, where a building company contracts with a highway authority to construct a new road, the road may be intended for the benefit of all road-users, but there will usually be no intention that individual road-users should

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47. See the New Zealand Contracts (Privity) Act 1982, s. 4: Appendix, para. 9.

48. The key distinction is therefore between intended and incidental beneficiaries. See the U.S. Restatement (Second) of Contracts (1981), s. 302: Appendix, para. 15.

49. (1968) 54 Va.L.R. 1166, 1188.

50. See para. 5.10 below.

have a right of action in the event of any delay in construction. Equally, persons who stood to benefit by reason of having their business premises adjacent to the new road would gain no enforceable rights against the building company. From this it follows that reform will not affect every case where a third party in fact derives a benefit from a contract or relies on its due performance. To take another example, a report prepared under a contract may be put into more or less general circulation, such as audited accounts of a public company. It may foreseeably be relied on by third parties for any one of a variety of different purposes which the maker of the statement has no specific reason to anticipate. In such circumstances, under the present law a duty of care in tort is unlikely to be found and the maker of the statement will not be liable to the third party.[51] This is not a situation which we aim to change by a reform of the third party rule since it is unlikely that the contracting parties in such cases would ever intend that the third party should be invested with a contractual right of suit.

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51. Caparo Industries plc v. Dickman [1990] 2 A.C. 605 (no duty owed to potential investor). Cf. Morgan Crucible Co. plc. v. Hill Samuel & Co. Ltd. [1991] Ch. 295, where it was held that the directors and financial advisers of a target company in a contested take-over bid could owe a duty of care to a known bidder regarding the accuracy of profit forecasts and financial statements made during the course of bidding on which the bidder detrimentally relied.

PART III

EXCEPTIONS AND CIRCUMVENTIONS OF THE THIRD PARTY RULE

3.1 This part of the consultation paper describes a number of situations in which the third party rule does not apply. Some are exceptions where the third party rule is simply overridden, as where an undisclosed principal is entitled to sue on a contract made by his agent.[1] In other situations, the third party claimant does not need to rely on the contract but is able to rely on a property right (including rights under a trust), a possessory right or is able to sue in tort. In a further category of cases, the courts have recognised devices which, although not inconsistent with the privity doctrine, have the effect of allowing third parties to enforce contracts made for their benefit. In some of these cases, there is both substantial and formal compliance with the third party rule but in others there may merely be formal compliance, sometimes by the use of fictions.

3.2 Whilst being a statement of the present law, the primary purpose of this part of the paper is to highlight the following points:

(a) the third party rule can lead to injustice and inconvenience, particularly in commercial contexts;

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1. See para. 3.37 below. Cf. the view of Viscount Simonds in Midland Silicones Ltd. v. Scruttons Ltd. [1962] A.C. 446, 472, and Brennan J. in Trident General Insurance Co. v. McNiece Bros. Pty. Ltd. (1988) 62 A.L.J.R. 508, 520, that there is no true exception at common law to the doctrine of privity.

(b) the law has striven to do justice, though often at the expense of consistency;

(c) the exceptions cast doubt on the coherency of the rule;

(d) nonetheless, there are legitimate concerns with any possible new rule giving rights to third parties (e.g. the effect it will have on the freedom of the contracting parties) which must be faced in any reform.

1. Recourse to other areas of the law

(a) The law of trusts

3.3 Equity allows a third party to enforce a contract where it can be construed as creating a completely constituted trust in his favour. The subject matter of a trust may be a chose in action, for instance a promise by A to pay B a sum of money for the benefit of C. Where there is a completely constituted trust, the basis of the third party's claim is his equitable interest in its subject matter: he is not merely relying on a contract made by others. The requirements for the creation of a trust of a promise are, as with any other trust, traditionally comprehended by the three certainties: certainty of intention to create a trust; certainty of subject-matter (both as to the trust property and the beneficial interest conferred); and certainty of objects (i.e. who is to benefit). In the context of trusts of promises, it is the issue of intention which has been problematic.

3.4 It is true that the courts were once prepared to infer an intention to create a trust from the simple

intention to benefit a third party,[2] an approach which reached its high water mark in Les Affreteurs Reunis S.A. v. Leopold Walford (London) Ltd.[3] The owners of a ship, by a clause in a charterparty negotiated by a broker, promised the charterers that they would pay to the broker a commission of 3% on the estimated gross amount of the hire. The House of Lords held that, although the broker was not privy to the charterparty, he could sue through the charterers who were trustees for him. To the extent that the courts were prepared to iyfer an intention to create a trust solely from a contractual manifestation of intention to benefit a third party, the use of the trust could be regarded as at best a circumvention and at worst a fictional circumvention of the third party rule. However, since Walford the exception has fallen into disfavour. Whereas in some cases the courts have found a trust,[4] in the majority of cases they have refused to do so,[5] primarily because they did not consider it legitimate to import into contracts the

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2. In Tomlinson v. Gill (1756) Amb. 330; 27 E.R. 221, D promised a widow that he would discharge her late husband's debts. Lord Hardwicke L.C. held that the widow was trustee of the promise for her husband's creditors, who could enforce the promise against D. Other influential cases include Fletcher v. Fletcher (1844) 4 Hare 67; 67 E.R. 564; Lloyd's v. Harper (1880) 16 Ch.D. 290; Re Flavell (1883) 25 Ch. D. 89.

3. [1919] A.C. 801. See MacIntyre, (1965) 2 U.B.C.L. Rev. 103, 104-105.

4. In Royal Exchange Assurance v. Hope [1928] Ch. 179 and Re Webb [1941] Ch. 225, life assurance policies expressed to be for the benefit of a third party were held to create a trust in the third party's favour.

5. See Re Foster [1938] 3 All E.R. 357 and Re Sinclair's Life Policy [1938] Ch. 799, which cannot logically be distinguished from Hope and Webb: Treitel, op. cit., p. 563. Cf. Trident General Insurance Co. v. McNiece Bros. Pty. Ltd. (1988) 62 A.L.J.R. 508, 523 ff. per Deane J.: Appendix, para. 7.

idea of a trust when the parties have given no indication that such was their intention.[6]

3.5 Finally, a trust of a voluntary covenant to settle after-acquired property is not completely constituted, so that volunteer beneficiaries have no rights to enforce the covenant against the settlor even where the settlor acquires the property the subject-matter of the covenant.[7] But it is well settled that a voluntary covenant to settle property on the issue of a marriage, if contained in an ante-nuptial marriage settlement, confers enforceable rights on the beneficiaries.[8] This apparent exception to the third party rule is in fact a circumvention. In Hill v. Gomme,[9] Lord Cottenham L.C. described the children of the marriage as quasi-parties to the contract, and it is clear that the basis of the rule is that the child-beneficiary is seen as being in privity.[10]

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6. Re Schebsman [1944] Ch. 83, 89, per Lord Greene M.R.: cf. Treitel, op. cit., p. 563, n. 43. See also Re Engelbach [1924] 2 Ch. 348; Vandepitte v. Preferred Accident Insurance Co. [1933] A.C. 70; Re Clay's Policy [1937] 2 All E.R. 548.

7. Re Pryce [1917] 1 Ch. 234; Re Kay's Settlement [1939] Ch. 329; Re Cook's Settlement Trusts [1965] Ch. 902; Barton, (1975) 91 L.Q.R. 236; Meagher & Lehane, (1976) 92 L.Q.R. 427.

8. Pullan v. Koe [1913] 1 Ch. 9.

9. (1839) 5 My & Cr 250, 254; 41 E.R. 368.

10. In Re Cook's Settlement Trusts [1965] Ch. 902, 916, Buckley J. said that the fiction by which a child of the marriage is treated as if he were a party to and as having given consideration for his parents' marriage settlement was associated with his intimate connection with the marriage which was in fact the consideration for it. Only the spouses and issue fall within the consideration. All others are

(b) The law of real property

3.6 Contracts for the benefit of third parties are already extensive in the area of real property, the law allowing certain agreements to run with land so as to benefit or burden people other than the original contracting parties.

(i) In the case of covenants between landowners, although the burden of a restrictive covenant could never run at law with the covenantor's land, it could run in equity under the doctrine of Tulk v. Moxhay.[11] The benefit of a restrictive covenant can run with the benefited land in equity, provided that the covenant touches and concerns the land of the covenantee and also that the current owner of the benefited land can show either: (a) that the benefit of the covenant has been annexed to the benefited land;[12] or (b) that the benefit of the covenant has been expressly assigned with the land; or (c) that the benefit of the covenant has passed to him under a "building scheme".[13]

(ii) In the case of leasehold covenants, if there is no privity of contract but there is privity of estate between

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10. Continued volunteers with no right of enforcement: Re Plumptre's Marriage Settlement [1910] 1 Ch. 609.

11. (1848) 2 Ph. 774.

12. Express words were often required as evidence of the intention to annex. In Federated Homes Ltd. v. Mill Lodge Properties Ltd. [1980] 1 W.L.R. 594, Brightman L.J. indicated that annexation could take place automatically. This approach would lead to a greater circumvention of privity.

13. See Law Com. No. 127, The Law of Positive and Restrictive Covenants (1984), at para. 3.26.

the parties,[14] a covenant is binding provided that it has been entered into for the benefit of the land in question and is not purely personal to the covenantee.[15]

(iii) There are also certain statutory provisions which have the effect of conferring rights on third parties. Under section 1 of the Matrimonial Homes Act 1983, a non-owning spouse under certain conditions has rights of occupation against the owning spouse's mortgagee or landlord. Another example arises under section 1 of the Landlord and Tenant Act 1988; where a lease contains a covenant against assigning without consent, there is a statutory duty on the landlord to give consent unless it is reasonable not to do so. Where the consent of a superior landlord as well as of the immediate landlord is required, the statutory duty enables the tenant who is in no contractual relationship yith the superior landlord to sue.[16]

3.7 It will be seen later that we do not recommend altering any of the existing exceptions in the law of real property.[17] However, reform could give rights to third parties where presently they do not possess them. For instance, residents of a new housing estate are unable to

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14. That is to say, the relationship of landlord and tenant, as where the original tenant assigns the lease to a sub-lessee or where the original owner assigns the reversion to a third party.

15. See ss. 141 and 142 of the Law of Property Act 1925.

16. Although the duty under section 1 is owed to the tenant, the Law Commission envisaged that a claim for breach of duty might be brought by others; Law Com. No. 161, Leasehold Conveyancing (1987), at para. 2.2.

17. See para. 5.38 below.

enforce an agreement between a developer and a local authority to construct estate roads or build new drains or sewers. Under our proposals, the residents would be able to enforce such an agreement where it was the intention of the contracting parties to allow them to do so,[18] although whether this would occur frequently is another matter.

(c) The law of tort

3.8 A contract between A and B may, in addition to creating obligations between the parties themselves, impose on A a duty of care towards a third party, C. Whereas third party rights in tort do not, strictly speaking, encroach on the third party rule, in practical terms those who contract to exercise their skills are aware that third parties who suffer loss may have a cause of action in negligence. Some economic loss claims in tort are attempts to circumvent the third party rule so as to give effect to legitimate third party expectations, although other attempts may have less acceptable consequences.[19] In any event, the courts are

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18. See para. 5.10 below.

19. It is arguably unsatisfactory that the building owner in Junior Books Ltd. v. Veitchi Ltd. [1983] 1 A.C. 520 could circumvent contractual exemptions between the contractor and sub-contractor by way of a tort action against the sub-contractor; likewise, that the buyer in Leigh & Sillivan Ltd. v. Aliakmon Shipping Ltd. (The Aliakmon) [1986] A.C. 785 could circumvent the Hague Rules by suing the carrier in tort. In the latter case, the House of Lords denied a tort claim to the buyer, although the danger against which they were guarding would not have existed according to the approach of Robert Goff L.J. in the Court of Appeal ([1985] Q.B. 350), viz. that any tort claim by the buyer against the carrier would have to be modified by the contractual terms under which the carrier undertook responsibility to the shipper. See also Blom, (1991) 70 Can Bar. Rev. 156. On the former case, see para. 3.10 below.

increasingly refusing to countenance such attempts.

3.9 Since Donoghue v. Stevenson,[20] it has been established that where A contracts with B, he may owe a duty of care to C in respect of physical injury and damage to property. The combination of a tort claim and the third party rule led to difficulties in cases such as Adler v. Dickson,[21] where a passenger, who was faced with an exemption clause in a contract with a shipping company, sued the company's employees in tort. The decision in Donoghue v. Stevenson allowed the passenger to sue in tort, whilst the third party rule prevented the employees from relying on the exemption clause, which was contained in a contract to which they were strangers. We shall see that, more recently, the courts have been more willing to extend the benefit of exclusion clauses to third parties.[22]

3.10 Meanwhile, from the 1960's onwards, there occurred a steady increase in the incidence of tort liability as against a contracting party in favour of third parties, particularly in the direction of the recovery of pure economic loss. It was established in Hedley Byrne & Co. Ltd. v. Heller & Partners Ltd.[23] that a person making a negligent misrepresentation could owe a duty of care to a third party suffering economic loss through reliance on that statement, though it was agreed that there had to be a special

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20. [1932] A.C. 562.

21. [1955] 1 Q.B. 158.

22. See para. 3.23 ff below.

23. [1964] A.C. 465.

relationship between the parties for a duty to arise.[24] After Anns v. Merton L.B.C.,[25] this requirement was relaxed, and for a while it appeared that liability in the law of negligence, including the recovery of pure economic loss, simply turned on a proximity requirement, mitigated where necessary by policy considerations. In Junior Books Ltd. v. Veitchi Co. Ltd.,[26] a building owner was able to recover in tort against a sub-contractor in respect of pure economic loss arising from the laying of a defective floor, in spite of the fact that since the owner was complaining that he had not received what he had bargained for, his complaint should arguably have been against the person with whom he had made his bargain, i.e. the main contractor. In this case, although the tort action was brought in a jurisdiction (Scotland) which does recognise a contractual ius quaesitum tertio, the requirements for the creation of such a right under Scots law were apparently not satisfied.[27] It is consequently not clear whether this case should be regarded as an attempt to circumvent the third party rule.

3.11 However, the retreat from Anns and Junior Books has been swift,[28] such that Junior Books is virtually

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24. See also Smith v. Eric S. Bush (a firm) and Harris v. Wyre Forest D.C. [1990] 1 A.C. 831; Caparo Industries plc v. Dickman [1990] 2 A.C. 605.

25. [1978] A.C. 728.

26. [1983] 1 A.C. 520.

27. On Scots law, see Appendix, para. 22.

28. For instance, Peabody Donation Fund v. Sir Lindsay Parkinson & Co. Ltd. [1985] A.C. 210; Candlewood Corp. v. Mitsui Ltd. (The Mineral Transporter) [1986] A.C. 1; Leigh & Sillivan Ltd. v. Aliakmon Shipping Co. (The Aliakmon) [1986] A.C. 785; D. & F. Estates v. Church Commissioners [1989] A.C. 177; Simaan General Contracting Co. v. Pilkington Glass Ltd. (No. 2) [1988] Q.B. 758; Greater Nottingham

unciteable,[29] and Anns has been expressly overruled.[30] It is now clear that whereas a manufacturer may be liable in tort for injury to persons or damage to property caused by a defective chattel, in the absence of a contract he is not liable in tort to purchasers of the chattel who suffer economic loss because it is defective in quality.[31] Similarly, after Caparo Industries plc v. Dickman,[32] liability for economic loss due to negligent misstatement is confined to cases where the statement or advice is given to a known recipient for a specific purpose of which the maker is aware and the recipient relies on that statement or advice to his detriment.

3.12 If some claims for economic loss in tort are illegitimate attempts to circumvent the third party rule which the courts have recently sought to resist, in other cases special circumstances may justify this result.[33] In Ross v. Caunters,[34] where an improperly executed will deprived a prospective beneficiary of an intended benefit,

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28. Continued
Co-operative Society Ltd. v. Cementation Piling & Foundations Ltd. [1989] Q.B. 71; Pacific Associates v. Baxter [1990] 1 Q.B. 993.

29. D & F Estates v. Church Commissioners for England [1989] A.C. 177, 202. However, Junior Books has been explained as an application of the Hedley Byrne principle: see Murphy v. Brentwood D.C. [1991] 1 A.C. 398, 466 per Lord Keith.

30. Murphy v. Brentwood D.C. [1991] 1 A.C. 398. See Fleming, (1990) 106 L.Q.R. 525; Cooke, (1991) 107 L.Q.R. 46; Wallace, (1991) 107 L.Q.R. 228; Stapleton, (1991) 107 L.Q.R. 248.

31. Ibid.

32. [1990] 2 A.C. 605.

33. Atiyah, An Introduction to the Law of Contract (4th ed., 1989), p. 395.

the prospective beneficiary was able to recover in tort against the negligent solicitor. In policy terms, the decision may be defensible on the grounds that, otherwise, the only person who had suffered a loss would have had no valid claim whereas the one person with a valid claim had suffered no loss.

3.13 However, the decision has attracted criticism. It is difficult to detect an undertaking to P and there is usually no reliance by P anticipated by D.[35] It may also be difficult to see what interest P has which is recognisable at law, since the testator remains free at any time during his lifetime to alter his will.[36] It seems odd that, at the time of the alleged negligence, the solicitor owes the potential beneficiary a duty whereas the testator does not.

3.14 It is arguable that this situation is an example of a contract made to benefit a third party. The source of the solicitor's liability to the intended beneficiaries of a will derives from the solicitor's promise to the testator. An intended beneficiary has been denied his expected benefit. Since the protection of expectations is traditionally the domain of contract, one would expect the

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34. [1980] Ch. 297.

35. Reynolds, (1985) 11 N.Z.U.L.R. 215, 225.

36. See Seale v. Perry [1982] V.R. 193, which did not follow Ross v. Caunters, and Luntz, "Solicitors' liability to third parties", (1983) 3 O.J.L.S. 284. See also Banque Keyser Ullman v. Skandia (U.K.) Insurance Co. Ltd. [1990] 1 Q.B. 665 (C.A.); Van Oppen v. Trustees of Bedford School [1990] 1 W.L.R. 235; Caparo Industries plc v. Dickman [1990] 2 A.C. 605.

third party's remedy to be contractual.[37] As for the suggestion that to give a beneficiary a right of action would prevent the testator from altering his will, the answer is that since the will is ambulatory, any benefit only crystallises at death, so that before death there could have been no intention that the would-be beneficiary should have a right of action against anybody.[38]

3.15 However, it has been argued that the situation is not an example of a contract to benefit a third party, on the ground that the contract of retainer between the testator and the solicitor does not itself contain a promise by the solicitor conferring or purporting to confer a benefit on the prospective beneficiary.[39] In other words, the contracting parties do not intend that the beneficiary should have rights under the solicitor/client contract. It is the will, rather than the contract of retainer, which confers the benefit.[40]

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37. In the United States, the California Supreme Court first recognised in Lucas v. Hamm 56 Cal. 2d 583 (1961) that a disappointed beneficiary could have a right of action against a lawyer. Subsequent cases, which have raised the question whether the third party's right should sound in contract or tort, have usually reached the conclusion that a contractual action ought to be recognised: Prince, (1985) 25 Boston College L. Rev. 919, 946.

38. See also Clarke v. Bruce Lance & Co. [1988] 1 W.L.R. 881.

39. Gartside v. Sheffield, Young & Ellis [1983] N.Z.L.R. 37, 42-49.

40. Coote, (1984) N.Z. Recent Law, 107, 112-113. If the undertaking to draw up a will for the benefit of a named person is best not characterised as a case of a contract for the benefit of a third party, it may fall within the German idea of contracts with protective effects vis-a-vis third parties or the idea of "transferred (or shifting) loss": see Appendix, para. 28.

3.16 Furthermore, since the limitation period in contract runs from breach, and mistakes in a defective will may lie dormant for many years before actually causing loss, a third party contractual action may be of questionable utility.[41] In such cases, a right of action in tort, where the limitation period begins from the time of loss, may be a necessary protection for the beneficiary.[42]

3.17 The category of contracts to make wills may be difficult because it is sui generis.[43] We will be inviting views on how to treat this question in any reform.[44]

(d) The law of bailment

3.18 Where A bails goods to B who in turn sub-bails the goods to C who damages them, A may wish to bring an action against C. The question is whether C can rely on the terms on which the goods were sub-bailed to him as a defence to A's action, and thus whether A can be so bound by the terms of the B-C relationship.[45]

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41. In Iron Trades Mutual Insurance Co. Ltd. v. J.K. Buckenham Ltd. [1989] 2 Lloyd's Rep. 85 it was held that the Latent Damage Act 1986 did not apply to contractual claims (including breaches of contractual duties of care).

42. Cf. Tai Hing Cotton Mill Ltd. v. Liu Chong Hing Bank Ltd. [1986] A.C. 80 (P.C.). See also Midland Bank Trust Co. Ltd. v. Hett, Stubbs and Kemp [1979] Ch. 384; Bell v. Peter Browne & Co. [1990] 2 Q.B. 495; Evans, (1991) 7 P.N. 50; Mullany, (1991) 54 M.L.R. 349; [1991] L.M.C.L.Q. 169.

43. Gartside v. Sheffield, Young & Ellis [1983] N.Z.L.R. 37, 42 per Cooke J.

44. See paras. 5.40-5.44 below.

45. See para. 2.3 (iii) above.

3.19 In Morris v. C.W. Martin & Sons Ltd.,[46] P sent a mink stole to a furrier to be cleaned. The furrier did not clean furs himself, so, with P's consent, he delivered it to DD, well-known cleaners. The contract between the furrier and DD, which was made by the furrier as principal and not as agent for P, contained an exemption clause. While it was with DD, the fur was stolen by one of their servants. When P claimed damages against DD, the latter sought to rely upon the conditions of their contract with the furrier. On the particular facts of the case, they failed. The relevant exemption clause was held not to apply since it covered only goods actually belonging to the furrier and not to the furrier's customers such as P. However, Lord Denning M.R. said that in principle DD could have relied on valid exempting conditions. He admitted that there were compelling equities on either side. On the one hand, it would be hard on P if her claim was defeated by exempting conditions of which she knew nothing and to which she was not a party. On the other hand, it would be hard on DD if they were held liable to a greater extent than they agreed to undertake. Lord Denning M.R. concluded that P would be bound by the conditions if she had expressly or impliedly consented to the bailee making a sub-bailment containing those conditions, but not otherwise.[47] Since P agreed that the furrier should send the fur to DD, she impliedly consented to his making a contract for cleaning on the terms current in the trade.[48]

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46. [1966] 1 Q.B. 716; Palmer, Bailment, (2nd ed., 1991), pp. 1618-1629.

47. At p. 729. Lord Denning M.R. cited with approval the speech of Lord Sumner in Elder Dempster & Co. Ltd. v. Paterson, Zochonis & Co. Ltd. [1924] A.C. 522, 564, which was based on the idea of a bailment on terms.

48. Although Diplock L.J. declined to take any view on the point, Salmon L.J., without forming a concluded opinion, declared himself to be "strongly

3.20 In Johnson Matthey & Co. Ltd. v. Constantine Terminals Ltd.,[49] PP consigned a tonne of silver for carriage by rail. The carrier arranged for safe custody of the silver until it was loaded, but it was stolen due to the negligence of the sub-bailee, a storage firm. When sued by PP, the sub-bailee sought to rely on an exemption clause in its contract with the carrier. Donaldson J. held that it could do so, although it was not in privity with PP. As there was no duty of care apart from that arising out of the bailment, PP could not show a duty and a breach of that duty by the sub-bailee without relying on all the terms of the sub-bailment, including the exemption clause. Donaldson J. went further than Lord Denning M.R., since he also held that a bailor is bound by any terms which constitute the consideration upon which the sub-bailee accepted the goods, irrespective of the bailor's consent. In Singer Co. (U.K.) Ltd. v. Tees and Hartlepool Port Authority,[50] Steyn J. endorsed Lord Denning M.R.'s view in Morris v. C.W. Martin & Sons Ltd. On the facts of the case, it was not necessary to to consider Donaldson J.'s wider approach in Johnson Matthey.[51]

3.21 To the extent that the bailor is a third party to the sub-bailment, he is bound by the exemption clause, rather than benefiting from it. While it could be said that

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48. Continued
attracted" by Lord Denning M.R.'s view: [1966] 1 Q.B. 716, 741. See also The Captain Gregos (No. 2) [1990] 2 Lloyd's Rep. 395, 405.

49. [1976] 2 Lloyd's Rep. 215, noted Beatson, (1977) 55 Can. B.R. 746, 748.

50. [1988] 2 Lloyd's Rep. 164.

51. Cf. Palmer, op. cit., pp. 1630-1632; Phang, (1989) 9 O.J.L.S. 418.

the sub-bailee is taking the benefit of the bailment between the bailor and the bailee, there are two difficulties with this view. First, the bailment need not always be a contract, so that the benefit taken by the third party sub-bailee need not always be the benefit of a contract. Secondly, on Donaldson J.'s view in Johnson Matthey, the sub-bailee's rights are not dependent on the original bailment but on the terms upon which he accepted the goods. It is therefore uncertain whether or not this device is an exception to the rule preventing third parties from enforcing contracts made for their benefit. However, once again, the bailment cases reflect a desire on the part of the courts to avoid uncommercial results which would follow from a rigid adherence to the third party rule.

2. Collateral contracts

3.22 A contract between two parties may be accompanied by a collateral contract between one of them and a third party. For instance, where A buys goods from B, there may be a collateral contract between A and the manufacturer in the form of a guarantee.[52] In Shanklin Pier Ltd. v. Detel Products Ltd.,[53] P instructed contractors engaged in repairing their pier to use D's protective paint in reliance on a representation that it would last seven years. When the paint proved unsatisfactory after three months, P recovered against D. It was held that, in addition to the main contract between D and the contractors, there was a

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52. Cheshire, Fifoot & Furmston's Law of Contract (12th ed., 1991), pp. 64-65; Treitel, op. cit., pp. 523-524. See also Charnock v. Liverpool Corpn. [1968] 1 W.L.R. 1498; Atiyah, op. cit., pp. 105-106.

53. [1951] 2 K.B. 854. See also Wells (Merstham) Ltd. v. Buckland Sand & Silica Ltd. [1965] 2 Q.B. 170.

collateral contract between P and D that the paint would last seven years, the consideration for which was that P should cause the contractors to enter the main contract. The use of collateral contracts has, however, been developed to the extent that fictitious collateral contracts have been found in hard cases. In The Eurymedon,[54] where the main contract was between the shipper and carrier, the Privy Council detected a contract between the shipper and the stevedores made through the agency of the carrier, to allow the stevedores the benefit of the carrier's exemption clauses in return for the unloading of the goods by the stevedores. This arrangement was binding on the buyers, by way of another fictitious contract, a so-called Brandt v. Liverpool contract,[55] which arose when they presented the bill of lading and took delivery. Hence, two parties became bound by reason of two implied contracts, in circumstances where the two original contracting parties dropped out of the picture altogether.

3. Exemption clauses

3.23 Where an exemption clause in a contract purports to benefit a person who is not a party to the contract, can that person take the benefit of the clause? In the last century, the general rule was that the benefit of such

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54. [1975] A.C. 154. Discussed more fully at para. 3.27 below.

55. See [1924] 1 K.B. 575. This approach depends on stretching normal contractual doctrine for commercial reasons; see Rights of Suit in Respect of Carriage of Goods by Sea (1991), Law Com. No. 196; Scot. Law Com. No. 130, paras. 2.11 & 2.12. Some courts are more willing to do this than others: cf. The Aramis [1989] 1 Lloyd's Rep. 213 with The Captain Gregos (No.2) [1990] 2 Lloyd's Rep. 395 and The Gudermes [1991] 1 Lloyd's Rep. 456.

clauses could not be taken, although the courts were astute to find exceptions to the rule, particularly in cases of carriage by rail.[56] In Hall v. North Eastern Railway Company,[57] P, travelling from Scotland to Newcastle, was given a ticket, issued by the North British Railway Company containing a clause exempting it from liability for personal injury. Since the North British Railway did not go to Newcastle, the journey was completed in D's train to which the carriage occupied by P was attached. At this stage, another of D's trains ran into it, and P was injured. His action failed on the ground that the North British Railway Company was acting as agent for D, who could thus take the benefit of the exemption clause. [58]

3.24 Much of the law concerning third party reliance on exemption clauses has been developed in commercial contexts, particularly involving bills of lading. The judicial favour towards third parties shown in the above mentioned cases was sanctioned by the House of Lords in Elder, Dempster & Co. Ltd. v. Paterson, Zochonis & Co. Ltd.[59] Bills of lading issued by the time charterers of a vessel provided that the shipowners[60] would not be liable for damage caused by negligent stowage. When a cargo of palm oil was damaged, the

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56. Bristol and Exeter Ry. v. Collins (1859) 7 H.L.C. 194; Martin v. Great Indian Peninsular Ry. (1867) 3 Ex. 9; Foulkes v. Metropolitan and District Ry. (1880) 5 C.P.D. 157.

57. (1875) 10 Q.B. 437.

58. This reasoning has been described as artificial, although face saving for the doctrine of privity: Treitel, op. cit., p. 553.

59. [1924] A.C. 522.

60. It was not disputed that this term included the charterers: [1923] 1 K.B. 420, 422.

shippers sued both charterers and shipowners. The charterers could rely on the excepted peril in the bill of lading because they had contracted with the shippers. The question was whether the shipowners could, as a defence to the shipper's action in tort, rely on this term although the contract of carriage had been made between the shipper and the charterer. The House of Lords held that they could, although the reasoning on which the result was based has proved very difficult to understand.[61]

(i) One reason is that when the shipowners received the oil from the shippers, they did so as bailees upon the terms of the bill of lading. In other words, an implied contract between shipper and shipowner arose from the bailment, incorporating the terms of (including the exceptions in) the bill of lading.[62]

(ii) Another reason is that the contract was entered between shipper and shipowner through the agency of the charterer.[63]

Both these reasons are consistent with the doctrine of privity, since both are predicated on the existence of a contract between shipper and shipowner.

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61. Treitel, op. cit., pp. 552-553; Palmer, op. cit., p. 1595. Carver, Carriage by Sea (13th ed., 1982), p. 529, refers to the case as a "mystery". Scrutton on Charterparties (19th ed., 1984), p. 251, n. 36, contends that no general principle is to be extracted from the case.

62. See Lord Sumner, at p. 564, with whom Lord Dunedin and Lord Carson agreed. See also para. 3.19 above.

63. Treitel, op. cit., p. 553, based on the speech of Viscount Cave, at p. 534, first sentence.

(iii) A third reason involved the so-called doctrine of vicarious immunity, according to which an agent who performs a contract is entitled to any immunity from liability which his principal would have had. Hence, although the shipowners may not have been privy to the contract of carriage (between shipper and charterer), they took possession of the goods on behalf of and as agents for the charterers, and so could claim the same protection as their principals.[64]

3.25 Although for many years the principle of vicarious immunity was generally accepted,[65] it did not survive Scruttons v. Midland Silicones Ltd.[66] The defendant stevedores, engaged by the carrier, negligently damaged a drum containing chemicals. When the consignees sued in tort, the stevedores unsuccessfully attempted to rely on the carrier's package limitation contained in the bill of lading. The majority of the House of Lords was not prepared to hold that the principle of vicarious immunity was the ratio of Elder, Dempster. Viscount Simonds distinguished Elder, Dempster and approved it only to the extent of its

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64. This was the basis of Scrutton L.J.'s judgment in the Court of Appeal: [1923] 1 K.B. 436, 441, and was supported by Viscount Cave, at p. 534, with whom Lord Carson agreed. See also Viscount Finlay, at p. 548.

65. See, for instance, Scrutton L.J. in Mersey Shipping & Transport Co. Ltd. v. Rea Ltd. (1925) 21 Ll.L.R. 375, and F.C. Bradley & Sons Ltd. v. Federal Steam Navigation Co. (1926) 24 Ll.L.R. 446; Pyrene Co. Ltd. v. Scindia Steam Navigation Co. Ltd. [1954] 2 Q.B. 402. But cf. Cosgrove v. Horsfall (1946) 62 T.L.R. 140 (where Elder, Dempster was not cited) and Adler v. Dickson [1955] 1 Q.B. 158.

66. [1962] A.C. 446.

particular facts. The only possible rationalisation was that since the master signed the bill of lading, the proper inference was that the shipowner received the goods into his possession on the terms of the bill of lading, although he was not a party thereto.[67] However, the result in Midland Silicones can also be reached where, as in the United States, there is general recognition of a doctrine of third party rights in contract. In Krawill Machinery Corp. v. Robert C. Herd & Co. Inc.[68] the Supreme Court of the United States held that there was nothing in the contract between the plaintiff shipper and the carrier to indicate that the contracting parties intended to limit the liability of the defendant stevedores in tort. We shall see below that suitably drafted bills of lading can circumvent the decisions reached in Midland Silicones and Krawill.

3.26 Midland Silicones is also significant for Lord Denning's powerful dissent. He noted that, if the buyer is able to sue a sub-contractor (e.g. a stevedore) in tort for what was in truth a breach of the contract of carriage, and the stevedore is not allowed the benefit of the terms of that contract, there exists an easy way for the buyer to avoid the terms of the contract of carriage. Indeed, the possibility of third party stevedores taking advantage of exemption clauses was not entirely ruled out.[69] Lord Reid said that there could exist a contract between the shipper and the stevedore made through the agency of the carrier, providing certain conditions were met:[70]

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67. [1962] A.C. 446, 470.

68. [1959] 1 Lloyd's Rep. 305.

69. Cf. Wilson v. Darling Island Stevedoring & Lighterage Co. Ltd. [1956] 1 Lloyd's Rep. 346, 364 (Fullagar J.).

70. [1962] A.C. 446, 474.

(i) the bill of lading makes it clear that the stevedore is intended to be protected by the provisions therein,

(ii) the bill of lading makes it clear that the carrier, in addition to contracting on his own behalf, is also contracting as agent for the stevedore,

(iii) the carrier has authority from the stevedore so to act, or perhaps later ratification by the stevedore would suffice,

(iv) consideration must move from the stevedore.

3.27 Lord Reid's speech encouraged the use of "Himalaya" clauses,[71] which purport to extend the defences of the carrier to servants, agents and independent contractors engaged in the loading and unloading process. In turn, these have given rise to several important cases. In The Eurymedon,[72] a drilling machine was shipped from Liverpool to New Zealand. The bill of lading contained a clause barring claims against the carrier after one year. A "Himalaya" clause extended this immunity to the carrier's servants, agents and independent contractors. Stevedores negligently damaged the machine. When sued by the consignees more than a year later, the stevedores sought to take advantage of the time bar in the bill of lading. It was accepted that the first three parts of Lord Reid's test had been satisfied. The important question was whether the difficulties of consideration had been overcome. By a bare

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71. Named after the vessel in Adler v. Dickson [1955] 1 Q.B. 158. See Powles, [1979] L.M.C.L.Q. 337.

72. [1975] A.C. 154 (P.C.).

majority, the Privy Council found in favour of the stevedores:

> "... the bill of lading brought into existence a bargain initially unilateral but capable of becoming mutual, between the shipper and the [stevedores], made through the carrier as agent. This became a full contract when the [stevedores] performed services by discharging the goods. The performance of these services for the benefit of the shipper was the consideration for the agreement by the shipper that the [stevedores] should have the benefit of the exemptions and limitations contained in the bill of lading."[73]

3.28 The reasoning has been much criticised as artificial,[74] primarily because it effectively rewrites the Himalaya clause, which was an agreement between the shipper and the carrier and from which it is difficult to detect an offer made by the shipper to the stevedore.[75] As for the problem of making the consignee a party to the offer made by the shipper to the stevedore, there are two main routes. One

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73. Ibid., pp. 167-168.

74. Reynolds, (1974) 90 L.Q.R. 301; Coote, (1974) 37 M.L.R. 453; Palmer, [1974] J.B.L. 101; Duggan, (1974) 9 Melbourne Univ.L.R. 753; Rose, (1975) 4 Anglo-Am. L.R. 7; Battersby, [1978] U. of Toronto L.J. 75; Waddams, (1977) 55 Can. Bar Rev. 327; Davies and Palmer, [1979] J.B.L. 337. For discussion of whether the better analysis is a unilateral or a "post-active" bilateral contract, see Palmer, op. cit., pp. 1598-1609.

75. Since the carrier desires the result that holders of the bill of lading should not sue his servants or independent contractors, he can achieve this by procuring that they promise not to sue, by contracting to indemnify the servants or agents against claims, and by making it clear to the consignor and holder of the bill that he has done so. The carrier would then be able to obtain the staying of any action against the third party in breach of this agreement. See Reynolds, (1974) 90 L.Q.R. 301, 304, and para. 3.41 ff below.

is via section 1 of the Bills of Lading Act 1855, which is in effect a statutory assignment of the shipper's rights to the indorsee of a bill of lading. The second is that the indorsee of a bill of lading may be bound by the stipulations therein by presenting the bill of lading to the ship and requesting delivery of the goods thereunder: a so-called Brandt v. Liverpool contract.[76] We have already seen that this reasoning is to an extent artificial.[77]

3.29 The Eurymedon was not received with universal enthusiasm in other jurisdictions,[78] such that the High Court of Australia in The New York Star[79] tried to restrict its application in a situation in which all four of Lord Reid's conditions could be said to have been satisfied. A cargo of razor blades was shipped from Canada to Australia under a bill of lading containing a Himalaya clause. Stevedores discharged the vessel, but the goods were subsequently stolen. More than a year later the consignees sued the stevedores in negligence. The stevedores were unsuccessful before the High Court of Australia. Stephen and Murphy JJ. thought that, as a matter of policy, a decision

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76. [1924] 1 K.B. 575.

77. See para. 3.22 above.

78. It was distinguished by the Supreme Court of British Columbia in The Suleyman Stalskiy [1976] 2 Lloyd's Rep. 609, and by the Kenyan High Court in Lummus Co. Ltd. v. East African Harbours Corpn. [1978] 1 Lloyd's Rep. 317, 322-323, because the carrier did not have authority to contract on behalf of the stevedore. See also Herrick v. Leonard & Dingley Ltd. [1975] 2 N.Z.L.R. 566.

79. Sub. nom. Port Jackson Stevedoring Pty. Ltd. v. Salmond & Spraggon (Australia) Pty. Ltd. [1981] 1 W.L.R. 138 (P.C.). See Palmer, op. cit. pp. 1600-1601 for the view that the case might have been decided on the bailment basis discussed in paras. 3.20-3.21 above.

in favour of the consignees would encourage carriers to insist on reasonable diligence on the part of its employers and contractors. Furthermore, a policy of extending protection to stevedores would merely benefit shipowning nations to the detriment of those countries, such as Australia, which relied on these fleets for their import and export trade. The Privy Council unanimously reversed the High Court of Australia. It warned against confining The Eurymedon to its facts, and stated that in the normal course of events involving the employment of stevedores by carriers, accepted principles enabled and required stevedores to enjoy the benefit of contractual provisions in the bill of lading.[80]

3.30 In other contexts the courts have been less attracted by the unilateral contract device though similar results have been achieved by other means. In Southern Water Authority v. Carey,[81] the court refused to extend the unilateral contract device to subcontracted engineers. The judge doubted that the principle of unilateral contract could be applied beyond the specialised practice of carriers and stevedores and described it as "uncomfortably

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80. At p. 143. Treitel, op. cit., pp. 555-556, submits that the principle of The Eurymedon should not be confined to cases where carriers and stevedores are associated companies or where there is some previous connection between them. He accepts that the protection of Himalaya clauses does not cover acts wholly collateral to contractual performance, see Raymond Burke Motors Ltd. v. The Mersey Docks and Harbour Co. [1986] 1 Lloyd's Rep. 155 (goods damaged while they were stored and not during any loading or unloading).

81. [1985] 2 All E.R. 1077. See also Kendall v. Morgan The Times, 2 December 1980 where The Eurymedon's approach was not applied in the context of a labour dispute.

artificial".[82] However, the sub-contractor successfully defended a claim for negligence by a firm of consultant engineers by relying on the terms of the main contract between the employer and a main contractor. Any prima facie duty of care owed by D to P was negatived by the contractual setting. A similar result was achieved in Norwich City Council v. Harvey,[83] where a building was damaged by fire as a result of the negligence of the sub-contractor. The main contract provided that the building owner was to bear the risk of damage by fire, and the sub-contractor contracted on the same terms and conditions as in the main contract. P sued the sub-contractor in tort. The Court of Appeal held that, although there was no direct contractual relationship between P and D, nevertheless they had both contracted with the main contractor on the basis that P had assumed the risk of damage by fire. Hence, D owed P no duty in respect of the damage which occurred. May L.J. said:

> "I do not think that the mere fact that there is no strict privity between the employer and the subcontractor should prevent the latter from relying upon the clear basis upon which all parties contracted in relation to damage to the employer's building caused by fire, even when due to the negligence of the contractors or subcontractors."[84]

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82. At p. 1084.

83. [1989] 1 W.L.R. 828.

84. At p. 837. This reasoning does not, however, explain the non-liability (at pp. 833-834) of the sub-contractor's employee who was also sued. This may be the ghost of Elder, Dempster rising from its watery grave, the reasoning being reminiscent of the now rejected doctrine of vicarious immunity (see para. 3.25 above); Palmer, op. cit., pp. 1596-1597; Hopkins, [1990] C.L.J. 21, 23, though cf. The Forum Craftsman [1985] 1 Lloyd's Rep. 291, 295 and The Kapetan Markos N.L. (No. 2) [1987] 2 Lloyd's Rep. 321, 331.

3.31 In conclusion, there have been several ways in which third parties have sought to take the benefit of exemption clauses limiting liability for negligence. These include the now rejected doctrine of vicarious immunity, the unilateral contract device and the idea of a contract limiting the scope of a duty of care in tort. By each of these techniques, the courts have striven to achieve commercially workable results. There is obvious common sense behind the Elder, Dempster doctrine of vicarious immunity:

> "It might be expected that where a principal has an immunity conferred upon him by contract, an agent working for him in respect of that contract would be entitled to the same immunity towards the third party. The notion of privity of contract, however, prevents this result being easily achieved".[85]

Similarly, the results in The Eurymedon and The New York Star were based on the realisation that, if stevedores could not rely on the terms of the contract of carriage, it would encourage cargo owners to circumvent the compulsory terms of internationally agreed rules, such as the Hague and Hague-Visby Rules, by suing stevedores and other third parties rather than the carrier.[86] However, where contractual analysis has been used, the courts have only managed to achieve these commercially workable results by a somewhat artificial extension of the relevant concepts.

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85. Bowstead on Agency (15th ed., 1985), p. 491.

86. While The Eurymedon and The New York Star may create a rational division of risk between the shipper and all those engaged in the carriage operation, in shifting loss from stevedores to cargo underwriters it shifts the loss away from those who are responsible for it and can be said to give stevedores no incentive to be careful: Powles, [1979] L.M.C.L.Q. 331, 335.

4. Documentary letters of credit

3.32 Documentary credits are central to the financing of international sales transactions.[87] The buyer will request the issuing bank to open a documentary credit in the seller's favour. The issuing bank notifies the seller, and a correspondent banker in the seller's country may confirm the credit. Clearly, there is a contract between the seller and the buyer and also between the buyer and the issuing bank. However, it is also established that an irrevocable credit constitutes a contract between the issuing bank and the seller, which imposes on the bank an absolute obligation to pay, irrespective of any dispute under the sale contract.[88] Thus, the operation of documentary credits does not infringe the third party rule but is rather an exception to the doctrine of consideration. However, the time at which the contract between seller and issuing bank is established and when it becomes irrevocable are matters of debate.[89]

5. Joint promisees

3.33 In Coulls v. Bagot's Executor & Trustee Co.

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87. See, generally, Benjamin's Sale of Goods (3rd. ed., 1987), ch. 23; Gutteridge & Megrah, Law of Bankers' Commercial Credits (7th ed., 1984).

88. Trans Trust S.P.R.L. v. Danubian Trading Co. [1952] 2 Q.B. 297; Hamzeh Malas v. British Imex Industries [1958] 2 Q.B. 127. See also Gutteridge & Megrah, op. cit., p.26 ff.

89. See Benjamin, op. cit., para. 2169, which prefers the view that the issuing bank's engagement becomes irrevocable as soon as the documentary credit reaches the seller's hands, rather than the view that irrevocability depends on whether the seller has acted on the credit, as by commencing performance of his contract with the buyer.

Ltd.,[90] the High Court of Australia said that, in principle, a joint promisee could enforce a contract notwithstanding that she had not in fact furnished any consideration. However the better view of the nature of a contract made with two or more persons jointly, is that the promise is made to them collectively, that the promise must be supported by consideration, but not necessarily by consideration furnished by them separately. It means a consideration given on behalf of them all, and therefore moving from all of them.[91] In other words, if a promise is made to A and B jointly, then it is made to an entity, (A+B). The promisee is (A+B), so (A+B) must provide the consideration. It is irrelevant that the price is actually paid by A so long as he does so on behalf of the entity, in which case the consideration does indeed move from the promisee.[92] On this analysis, the joint promisee principle does not represent an exception to the third party rule.

6. Assignment

3.34 Except when personal considerations are at its foundation,[93] the benefit of a contract may be transferred, or assigned, to a third party, the original party withdrawing from the contract and being replaced by a third

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90. (1967) 40 A.L.J.R. 471. See also para. 2.7 above.

91. At p. 483 per Windeyer J. It has been pointed out that if joint promisees could not enforce the promise, the promise could not be enforced at all; for, if one party tried to sue alone, he would be defeated by the rule that all promisees must be party to the action: Treitel, op. cit., p. 522. See also (1976) 50 A.L.J. 439, 445.

92. Kincaid, [1989] C.L.J. 243, 261; Coote, [1978] C.L.J. 301, 304-305.

93. Farrow v. Wilson (1869) L.R. 4 C.P. 744.

party.[94] Again, the law is willing to regard a contractual right as a res which can be treated in the same way as something tangible.[95] In addition to assignment by an act of the parties, there also exists assignment by operation of law.[96] The assent of the promisor is not necessary for an assignment. This is an important consideration when assessing the arguments against the recognition of third party rights based on the nature of contracts and the rights of the contracting parties to rescind or vary their contract.[97] Assignment is an example of a supervening event which may deprive promisors of their chosen contracting party, although safeguards are imposed to protect promisors. While an equitable assignment is usually fully effective even without notice,[98] notice is desirable and there are circumstances in which failure to give notice may leave the equitable assignee unable to exercise rights enjoyed by the assignor.[99] In addition, an assignee takes "subject to equities",[100] i.e. subject to any defences which the promisor has and any defects in the assignor's title.

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94. Cheshire, Fifoot & Furmston, op. cit., ch.16; Treitel, op. cit., ch. 16.

95. See also para. 3.3 above.

96. For instance, when a party to a contract is declared bankrupt, rights of action forming part of his estate are "deemed to have been assigned" to his trustee in bankruptcy: Insolvency Act 1986, s. 311(4).

97. See para. 4.3 below and, on variation and cancellation, para. 5.27 ff below.

98. Gorringe v. Irwell India Rubber (1886) 34 Ch.D. 128.

99. The failure to give notice of the equitable assignment of an option may mean that the option is not exercisable by the assignee: Warner Bros. Records v. Rollgreen [1976] Q.B. 430. Notice of a statutory assignment must be in writing: Law of Property Act 1925, s. 136(1).

3.35 Although it could be argued that assignment is a circumvention of privity, since the assignee becomes a party to the contract and asserts the right as a party, it is probably best seen as an exception: the promisor is faced with an action brought on the contract by a person whom he did not regard as a party and whom he may not have intended to benefit. The practical importance of assignment is considerable; the whole industry of debt collection and credit factoring depends upon it.

7. Agency

3.36 Many contracts are made through intermediaries and will be subject to the law of agency. Agency is the relationship which exists between two persons, one of whom (the principal) expressly or impliedly consents that the other should act on his behalf, and the other of whom (the agent) similarly consents so to act or so acts.[101] Where the principal is disclosed, whether named or unnamed, it is not accurate to describe the principal as a third party. The principal has supplied the consideration and his existence is known to the other party.

3.37 More difficult is the doctrine of the undisclosed principal. If an agent within his authority contracts in his own name and purportedly on his own behalf, the undisclosed principal may in certain circumstances intervene to sue and be sued on the contract.[102]

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100. Cheshire, Fifoot & Furmston, op. cit., pp. 516-7; Treitel, op. cit., pp. 592-595.

101. Bowstead op. cit., p. 1.

102. Ibid., p. 312.

"The third party who has no knowledge of the principal's existence may thus find that he has made a contract with a person of whom he has never heard, and with whom he never intended to contract."[103]

3.38 It has been said that the law as to the rights and liabilities of an undisclosed principal is inconsistent with the elementary law of contract,[104] although the doctrine did appear before general principles of the law of contract had properly emerged.[105] Whilst there are dicta that the contract is made with the undisclosed principal,[106] this seems inconsistent with the fact that the agent himself remains entitled to sue. Whereas it might simply be asserted that both the principal and the agent are parties to the contract,[107] the preferable view seems to be that the undisclosed principal is a third party who is permitted to intervene in a contract which he did not make for reasons of commercial convenience.[108]

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103. Atiyah, op. cit., p. 381.

104. Pollock, (1887) 3 L.Q.R. 358, 359.

105. Bowstead, op. cit., p. 312. Cf. Scrimshire v. Alderton (1743) 2 Strange 1182; 93 E.R. 1114, where the jury clearly resented the intervention of the undisclosed principal.

106. Keighley, Maxsted & Co. v Durant [1901] A.C. 240, per Lord Halsbury, at p. 244; per Lord Davey, at p. 256; per Lord Lindley, at pp. 261-2; Higgins v Senior (1841) 8 M & W 834, 151 E.R. 1282, per Parke B., at p. 844.

107. Wylie (1966) 17 N.I.L.Q. 351, 382.

108. Bowstead, op. cit., p. 313; Cheshire, Fifoot & Furmston, op. cit., p. 489; Treitel, op. cit., p. 631. The ability of the undisclosed principal to sue may be excluded if inconsistent with the terms of the contract: Bowstead, op. cit., p. 321.

8. Promisee assisting the third party

3.39 Akin to the rule preventing a third party from enforcing a contract made for his benefit is the general rule that a promisee can recover only in respect of his own loss. In Forster v. Silvermere Golf & Equestrian Centre,[109] P owned property which she and her two children occupied. She transferred the property to D, who undertook to construct a house for P and her children who could live there rent-free for life. When D breached this undertaking, P recovered damages for her own loss. However, she could not claim damages for the loss of rights of occupation after her death which her children would have enjoyed. Dillon J. described this as "a blot on our law and most unjust".

3.40 However, in certain circumstances the promisee may be able to assist the third party. In Beswick v. Beswick,[110] a third party beneficiary of a promise who was unable to sue in her own right was able to enforce the promise by way of specific performance qua administratrix of her husband's estate. In Jackson v. Horizon Holidays Ltd.,[111] P booked a holiday for himself, his wife and their children, through DD, a travel company. The standard of the hotel proved so unsatisfactory that the family suffered discomfort, vexation, inconvenience and distress. It was held that, in assessing damages, the suffering of the wife and children could be taken into account in addition to that of P. However, Lord Denning M.R.'s judgment relied heavily on a dictum of Lush L.J. in Lloyd's v. Harper,[112] which is

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109. (1981) 125 S.J. 397.

110. [1968] A.C. 58. See para. 4.23 below.

111. [1975] 1 W.L.R. 1468.

112. (1880) 16 Ch.D. 290, 321.

abstracted from its context and is distinguishable since it concerns a trust.[113] In Woodar Investment Development Ltd. v. Wimpey Construction (U.K.) Ltd.,[114] Lord Wilberforce disapproved of Lord Denning's reasoning, although he was not prepared to disagree with the actual result of the case:

> "It may be supported either as a broad decision on the measure of damages (per James L.J.) or possibly as an example of a type of contract - examples of which are persons contracting for family holidays, ordering meals in restaurants for a party, hiring a taxi for a group - calling for special treatment."[115]

3.41 Furthermore, in the case of a promise not to sue a third party, the promisee may assist the third party beneficiary by seeking a stay of any action by the promisor against the third party under section 49(3) of the Supreme Court Act 1981. This preserves the power of the Court to stay any proceedings before it, where it thinks fit to do so, whether on its own motion or on the application of any person.

3.42 In Gore v. Van der Lann,[116] the question was

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113. He also failed to consider authorities such as Vandepitte v. Preferred Accident Insurance Corporation of New York [1933] A.C. 70 and Green v. Russell [1959] 2 Q.B. 226.

114. [1980] 1 W.L.R. 277.

115. At p. 283. In Calabar Properties Ltd. v. Stitcher [1984] 1 W.L.R. 287, 290, there was no dispute that a tenant's damages for breach of the landlord's covenant to repair might include compensation for "bouts of ill-health" suffered thereby by the tenant's husband.

116. [1967] 2 Q.B. 31. See Davies, (1981) 1 L.S. 287.

whether Liverpool Corporation could restrain the holder of a free 'bus pass from suing a 'bus conductor for negligence, given that the free pass contained a clause excluding liability for personal injury on the part of the Corporation or its servants. On the facts, the clause was void under section 151 of the Road Traffic Act 1950. However, the Court of Appeal said that the Corporation could have obtained a stay, if: (a) the clause could have been construed as a promise by Mrs. Gore not to sue (which on the facts it was not) and, (b) if the Corporation had a sufficient interest so as to entitle it to a stay, for instance if it been required to indemnify its servants in respect of torts committed by the latter.[117] In Snelling v. John G. Snelling Ltd.,[118] Ormrod J. said that it did not follow from Gore that there had to be an express promise not to sue. It was sufficient that it was a necessary implication of the agreement that P could not sue. In that case, a family business was substantially indebted to three directors who were brothers. They agreed that, in the event of any director resigning, he would forfeit the debt owed to him by the company. P resigned and sued the company. The latter was a stranger to the brothers' agreement which was thus no defence to P's claim. Nevertheless, the other brothers applied to be joined as defendants and pleaded the agreement. Ormrod J. would have granted a stay, but as the

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117. In European Asian Bank v. Punjab & Sind Bank [1982] 2 Lloyd's Rep. 356, 369, Ackner L.J. said that for the promisee to obtain a stay it would be necessary to establish an express or implied promise not to sue and some legal or equitable right to protect, such as an obligation to indemnify D. In these circumstances it would be a fraud on the promisee for the proceedings to continue.

118. [1973] Q.B. 87.

brothers had made out their case he went further and dismissed the action.[119]

3.43 In The Elbe Maru,[120] a bill of lading provided an undertaking that the holder would not make any claim against the carriers' sub-contractors. Whilst the goods were in the custody of a firm of hauliers, who were sub-contractors of the carriers, they were stolen. The indorsees of the bill of lading claimed damages against the sub-contractors, the action against the original carriers being time barred. The carriers applied for a stay, which was granted. Unlike Gore, this was a clear case of a promise not to sue. However, the remedy being discretionary, Ackner J. said that it was not enough to show a clear promise not to sue. But where an applicant could show a real possibility of prejudice if the action were not stayed, as here by being exposed to an action by its agents, the discretion would be exercised in their favour.[121]

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119. It has been argued that Snelling is difficult to reconcile with the requirement of sufficient interest as explained in Gore, but is nonetheless consistent with the spirit of Beswick v. Beswick: Chitty on Contracts (26th ed., 1989), para. 1348.

120. [1978] 1 Lloyd's Rep. 206.

121. Ibid., at p. 210. In The Chevalier Roze [1983] 2 Lloyd's Rep. 438, 443, Parker J., having referred to The Elbe Maru, respectfully doubted whether it was correct that P had done enough if he merely showed a possibility of prejudice. Where P was seeking to prevent D from asserting a possibly good claim, and where D had raised a triable issue which could not be determined without a further investigation of the facts, he found it difficult to see how it could be a fraud on P to allow D's action to proceed.

3.44 The device may be seen as an exception to the third party rule to the extent that the grant of a stay has the effect of enforcing the contract in favour of the third party. However, since it is the promisee who obtains the stay rather than the third party, the cases are better seen as examples of promisees assisting the third party to secure the promised benefit. As such, they are not inconsistent with the third party rule.

9. Statutory exceptions

3.45 This section will outline some of the major legislative exceptions[122] to the third party rule.

Price maintenance agreements[123]

3.46 By reason of the third party rule, a manufacturer or wholesaler who did not have a direct contract with the ultimate seller of goods could not enforce against him any condition as to the resale price of the goods contained in the original contract of supply.[124] The Restrictive Trade Practices Act 1956 circumvented the effect in such cases of

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122. It is also possible to create a ius quaesitum tertio under a contract by the operation of public law. Thus, where a statute empowered a regulatory body to make rules concerning liability insurance for a profession, and rules provided for a compulsory group scheme, individuals were able to sue on, and were subject to the duties of an assured under, the policy; Swain v. Law Society [1983] 1 A.C. 598.

123. Cheshire, Fifoot & Furmston, op. cit., pp. 466-468; Treitel, op. cit., pp. 568-569.

124. Taddy v. Sterious [1904] 1 Ch. 354; McGruther v. Pitcher [1904] 2 Ch. 306.

the third party rule by giving to suppliers of goods a right to enforce against any subsequent acquirer of those goods any condition as to their resale price which was contained in the original contract of sale, provided that the subsequent acquirer obtained the goods with notice of the condition.[125] The scope of this freedom has, however, been substantially limited by subsequent provisions[126] that prohibit the imposition of conditions as to minimum prices only in respect of goods in categories that have been exempted by the Restrictive Practices Court from the resale prices legislation; conditions as to maximum resale prices remain unaffected.

Insurance

Life Insurance

3.47 By section 11 of the Married Women's Property Act 1882, a policy of assurance effected by someone on his or her own life, and expressed to be for the benefit of his or her spouse or children, creates a trust in favour of the objects therein named. The Law Revision Committee recommended that section 11 of the 1882 Act should be

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125. Although the genesis of such a condition has to be in the original supply contract, the need to give notice of it to any subsequent acquirer means that in practice it is attached to, and in effect "runs with", the goods: see, for instance, the notice commonly included in books which are sold subject to the standard conditions approved under the net books agreement.

126. See now sections 14 & 26 of the Resale Prices Act 1976.

extended to all life, endowment and education policies in which a particular beneficiary is named.[127]

Fire Insurance

3.48 Under section 83 of the Fire Prevention (Metropolis) Act 1774, where an insured house or building is destroyed by fire, the insurer may be required "upon the request of any person or persons interested" to lay out the insurance money for the restoration of the building.[128]

Motor Insurance

3.49 Under section 148(7) of the Road Traffic Act 1988, a person issuing a policy under section 145 of the Act shall be liable to indemnify the persons or classes of person specified in the policy in respect of any liability which the policy purports to cover in the cases of such persons. In addition to any rights which an injured third party may have under the Third Parties (Rights Against Insurers) Act 1930,[129] victims of motor accidents caused by untraced or uninsured drivers may have rights under an agreement between the Motor Insurers' Bureau and the Secretary of State for the Environment. This agreement provides that the Bureau will pay any unsatisfied judgment in respect of any liability which is required to be covered by a policy of insurance. Although injured third parties could be met by the defence that they are not parties to the agreement, the

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127. 6th Interim Report, Cmd. 5449. See para. 4.30 ff below.

128. See Colinvaux's Law of Insurance (ed. Merkin) (6th ed., 1990), pp. 194-195.

129. See para. 3.50 below.

practice of the Motor Insurers' Bureau is not normally to rely on the third party rule.[130]

Third Parties' Rights against Insurers

3.50 A contract of insurance may insure the policy-holder against liability to third parties. By section 1 of the Third Parties (Rights Against Insurers) Act 1930, where an insured becomes, inter alia, bankrupt or wound up, if before or after that time he incurs liability to a third party, the insured's rights under the contract of insurance are transferred to the third party. In other words, the third party has a direct action against the insurer. However, the third party only has transferred to him the rights which the insured would have had. Difficulties have arisen where (a) the insured had no claim against the insurers until its own liability to the third party could be established, which itself was prevented by its own dissolution;[131] (b) the insured's right to recover against its insurer depended on a special "pay to be paid" provision, so that where the insured had not paid out before being wound up, there was no existing right to be indemnified from the insurer which could be transferred to the third party. In The Fanti & The Padre Island,[132] a shipowner had insured himself with a P. & I. club against liability to a third party for cargo claims. The third party had suffered cargo damage and obtained judgment for damages against the shipowner. However, in each case the shipowner was ordered to be wound up before settlement of the judgment

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130. Cf. Gardner v. Moore [1984] A.C. 548.

131. Bradley v. Eagle Star Insurance Co. Ltd. [1989] A.C. 957. But see now section 141 of the Companies Act 1989.

132. [1990] 3 W.L.R. 78.

debt. When each third party sought to recover his loss from the owners' P. & I. clubs, the clubs were able successfully to rely upon the "pay to be paid" provision in their rules, whereby payment of any liability to the third party was a condition precedent to the member's right to claim indemnity from the club. However, given the purpose of liability insurance, it is arguable that the scope of the 1930 Act should be extended to allow the third party to recover in these circumstances.[133]

Insurance by those with limited interests

3.51 In general, a person with a limited interest in property can insure and recover its full value, holding any amount above his own interest on account for others similarly interested.[134] Section 14(2) of the Marine Insurance Act 1906 states that a "mortgagee, consignee or other person having an interest in the subject-matter insured may insure on behalf and for the benefit of other persons interested as well as for his own benefit". Likewise, section 47 of the Law of Property Act 1925 provides that any insurance money received by the seller between contract and conveyance shall be held on behalf of the buyer and be paid to him.

Bills of exchange

3.52 In general, negotiable instruments (such as bills of exchange, cheques and promissory notes), are transferable

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133. See further paras. 4.22 and 5.38 below.

134. See Treitel, op. cit., p. 570.

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by delivery and give to the transferee for value, who acts in good faith, ownership of the instrument free from equities. Under the Bills of Exchange Act 1882,[135] the holder of a bill of exchange may sue on the bill in his own name. If a bill of exchange is dishonoured, the drawer, acceptor and indorsers are all liable to compensate the holder in due course.[136]

Bills of lading

3.53 Where goods are to be carried by sea, the shipper will typically enter into a contract of carriage with a carrier, which is evidenced by a bill of lading. The goods are then usually consigned to the buyer, to whom the bill will be indorsed. At common law the buyer was not able to sue the carrier on the contract of carriage, say for non-delivery or short-delivery, because he was not in privity with him.[137] It was to remedy this defect that the Bills of Lading Act 1855 was passed. Section 1 effects a statutory transfer of the shipper's rights and liabilities, vis-a-vis the carrier, to a named consignee or indorsee to whom property in the goods passes upon or by reason of the consignment or endorsement.[138] A pledgee of a bill of lading, to whom the full property in the goods does not pass, cannot sue under the 1855 Act.[139] However, where the

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135. Section 38(1).

136. Sections 54-56.

137. Thompson v. Dominy (1845) 14 M.& W. 403; 15 E.R. 532.

138. See Law Com. No. 196; Scot. Law Com. No. 130, "Rights of Suit in Respect of Carriage of Goods by Sea" (1991), for recommendations to reform the Bills of Lading Act 1855.

139. Sewell v. Burdick (1884) 10 App. Cas. 74.

pledgee takes delivery of the goods and pays any carriage charges such as freight or demurrage, there may come into existence an implied contract between the pledgee and the carrier on the terms of the bill of lading. Such a contract, known as a Brandt v. Liverpool contract,[140] is a further circumvention of the third party rule.

Section 56(1) of the Law of Property Act 1925

3.54 Whereas at common law, no person could sue on a deed inter partes unless he was a party to that deed, section 56(1) of the Law of Property Act 1925 states:

> "A person may take an immediate or other interest in land or other property, or the benefit of any condition, right of entry, covenant or agreement over or respecting land or other property, although he may not be named as a party to the conveyance or other instrument."

3.55 Although Denning L.J., in Drive Yourself Hire Co. (London) Ltd. v. Strutt,[141] took the view that this abolished the rule in Tweddle v. Atkinson, it is clear from Beswick v. Beswick[142] that section 56(1) does not apply to a mere promise by A to B that money will be paid to C. The exact scope of section 56(1) remains unclear. It may be confined (i) to real property; (ii) to covenants running with the land; (iii) to cases in which the instrument is not

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140. Brandt v. Liverpool, Brazil & River Plate Steam Navigation Co. Ltd. [1924] 1 K.B. 575; The Aramis [1989] 1 Lloyd's Rep. 213; The Captain Gregos (No. 2) [1990] 2 Lloyd's Rep. 395; The Gudermes [1991] 1 Lloyds Rep. 456.

141. [1954] 1 Q.B. 250, 274.

142. [1968] A.C. 58.

solely for the benefit of the third party but purports to contain a grant to or covenant with him; (iv) deeds strictly inter partes.[143] It does appear, however, that a person cannot take the benefit of a covenant under section 56(1) unless he or his predecessor in title was in existence and identifiable when the covenant was made.[144]

Section 14 of the Companies Act 1985

3.56 Under section 14 of the Companies Act 1985, the registered memorandum and articles of a company bind the company and its members to the same extent as if they respectively had been signed and sealed by each member.

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143. Chitty, op. cit., para. 1362.

144. Ibid.; Megarry & Wade, The Law of Real Property (5th ed., 1984), p. 764.

PART IV

THE CASE FOR REFORM

4.1 Having examined the meaning and development of the rule preventing people from suing on contracts to which they are strangers, and the exceptions to and circumventions of the rule, we turn to the case for reform. This rests on a number of considerations. First, the fact that the rule prevents effect being given to the intentions of the contracting parties has caused difficulties in practice. Secondly, the rule has led to unnecessary complexity and uncertainty in the law in view of the number of common law and statutory exceptions to it.[1] The technical hurdles which must be overcome if one is to circumvent the rule by drafting also lead to uncertainty since it will often be possible to raise plausible arguments that some requirement has not been satisfied. This uncertainty is commercially inconvenient and may lead to inefficient duplication of insurance cover.[2] The combination of the denial of rights to the third party and the rule that the promisee when suing can only recover for his own loss, and not that of another, may also lead to injustice. Finally, the justifications of the rule are unconvincing.

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1. For the status of existing statutory exceptions in the event of reform of the third party rule, see para. 5.38 below.

2. In the context of carriage of goods by sea, see, e.g. Palmer, op. cit., p. 1594.

4.2 We shall first assess the perceived merits of, and justifications for, the third party rule and then turn to an examination of the difficulties it has caused in practice in a number of contexts.

1. An overall assessment of the rule

4.3 The case for the third party rule rests on a number of factors:-[3]

(i) Although English law does not as a general rule permit the creation of contractual rights in third parties it does not prohibit the achievement of the same result in practice, providing that the appropriate drafting is used.[4]

(ii) Contracts are personal transactions whose ambit only extends to the contracting parties.

(iii) It is undesirable for the promisor to be liable to two actions from both the promisee and the third party.

(iv) It is unjust that a person could be treated as a party to a contract for the purpose of suing upon it when he could not be sued.

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3. See, for instance, Collins, The Law of Contract, (1986), pp. 106-108; Treitel, op. cit., pp. 527-528. See also Andrews, (1988) 8 L.S. 14, 16-17.

4. For instance, by the use of collateral contracts and the joint promisee principle: see paras. 3.22 and 3.33 above.

(v) Since a contract is of its nature a bargain, a third party cannot sue because he has not provided any consideration, i.e. he is getting something for nothing. If a promisee must furnish consideration, it would appear anomalous that a gratuitous third party beneficiary could be in a better position than a gratuitous promisee.

(vi) If third parties could enforce contracts made for their benefit, the rights of contracting parties to rescind or vary such contracts would be affected.

(vii) The third party rule imposes to limit on the potential liability of a contracting party to a wide range of possible third party plaintiffs.[5]

4.4 We do not regard any of the explanations outlined in paragraph 4.3 as convincing justifications of the rule.

(i) Whereas situations exist where properly advised parties can draft around the third party rule,[6] the reality is that laymen left to themselves may understandably fail to do so. Indeed, the rule has caused problems even where the parties have taken

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5. See Trident General Insurance Co. Ltd. v. McNiece Bros. Pty. Ltd. (1988) 62 A.L.J.R. 508, 514; Pearson, (1982) 5 Otago L. Rev. 316, 326. This is of particular significance in the context of public contracts, see paras. 2.19 above and 5.9 below.

6. For instance, in Tweddle v. Atkinson (1861) 1 B. & S. 393; 121 E.R. 762, the husband could have been made a joint promisee.

legal advice,[7] or have taken steps to draft around the third party rule.[8]

(ii) To say that third parties cannot sue because contracts are a personal affair between the contracting parties is simply a deduction from a proposition which itself requires justification. One such justification is the notion that contracts need an element of consent which is provided by making an offer or accepting one. It would follow that since a third party has, by definition, not made an offer or accepted one, and thus not consented, he should not obtain any contractual rights. However, presumably the purpose of requiring consent is the protection of personal autonomy. Allowing third parties to enforce contracts made for their benefit will not undermine this autonomy as only the question of giving third parties benefits (and not that of imposing burdens) is in issue. Furthermore, when both parties have agreed to benefit a third party, allowing the third party an enforceable claim gives effect to their intention and promotes the idea of agreement. Indeed, wider community interests in security of transactions are undermined when a bargain is disregarded.[9]

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7. As in Beswick v. Beswick [1968] A.C. 58 (see [1966] Ch. 538, 549) and Woodar Investment Development Ltd. v. Wimpey Construction (U.K.) Ltd. [1980] 1 W.L.R. 277.

8. Two visits to the Privy Council were necessary before the law was finally settled on the effect of Himalaya clauses in bills of lading: The Eurymedon [1975] A.C. 154 and The New York Star [1981] 1 W.L.R. 138, and para. 3.27 ff. above.

9. Catzman, [1975] L.S.U.C. Spec. Lect. 305, 307.

(iii) The argument that the promisor could be faced with actions from both the promisee and the third party can be addressed in several ways.[10] One answer is that there is only one promise which can give rise to only one cause of action. Once the promise is enforced, it is extinguished and the promisor will no longer be liable.

(iv) As for the argument that it is unfair that a person should be able to sue when he cannot be sued, this should not in fact be an impediment to enforceability since unilateral contracts in which only one person is obliged to perform are enforceable.[11] Furthermore, even if the third party is immune from reciprocal suit by the promisor, the promisor's interests are protected by having a claim against the promisee.[12]

(v) To say that a third party cannot sue because he is not a party to a bargain is to confuse two issues. Whereas the third party rule relates to the question who may enforce a contract, the doctrine of consideration decides which promises may be enforced.[13] Where consideration has been furnished, albeit by the promisee and not the third party, there is a bargain and the promisor's promise has been "paid for" albeit not by the third

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10. See para. 5.34 below.

11. Treitel, op. cit., pp. 36, 528.

12. Beyleveld & Brownsword, (1991) 54 M.L.R. 48, 61.

13. See paras 2.5-2.9 above.

party. This explains the apparent anomaly that the gratuitous third party has rights which the gratuitous promisee does not have. The gratuitous third party has rights under a valid contract, whereas in the case of the gratuitous promisee there is, ex hypothesi, no valid contract.

(vi) & (vii) It is true that reform of the third party rule might prejudice the rights of the contracting parties to vary or rescind the contract, and would expose the promisor to a wider range of possible third party plaintiffs. These are issues which must be considered, but which do not necessarily preclude reform. It is possible to have a reform which respects the rights of the contracting parties even though third parties are given enforceable rights.[14] Similarly, a sufficiently circumscribed test of who is a third party beneficiary will prevent a flood of litigation.

4.5 Although the development of English contract law has been pragmatic and not the outcome of one particular theory, it appears that the third party rule is not a necessary part of any of the supposed theoretical foundations of contractual liability.

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14. See paras. 5.27 ff. below.

(a) According to the "will" theory of contract, liability is based on a person's intention, will or promise,[15] such that the law of contract is designed to give effect to the intentions of the parties, regardless of any element of benefit or detrimental reliance. It would not appear that the will theory requires the third party rule, particularly where it is the manifest intention of both parties that a third party should have enforceable rights.[16]

(b) According to the "bargain" theory of contract, the courts only enforce agreements where there has been an exchange of, or a promise to exchange, value. However, even where the third party is not a party to the bargain, and yet where value has been exchanged between the parties on the basis that the third party is to have enforceable rights, the bargain may be defeated if the third party does not in fact have such rights.

(c) Whether or not the law of contract has as its main purpose the protection of expectations reasonably created, or the protection of reliance reasonably incurred, it would not appear that the third party rule is required. A contract made between A and B for the benefit of C may create a reasonable expectation in C that it will be performed. Likewise, C may act in

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15. Atiyah, The Rise and Fall of Freedom of Contract, (1979), pp. 212-216; Fried, Contract as Promise (1981), pp 18-19.

16. In Tweddle v. Atkinson (1861) 1 B.& S. 393; 121 E.R. 762, the agreement expressly stated that the third party would be able to enforce it in any Court of Law or Equity.

reliance on this. On either theory, C should have a legal right to enforce performance.[17]

4.6 In many commercial situations there exists a complex pattern of relationships, from which it may be difficult to discern the traditional requirements of offer, acceptance and consideration.[18] In these situations, paradigm examples of which are building and carriage contracts considered below, it may be contrary to the commercial reality of the situation to preclude a third party, who is in a continuing relationship with the parties to a contract, from enforcing rights under it which are given for his benefit. It has been suggested that within a "network" of linked commercial contracts, that is to say a group of contracts which have collectively as their object the attainment of a common underlying purpose, the doctrine should have no application.[19]

4.7 We now turn to the difficulties in practice caused by the third party rule. These have been particularly acute in a number of contexts which are considered below, in some of which it is clear, or at least arguable, that the

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17. Of course, the choice of theory will affect the circumstances in which C would be accorded a legal right to enforce performance. On a reliance theory, he would not have any right until he actually acted in reliance, whereas under an expectation theory no such reliance would be necessary.

18. See The Eurymedon [1975] A.C. 154, 167.

19. Adams and Brownsword, (1990) 10 L.S. 12; Beyleveld & Brownsword, (1991) 54 M.L.R. 48, 67-68.

contract is intended to benefit the third party. Some of the difficulties have been addressed by the various conceptual techniques which the law has devised by way of exception to, or circumvention of, the third party rule and which have been examined in Part III. However, we have seen the limits of those techniques. Where they cannot be used the tensions between the interests of the third party and the contracting parties or possibly outsiders such as the creditors of the promisee have led to the development of fine and sometimes unhappy distinctions.[20]

2. Shipping

4.8 In this area of the law the problems are twofold: those involving third parties attempting to sue on contracts to which they are not a party,[21] and those involving third parties attempting to rely on defences and immunities in contracts to which they are not a party.[22]

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20. For instance, see the distinction drawn in Re Stapleton-Bretherton [1941] Ch. 482 and Re Schebsman [1944] Ch 83 between cases where the promisor is said to have no interest in the identity of the payee and where the promisee (or his trustee in bankruptcy) can therefore direct to whom payment is to be made and cases where such an interest is said to exist and the promisee (or his trustee in bankruptcy) cannot divert the money from the third party.

21. e.g. Leigh & Sillivan Ltd. v. Aliakmon Shipping Co. (The Aliakmon) [1986] A.C. 785; The Aramis [1989] 1 Lloyd's Rep. 213.

22. e.g. Elder, Dempster & Co. Ltd. v. Paterson, Zochonis & Co. Ltd. [1924] A.C. 522; The Eurymedon [1975] A.C. 154.

4.9 The most serious problem of a third party being unable to sue at common law was the inability of the marine cargo buyer to sue a sea carrier for loss, damage and so forth in those cases where the buyer was not privy to the contract of carriage. The Bills of Lading Act 1855 solved the problem so far as concerned consignees named in, and indorsees of, bills of lading who became the owner of goods upon or by reason of the consignment or indorsement. However, the Act has proved to be of no avail in those cases where the buyer either does not become the owner of the goods or becomes the owner of the goods before, after or independently of the consignment or indorsement.[23] Equally, the Act is of no avail where documents other than bills of lading (for instance sea waybills and ship's delivery orders) are issued by the carrier. The Law Commissions have recently recommended the enactment of legislation which accords rights of action in these cases.[24]

4.10 As for actions against third parties who wish to rely on defences and immunities in contracts to which they are not a party, one aspect of this problem is associated with "Himalaya" clauses which are designed to extend to servants, agents and sub-contractors the protections of the main contract. The problem has been

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23. See Reynolds, (1990) 106 L.Q.R. 1.

24. Rights of Suit in Respect of Carriage of Goods by Sea (1991), Law Com. No. 196; Scot. Law Com. No. 130. See para. 5.38 below on how these proposals would stand in the event of a reform of the third party rule. In the United States, there are detailed statutory provisions on bills of lading (contained in the Federal Bills of Lading Act 1916) in addition to the general law on third party beneficiaries.

resolved as a result of The Eurymedon,[25] and The New York Star,[26] although, as we have seen in Part III above, the reasoning is complicated, involving as it does an implied contract between shipper and stevedore made through the agency of the carrier which becomes binding on the ultimate buyer by reason of another implied contract when he presents the bill of lading and takes delivery.[27] In International Technical Operators Ltd. v. Miida Electronics Inc.[28] it was suggested in the Supreme Court of Canada that reform of the third party rule was a preferable solution to the problem of third party reliance on contractual defences and immunities than the implied contract analysis.

4.11 Another example of third parties seeking to rely on contracts to which they are not privy is that of the shipowner seeking to rely on exemptions contained in a bill of lading issued by a charterer. The reasoning in Elder Dempster allows the shipowner to do so, although we have seen that the House of Lords had conceptual difficulties justifying the result.[29] In addition, the use of a demise clause in bills of lading issued by charterers enables the

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25. [1975] A.C. 154.

26. [1981] 1 W.L.R. 138.

27. It is also conceivable that an attack could be made on the second stage of the reasoning given the strictures put on the implication of Brandt v. Liverpool contracts in The Aramis [1989] 1 Lloyd's Rep. 213, though cf. The Captain Gregos (No. 2) [1990] 2 Lloyd's Rep. 395 and The Gudermes [1991] 1 Lloyd's Rep. 456.

28. (1986) 28 D.L.R. (4d) 641, 666-667 (per McIntyre J).

29. At para. 3.24 above.

contract of carriage to take effect as between shipper and shipowner (or demise charterer) rather than the person issuing the bill,[30] although its use has been criticised by some writers and may be invalid in some jurisdictions.[31]

3. Construction

4.12 Building and engineering projects typically involve a number of different contracts between the developer, architects, the head contractor, sub-contractors and financiers. In view of the third party rule, those not privy to a particular contract have not been able to rely on its provisions either to found a contractual action or as providing a defence. Recourse has been had to the law of tort. A case which has attracted much comment is Junior Books Co. Ltd. v. Veitchi Ltd.,[32] where the House of Lords held that a building owner was able to sue a sub-contractor in tort for economic loss occasioned by the latter's negligence.

4.13 However, in D & F Estates Ltd. v. Church Commissioners for England,[33] it was held that a builder was

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30. See, for example, The Jalamohan [1988] 1 Lloyd's Rep. 443; Roskill, "The Demise Clause" (1990) 106 L.Q.R. 403.

31. Tetley, Marine Cargo Claims (3rd ed., 1988) pp. 248 ff; Reynolds, [1990] L.M.C.L.Q. 494.

32. [1983] 1 A.C. 520, although, see para. 3.10 above, it was a Scots case and Scots law accepts in principle the existence of a ius quaesitum tertio; Appendix, para. 22.

33. [1989] A.C. 177.

not liable in tort to a subsequent purchaser in respect of the cost of repair of defects in the quality of the building. A builder, in the absence of a contractual duty or a special relationship of proximity sufficiently akin to contract[34] to introduce the element of reliance such that the owner owes a duty to prevent economic loss,[35] owes no duty of care in tort in respect of the quality of his work. This was followed in Murphy v. Brentwood D.C.,[36] where it was additionally held that the liability of a local authority, which negligently failed to ensure that the builder complied with building by-laws and regulations, did not exceed that of the builder.

4.14 As a result of cases such as Murphy and D & F Estates, third parties (such as property financiers, purchasers and tenants) frequently seek to protect themselves by means of collateral warranties made with the developer, contractor, sub-contractors and professionals such as architects, surveyors and structural engineers. In

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34. If in Junior Books the relationship of owner and sub-contractor was as close as it could have been short of actual privity of contract, in Greater Nottingham Co-operative Society Ltd. v. Cementation Piling & Foundations Ltd. [1989] Q.B. 71, there was actual privity of contract. However, the contract only imposed on the sub-contractor a duty to exercise due skill and care in the design of the contract works, not their actual execution. There was thus no breach of the collateral contract, and no wider duty in tort. If the collateral contract had imposed on the sub-contractor a duty to carry out the works with due care, the sub-contractor would have been liable for economic loss caused by the breach of contract.

35. The only ground on which Hedley Byrne and Junior Books are explicable.

36. [1991] 1 A.C. 398. See Fleming, (1990) 106 L.Q.R. 525;

the case of an average shopping centre, one professional may be expected to enter into separate warranty transactions with the financiers, the purchaser and 50 or more tenants.[37] One possible effect of any reform could be to reduce the present complexity by removing the need for so many separate documents. If the contract between developer and contractor were expressed to be for the benefit of financiers, purchasers and tenants alike, it could remove the need for collateral warranties.

4. Liability from the making of statements

4.15 There have been a number of misstatement cases which could be susceptible of a contractual solution if the third party rule were reformed. In Candler v. Crane, Christmas & Co.,[38] accountants had agreed to prepare accounts for a company and had been authorised to discuss them with P, a potential investor. The accounts were inaccurate and P, who invested in the company in reliance on them suffered loss. In Smith v. Eric S. Bush (a firm) and Harris v. Wyre Forest D.C.,[39] PP bought houses in reliance on negligent valuations made by surveyors acting for

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36. Continued
Cooke, (1991) 107 L.Q.R. 46; Wallace, (1991) 107 L.Q.R. 228; Cane, Tort Law and Economic Interests (1991), pp. 511-518.

37. Bates, (1990) E.G. October 13, p. 57, 58.

38. [1951] 2 K.B. 164. See also Caparo Industries plc v. Dickman [1990] 2 A.C. 605.

39. [1990] 1 A.C. 831.

mortgagee lenders, suffering financial loss when the true state of the houses became apparent.

4.16 In these cases, the person giving the advice pursuant to a contract knew that the advice (which was required for a purpose, whether particularly specified or generally described) would be communicated to P, that P was contemplating a particular transaction or a transaction of a particular kind, that it was very likely that P would rely on that advice in deciding to go ahead with the transaction and in fact it was acted upon to his detriment.[40] Before Hedley Byrne Co. Ltd. v. Heller & Partners Ltd.,[41] there was neither a contractual nor a tortious basis for a claim by P but it is arguable that the contracts made by the accountants (Candler) and surveyors (Smith v. Bush) were for the benefit of the potential investor and the mortgagor borrowers respectively in one of the senses used above.[42] These cases involve what would be characterised in Germany as contracts with protective effects vis-a-vis third parties.[43] Under a reform of the third party rule, P could in principle sue as a third party beneficiary.[44] The crucial factor will be construction of the contract, in particular

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40. Caparo Industries plc v. Dickman [1990] 2 A.C. 605, 638.

41. [1964] A.C. 465 (not susceptible of a contractual solution since the defendant bank's statement on the financial stability of its customer made to the plaintiff's bank was not made pursuant to a contract).

42. At para 2.18.

43. See Appendix, para. 29.

44. See Lorenz, "Some thoughts about contract and tort", in Essays in Memory of Professor F.H. Lawson (1986), p. 86.

whether the parties intended the third party to have enforceable rights and whether the benefit to the third party was intended or incidental.

4.17 However, it is arguable that reform of the third party rule will have little effect on the present law on misstatements. Several factors are likely to be important in deciding whether a tortious duty of care exists: (i) the purposes for which the statement was made and communicated; (ii) the relationship between the maker of the statement, the person relying on it and anyone to whom it was originally intended to be communicated; (iii) the size of the class to which the person relying on it belongs; (iv) whether the maker knew or ought to have known that the advice would be relied upon by a particular person or class of persons; (v) whether P actually relied on the statement, whether he was entitled so to rely and whether he should have sought independent advice.[45]

4.18 Whereas tortious liability for economic loss caused by misstatements is more likely to be found where there is a relationship "equivalent" or "akin" to contract,[46] it is

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45. James McNaughton Paper Group Ltd. v. Hicks, Anderson & Co. [1991] 2 Q.B. 113, where P unsuccessfully sued D, the accountants of a company which was taken over by P in reliance on the accounts. Among the factors militating against a duty of care were: (i) the accounts were not final; (ii) they disclosed that the company was performing badly; (iii) it was to be anticipated that P would have access to and consult with his own advisers.

46. Hedley Byrne v. Heller [1964] A.C. 465, 530 per Lord Devlin; Smith v. Eric S. Bush (a firm) [1990] 1 A.C. 831.

doubtful whether cases such as Candler and Smith v. Eric S. Bush (a firm) would be decided differently under the approach which, subject to consultation, we are inclined to favour since this posits the agreement of the promisor to be bound to the third party.[47] The surveyor in the latter case did not agree and would not have agreed without an extra fee, such that an agreement could hardly be implied. Nevertheless, liability was imposed in tort because it was thought just and reasonable, no doubt partly because the relationship between the promisor and the third party was akin to contract. As under the present law, it is likely that different factual situations will call for different solutions. Caparo Industries plc v. Dickman[48] and Smith v. Eric S. Bush (a firm) were decided differently either because of the different economic relationships between the parties and the difference in the nature of the markets in which they were operating[49] or because of the differences in the knowledge and intentions of the party making the misstatement.[50] The extent to which defendants who are at present not liable in tort will be subjected to liability

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47. See paras. 5.8 ff and 6.3 below.

48. [1990] 2 A.C. 605. P made a successful take-over bid for a company after its directors publicised accounts which had been audited by DD, which accounts were allegedly inaccurate and which led to financial loss by P. It was held that the auditor owed no duty of care to potential investors, whether shareholders or members of the public who relied on the accounts to buy shares, since the purpose of the auditing was to provide an account of the stewardship of the directors to the shareholders, rather than to enable individual shareholders to make investment decisions with a view to profit.

49. Morgan Crucible Co. plc. v. Hill Samuel & Co. Ltd. [1991] Ch. 295, 303-305 per Hoffmann J.; Fleming (1990) 106 L.Q.R. 349, 350.

50. Morgan Crucible Co. plc. v. Hill Samuel & Co. Ltd. [1991] Ch. 295, 318-319, 320-321 per Slade L.J.

will depend on which test of enforceable benefit is adopted.[51] On the approach that, subject to consultation, we provisionally recommend, it seems doubtful whether the recognition of the right of third parties to sue on contracts made for their benefit would allow a significant number of misstatement claims by third parties which are not already caught under the law of negligence.

5. Sale of Goods

4.19 There were formerly two common situations in which the third party rule restricted those who had suffered damage due to the sale of defective goods from recovering for that damage. The first was when the victim was the purchaser from a retailer or other intermediary, and the rule prevented him from suing the manufacturer. The second was where another party had bought the goods for the victim's use. Since no contract existed in the first case between victim and manufacturer and in the second between victim and seller, the victim, in the absence of negligence by the manufacturer or seller respectively, had no remedy.[52] These injustices have been remedied, to some extent, by Part 1 of the Consumer Protection Act 1987. Manufacturers and suppliers are now strictly liable for damage caused by defects in their products. The statutory definition of damage in section 5, however, is limited to death, personal

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51. See para. 5.8 below.

52. Cf. the position in some of the United States of America, where third parties may sue manufacturers on an implied statutory warranty of merchantability: see, for instance, Henningsen v. Bloomfield Motors Inc. 161 A. 2d. 69 (1960), and Benjamin, op. cit., para. 1046.

injury or damage to other property. There is no provision for economic loss, which means that the third party rule is still capable of causing difficulties.

4.20 In Simaan General Contracting Co. v Pilkington Glass Ltd. (No.2),[53] a sheikh wished to have a building constructed and contracted with P to build it. He wanted the glass in the building to be a uniform shade of green. P approached Y, experts in glazing, and Y ordered green glass by sample from D, a glass manufacturer. P contracted with Y to fit the glass, which did not come up to standard: there were different shades of green and parts of the glass looked red. The sheikh withheld payment from P until the glass was replaced. P suffered considerable economic loss and sued D in tort. However, since this was pure economic loss, P was unable to recover by means of a direct action in tort.

4.21 The third party rule prevents a direct action in contract by P against D, which may lead to unsatisfactory results: for instance on the facts of Simaan, if Y, the contracting company, had in the meantime been dissolved, P may have been without any remedy. There may be further reasons why it is desirable for D to be liable to P. D is in a position to exercise quality control and may be better able than Y to cover the risk by insurance. It is arguably preferable to deal with the matter in one action rather than two or more indirect actions, which is more cumbersome although reflecting the contractual obligations undertaken by the various parties in the chain. However, it is

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53. [1988] Q.B. 758.

debatable whether the contract between D and Y could be characterised as for the benefit of P. Although this contract may have been made for the purpose of fulfilling Y's contract with P, it is another matter to say that D and Y intended that P should have an enforceable right of action in respect of any breach of their contract.

6. Insurance

4.22 In a number of situations where insurance policies are taken out for the benefit of third parties, they are still technically unenforceable by those parties, as when employers take out insurance for their employees or where retailers insure against their liability to consumers.[54] Particular problems may be faced when the insured is insolvent. Under the Third Parties (Rights Against Insurers) Act 1930, a third party may have a direct action against an insurer by virtue of the insured's rights under the contract of insurance being transferred to him. However, we have seen that the Act has not been without its problems.[55]

7. Contracts to pay money to a third party

4.23 The cases which have, over recent years, attracted the strongest criticism of the third party rule from the House of Lords involved simple arrangements between

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54. Green v. Russell [1959] 2 Q.B. 226; Atiyah, An Introduction to the Law of Contract (4th ed., 1989), p. 384.

55. See para. 3.50 above and para. 5.38 below.

A and B to pay money to C. In Beswick v. Beswick,[56] a nephew promised his uncle to pay £5 per week to his aunt after the uncle's death, in return for which the uncle sold his business to the nephew. In Woodar Investment Development Ltd. v. Wimpey Construction U.K. Ltd.,[57] D agreed to buy land from P, part of the purchase price to be paid to a third party. In Beswick, when the nephew stopped the payments, the aunt sought an order of specific performance in her personal capacity and as administratrix of her husband's estate. The House of Lords refused to allow the claim in her own right, but granted her the order in her capacity as administratrix. There was therefore no actual hardship, but only because the promisee (in the guise of his administratrix) was willing to bring an action, and indeed because the promise was susceptible to an order for specific performance. Where specific performance is not available, and where the promisee is dead and in the absence of the coincidence that the beneficiary is also the executor or administratrix, the third party rule may prevent justice being done. On the other hand, the facts of Beswick do not, perhaps, provide the strongest case for reform since it would have been possible for the agreement to have been drafted so as to have given the aunt an enforceable right. In Woodar, the question of the third party's right to sue (or the promisee's right to recover on his behalf) did not arise before the House of Lords.

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56. [1968] A.C. 58.

57. [1980] 1 W.L.R. 277.

4.24 In Coulls v. Bagot's Executor & Trustee Co. Ltd.,[58] a written agreement was made whereby Mr. Coulls granted to a company the right to quarry and remove stone from land belonging to him. The final clause of the document read: "I authorise the above company to pay all money connected with this agreement to my wife ... and myself ... as joint tenants." The signatories were Mr. Coulls, his wife and the company. In the administration of the deceased's estate, the High Court of Australia held by a majority that, after the death of Mr. Coulls, the company was bound to pay the royalties to the deceased's executors as part of his estate since there was no promise by the company to the husband to pay the wife, but merely a mandate allowing the company to pay the wife, a mandate which was revoked on the death of the husband. Thus, the wife had no rights as she was not a party to the contract, albeit a signatory to it. It is arguable that the intentions of the signatories were defeated by the third party rule, although on the basis of the court's construction of the document no question arose on the issue of third party rights.

8. Wills

4.25 One area where the inability of third parties to sue in contract has been ameliorated by actions in tort for pure economic loss is that of improperly executed wills. In Ross v. Caunters,[59] where a prospective beneficiary was deprived of an intended benefit, he was able to recover in

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58. [1967] A.L.R. 385.

59. [1980] Ch. 297. See also Re Wilson's Settlements [1972] N.Z.L.R. 13.

tort against the negligent solicitor. We have seen that this is a controversial area,[60] and one on which we seek views on how best it can, if at all, be dealt with in the event of any reform of the third party rule.[61]

9. Contractual Licences

4.26 In Binions v. Evans,[62] a landowner allowed a third party to occupy his land under a contractual licence. He subsequently sold the land to a buyer who promised not to disturb the third party. It was held that the third party had a defence to an ejectment action based on the promise between the landowner and the buyer.[63] Although this was effectively a contract for the benefit of a third party, the third party rule meant that there were theoretical difficulties in justifying the end result. Both the constructive trust mechanism adopted by Lord Denning M.R., and the Settled Land Act settlement found by the majority of the Court of Appeal, are not without their difficulties.[64]

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60. See paras. 3.12-3.17 above.

61. See para. 5.40 below.

62. [1972] Ch. 359; Birks, (1975) 1 Poly L.R. 39.

63. See also DHN Food Distributors Ltd. v. London Borough of Tower Hamlets [1976] 1 W.L.R. 852; Re Sharpe [1980] 1 W.L.R. 219; Lyus v. Prowsa Developments Ltd. [1982] 1 W.L.R. 1044.

64. Baker, (1972) 88 L.Q.R. 336; Oakley, (1972) 35 M.L.R. 551.

10. Limits on the ability of the promisee to assist the third party

4.27 The case for reform is also supported by a number of difficulties in practice which are caused by a combination of the third party rule and the rule that remedies for breach of contract are intended to compensate the loss suffered by the promisee, not that suffered by a third party. Thus, even if the promisee is willing to enforce a contract made for the benefit of a third party, we have seen that his own loss will attract only nominal damages.[65] If, of course, the contract is susceptible to the equitable remedy of specific performance, as in Beswick v. Beswick, the third party will be no worse off for the fact that he himself has had no right to sue.

4.28 It could, therefore, be suggested that reform of the law of remedies would be sufficient to prevent injustice caused by the third party rule. This could take the form of increasing the ambit of specific performance. However, this may be unsatisfactory since there are good reasons why a number of categories of contract should generally not be specifically enforced, such as those involving personal service and those requiring constant supervision. The promisee could also be allowed to recover the third party's loss in damages. As was recognised in Woodar Investment Development Ltd. v. Wimpey Construction (U.K.) Ltd.,[66] promisees can already recover in certain special situations, such as the booking of family holidays or the ordering of

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65. See para. 3.39 ff. above.

66. [1980] 1 W.L.R. 277.

meals in restaurants.[67] On facts such as those in Beswick and Woodar an alternative solution would be to give the promisee the right to sue for the agreed sum.

4.29 However, we believe that reform of the law of remedies is not the way forward in the present context. In almost every area of the law, there are likely to be cases where the promisee would refuse to enforce the contract. For instance, in Beswick v. Beswick,[68] what if the uncle had made his nephew the administrator of his estate? It is arguable that the directors of the selling company in The Aliakmon[69] would have been in breach of their fiduciary duties to the shareholders if they began to litigate on behalf of the buyers, with whom they had no other relationship than the trade which passed between them. Further, reform of remedies would not help stevedoring firms who are seeking to rely on exemption clauses contained in contracts to which they are not parties. Such firms are necessarily litigating themselves since they are being sued and are purporting to rely on the contract made for their benefit as a defence.[70] We believe that a simple reform of

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67. See also Jackson v. Horizon Holidays Ltd. [1975] 1 W.L.R. 1468, para 3.40 above.

68. [1968] A.C. 58.

69. [1986] A.C. 785.

70. This problem may best be solved by the carrier procuring a promise from holders of bills of lading not to sue stevedores, such that any action could be stayed on the principles laid down in Gore v. Van der Lann [1967] 2 Q.B. 31: Reynolds, (1974) 90 L.Q.R. 301, 304, and paras. 3.41-3.44 above.

the remedy rule would be an inadequate substitute for reform of the third party rule.

11. The Report of the Law Revision Committee

4.30 In its Sixth Interim Report,[71] the Law Revision Committee took the view that the case for reform of the third party rule had been made out, recommending "... that where a contract by its express terms purports to confer a benefit directly on a third party, the third party shall be entitled to enforce the provision in his own name, provided that the promisor shall be entitled to raise as against the third party any defence that would have been valid against the promisee. The rights of the third party shall be subject to cancellation of the contract by the mutual consent of the contracting parties at any time before the third party has adopted it either expressly or by conduct."[72]

4.31 The Committee indicated that this recommendation alone would not have gone far enough to cover the situation which arose in Re Engelbach's Estate,[73] where a father took out an insurance policy which he wished to be for his daughter's benefit, but failed to say so expressly in the policy, with the result that the policy monies went to his estate and not to the daughter. The Committee therefore

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71. (1937), Cmd. 5449.

72. Para. 48. The Law Revision Committee's proposals were supported by the Law Commission of India: Indian Law Com. No. 13.

73. [1924] 2 Ch. 348.

further recommended[74] that the provisions of section 11 of the Married Women's Property Act 1882 be extended to all life, endowment and education policies in which a particular beneficiary is named.

4.32 Although these recommendations proved influential in several Commonwealth jurisdictions which subsequently reformed the third party rule,[75] they have not entirely escaped criticism.[76] First, a third party would only acquire an enforceable right if the contract contained an express provision to that effect. However, the third party question may arise under contracts which have been made without legal advice and which are therefore unlikely to contain an express third party clause. Secondly, although the proposal allows the promisor any defence against the third party which he would have had against the promisee, a court might find it unsatisfactory, without more, to determine the liability of the promisee in his absence. It has been suggested[77] that the solution is to require the third party to join the promisee in any action. Thirdly, the concept of "adopting" a contract may be said to lack precision. Finally, it has been said that there are cases in which it is arguable that the third party's rights should not be subject to the contracting parties' right of cancellation.[78]

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74. Para. 49.

75. For instance, section 11 of the Western Australia Property Law Act 1969, and section 55 of the Queensland Property Law Act 1974: see Appendix.

76. Myers, (1953) 27 A.L.J. 175, 177 ff.

77. Ibid., p. 178.

78. Treitel, op. cit. p. 575.

These issues will be discussed in our provisional recommendations in Part V below.

12. Contracts burdening third parties

4.33 This consultation paper is directed to the question of contracts for the benefit of third parties, rather than the other basic aspect of privity of contract, viz. that as a general rule contracting parties cannot impose duties on third parties. These two aspects of the privity rule involve different policy considerations. Whereas we have seen that the general rule preventing third parties from enforcing contracts made for their benefit is difficult to justify, the general rule prohibiting the imposition of duties on strangers to a contract is self evidently desirable: for two people, without more, to be able to impose contractual duties on a third party offends elementary principles of justice. This is not to say that a person can never be burdened by the terms of a contract to which he is a stranger. There are cases in which a third party may be enjoined from acting in a fashion which prevents a contract to which he is not a party from being performed.[79] In Lord Strathcona S.S. Co. v. Dominion Coal Co.,[80] B, a shipowner, time chartered his vessel to A and thereafter sold it to C. It was held that C, who bought with notice of A's rights

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79. Lumley v. Gye (1853) 2 E. & B. 216. See further Treitel, op. cit., pp. 545-550; Cheshire, Fifoot & Furmston, op. cit., pp. 461-466; Gardner, (1982) 98 L.Q.R. 279; Tettenborn, (1982) 41 C.L.J. 58. See also para. 5.36 below.

80. [1926] A.C. 108, following De Mattos v. Gibson (1858) 4 De G. & J. 276. See also Swiss Bank Corp. v. Lloyd's Bank Ltd. [1979] Ch. 548; [1982] A.C. 584.

under the charterparty, could be restrained from dealing with the ship otherwise than in accordance with the charterparty. The approach in Strathcona has, however, been criticised.[81] The decision proceeded on the basis that C was in the same position as if he had bought land with notice that it was affected by a restrictive covenant. However, this is open to question since it is doubtful whether A could be said to have a proprietary interest in the subject matter of the contract. However, even if the restrictive covenant analogy is false the decision may be justifiable on other grounds. Thus, it has been suggested that the relevant analogy is with the tort of inducing breach of contract.[82] Furthermore, in similar situations, where the original contract between A and B is specifically enforceable, it is possible that A's equitable interest in its subject matter will suffice to justify enforcing C.[83]

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81. In Port Line Ltd. v. Ben Line Steamers Ltd. [1958] 2 Q.B. 146, Diplock J. refused to follow Strathcona (a Privy Council case) as being wrongly decided, holding in the alternative that it was confined to cases where C had actual notice of the charterparty terms. On this analysis, the charterer's remedy would lie primarily against the shipowner with whom he contracted, rather than the third party buyer. Scrutton on Charterparties (19th ed., 1984), p. 24, also takes the view that Strathcona was wrongly decided.

82. Swiss Bank Corp. v. Lloyd's Bank Ltd. [1979] Ch. 548, 575.

83. Cheshire, Fifoot and Furmston, op. cit., p. 465; Treitel, op. cit., pp. 546, 549-550.

D

Summary

4.34 By way of a summary of the case for reform, we would stress the following considerations:

(i) The rule is a comparatively modern development in English law, the juridical basis of which is obscure.[84]

(ii) The present law causes hardship and defeats the intentions of parties to a contract who wish to benefit a third party. Although many difficulties have been addressed by improving the remedies available to the promisee, by the implication of collateral contracts and by the recognition of exceptions to the rule, these techniques have their limits and areas remain which have not been protected from the rule in these ways.

(iii) The present law is unsatisfactory in that many of the exceptions have been created on an ad hoc basis with little thought for the overall development of the law. Moreover, some of the techniques for circumvention are artificial and subject to limits which are not obviously related to wider policy considerations. The overall effect is a complex and unduly technical body of law. The number of common law and statutory exceptions to the rule and methods found to circumvent it shows how unfair or inconvenient the third party rule can be and also judicial and legislative unease with the policy which it embodies.

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84. However, under Roman law there was no general doctrine of ius quaesitum tertio, nor was there any relief afforded by a doctrine of agency: see Nicholas, An Introduction to Roman Law (1962), p. 199 ff; Buckland and McNair, Roman Law and Common Law (2nd ed., 1965), p. 214 ff.

(iv) Over 50 years ago, the Law Revision Committee recommended the abolition of the third party rule in a report which was welcomed by judges and a wide range of commentators and which has influenced developments in some other common law jurisdictions. Nothing has happened since the Law Revision Committee's Report to suggest that its recommendations were misguided. Indeed, the greater complexity of the law as further exceptions and circumventions have developed, and the experience of statutory reform elsewhere,[85] reinforce its conclusions.

(v) The House of Lords has, on more than one occasion, indicated that there ought to be reconsideration of the rule.[86] There have also been several judicial statements to the effect that if there is to be a radical change in the common law, such as reform of the third party rule, it should come from the legislature rather than the judiciary.[87] We agree with this view. The rule is sufficiently established and involves such complex issues that, if there is to be reform, it should be by means of legislation.[88]

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85. See Appendix.

86. See para. 1.2 above. The more recent pronouncements of the House of Lords, in such cases as Murphy v. Brentwood D.C. [1991] 1 A.C. 398, on the question of the boundaries of judicial development of doctrine, also point to legislative rather than judicial reform as the way forward.

87. Midland Silicones Ltd. v. Scruttons Ltd. [1962] A.C. 446, 467-468, per Viscount Simonds; Trident General Insurance Co. Ltd. v. McNiece Bros. Pty. Ltd. (1988) 62 A.L.J.R. 508, 520, 532 per Brennan & Dawson JJ.

88. See also Reynolds, (1989) 105 L.Q.R. 1, 3-4, commenting on the variety of approaches and the number of issues left unresolved by the High Court of Australia in

4.35 The case against reform[89] is essentially based on three considerations:

(i) that existing techniques are adequate to deal with most practical problems;

(ii) that there are few actual cases of injustice, given that it is permissible to draft around the rule;

(iii) that the complexity of any reform may create as many problems as it solves.[90]

4.36 We invite comments on the question whether there should be reform of the third party rule. For the reasons summarised in para. 4.34 above, it is our provisional conclusion there should be reform of the rule. In the next part of the paper, we discuss the main issues which will need to be examined in any reform.

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88. Continued
Trident General Insurance Co. Ltd. v. McNiece Bros. Pty. Ltd. (1988) 62 A.L.J.R. 508: see Appendix, para. 6.

89. See also para. 4.3 above.

90. In Trident General Insurance Co. Ltd. v. McNiece Bros. Pty. Ltd. (1988) 62 A.L.J.R. 508, 520, Brennan J. said: "The field of ius quaesitum tertio may look greener, but the brambles are no fewer".

PART V

THE MAIN ISSUES EXAMINED

1. Scope of legislation

5.1 In the light of our provisional recommendation that there should be legislative reform of the third party rule, there are several possible options:

(a) Further exceptions to the third party rule could be made in specific instances.

(b) The rule preventing the promisee from recovering the third party's loss could be reformed.

(c) There could be a provision that no third party be denied enforcement of a contract made for his benefit on the grounds of lack of privity.

(d) The law could be reformed by means of a detailed legislative scheme.

It would also be possible to combine some of these possibilities, for instance, (a) and (c).

5.2 **Further exceptions could be made in specific instances.** The Law Commissions have proposed an extension of third party rights in cases involving contracts for the carriage of goods by sea.[1] Further reform might be by

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1. Rights of Suit in Respect of Carriage of Goods by Sea (1991), Law Com. No. 196; Scot. Law Com. No. 130.

specific and detailed proposals tied to particular contexts. For instance, a general exception for insurance contracts could be made, as in recommendation 10 of the Law Revision Committee's 1937 report and also the Australian Insurance Contracts Act 1984.[2] One advantage of specific reform is that the needs of a particular context can be addressed in detail.[3] Another is that the question whether there is an intent to give the third party an enforceable right is addressed in a specific way. We invite the views of consultants whether reform should be on these lines and, if so, which particular contexts should be addressed. This consultation paper has not explored the possibility of merely reforming particular contexts because we believe (as did the Law Revision Committee) that the third party rule is generally flawed. A positive disadvantage of this technique is that, given that the number and variety of exceptions has produced an already complicated body of law, the creation of further exceptions would further complicate the position and could forestall any possible judicial reform.

5.3 **The rule preventing the promisee from recovering the third party's loss in damages could be abolished.** The advantage of reforming the remedy rule is that there would be no need to address several difficult questions which would arise if third parties were given rights, such as: what is a contract for the benefit of a third party; can the

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2. See Appendix, para. 5.

3. In the draft Bill appended to Law Com. No. 196, it was possible to deal with a number of specific issues in addition to the basic reform granting third parties rights of suit: e.g. the rights of original contracting parties and those intermediately entitled; the question of liabilities; special rules for particular documents; electronic transactions. See Beatson & Cooper, [1991] L.M.C.L.Q. 196.

original parties vary or rescind the contract; can the promisee sue in addition to the third party; is the promisor entitled to rely on defences available against the promisee, and the other questions discussed below. However, it is our provisional view that this would not be an adequate method of reform, largely for the reasons that the promisee may be either unwilling or unable to enforce a contract made for a third party.[4]

5.4 **There could be a provision that no third party be denied enforcement of a contract made for his benefit on the grounds of lack of privity.** The preferred method of reform advocated by the Ontario Law Reform Commission was that "there should be enacted a legislative provision to the effect that contracts for the benefit of third parties should not be unenforceable for lack of consideration or want of privity".[5] The Ontario Commission preferred this approach to a detailed legislative scheme for several reasons:

(i) It was thought better that the courts should be permitted some flexibility in dealing with the variety of issues which would undoubtedly arise under any reform.

(ii) Since third party beneficiary cases arise in widely different contexts (from contracts to pay money to relatives to contracts involving the extension of defences in bills of lading to stevedores), it was thought that legislation could not satisfactorily deal with all such problems and that anomalies were likely to arise if the same set of rules were to apply to such widely different circumstances.

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4. See para. 4.29 above.

5. Report on Amendment of the Law of Contract, (Toronto 1987): see Appendix, para. 20.

(iii) The problem of defining the class of beneficiaries entitled to sue and the question of variation and rescission were regarded as particularly intractable.

5.5 This method of reform has the attraction of making the change of principle a legislative matter while leaving subsequent development to the courts.[6] However, it is our provisional view that the problems involved are too complex and numerous to lend themselves to such a generalised approach. In this part of the paper, we consider a number of important issues. To leave these issues to the courts with no legislative guidance could be said to be an abdication of responsibility when we are aware that they involve questions of principle which will at some stage have to be faced, if not by the legislature by the courts. The general approach also achieves flexibility at the expense of clarity and certainty. The development of the law in the United States, even with the assistance of the Restatements, illustrates some of the disadvantages of a generalised approach.[7]

5.6 **The law could be reformed by means of a legislative scheme.** This was the approach adopted in Western Australia,[8] Queensland[9] and New Zealand.[10] On this approach, policy would be determined and provision made for such matters as

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6. See also French and German law: Appendix, paras. 24-29.

7. However, the U.S. analogy may not be entirely convincing, given that the detailed body of statutory exceptions which exists in England is largely absent there.

8. Property Law Act 1969, s. 11: Appendix, para. 2.

9. Property Law Act 1974, s. 55: Appendix, para. 4.

10. Contracts (Privity) Act 1982: Appendix, para. 9.

the rights of contracting parties to modify or terminate the contract, promisors' defences and the types of remedy available to third parties. The two main advantages of this approach are certainty and clarity.

5.7 It is our provisional recommendation that, of the four methods of legislative reform which we have considered, the most satisfactory is that detailed legislation should be enacted to grant a right to third parties to enforce contracts made for their benefit. There can, of course, be different approaches to the details of the scheme and the case for reform depends in part upon the extent and shape of what is proposed. In the remainder of this part, we will examine the main issues which require examination in any statutory reform of the third party rule and, in respect of many of these, state the approach which, subject to views expressed on consultation, we are inclined to favour. Comments are invited on all these issues and our provisional recommendations, which are summarised in Part VI below.

2. Test of enforceable benefit

5.8 This is the central issue involved in reform of the third party rule. It is an issue on which there is no consensus among the various jurisdictions which we have examined.[11] There are several options, including the following:

(i) A third party may enforce a contract which expressly in its terms purports to confer a benefit directly on him.[12]

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11. See Appendix.

12. See section 11(2) of the Western Australia Property Law Act 1969.

(ii) A third party may enforce a contract in which the parties intend that he should receive the benefit of the promised performance, regardless of whether they intend him to have an enforceable right of action.

(iii) A third party may enforce a contract in which the parties intend that he should receive the benefit of the promised performance and also intend to create a legal obligation enforceable by him.[13]

(iv) A third party may enforce a contract where to do so would effectuate the intentions of the parties and either the performance of the promise satisfies a monetary obligation of the promisee to him or it is the intention of the promisee to confer a gift on him.[14]

(v) A third party may enforce a contract on which he justifiably and reasonably relies, regardless of the intentions of the parties.

(vi) A third party may enforce a contract which actually confers a benefit on him, regardless of the purpose of the contract or the intentions of the parties.

5.9 We think that the options of allowing a third party to sue on any contract which happens to confer a benefit on him or on which he justifiably and reasonably relied would be unacceptably wide. They raise the possibility of an unacceptable volume of litigation and leave promisors open

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13. See the law in Queensland, New Zealand and Scotland: Appendix, paras. 4, 9 & 22. We will refer to this as the "dual intention" test.

14. See sections 302 & 304 of the Restatement (Second) of Contracts: Appendix, para. 16.

to liability to a potentially indeterminate class of third parties. The option of allowing a third party to sue on a contract which expressly in its terms purports to benefit him would not cater for those contracts under which the parties intend to confer an enforceable benefit on him but have not spelled this out expressly. Likewise, we do not think it sufficient that the contracting parties intend that the third party should receive the benefit of the promised performance: again, for the reasons that the parties' intentions could be defeated and an unacceptably large number of potential plaintiffs created. For instance, in the example discussed earlier[15] of a building company contracting with a highway authority for the construction of a new road, the road may be intended for the benefit of all road-users, or even for an identified number of users (such as the residents of a private estate). However, it is a different issue whether individual road-users should have a right of action on the agreement in the event of delay in construction.

5.10 We provisionally recommend that a third party should be able to enforce a contract in which the parties intend that he should receive the benefit of the promised performance and also intend to create a legal obligation enforceable by him. From this it follows that the creation of a right in a third party should not be inferred from the mere fact that he will derive benefit from performance of the contract. Equally, a third party should not be allowed to sue on any contract which is simply made for his benefit or which merely happens to benefit him or on which he has happened to rely.

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15. At para. 2.19 above.

5.11 The basic principle on which our proposal rests is to allow a remedy to the third party when to do so would give effect to the intentions of the contracting parties. Intention should not necessarily be associated with motive. If A, in buying property from B, promises to pay the purchase price to C, A's motive or purpose in making the promise may be simply to comply with the proposed bargain. Likewise, the reason why B extracted the promise may have been to make a gift to a close friend or to fulfil a duty to a sworn enemy. Whether or not a contract is intended to create a legal obligation enforceable by the third party is to be derived from the terms of the contract and the surrounding circumstances.[16]

5.12 Furthermore, it is the objectively determined intentions of the parties which matter rather than their private thoughts.[17] Parties to the contract may frequently omit provisions from their contract, whilst relying on prior dealing, trade customs or other shared beliefs. We provisionally recommend that reform should enable consideration of the circumstances surrounding the making of the contract when deducing the parties' intentions.[18]

5.13 Although we provisionally recommend the dual intention test, we are aware of the criticisms of it.

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16. See also Art. 328 of the German Civil Code: Appendix, para. 28.

17. On contractual intention, see Treitel, op. cit., Ch. 4.

18. See also Appendix, para. 17.

(i) Where the contract is silent or ambiguous on the question of enforcement by a third party, the ascertainment of a contractual intention may be difficult.[19]

(ii) Concentration on the intention of the parties has been argued to be a substitute for the real enquiry, which should be on the third party's actual reliance and the needs of the market in which the parties operate.[20] Where a third party becomes involved, generally by reliance on the contract, a court may be unduly restricted if it only has regard to the intent of the contracting parties.[21]

5.14 However, we do not regard these criticisms as convincing. First, the problem of detecting an unexpressed intention is a familiar one for courts as is the idea of giving effect to the intentions of the parties. We do not think that ascertainment of the parties' intentions in a three party situation poses any more difficulties than in a two-party situation. Indeed, even if such ascertainment is difficult, this does not of itself point in favour of a laxer rule which may not reflect the intentions of the contracting parties. Secondly, we have already stated why we think that it would be unacceptable if a third party could sue on any contract on which he justifiably and reasonably relied.[22]

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19. Trident General Insurance Co. Ltd. v. McNiece Bros. Pty. Ltd. (1988) 62 A.L.J.R. 508, 514 per Mason C.J. and Wilson J. See also the Ontario Law Reform Commission's Report on Amendment of the Law of Contract (1987), p. 70.

20. (1968) 54 Va. L.R. 1166.

21. Ibid., p. 1186.

22. See para. 5.9 above.

5.15 A reform of the third party rule would allow, in principle, contractual actions by consumers against manufacturers if the contract between manufacturer and wholesaler/retailer were to be construed as a contract for the benefit of a third party within the terms discussed earlier. Whether or not this would occur frequently in practice is debatable, since under our provisional recommendations, if the parties to the contract do not make it clear that they intend to create a legal obligation enforceable by the third party, the third party will have no remedy.[23] In a context in which such intent may be inferred by the court it is open for the contracting parties to make the position clear by inserting a contractual term in effect excluding any action by a third party. In the context of section 4 of the New Zealand Contracts (Privity) Act 1982, one commentator has noted that if the parties wish to escape the application of the Act, they need only to declare in their contract, in a manner clear enough to be proof against interpretation contra proferentem, their intention that the third party beneficiary be not entitled to sue.[24] We are of the provisional view that the ability of parties to do this is an important component of any reform which is to be compatible with a consensual view of contractual relations.

3. Range of benefits

5.16 We provisionally recommend that rights created against a contracting party should be governed by the

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23. Arguably, the dual intention test would not normally operate to give to the consumer contractual rights against the manufacturer.

24. Coote, (1984) N.Z. Recent Law 107, 112.

contract and be valid only to the extent that it is valid,[25] and may be conditional upon the other contracting party performing his obligations under it.[26] Thus, if, at the time of its formation, the contract is affected by misrepresentation or lack of formalities, or if it subsequently is or is liable to be discharged, as by supervening impossibility or breach, the third party's rights should be limited accordingly. Section 55(1) of the Queensland Property Law Act 1974 stipulates that valuable consideration must move from the promisee, a requirement which we do not recommend since it would not cover promises contained in contracts made by deed.[27] Equally, where the contract is made by deed or consideration moves from the promisee, it follows that the third party should not have to furnish consideration to be able to acquire contractual rights.[28] Also important is the fact that the third party's rights will generally be conditional upon performance being made to the promisor. An insurance policy taken out by a father in favour of his son will be of no avail to the son if the father fails to pay the annual premiums.

5.17 We also provisionally recommend that rights which may be created in favour of a third party extend (a) both to the right to receive the promised performance from the promisor where this is an appropriate remedy and to the

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25. As under section 309(1) of the Restatement (Second) of Contracts.

26. As under section 309(2) of the Restatement (Second) of Contracts.

27. There is no such requirement in the New Zealand Contracts (Privity) Act 1982.

28. See the New Zealand Contracts and Commercial Law Reform Committee's Report on Privity of Contract (1981), p. 57.

right to pursue any remedies for delayed or defective performance, and (b) to the right to rely on any provisions in the contract restricting or excluding the third party's liability to a contracting party as if the third party were a party to the contract.

5.18 The first part of this recommendation states the central point that the third party beneficiary is entitled to performance of the promise,[29] or damages for its non-performance. The second part of the recommendation allows third parties to be able to take advantage of exemption clauses agreed for their benefit,[30] thus achieving the result reached in The Eurymedon and The New York Star[31] more directly.

4. Designation of third party

5.19 It is our provisional view that to require the third party to be named in the contract would be too restrictive. If the parties intend, for instance, to benefit stevedores or other independent contractors, it should not be necessary that they be actually named in the contract, since such people may not be identifiable at the time of the making of the contract. Under section 4 of the New Zealand Contracts (Privity) Act 1982, a third party may be

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29. Section 307 of the Second Restatement allows a third party to maintain a suit for specific performance where this is an appropriate remedy.

30. On the question whether he who takes the benefit of an exemption clause should take any corresponding burden, see paras. 5.36-5.37 below.

31. See paras. 3.27-3.29 above. Cf. Appendix, para. 10 and Reynolds, (1985) 11 N.Z.U.L.R. 215, 221, n. 41.

"designated by name, description or reference to a class".[32] We invite views on whether there should have to be a particular form of designation: whether express designation (e.g. the third party's name) or implied designation, including a description of the type of employment (e.g. stevedores) or class of employment (e.g. sub-contractor) or type of interest (e.g. consignee).

5. Ascertainability and Existence of third party

5.20 This issue concerns whether the third party must have been ascertainable or indeed in existence when the contract was made, and raises the particular question of the status of pre-incorporation contracts. It is our provisional view that rights may be created in a third party even though he is not in existence or ascertained at the time the contract is made,[33] since otherwise a remedy would be denied to prospective beneficiaries such as an unborn child or a future spouse. The existing statutory exceptions in the insurance context do not require such ascertainment, nor probably does the common law in the way in which it has accorded protection to stevedores. Under section 308 of the Restatement (Second) of Contracts, it is not essential to the creation of a right in an intended beneficiary that he be identified when the contract is made. However, the fact that someone cannot be identified may be relevant in determining whether or not there was an intention to confer on him a right to the promised performance.

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32. See Appendix, para. 9.

33. See section 55(6)(b) of the Queensland Property Law Act 1974: Appendix, para. 4.

5.21 The Queensland Property Law Act 1974 requires that a beneficiary be identified and in existence at the time of "acceptance", which is an assent by words or conduct communicated by the beneficiary to the promisor and which is a pre-condition to the enjoyment by the beneficiary of any enforceable rights.[34] This may have adverse consequences for some members of a class of beneficiaries. For example, where an employer has agreed with union representatives to review employees' salaries at regular intervals, would the benefit of this agreement be enjoyed only by those members of the work-force who "accepted" it at its inception, and not those who subsequently joined the company? There is no requirement under the New Zealand Contracts (Privity) Act 1982 that a third party be identified or in existence at the time of acceptance, nor do we recommend such a requirement.

5.22 The issue of the non-existence of the third party at the time of the making of the contract raises the question of pre-incorporation contracts. Under English law, a company can neither take the benefit nor the burden of a contract made before its incorporation, nor can it subsequently ratify such a contract,[35] a state of affairs which has been described as "one of the weakest points of English company law".[36] The question arises whether this position would, or should, be altered by legislation on

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34. See ss. 55(1), 55(6)(a) & 55(6)(b): Appendix, para. 4.

35. See Pennington's Company Law (6th ed., 1990), p. 87 ff. Under section 36C(1) of the Companies Act 1985, inserted by the Companies Act 1989, s. 130 (4), a pre-incorporation contract presumptively takes effect as a personal contract with those purporting to act on the company's behalf who thus become personally liable.

36. Gross, (1971) 87 L.Q.R. 367.

third party rights, especially were legislation expressly to state that rights can be created in a third party even though not in existence at the time that the contract was made.

5.23 The New Zealand Contracts and Commercial Law Reform Committee's Report on Privity of Contract[37] took the view that the rule preventing a company from ratifying a pre-incorporation contract was not truly an example of the privity doctrine but was an application of the law of agency resting on the rule that agency can subsist only whilst the principal is in existence. Accordingly, it took the view that the matter was outside the scope of its report. Several other jurisdictions have dealt with this matter in the context of company law legislation.[38] However, it has been argued that section 4 of the New Zealand Contracts (Privity) Act 1982 does cover contracts between principals in favour of a company yet to be formed, though not pre-incorporation contracts which are nullities at common law.[39] We invite views on whether, and if so how, the issue of pre-incorporation contracts should be addressed in any reform of the third party rule, or whether it is best left to specialist company legislation.

6. Defences and joinder

5.24 The third main question considered in para. 2.3 above was whether D could rely on defences in his own

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37. (1981), p. 11. This Report led to the Contracts (Privity) Act 1982.

38. Gross, op. cit., p. 395.

39. Coote, (1988) 13 N.Z.U.L.R. 160, 170.

contract to which P was not a party. It is our provisional view that the rights of the third party against the promisor should be subject to the promisor's defences, set-offs and counterclaims which would have been available to the promisor in an action by the promisee.[40] Under New Zealand law,[41] the promisor's defences, counterclaims and set-offs against the third party include those which could have been raised had the action been brought by the promisee. Such a rule is analogous to the rule that an assignee of a chose in action takes "subject to equities".

5.25 In the case of defences, set-offs and counterclaims, a question arises as to the scope of what the promisor may rely upon. For instance, can the third party be met by allegations of waiver, estoppel or laches which the promisor could have raised against the promisee? In the case of set-offs and counterclaims, may the promisor only rely on matters arising from the contract in which the promise is contained? Section 9(3) of the New Zealand legislation[42] states that the promisor may set up against the third party defences founded upon the contract from which the third party derives his right, but not those arising out of other

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40. See also Morris v. C.W. Martin & Sons Ltd. [1966] 1 Q.B. 716; Pyrene Co. Ltd. v. Scindia Navigation Co. Ltd. [1954] 2 Q.B. 402.

41. Contracts (Privity) Act 1982, s. 9(2). See also the Western Australia Property Law Act 1969, s. 11(2)(a): Appendix, para. 2.

42. "The promisor may, in the case of a set-off or counterclaim... against the promisee, avail himself of that set-off or counterclaim against the beneficiary only if the subject-matter of that set-off or counterclaim arises out of a right or claim conferred by the deed or contract in which the promise is contained." See also Article 1413 of the Italian Civil Code: Millner, (1967) 16 I.C.L.Q. 446, 461.

relations between promisor and promisee.[43] The contrary position is that the promisor should be allowed, as against the third party, to take advantage of any defence, set-off or counterclaim he had against the promisee, whether or not it arises out of the contract containing the promise in favour of the third party.[44] Much depends on whether the third party's rights are seen as direct or derivative, and whether contracting parties intend that their state of account, i.e. outstanding balances on previous transactions, will govern performance of the contract. We invite views on this question.

5.26 Given that we recommend that a promisor may in principle rely against the third party on defences, set-offs and counterclaims which he has against the promisee, we invite views on whether there should be a requirement[45] that the promisee, as well as the promisor, be a party to the litigation when a third party sues to enforce a contract made for his benefit.[46] The New Zealand legislation does not require this, on the grounds that such a requirement could lead to unnecessary expense and possible problems as to service of the proceedings.[47] Indeed, such a joinder

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43. See also section 309(3) of the Second Restatement.

44. Section 8(2) of the Irish Married Women's Status Act, No. 5 of 1957, provides: "The right conferred on a third person by this section shall be subject to any defence that would have been valid between the parties to the contract."

45. See R.S.C. Ord. 15 r. 4 for those cases where joinder is permitted with or without leave of the court.

46. As in section 11(2)(b) of the Western Australia Property Law Act 1969.

47. New Zealand Contracts and Commercial Law Reform Committee's Report on Privity of Contract (1981), p. 49.

requirement did not prevent the result in Westralian Farmers Co-op. Ltd. v. Southern Meat Packers Ltd.[48] that the promisor was held liable to pay the third party even though he had already paid the promisee. We discuss below the substantive question whether the promisee should be able to sue in addition to the third party.[49]

7. Variation and cancellation

5.27 Just as it is possible under the present law when enforceable rights are conferred under a trust to make those rights subject to provisions allowing the original contracting parties to vary or cancel the contract, so we provisionally recommend that any reform should allow the parties to contract for such reservations to the rights of third parties. The following account deals with those cases where no such reservation is made. In such circumstances, it is possible to argue that the original contracting parties should be able to vary or cancel the contract:

(a) at no time;[50]

(b) until the third party is aware of the contract;

(c) until the third party adopts the contract either expressly or by conduct;[51]

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48. [1981] W.A.R. 241: see Appendix, para. 3.

49. See para. 5.34 below: see Appendix, para. 2.

50. As in Scotland: Blumer v Scott (1874) 1 R 379.

51. As in s. 11(3) of the Western Australia Property Law Act 1969, and s. 8(3) of the Irish Married Women's Status Act, No.5 of 1957: Appendix, paras. 2 and 21. This was also the recommendation of the Law Revision Committee.

(d) until the third party accepts or assents to the contract;[52]

(e) until the third party materially alters his position in reliance on the contract;[53]

(f) until the third party either materially changes his position in justifiable reliance on the promise or brings suit on it or manifests assent to it at the request of the promisor or promisee;[54]

(g) at any time.

5.28 The question of whether and if so when variation or discharge should be allowed is central to any proposed reform. The freedom to vary obligations is an important contractual right: the promisee may wish to rescind or modify the contract with the promisor's assent, arrive at a compromise or assign his contractual rights, or even divert to himself the benefit initially intended for the third party.[55] Any provision designed to protect third party rights is liable to make inroads into the rights of the contracting parties.

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52. As in the Queensland Property Law Act 1974, s. 55(2) & s. 55(6)(a), and Art. 1121 of the French Civil Code: Appendix, paras. 4 and 24.

53. As in New Zealand: Contracts (Privity) Act 1982, s. 5: Appendix, para. 9.

54. As in the United States: section 311(3) of the Restatement (Second) of Contracts: Appendix, para. 19.

55. Trident General Insurance Co. Ltd. v. McNiece Bros. Pty. Ltd. (1988) 62 A.L.J.R. 508, 514.

5.29 It is arguable that where the parties agree to confer an irrevocable benefit on a third party, effect should be given to the agreement.[56] Nevertheless, the parties may thereafter wish to change their minds, and giving crystallised rights to third parties may prevent them from doing so. Our aim is to achieve a balance between the interests of the contracting parties (and their creditors) and those of the third party. In this respect, the option that contracting parties should never be able to vary the contract may be too one-sided, as is the option allowing parties to the contract to vary their obligations at any time. We think that the options for reform rest between the Australian formulae based upon the notion of a beneficiary "adopting" the contract either expressly or by conduct[57] or "accepting" the contract,[58] and the New Zealand formula which allows variation until the beneficiary has materially altered his position in reliance on the promise. The balance between the interests will vary according to the facts. For instance, the Australian legislation seems to give greater protection to the third party than the New Zealand legislation, since "adoption" or "acceptance" may be effected without any sort of reliance. However, a third party who has relied on the contract but has not communicated acceptance to the promisor will have more protection under the New Zealand legislation than the Queensland legislation.

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56. See section 311(1) of the Restatement (Second) (discharge or modification by contracting parties ineffective if a term of the promise creating the duty so provides).

57. Section 11(3) of the Western Australia Property Law Act 1969: Appendix, para. 2.

58. Under section 55(6)(a) of the Queensland Property Law Act 1974, "acceptance means an assent by words or conduct communicated by or on behalf of the beneficiary to the promisor ...".

5.30 The New Zealand Contracts and Commercial Law Reform Committee compared a third party beneficiary to the donee of an incomplete gift.[59] The donee has no right to require completion of the gift, although the estoppel doctrine recognises that there may be injustice where an expectation has been created in a person, causing him to alter his position in reliance on that expectation. The principle underlying estoppel can be applied in the context of third party beneficiaries. The requirement that the beneficiary must first change his position in reliance on the promise, before the parties to the contract lose their right to vary or cancel, may best maintain the balance of equities amongst all concerned. However, the parties to the contract may not know whether the third party has relied on the promise and there could thus be uncertainty as to their entitlement to vary or cancel. It has also been argued that if reliance is the reason for enforcement, why should the recovery not be limited to protection of the third party's reliance?[60]

5.31 A provision which prevented parties to the contract from varying their obligations once a third party had merely "accepted" the contract (e.g. by saying "thank you") could be criticised for the reason that the beneficiary, as a volunteer, is getting something for nothing. Furthermore, if the contract would normally allow for variation, why should the third party's assent affect the matter?[61] There have also been cases in the U.S.A. where the third party is simply presumed to have accepted the benefit, particularly

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59. In its report, Privity of Contract (1981), p. 59.

60. Ontario Law Reform Commission's Report on Amendment of the Law of Contract (1987), p. 71. See also, Appendix, para. 20.

61. Ibid.

in divorce settlements involving provision for minors.[62] If this pattern were to be repeated, the substance of the adoption or acceptance test would be illusory, and the balance shifted in favour of the third party at the expense of the contracting parties. Where the purpose of the contract is not to make a gift but to satisfy a duty already owed by the promisee to the beneficiary,[63] different considerations may apply.[64] The third party may argue that since he has already provided consideration to the promisee, he should be able to enforce the agreement between promisee and promisor without the detriment required by the New Zealand provision. However, where the purpose of the arrangement is to make a gift to the third party, who is thus merely a gratuitous promisee, it is arguable that the parties' ability to vary or rescind should be less easily restricted, particularly since the financial position of the donor might change or the conduct of the third party prove to be so unworthy as to make unthinkable the idea of a gift to him.[65] Although the policy arguments in favour of the New Zealand formula may be weaker in the case of "creditor beneficiaries", it may be better not to apply different tests to different categories of beneficiary, as the confused case law which followed the categorisation approach of the first Restatement of Contracts shows.[66] In any event, even if variation is effected after "acceptance", a creditor

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62. Smith v. Smith 218 N.E. 2d. 473 (1964); James v. Pawsey 328 P. 2d. 1023, 162 Cal. App. 2d. 740 (1958); Rhodes v. Rhodes 266 S.W. 2d. 790 (1953).

63. This is the distinction between donee beneficiaries and creditor beneficiaries, as used in the first Restatement of Contracts (1932): see Appendix, para. 15.

64. See Stoljar, (1988) 13 N.Z.L.R. 68, 72 ff.

65. Ibid., pp. 73, 95.

66. See Appendix, para. 16.

beneficiary still has a right of action against the promisee.[67] We invite views on the various issues raised in this section, in particular:

(i) whether (in the absence of an agreement between the contracting parties and the third party) acceptance, adoption or material reliance should be required before modification is prevented;

(ii) whether such adoption, acceptance or material reliance should be known to the parties (or at least the promisee) or be such that the promisee could reasonably have anticipated it;

(iii) whether modification should be permitted where the contract allows it (either expressly or impliedly) regardless of adoption, acceptance or material reliance or at least where the third party knows (or should reasonably have been aware) that the contract permits modification even though he subsequently adopts, accepts or materially relies on the contract.

8. Discretion to order variation or discharge for reasons of justice

5.32 On the assumption that variation or cancellation by the parties is in principle allowed, the question arises whether the courts should have any discretion to order or prohibit variation or discharge for reasons of justice. Section 7(1) of the New Zealand Contracts (Privity) Act 1982 enables the court, where it considers it "just and practicable", to order variation or discharge of the promise. This power may be exercised at any time, even where

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67. See para. 5.35 below.

the third party has materially altered his position in reliance on the promise. The merit of the provision is that it can be invoked to avoid injustice where unforeseen factors make performance by the promisor more onerous. However, we do not think that there is a particular need for such a provision in a three-party case any more than in a two-party case. Section 7(2) balances the protection given to the contracting parties, by providing that if the beneficiary has been injuriously affected by reliance on the promise:

> "... the Court shall make it a condition of the variation or discharge that the promisor pay to the beneficiary, by way of compensation, such sum as the Court thinks just."

5.33 However, the basis on which such compensation should be assessed may cause difficulties. Let us take the example of the employer and employee who are parties to a pension scheme which includes a widow's benefit.[68] If the employer and employee wish to alter this so as to provide a lump sum to the employee on his retirement, there is the problem that the wife, in reliance on the promise of the widow's benefit, may not have taken out any life insurance for herself. The insurance prospects of a young and healthy wife aged 30 are clearly better than those of a wife aged 60 in poor health. The sum which the court can order to be paid under section 7(2) will no doubt depend on such matters as age and health. Clearly, a provision such as section 7 would have to be used sparingly. We provisionally recommend that the courts should not have a residual discretion to order variation or discharge for reasons of justice.

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68. See Coote, (1984) N.Z. Recent Law 107, 114.

9. Can the promisee sue in addition to the third party?

5.34 On the question of an overlap of remedies by the promisee and the third party, one possibility would be a provision that the third party acquires rights at the expense of the promisee. Another possibility would be to provide that the third party's rights were in addition to those of the promisee, in which case one would need principles governing a contest between the two. We have reached the provisional conclusion that the promisor's duty to perform is owed both to the third party and the contractual promisee,[69] but so far as he makes performance to or is released from performance by the third party he discharges his duty under the contract and all remedies against him for any breach of the contract are available to the third party and may be pursued by him in preference to the contractual promisee.[70] This issue is related to the procedural question of whether joinder should be required of all the relevant parties.[71] We invite views on what should be the position where the promisor has made performance to the promisee and then the third party seeks to enforce the contract. So long as the contract can still be varied, performance in favour of the promisee should arguably discharge the promisor and the third party would have no

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69. See also section 305(1) of the Restatement (Second) of Contracts; a promise in a contract creates a duty in the promisor to the promisee to perform the promise even though he also has a similar duty to an intended beneficiary. Section 307 allows the promisee (in addition to the third party) to maintain a suit for specific performance when this is an appropriate remedy.

70. See also section 305(2) of the Restatement (Second); whole or partial satisfaction of the promisor's duty to the beneficiary satisfies to that extent the promisor's duty to the promisee.

71. See para. 5.26 above.

rights.[72] Once the contract cannot be varied, the promisor should arguably have to perform in favour of his creditor, i.e. the third party.[73]

10. Overlap of remedies against both contracting parties

5.35 Where the promisor's performance is designed to discharge an existing obligation of the promisee to the third party, (i.e. the third party is a creditor beneficiary), the latter already has a right against the promisee. The contract made for his benefit gives him a further right against the promisor. We provisionally recommend that the third party should be able to pursue claims against either the promisor or the promisee, and his acceptance of benefits under the contract should discharge his rights against the promisee only to the extent that such obligation is thereby fulfilled.[74] Thus, if the creditor beneficiary sues and recovers from the promisor, the contractual promisee will be released to the extent of the recovery. If, however, the beneficiary chooses to sue the promisee on the promisor's non-performance, the promisee would in turn be able to claim indemnity as against the promisor.[75] It is for consideration whether, in

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72. Mitchell v. Ede (1840) 11 Ad. & E. 888; 113 E.R. 651; The Lycaon [1983] 2 Lloyd's Rep. 548 (shipper able to direct a carrier to deliver to someone other than the named consignee in a bill of lading before the latter has acquired any rights): see Benjamin's Sale of Goods (3rd ed., 1987), paras. 1437-1438.

73. Any dispute between the promisee and the third party would, so far as the promisor was concerned, be res inter alios acta.

74. See section 310(1) of the Restatement (Second).

75. See section 310(2) of the Restatement (Second).

circumstances where the third party has "accepted" the promise made in his favour, he should have to resort first to his remedy against the promisor.

11. No creation of duties in third parties

5.36 This issue raises the question whether the parties to a contract should be able to impose duties on a third party or be able to impose conditions upon the enjoyment of any benefit conferred on him. We provisionally recommend that the parties to a contract cannot by the contract impose duties on a third party but may impose conditions upon the enjoyment of any benefit by him. That the parties to a contract cannot by agreement between themselves impose contractual obligations upon a third party is universally accepted as a reasonable rule. However, a contract creating a right in favour of a third party may make that right dependent on the fulfilment of a condition. For instance, where a contracting party agrees to afford the third party a right of way over his land on condition that the third party keeps the roads in repair,[76] the third party does come under an obligation but the obligation is not imposed on him by the parties to the contract but by his own implied agreement.

5.37 The natural corollary of P suing on a contract to which he is not a party is that D should be able to rely on defences etc. in that contract even though P is not a party: in other words, if P takes the benefit of a contract to which he is not a party, he must also take the burden.[77] In

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76. See Halsall v. Brizell [1957] Ch. 169.

77. See also para. 5.24 ff above.

Pyrene Co. Ltd. v. Scindia Navigation Co. Ltd.,[78] which involved a contract of carriage between a shipowner and f.o.b. buyer,[79] the shipowner negligently damaged goods before they crossed the ship's rail and thus when the seller still owned them. The seller sued the shipowner, who in turn sought to rely on contractual exceptions in the bill of lading. Devlin J. held that there was nothing novel in third party beneficiaries enforcing a contract made for his benefit.[80] It was the intention of all three parties that the seller could participate in the contract of carriage so far as it affected him. He could therefore take the benefit of the contract by suing the shipowner, but subject to whatever qualifications the contract imposed, including the provisions of the Hague Rules limiting the shipowner's liability. On facts such as those in Junior Books, under a reform of the third party rule the owner would in principle be able to raise a contractual action for economic loss caused by the sub-contractor's breach of contract if he was a third party beneficiary under the contract between the main contractor and the sub-contractor. Equally, the sub-contractor would be able to raise defences under the sub-contract, on the benefit-burden principle. Indeed, it

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78. [1954] 2 Q.B. 402.

79. Devlin J. distinguished several types of f.o.b. contract: (i) S puts goods on board a vessel nominated by B, and is party to the contract of carriage, taking out a bill of lading in B's name; (ii) in addition to the above, S also makes the shipping arrangements; (iii) B makes the shipping arrangements (as in Pyrene itself). It is in the latter case that there are doubts whether S is party to the contract of carriage.

80. Relying on Smith & Snipes Hall Farm Ltd. v. River Douglas Catchment Board [1949] 2 K.B. 500 and Les Affreteurs Reunis S.A. v. Leopold Walford (London) Ltd. [1919] A.C. 801. Although Pyrene v. Scindia has never been overruled, this aspect of the decision is doubtful in view of Midland Silicones Ltd. v. Scruttons Ltd. [1962] A.C. 446.

would follow from our main recommendation that the sub-contractor would be able to rely on the main contract if it was intended to give him enforceable rights. Although it has been suggested that a sub-contractor should only be able to rely on defences in the sub-contract, and not the main contract,[81] we see no reason why a sub-contractor should be denied the protection of the main contract if intended to give him rights.[82]

12. Existing exceptions

5.38 This issue relates to the future of existing exceptions to the third party rule in the event of reform. At present, there are many exceptions to the third party rule, including several specific statutory exceptions.[83] We provisionally recommend that, in the interests of certainty, existing legislative exceptions to the third party rule should be preserved. To draw a parallel with the law of the United States, it has never been suggested that the Federal Bills of Lading Act 1916[84] is unnecessary because of the recognition in the United States of the right of third

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81. Markesinis, (1990) 106 L.Q.R. 556.

82. See Norwich City Council v. Harvey [1989] 1 W.L.R. 828, para. 3.30 above, where a tortious duty of care was negatived by the contractual setting and in this sense a third party sub-contractor was allowed to rely on an exemption clause in a contract to which he was not a party.

83. See paras. 3.45 ff above.

84. Which gives rights to holders of bills of lading, who are third parties to the carriage contract made between the shipper and the carrier. In this context see also the views of the Scottish Law Commission; Bulk Goods : Section 16 of the Sale of Goods Act 1979 and Section 1 of the Bills of Lading Act 1985; Discussion Paper No. 83 (1989), para. 3.9; Appendix, para. 22.

parties to sue in contract. Neither do we wish to change the existing law on freehold and leasehold covenants or any other established exception in the law of property, trusts, agency and so on.[85] However, we invite views from consultants on whether existing exceptions raise particular policy issues which should be addressed in any legislative reform.[86] We have seen that there have been certain difficulties with the scope of the Third Parties (Rights Against Insurers) Act 1930,[87] such that reform of that statute might be desirable. We invite views on this question. In addition to its general proposal to give rights to third parties, the Law Revision Committee specifically recommended that section 11 of the Married Women's Property Act 1882 be extended to all life, endowment and education policies in which a particular beneficiary is named.[88] We invite views on this proposal.

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85. See also section 14 of the New Zealand Contracts (Privity) Act 1982: Appendix, para. 9. Clearly, though, reform will mean that the courts will not have to resort to some of the more elaborate and artificial techniques to circumvent the third party rule, for which see Part III above.

86. In Rights of Suit in Respect of Carriage of Goods by Sea (1991), Law Com. No. 196; Scot. Law Com. No. 130, we recommended a statutory reform of the third party rule as it affects contracts of carriage of goods by sea. In any reform of the third party rule, it is for consideration what would be the fate of such enacted proposals.

87. See paras. 3.50 & 4.22 above.

88. See para. 4.31 above and see the more general provisions of the Australian Insurance Contracts Act 1984, Appendix, para. 5.

13. Concurrent actions

5.39 This issue relates to whether the creation of third party contractual rights should be in addition to, or to the exclusion of, rights in tort. So long as there are different limitation periods in contract and tort actions, there will remain procedural advantages in framing a cause of action in one way rather than the other.[89] It would, of course, be possible for implementing legislation to state that any third party contractual rights were to the exclusion of rights in tort.[90] Arguably, when parties are in a contractual relationship, an action in tort with potentially different consequences should not be allowed to subvert the agreed allocation of risk. On the other hand, it is also arguable that it would be controversial to legislate so that the duty of care is excluded in certain situations. It might also be inopportune to legislate so as to exclude tort actions at a time when the courts are, in any event, more reluctant to find concurrent duties in contract and tort than they once were. The question of concurrent actions in contract and tort is a general problem of the law of contract which also arises in two-party situations. It is our provisional view that implementing legislation should not deal with this question.

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89. For instance, the Latent Damage Act 1986 will favour the plaintiff in a tort action (as opposed to a contract action) against a negligent solicitor where a defect in advisory or drafting work has remained dormant for between six and fifteen years.

90. In Tai Hing Cotton Mill Ltd. v. Liu Chong Hing Bank Ltd. [1986] A.C. 80, the Privy Council took the view that there was no advantage for the development of the law in searching for a liability in tort where the parties were in a contractual relationship.

14. Third party beneficiaries under wills

5.40 We have seen that a situation which causes particular difficulty is that of the improperly executed will which deprives a prospective beneficiary of an intended benefit.[91] Although Ross v. Caunters[92] allowed an action in tort by a disappointed beneficiary against a negligent solicitor, its authority is perhaps suspect in view of recent developments against recovery for pure economic loss.[93] There are several questions to consider:

(i) Should the disappointed beneficiary have a remedy, and if so, should it be contractual or tortious?

(ii) If contractual, should it fall under our general proposals, or should there be a specific rule governing this type of case?

(iii) Does this issue raise wider questions which go beyond the scope of reform of the third party rule?

5.41 The main arguments in favour of granting the beneficiary a remedy are: (i) he was in the direct contemplation of the solicitor when the will was being executed, the whole purpose of that aspect of the transaction being to benefit him; (ii) if the beneficiary cannot recover, the solicitor can be negligent with impunity, since the only person who has suffered loss is

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91. See paras. 3.12-3.17 and para. 4.25 above.

92. [1980] Ch. 297.

93. See para. 3.8 ff above.

unable to sue,[94] whereas the only person able to sue has suffered no loss and so could not recover substantial damages. The main arguments against liability of any kind are that (i) the beneficiary has no recognised interest because the testator remains free to alter his will, so that the solicitor should not be liable for failing to do what the testator was not required to do; (ii) there is no undertaking by the solicitor to the intended beneficiary such as to ground contractual liability; (iii) there is no reliance by the beneficiary anticipated by the solicitor, the general rule being that recovery for pure economic loss caused by negligent misstatement or services is not actionable in the absence of reliance.[95]

5.42 We have seen above that there are conflicting views on whether this situation falls within the category of contracts for the benefit of third parties.[96] On the one hand, the purpose of the contract of retainer between solicitor and testator is to draft a will which, if unrevoked, will confer a benefit on the intended beneficiary whose intended interest will otherwise be defeated. On the other hand, it can be said that the parties intend to confer a benefit by the will (which can always be changed) and not by virtue of the contract of retainer which does not itself contain a promise by the solicitor for the benefit of the third party. Assuming that the beneficiary should have a remedy, it may therefore be necessary to have a special

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94. Where the intended legatee is the spouse, former spouse, or a child or dependant of the testator, a claim can be made under the Inheritance (Provision for Family and Dependants) Act 1975.

95. See Cane, Tort Law and Economic Interests (1991), p. 191 ff.

96. At paras. 3.14-3.15 above.

provision in implementing legislation in addition to the general reform proposals.

5.43 It may be thought that this question raises issues which go beyond the scope of our project. In principle similar issues could arise in all cases of contracts to make dispositions in favour of volunteers. However, in contexts other than wills the problems arising out of ineffective dispositions may be cured by rectification. A will can only be rectified if it fails to carry out the intentions of the testator in consequence of a clerical error or a failure to understand his instructions.[97] Since in practice the problems have concerned wills, it may be that the solution (if one is thought necessary) is to reform the law of wills so as to give effect to the intentions of the testator. This would cover cases like Ross v. Caunters and other cases where wills have not been executed with the requisite formalities.[98]

5.44 We invite comments on how best, if at all, to deal with the question of improperly executed wills prejudicing prospective third party beneficiaries.

15. Conclusion

5.45 Our provisional recommendations are designed to ensure that the creation and protection of third party interests does not compromise the rights and position of the parties to the contract, notably the promisor. We are

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97. Section 20 of the Administration of Justice Act 1982.

98. See Luntz, (1983) 3 O.J.L.S. 284.

anxious that any reform should not replace present injustice to the third party by future injustice to the promisor.

5.46 We are now in a position to re-examine in the light of our recommendations the questions raised in paragraph 2.3 above.

(i) P will, in principle, be able to sue on a contract to which he is not a party if he is a third party beneficiary within the requirements discussed above, in particular that the parties intend that he should receive the benefit of the promised performance and also to create a legal obligation enforceable by him.

(ii) Similarly, D will be able to rely on defences in a contract to which he was not a party, again if he is a third party beneficiary within the requirements discussed above.

(iii) Likewise, D will be able to rely on defences in his own contract to which P was not a party for the reason that if P takes the benefit of such a contract, he also has to take the burden. He takes the contract as he finds it, including terms for D's benefit.

(iv) However, P will not without more be able to enforce his own contract against a third party. It is one thing to allow D to take the benefit of a contract when P is suing as a beneficiary of that contract. It is another to impose on D terms of a contract with which he has nothing whatever to do.

PART VI

SUMMARY OF OUR PROVISIONAL RECOMMENDATIONS FOR REFORM ON WHICH WE INVITE COMMENTS

A. IS REFORM NECESSARY

6.1 For the reasons given in Part IV, it is our provisional recommendation that there should be a reform of the law to allow third parties to enforce contractual provisions made in their favour.

B. SCOPE OF LEGISLATION

6.2 Of the various options for reform which we have examined,[1] it is our provisional recommendation that reform should be by way of a detailed legislative scheme.

C. THE MAIN ISSUES

1. Test of enforceable benefit[2]

6.3 We provisionally recommend that a third party should be able to enforce a contract in which the parties intend that he should receive the benefit of the promised performance and also intend to create a legal obligation enforceable by him.

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1. See paras. 5.1-5.7 above.

2. See paras. 5.8-5.15 above.

6.4 We provisionally recommend that reform should enable consideration of the circumstances surrounding the making of the contract when deducing the parties' intentions.

2. Range of benefits[3]

6.5 We provisionally recommend that rights created against a contracting party should be governed by the contract and be valid only to the extent that it is valid, and may be conditional upon the other contracting party performing his obligations under it.

6.6 We provisionally recommend that rights which may be created in favour of a third party extend (a) to the right to receive the promised performance from the promisor where this is an appropriate remedy and also to the right to pursue any remedies for delayed or defective performance, and (b) to the right to rely on any provisions in the contract restricting or excluding the third party's liability to a contracting party as if the third party were a party to the contract.

3. Designation of third party[4]

6.7 We invite views on whether there should have to be a particular form of designation: whether express designation (e.g. the third party's name) or implied designation, including a description of the type of

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3. See paras. 5.17-5.19 above.

4. See para. 5.20 above.

employment (e.g. stevedores) or class of employment (e.g. sub-contractor) or type of interest (e.g. consignee).

4. Ascertainability and Existence of third party[5]

6.8 We provisionally recommend that rights may be created in a third party even though he is not in existence or ascertained at the time the contract is made.

6.9 We invite views on whether the issue of pre-incorporation contracts should be addressed in any reform of the third party rule, or whether it is best left to specialist company legislation.

5. Defences and joinder[6]

6.10 We provisionally recommend that the rights of the third party against the promisor should be subject to the promisor's defences, set-offs and counterclaims which would have been available to the promisor in an action by the promisee. We invite views on whether, in the case of a set-off or counterclaim, a promisor may only rely on matters arising from the contract in which the promise is contained or may also set up against the third party defences arising out of other relations between promisor and promisee.

6.11 We invite views on whether there should be a requirement that the promisee, as well as the promisor, be a

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5. See paras. 5.20-5.23 above.

6. See paras. 5.24-5.26 above.

party to the litigation when a third party sues to enforce a contract made for his benefit.

6. Variation and cancellation[7]

6.12 We invite views on (i) whether (in the absence of an agreement between the contracting parties and the third party) acceptance, adoption or material reliance should be required before modification is prevented; (ii) whether such adoption, acceptance or material reliance should be known to the parties (or at least the promisee) or be such that the promisee could reasonably have anticipated it; (iii) whether modification should be permitted where the contract allows it (either expressly or impliedly) regardless of adoption, acceptance or material reliance or at least where the third party knows (or should reasonably have been aware) that the contract permits modification even though he subsequently adopts, accepts or materially relies on the contract.

7. Discretion to order variation or discharge for reasons of justice[8]

6.13 We provisionally recommend that the courts should not have a residual power to order variation or discharge of a contract for reasons of justice.

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7. See paras. 5.27-5.31 above.

8. See paras. 5.32-5.33 above.

8. Can the promisee sue in addition to the third party?[9]

6.14 We provisionally recommend that the promisor's duty to perform is owed both to the third party and the contractual promisee, but in so far as he makes performance to or is released from performance by the third party he discharges his duty under the contract and all remedies against him for any breach of the contract are available to the third party and may be pursued by him in preference to the contractual promisee.

6.15 We invite views on what should be the position where the promisor has made performance to the promisee and then the third party seeks to enforce the contract.

9. Overlap of remedies against both contracting parties[10]

6.16 We provisionally recommend that, where the promisor's performance is designed to discharge an existing obligation of the promisee to the third party, the third party should be able to pursue claims against either the promisor or the promisee, and his acceptance of benefits under the contract should discharge his rights against the promisee only to the extent that such obligation is thereby fulfilled.

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9. See para. 5.34 above.

10. See para. 5.35 above.

10. No creation of duties in third parties[11]

6.17 We provisionally recommend that the parties to a contract cannot by the contract impose duties on a third party but may impose conditions upon the enjoyment of any benefit by him.

11. Existing Exceptions[12]

6.18 We provisionally recommend that, in the interests of certainty, existing legislative exceptions to the third party rule should be preserved. We similarly provisionally recommend that any reform should be without prejudice to any other established exceptions in the law of property, trusts, agency and so on. We invite views on whether existing exceptions raise particular policy issues which should be addressed in any legislative reform.

6.19 We also invite views on the proposal made by the Law Revision Committee to extend section 11 of the Married Women's Property Act 1882 to all life, endowment and education policies in which a particular beneficiary is named.

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11. See paras. 5.36-5.37 above.

12. See para. 5.38 above.

12. Concurrent actions[13]

6.20 We provisionally recommend that implementing legislation should not deal with the question of concurrent actions in contract and tort.

13. Third party beneficiaries under wills[14]

6.21 We invite comments on how best, if at all, to deal with the question of improperly executed wills prejudicing prospective third party beneficiaries.

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13. See para. 5.39 above.

14. See paras. 5.40-5.44 above.

APPENDIX

CONTRACTS FOR THE BENEFIT OF THIRD PARTIES IN OTHER JURISDICTIONS[1]

1. The purpose of this appendix is to describe the law on third party rights in other jurisdictions. A systematic account of the law in the major common law and civilian systems would be a considerable enterprise which we have not sought to undertake. Throughout this paper, we have made references to foreign law when it was appropriate, usually to illustrate how different systems have dealt with the main issues to be faced under a reformed third party rule. The following does not purport to be anything more than an outline which brings together this comparative material. In the case of common law jurisdictions which have reformed the third party rule, we have generally confined our treatment to setting out the main statutory provisions with the minimum comment. In the case of civilian systems, we have considered French and German law, on which most other civilian jurisdictions have based their law.[2]

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1. See, generally, Dold, Stipulations for a Third Party: A Comparative Study with Special Reference to Continental Law (1948); Millner, "Ius Quaesitum Tertio: Comparison and Synthesis", (1967) 16 I.C.L.Q. 446.

2. Dold, op. cit., ch. 10.

Western Australia

2. Sections 11(2) and (3) of the Property Law Act 1969 implement the recommendations of the English Law Revision Committee:[3]

> "(2) Except in the case of a conveyance or other instrument to which subsection (1) of this section applies, where a contract expressly in its terms purports to confer a benefit directly on a person who is not named as a party to the contract, the contract is, subject to subsection (3) of this section, enforceable by that person in his own name but -
>
> (a) all defences that would have been available to the defendant in an action or proceeding in a court of competent jurisdiction to enforce the contract had the plaintiff in the action or proceeding been named as a party to the contract, shall be so available;
>
> (b) each person named as a party to the contract shall be joined as a party to the action or proceeding; and
>
> (c) such defendant in the action or proceeding shall be entitled to enforce as against such plaintiff, all the obligations that in the terms of the contract are imposed on the plaintiff for the benefit of the defendant.
>
> (3) Unless the contract referred to in subsection (2) of this section otherwise provides, the contract may be cancelled or modified by the mutual consent of the persons named as parties thereto at any time before the person referred to in that subsection has adopted it either expressly or by conduct."

3. In Westralian Farmers Co-op. Ltd. v. Southern Meat Packers Ltd,[4] W (acting as agent for the owners) sold to S 36 head of cattle. The contract of sale provided that:

> "To enable the agents (W) to protect themselves as del credere agents in the sale, the full purchase price shall be payable by the buyer to and be recoverable by the agents alone."

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3. (1937), Cmd. 5449.

4. [1981] W.A.R. 241; Longo, (1983) 15 W.A.L.Rev. 411.

The cattle were delivered pursuant to the contract, but S paid the owners. W, having already credited the owners' account with the purchase price less its commission, demanded payment from S who refused. The Supreme Court held that, on its true construction, W was the beneficiary of a contract between the owners and S, the benefit being that the full purchase price was payable to W. Although the joinder procedure did not prevent the promisor paying twice for the cattle, arguably S had only themselves to blame in disregarding the contractual payment term.

Queensland[5]

4. Section 55 of the Queensland Property Law Act 1974 states, inter alia:

> "(1) A promisor who, for a valuable consideration moving from the promisee, promises to do or refrain from doing an act or acts for the benefit of a beneficiary shall, upon acceptance by the beneficiary, be subject to a duty enforceable by the beneficiary to perform that promise.
>
> (2) Prior to acceptance the promisor and promisee may without the consent of the beneficiary vary or discharge the terms of the promise and any duty arising therefrom.
>
> (3) Upon acceptance -
>
> (a) the beneficiary shall be entitled in his own name to such remedies and relief as may be just and convenient for the enforcement of the duty of the promisor; and relief by way of specific performance, injunction or otherwise shall not be refused solely on the ground that, as against the promisor, the beneficiary may be a volunteer;
>
> (b) the beneficiary shall be bound by the promise and subject to a duty enforceable against him in his own name to do or refrain from doing such act or acts (if any) as may by the terms of the promise be required of him;

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5. See Vroegop (1984) 58 A.L.J. 5.

(c) the promisor shall be entitled to such remedies and relief as may be just and convenient for the enforcement of the duty of the beneficiary;

(d) the terms of the promise and the duty of the promisor or the beneficiary may be varied or discharged with the consent of the promisor, the promisee and the beneficiary.

(4) Subject to subsection (1), any matter which would in proceedings not brought in reliance on this section render a promise void, voidable or unenforceable, whether wholly or in part, or which in proceedings (not brought in reliance on this section) to enforce a promissory duty arising from a promise is available by way of defence shall, in like manner and to the like extent, render void, voidable or unenforceable or be available by way of defence in proceedings for the enforcement of a duty to which this section gives effect.

(6) In this section-

(a) "acceptance" means an assent by words or conduct communicated by or on behalf of the beneficiary to the promisor, or to some person authorised on his behalf, in the manner (if any), and within the time, specified in the promise or, if no time is specified, within a reasonable time of the promise coming to the notice of the beneficiary".

(b) "beneficiary" means a person other than the promisor or promisee, and includes a person who, at the time of acceptance is identified and in existence, although that person may not have been identified or in existence at the time when the promise was given;

(c) "promise" means a promise-

(i) which is or appears to be intended to be legally binding; and

(ii) which creates or appears to be intended to create a duty enforceable by a beneficiary,

and includes a promise whether made by deed, or in writing, or, subject to this Act, orally, or partly in writing and partly orally;

(7) Nothing in this section affects any right or remedy which exists or is available apart from this section."

5. By section 48 of the Insurance Contracts Act 1984:

"(1) Where a person who is not a party to a contract of general insurance is specified or referred to in the contract, whether by name or otherwise, as a person to whom the insurance cover provided by the contract extends, that person has a right to recover the amount of his loss from the insurer in accordance with the contract, notwithstanding that he is not a party to the contract.

(2) Subject to the contract, a person who has such a right -

(a) has, in relation to his claim, the same obligations to the insurer as he would have if he were the insured;[6] and

(b) may discharge the insured's obligation in relation to his loss.

(3) The insurer has the same defences to an action under this section as he would have in an action by the insured.

(4) Where a contract of life insurance effected by a person upon his own life is expressed to be for the benefit of a person specified or referred to in the contract, whether by name or otherwise, that second-mentioned person has a right to recover the moneys payable under the contract from the insurer in accordance with the contract notwithstanding that the second-mentioned person is not a party to the contract, and the moneys payable under the contract do not form part of the estate of the person whose life is insured and are not subject to his debts.

(5) Section 94 of the Life Insurance Act 1945 does not apply in relation to a policy within the meaning of that Act that is entered into after the commencement of this Act."

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6. Like section 55(3)(b) of the Queensland Act, section 48(2)(a) imposes obligations on the third party. Quaere how this obligation relates to the duty of disclosure?

6. The Insurance Contracts Act 1984 was made without retrospective effect, and thus could not be applied in Trident General Insurance Co. Ltd. v. McNiece Bros. Pty. Ltd.[7] Blue Circle had taken out a liability insurance policy with Trident to cover construction contracts. The insured was named as "Blue Circle Southern Cement Ltd., all its subsidiary associated and related companies, all contractors and sub-contractors and/or suppliers". Subsequently, McNiece were employed as subcontractors, and were responsible for the injury of an employee of another sub-contractor. McNiece claimed under the policy but the insurers refused to pay.

7. McNiece succeeded before the High Court of Australia,[8] in a decision which effectively reversed the decision of the legislature not to make the 1984 Act retrospective. However, a variety of reasons were given by the majority. Mason C.J., Wilson and Toohey JJ., all believed an exception could be created to the privity rule to allow third parties to sue, although their approach is confined to insurance contracts and possibly liability insurance. Two reasons were advanced. First, it would be unjust not to give effect to the contracting parties' intentions. Secondly, it was likely that third party beneficiaries would rely on the policy and not insure separately. Of the other judges, Deane J. supported the majority decision, but declined to create an exception to the rule. He preferred to make use of the trust doctrine to give the third party a right of action.[9] Gaudron J. sought

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7. (1988) 62 A.L.J.R. 508; Reynolds, (1989) 105 L.Q.R. 1.

8. Brennan and Dawson JJ. dissenting.

9. Deane J. also took the view that, in an appropriate case, if an insurer by his conduct induced a third party to act to his detriment on the assumption that he was effectively indemnified (or that he would in future be protected by the policy), the insurer might be estopped

to base P's cause of action on the principle of unjust enrichment on the ground that a promisor who has been paid for a promise to confer a benefit is unjustly enriched if he does not fulfil his promise. This novel approach appears to use unjust enrichment as a principle to protect contractual expectations rather than to restore benefits acquired "at the expense of" the plaintiff who, in this case, had not paid the premiums.[10]

8. Although the case does not create a general exception to the privity doctrine, it nevertheless reveals an antipathy amongst the Australian judiciary towards the third party rule.

New Zealand

9. The New Zealand Contracts and Commercial Law Reform Committee's Report on Privity of Contract led to the Contracts (Privity) Act 1982, the main sections of which are as follows:

"**2. Interpretation-** In this Act, unless the context otherwise requires,-

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9. Continued
from denying the enforceability of such indemnity. Cf. Argy Trading Co. Ltd. v. Lapid Developments Ltd. [1977] 1 W.L.R. 444, 456-457 (where P unsuccessfully argued that, by reason of representations made by an insurer, he had acted to his detriment by not taking out insurance cover) which re-iterates the orthodox view that estoppel by representation requires a representation of existing fact and that promissory estoppel is merely defensive in its operation.

10. Soh, (1989) 105 L.Q.R. 4; Jackman, (1989) 63 A.L.J. 368.

"Benefit" includes-

(a) any advantage; and

(b) any immunity; and

(c) any limitation or other qualification of-

(i) An obligation to which a person (other than a party to the deed or contract) is or may be subject; or

(ii) A right to which a person (other than a party to the deed or contract) is or may be entitled; and

(d) Any extension or other improvement of a right or rights to which a person (other than a party to the deed or contract) is or may be entitled.

4. Deeds or contracts for the benefit of third parties- Where a promise contained in a deed or contract confers, or purports to confer, a benefit on a person, designated by name, description, or reference to a class, who is not a party to the deed or contract (whether or not the person is in existence at the time when the deed or contract is made), the promisor shall be under an obligation, enforceable at the suit of that person, to perform that promise:

Provided that this section shall not apply to a promise which, on the proper construction of the deed or contract, is not intended to create, in respect of the benefit, an obligation enforceable at the suit of that person.

5. Limitation on variation or discharge of promise-

(1) Subject to sections 6 and 7 of this Act, where, in respect of a promise to which section 4 of this Act applies,-

(a) The position of a beneficiary has been materially altered by the reliance of that beneficiary or any other person on the promise (whether or not that beneficiary or that other person has knowledge of the precise terms of the promise); or

(b) A beneficiary has obtained against the promisor judgment upon the promise; or

(c) A beneficiary has obtained against the promisor the award of an arbitrator upon a submission relating to the promise,-

the promise and the obligation imposed by that section may not be varied or discharged without the consent of that beneficiary.

6. Variation or discharge of promise by agreement or in accordance with express provision for variation or discharge- Nothing in this Act prevents a promise to which section 4 of this Act applies or any obligation imposed by that section from being varied or discharged at any time -

(a) By agreement between the parties to the deed or contract and the beneficiary; or

(b) By any party or parties to the deed or contract if -

(i) The deed or contract contained, when the promise was made, an express provision to that effect; and
(ii) The provision is known to the beneficiary (whether or not the beneficiary has knowledge of the precise terms of the provision); and
(iii) The beneficiary had not materially altered his position in reliance on the promise before the provision became known to him; and
(iv) The variation or discharge is in accordance with the provision.

7. Power of Court to authorise variation or discharge-
(1) Where, in the case of a promise to which section 4 of this Act applies or of an obligation imposed by that section,-
(a) The variation or discharge of that promise or obligation is precluded by section 5(1)(a) of this Act; or
(b) It is uncertain whether the variation or discharge of that promise is so precluded,-
a Court, on application by the promisor or promisee, may, if it is just and practicable to do so, make an order authorising the variation or discharge of the promise or obligation or both on such terms and conditions as the Court thinks fit.
(2) If a Court-
(a) Makes an order under subsection (1) of this section; and
(b) Is satisfied that the beneficiary has been injuriously affected by the reliance of the beneficiary or any other person on the promise or obligation,-
the Court shall make it a condition of the variation or discharge that the promisor pay to the beneficiary, by way of compensation, such sum as the Court thinks just.

8. Enforcement by beneficiary-The obligation imposed on a promisor by section 4 of this Act may be enforced at the suit of the beneficiary as if he were a party to the deed or contract, and relief in respect of the promise, including relief by way of damages, specific performance, or injunction, shall not be refused on the ground that the beneficiary is not a party to the deed or contract in which the promise is contained or that, as against the promisor, the beneficiary is a volunteer.

9. Availability of defences-(1) This section applies only where, in proceedings brought in a Court or an arbitration, a claim is made in reliance on this Act by a beneficiary against a promisor.
(2) Subject to subsections (3) and (4) of this section, the promisor shall have available to him, by way of defence, counterclaim, set-off or otherwise, any matter which would have been available to him-

(a) If the beneficiary had been a party to the deed or contract in which the promise is contained; or
(b) If -
(i) The beneficiary were the promisee; and
(ii) The promise to which the proceedings relate had been made for the benefit of the promisee; and
(iii) The proceedings had been brought by the promisee.

(3) The promisor may, in the case of a set-off or counterclaim arising by virtue of subsection (2) of this section against the promisee, avail himself of that set-off or counterclaim against the beneficiary only if the subject-matter of that set-off or counterclaim arises out of or in connection with the deed or contract in which the promise is contained.

(4) Notwithstanding subsections (2) and (3) of this section, in the case of a counterclaim brought under either of those subsections against a beneficiary,-

(a) The beneficiary shall not be liable on the counterclaim, unless the beneficiary elects, with full knowledge of the counterclaim, to proceed with his claim against the promisor; and
(b) If the beneficiary so elects to proceed, his liability on the counterclaim shall not in any event exceed the value of the benefit conferred on him by the promise.

13. Repeal-Section 7 of the Property Law Act 1952 is hereby repealed.[11]

14. Savings-(1) Subject to section 13 of this Act, nothing in this Act limits or affects-
(a) Any right or remedy which exists or is available apart from this Act; or
(b) The Contracts Enforcement Act 1956 or any other enactment that requires any contract to be in writing or to be evidenced by writing; or
(c) Section 49A of the Property Law Act 1952; or
(d) The law of agency; or
(e) The law of trusts.

(2) Notwithstanding the repeal effected by section 13 of this Act, section 7 of the Property Law Act 1952 shall continue to apply in respect of any deed made before the commencement of this Act.

15. Application of Act-Except as provided in section 14(2) of this Act, this Act does not apply to any promise, contract, or deed made before the commencement of this Act.

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11. Section 7 of the Property Law Act 1952 stated: "Any person may take an immediate benefit under a deed although not named as a party thereto".

10. A detailed discussion of these provisions can be found elsewhere.[12] Our discussion will be confined to the following brief comments. The central section of the Act, section 4, provides that in order for a third party to have contractual rights, the agreement must be intended for his benefit and also be intended that he should be able to enforce that benefit. Nevertheless, whereas the definition of benefit in section 2 includes "any immunity" and so reveals an intention to cover exemption clauses as used in The Eurymedon,[13] section 4 arguably presupposes that it is the beneficiary bringing the action, and is perhaps not suited to cover the assertion of a benefit by way of defence.[14]

11. It does, however, appear that courts will require clear evidence of the contracting parties' intentions before allowing the third party to enforce a promise.[15] In Gartside v. Sheffield, Young and Ellis,[16] a testatrix gave instructions to the defendant solicitors to draw up a new will, in which she intended to benefit P. Before the will was completed the testatrix died, and probate was granted of her previous will. The New Zealand Court of Appeal held that P could not take advantage of the 1982 Act. There was no provision for the benefit of a third party in the contract between solicitor and client; the benefit would only arise

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12. See Newman, (1983) 4 Auckland Univ. L.R. 339; Cheshire, Fifoot & Furmston's Law of Contract (7th N.Z. ed., 1988), pp. 388-395.

13. [1975] A.C. 154.

14. Reynolds, (1985) 11 N.Z.U.L.R. 215, 221 n. 41. Cf. Coote, (1988) 13 N.Z.U.L.R. 160, 170.

15. Cheshire, Fifoot & Furmston, op. cit. (N.Z. ed.), p. 390.

16. (1983) N.Z.L.R. 37.

once the contract was executed. However, it is significant that P succeeded in a negligence action against the solicitor.

12. It has been suggested that third party beneficiary regimes, such as the New Zealand Contracts (Privity) Act 1982,[17] only envisage a third party enforcing performance of a contract's main obligation.[18] They would, accordingly, be unsuited to the facts of a case like Cavalier v. Pope,[19] where the wife of a tenant was injured as a result of the defective state of the landlord's leased premises. Clearly the wife would not have been intended to enforce the primary obligation of the contract, i.e. demand the lessor to deliver the leased premises. Instead, her claim would have to be based on a breach of a secondary obligation, for instance to keep the premises in repair. However, the reference in section 4 to "a promise contained in a contract" suggests that there may be more than one promise which confers a benefit. Therefore, the issue is whether the third party was intended to take the benefit of the particular promise in question. There is nothing in the wording of section 4 which prevents the application of the dual intention test to the lessor's obligation to keep the premises in repair, but not to other obligations.

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17. See Appendix, para. 9.

18. Markesinis, (1987) 103 L.Q.R. 354, 358 who however, uses the terms "primary" and "secondary" obligations. His use is not consistent with Lord Diplock's use of those terms in Photo Production Ltd. v. Securicor Transport Ltd. [1980] A.C. 827, according to which the duty to keep the premises in repair would be a primary obligation, nor with that of Coote, Exception Clauses (1964), p.3.

19. [1906] A.C. 428.

13. On the question of variation and discharge, there have been differing views. One commentator has warned against the perils of judicial discretion,[20] whilst another has welcomed the flexibility the new legislation provides.[21] However, the complexity of the scheme, coupled with the residuary judicial discretion, may be considered unattractive.

United States of America

14. There is a vast literature on third party rights in the United States,[22] which no short account can adequately summarise. The following merely highlights some of the main difficulties revealed by the case law.

15. Since the decision of the New York Court of Appeals in Lawrence v Fox,[23] it has become generally accepted that a third party is able to enforce a contractual obligation made for his benefit. However, the problem of defining what is meant by a third party beneficiary has never adequately been solved. Section 133 of the first Restatement of Contracts published in 1932 distinguished donee

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20. Newman, op. cit., p. 348.

21. Rogers, Essays in Contract (ed. Finn) (1987), p. 101.

22. See the standard accounts in Corbin and Williston, which well illustrate the complexity of American law, and also Summers, (1982) 67 Cornell L. Rev. 880; De Cruz, (1985) 14 Anglo-Am. L. Rev. 265; Prince, (1985) 25 Boston College L. Rev 919; Waters, (1985) 98 Harvard L. Rev. 1109. See also the Ontario Law Reform Commission's Report on Amendment of the Law of Contract (1987), pp. 55-58.

23. 20 N.Y. 268 (1859).

beneficiaries, creditor beneficiaries, and incidental beneficiaries: only donee and creditor beneficiaries could enforce contracts made for their benefit. A person was a "donee beneficiary" if the purpose of the promisee was to make a gift to him, or to confer upon him a right not due from the promisee. A person was a "creditor beneficiary" if performance of the promise would satisfy an actual or asserted duty of the promisee to him. A person was an incidental beneficiary if the benefits to him were merely incidental to the performance of the promise.

16. It became apparent that a number of third party beneficiaries did not fall within the "donee" and "creditor" categories,[24] such that some courts simply disregarded the categorisation approach and allowed beneficiaries to recover who were neither creditors nor donees.[25] The inflexibility of the categorisation approach led to changes in the second Restatement of Contracts published in 1981, under which intended beneficiaries, who can enforce contracts, are contrasted with incidental beneficiaries, who cannot. Section 302 of the Restatement (Second) provides:

> "(1) Unless otherwise agreed between promisor and promisee, a beneficiary of a promise is an intended beneficiary if recognition of a right to performance in the beneficiary is appropriate to effectuate the intention of the parties and either,

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24. In a private construction context, subcontractors were neither donee nor creditor beneficiaries: Summers, op. cit., p. 884.

25. Ibid.

(a) the performance of the promise will satisfy an obligation of the promisee to pay money to the beneficiary;[26] or

(b) the circumstances indicate that the promisee intends to give the beneficiary the benefit of the promised performance.[27]

(2) An incidental beneficiary is a beneficiary who is not an intended beneficiary."[28]

17. However, the Restatement (Second) fails properly to explain the distinction between intended and incidental beneficiaries, given that "the parties, or more simply the promisee, may intend a third party to receive a benefit but not intend that party to have standing to enforce that promise."[29] The "intent to benefit" test has, in practice, failed to achieve consistent results,[30] in particular in the field of public service contracts.[31]

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26. e.g. where B promises A to discharge a debt owed by A to C.

27. e.g. where B promises A to make a gift to C.

28. e.g. where B promises A to build a structure which has the effect of enhancing the value of C's land.

29. Prince, op. cit., p. 979.

30. There have been several varieties of the "intent to benefit" test: the contract must have been for the "sole and exclusive" benefit of the third party; the "primary intention" of the promisee must have been to benefit the third party; the contract must have been "necessarily" for the benefit of the third party; the direct benefit must have been "express or unmistakeable" or "sufficiently immediate": Prince, op. cit., pp. 934-937.

31. Fuzie v. Manor Care 461 F. Supp. 689 (N.D.Ohio 1977); Waters, op. cit., pp. 186-188.

18. Other difficult questions under the Restatement (Second) include the following. Should reference be made to the contract alone, or to all the prevailing circumstances when determining whether the appropriate intention exists? The case law is divided on this point, although the better view would appear to favour the latter option.[32] Another issue is that of whose intent is required. Section 302(1) refers to the intentions of the parties, although section 302(1)(b) refers to the promisee's intention. Different jurisdictions apply different tests:[33] one requires proof only of the promisee's intention; another focuses upon the intent of both parties; a third requires additionally that the promisor have reason to know of the promisee's intent to benefit a third party.[34]

19. On the question whether the contracting parties may vary or revoke their promise, section 311 of the Restatement (Second) provides that the contracting parties may create rights that cannot be modified, but that otherwise they are free to modify unless the beneficiary "materially changes his position in justifiable reliance on the promise or brings suit on it or manifests assent to it at the request of the promisor or promisee".

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32. See Prince, op. cit., pp. 926-931. In Beckman Cotton Company v. First National Bank of Atlanta (1982) 66 F. 2d 181, by considering the surrounding circumstances, the court was able to confer a right of enforcement on a third party beneficiary, although not named in the contract.

33. Prince, op. cit. p. 931.

34. On one view, only the promisee's intention should be relevant, since the promisor's motivation for entering into the contract will frequently be the consideration he receives from the promisee. However, this is not invariably so: the promisor may have an interest in seeing that the third party is benefited, as where he is a relative: Re Stapleton-Bretherton [1941] Ch. 482.

20. The Ontario Law Reform Commission[35] was influenced by the United States experience in rejecting a detailed legislative scheme. It recommended instead a general provision that no third party should be denied enforcement of a contract made for his benefit on the grounds of lack of privity or want of consideration. It concluded that the principal difficulties facing the draftsman of a specific provision were the definition of the class of beneficiaries entitled to sue, and the problem of variation by the original parties. On the former question, the Commission drew attention to the fact that the categories of donee and creditor beneficiary in the first Restatement of Contracts proved too restrictive, and also that the category of intended beneficiaries in the Restatement (Second), though flexible, abandoned the certainty which is supposed to be the chief merit of specific legislation. On the latter question, the Commission also criticised the Restatement (Second): why, for example, if reliance is the reason for enforcement, should recovery not be limited to protection of the beneficiary's reliance; and if the contract is one that would ordinarily allow for modification, why should the beneficiary's consent affect the matter?[36]

Ireland

21. The Irish Parliament made several reforms affecting married women in the Married Women's Status Act, No.5 of 1957, the general intent of which was to bring Irish law more closely into line with that of England. But in two particulars the Irish law goes further than the English. First, section 7 of the Irish Act, which replaces section 11

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35. Report on Amendment of the Law of Contract (1987), ch. 4.

36. Ibid., p. 71. See para. 5.30 above.

of the Married Women's Property Act 1882, applies not only to a policy of life insurance but also to an endowment policy; and whether "expressed to be for the benefit of" or "by its express terms purporting to confer a benefit upon" the wife, husband or child of the insured, such policies create trusts in favour of the objects named. Secondly, section 8 of the Act of 1957 creates a new species of third party rights by way of contract. It provides:

> "(1) When a contract (other than a contract to which section 7 applies) is expressed to be for the benefit of, or by its express terms purports to confer a benefit upon, a third person being the wife, husband or child of one of the contracting parties, it shall be enforceable by the third person in his or her own name as if he or she were a party to it.
> (2) The right conferred on a third person by this section shall be subject to any defence that would have been valid between the parties to the contract.
> (3) Unless the contract otherwise provides, it may be rescinded by agreement of the contracting parties at any time before the third person has adopted it either expressly or by conduct."

Scotland

22. Scots law recognises a ius quaesitum tertio, i.e. a right vested in a third party by a contract to which he was not privy. There are several requirements for the creation of such a right:

> "It must appear that it was the contracting parties' common object to benefit him and intention that the tertius should have a title to enforce the contract. This is shown by its being apparent that the stipulation was intended for his benefit and his being named or identified or referred to in the contract, and by delivery of the contractual document to the tertius, or putting it outwith the power of the original contractors to deal with it, as by registration for publication in the books of Council and Session, or intimation to the tertius, or the tertius having come under onerous engagements on the faith of his having a ius quaesitum. ... A ius quaesitum tertio can accordingly arise in any

case where it is apparent that an irrevocable intention of a contract between A and B was to benefit C."[37]

It can be seen that these requirements are strict. Furthermore, the Scottish common law on third parties' rights under contracts is not well developed and rests on statements by institutional writers and decisions by judges which have given rise to much academic debate.[38] These factors may explain why, in Junior Books Ltd. v. Veitchi Co. Ltd.,[39] the owner did not seek to argue that he was a third party beneficiary of the contract between the contractor and sub-contractor.

23. The question of stipulations in favour of third parties has been considered by the Scottish Law Commission.[40]

(i) The Commission considered the question of revocation,[41] and the choice between whether terms in favour of third parties should be presumed to be irrevocable unless a contrary intention be proved, or whether they should be

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37. Walker, The Law of Contracts and Related Obligations in Scotland (2nd ed., 1985), pp. 455-458.

38. Bulk Goods: section 16 of the Sale of Goods Act 1979 and section 1 of the Bills of Lading Act 1855, Scot. Law Com. Discussion Paper No. 83 (1989), para. 3.9.

39. [1983] 1 A.C. 520.

40. Scot. Law Com. Memorandum No. 38, Constitution and Proof of Voluntary Obligations: Stipulations in Favour of Third Parties (1977).

41. Irrevocability is a condition, not a consequence, of a ius quaesitum tertio, such that if a right is revocable, there can be no ius quaesitum tertio: Walker, op. cit., pp. 456-458, though this is a controversial question: see also McBryde, The Law of Contract in Scotland (1987), p. 412 ff.

presumed to be revocable in the absence of a proven intention to treat them as irrevocable.[42] The Commission concluded that if a contract contains a term in favour of a third party, then unless the parties have provided in the contract for the cancellation or variation of that term, it should be irrevocable except with the consent of the third party. This would mean that a third party's acceptance of, adoption of, or reliance on a promise would be irrelevant.

(ii) The Commission also recommended that any defences (apart from those not connected with the contract) available to a promisor against a promisee should also be available against a third party.

(iii) On the question whether the promisee who has retained no interest in performance can sue the promisor if the latter fails to implement his obligation to the third party, the Commission made no recommendation. However, it envisaged that if the promisee did have a right of action to enforce a term made in favour of a third party, he could only do so in a representatitve capacity, i.e. as the third party's agent and therefore not against his wishes.

France[43]

24. Under Article 1119 of the Civil Code, an agreement between a promisor and promisee (or stipulator) which is intended to benefit or bind a third party is ineffective even as between the contracting parties. Article 1165 states that agreements have effect only between the parties to them

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42. MacCormick, (1970) J.R. 228, 236.

43. See, generally, Nicholas, French Law of Contract (1982), pp. 164-193; Weill and Terre, Droit Civil: les obligations (1990, 4th ed.)

and can neither benefit nor bind a third party. However, by way of exception, Article 1121 states:

> "One may likewise stipulate for the benefit of a third party, when such is the condition of a stipulation which one makes for oneself or of a gift which one makes to another. He who has made such a stipulation cannot revoke it if the third party has declared his wish to take advantage of it."[44]

25. Article 1121 creates two exceptions to the third party rule. First, where the promisee inserts a penalty clause into the contract whereby the promisor agrees to make payment to the promisee in the event of non-execution of a promise in favour of a third party. Secondly, where the promisee makes a donation to the promisor on condition that the promisor pays an annuity to a third party (the donatio sub modo of Roman law), the third party can enforce the stipulation made for his benefit.[45] Indeed, largely in order to regulate contracts of life assurance,[46] the courts have succeeded in transforming the limited exceptions in Article 1121 into a general principle that wherever there is an agreement between the promisor and promisee which is intended to confer a benefit on a third party, the latter can claim the benefit from the promisor. Third party rights, however, are subject to the promisor setting up any defences which he would have had against the promisee,[47] and to unilateral revocation by the promisee.[48]

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44. See also Article 1029 of the Quebec Civil Code.

45. See Amos and Walton's Introduction to French Law (3rd ed., 1967), p. 176, for other examples.

46. See now: Loi du 13.7.1930, art. 67.

47. Nicholas, op. cit., p. 180.

48. Ibid., p. 187.

26. One difficulty which has arisen is the question of an implied promise for a third party, a device which was developed to provide a remedy for a party whose claim might otherwise fail in delict. However, there has been little discussion of the test to decide whether such a promise exists. In one case, a blood transfusion centre provided a blood donor to a hospital for a specific patient, P. The donor had syphilis which was transmitted to P, to whom the centre was held contractually liable on the ground of an implied stipulation for his benefit. One suggestion has been that the criterion is one of remoteness or foreseeability.[49] The true details remain largely concealed within the wide discretion exercised by the courts.

27. Recent developments have seen the implied promise for a third party extended to cover cases involving economic loss.[50] An expansion of the area of contractual liability has also been achieved by two other techniques. The so-called "action directe" stems from Article 1641 of the Civil Code. If manufacturer A sells his product to B, who re-sells to C, A remains contractually liable if C suffers loss from latent defects. This has been adapted to the situation where B purchases A's product to do work for C,[51] and was taken further when such a situation was stated to fall within the realm of the ordinary law of contract and beyond the special scheme of Article 1641 with its much

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49. Ibid., p. 186: quaere whether the stipulation would have applied to other non-specified patients in the hospitals, or (more remotely) to one who caught syphilis from P?

50. Cass. civ. 21.11.1978 and Cass. civ. 14.6.1989.

51. Cass. civ. 29.5.1984.

shorter limitation period.[52] Further erosion of the contract-delict boundary has occurred with the emergence of the concept of a "groupe de contrats". This "groups" together individual contracts which are factually connected. In the construction industry, for example, this might link main contractors, subcontractors, architects and suppliers. Any claim by a party with some contractual link into this group would be governed by contractual principles, even in the absence of a contract between the victim and the member of the group who actually caused the loss.[53]

Germany[54]

28. Article 328 of the German Civil Code, the Bürgerliches Gesetzbuch (BGB), contains the notion of contracts for the benefit of third parties:[55]

> "One can stipulate by contract for a performance to a third party with the effect that the latter acquires the direct right to demand performance. In the absence of

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52. See the decision of the Assemble Pleniaire of 7.2.1986, as confirmed in Cass. civ. 8.3.1988.

53. Cass. civ. 1.6.1988.

54. For an introduction to the German law on third party rights, see E.J. Cohn, Manual of German Law, 2 Vols. (1968, 1971); Fleming, "Comparative Law of Torts", (1984) 4 O.J.L.S. 235, 238-240; Lorenz, "Some thoughts about contract and tort", in Essays in Memory of Professor F.H. Lawson (1986), p. 86; Markesinis, "An Expanding Tort Law - The Price of a Rigid Contract Law", (1987) 103 L.Q.R. 354, 356-371; Markesinis, The German Law of Torts (2nd ed., 1990), pp. 43-50. See also ch. 4 of the Israeli Contracts (General Part) Law 1973, which is based on German law, and Shalev, (1974) 9 Is. L. Rev. 274; (1976) 11 Is. L. Rev. 315; (1978) 13 Is. L. Rev. 474.

55. Verträge zugunsten Dritter.

any special disposition, it must depend on the circumstances, and particularly on the object of the contract, whether such third party acquires any right, whether such right of the third party accrues forthwith or only in certain contingencies, and whether power is reserved to the contracting parties to cancel or alter the right of such third party without his consent."[56]

29. Since it may be inappropriate that the third party should be able to demand specific performance or claim damages when the promisor is not obliged to render him performance,[57] the courts have developed the idea of contracts with protective effects vis-a-vis third parties[58] and the idea of shifting loss.[59] In the case of contracts with protective effects, the ambit of the contract is extended in favour of third parties who, though not being entitled to demand performance of the contract, are entitled to sue in respect of misperformance.[60] The notion of shifting or transferred loss is designed to prevent a situation arising whereby, as a result of the shifting of loss from a contracting party to a third party, the person

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56. Translation by Dold, op. cit., pp. 128-129.

57. On the facts of Ross v. Caunters [1980] Ch. 297, the lawyer was contractually obliged to make the will to the testator alone. Likewise, if B agrees with A to value some land which is to be bought by C, it is arguable that only A should be able to require B to carry out the valuation, although in the event of misperformance which affects C, the latter should arguably be able to claim the benefit of the contract.

58. Verträge mit Schutzwirkung zugunsten Dritter.

59. Drittschadensliquidation.

60. Markesinis, The German Law of Torts (2nd ed., 1990), p. 46. In Junior Books, although the sub-contractor's undertaking was not intended to confer a direct right to performance on the building owner, the head contractor's duty of protection to the owner could give protective effect to the sub-contractor's undertaking: Fleming, op. cit., p. 240.

with standing to sue has suffered no loss and can recover only nominal damages whereas the person who has suffered loss has no standing to sue. It enables the third party to vindicate a legally protected interest in lieu of the promisee.[61]

Roman-Dutch law

30. Although Roman law had a strict notion of privity of contract,[62] stipulations in favour of third parties may be enforced by the latter under modern South African law.[63]

> "The concept ... has proved of immense practical value, being applicable in an almost unlimited variety of situations including such diverse promises as: on behalf of an unformed company; to a chief for the benefit of his people; between a township developer and purchasers for the benefit of present and future lotholders; ensuring that a medical practitioner will be paid for attending a servant; facilitating a form of representative action; enabling a named beneficiary to claim on a life policy."[64]

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61. Fleming, op. cit., p. 239. Cases which could be solved by this theory include Ross v. Caunters [1980] Ch. 297, where the contract was made between the testator and solicitor in circumstances where the loss was suffered by the disappointed beneficiary, and The Aliakmon [1986] A.C. 785, where the contract was made between shipper and carrier but where by reason of a transfer of risk, the ultimate buyer suffered the loss. In the Court of Appeal ([1985] Q.B. 350), Robert Goff L.J. developed a theory of transferred loss with the important difference (in view of the third party rule) that it would have allowed a tort action to the third party.

62. Nicholas, An Introduction to Roman Law (1962), p. 199.

63. See The Law of South Africa, Vol. 5 (ed. Joubert), para. 165.

64. Christie, The Law of Contract in South Africa (1981), p. 258.

31. The third party acquires a right only when he accepts the stipulation in his favour, whether by express communication or otherwise depending on the circumstances.[65] In this respect, South African law is similar to the Queensland legislation.[66]

65. See Millner, (1967) 16 I.C.L.Q. 446, 450-1.

66. See para. 4 above.

OTHER JURISDICTIONS: A SUMMARY

	Eire	France	Germany	Western Australia	Queensland	New Zealand	USA 2nd Restatement
1. Scope of Legislation	Contracts made for the benefit of spouse or children of the contracting parties.	General right created by Art. 1121 of civil code and subsequent case law.	Art. 328 enables TP to enforce primary obligations of contract. Theory of contracts with protective effects gives further protection to TP.	General - subject to exceptions, notably conveyancing.	General - includes oral promises.	General - includes oral and implied promises.	General.
2. Rights which can be created in favour of TP	Enforcement of promise.	Direct right of enforcement.		Enforcement of promise.	Enforcement of promise.	Enforcement of promise. Benefit of a promise specifically defined to include "immunities".	Enforcement of promise.
3. Identification of TP (a) Express/ Named				Yes		Yes	

	Eire	France	Germany	Western Australia	Queensland	New Zealand	USA 2nd Restatement
3 Identification of TP (cont'd)							
(b) Existence at time of promise		Not necessary except in the case of gratuitous promises.			Not necessary	Not necessary	Not necessary
(c) Implied					Yes	Yes	Yes
(d) Designated						Yes	
4. Test of enforceable benefit							
(a) Intent to benefit				Yes			
(b) Intent to benefit and create right of enforcement					Yes	Yes	Yes
(c) Contract creates a benefit for TP							
5. Defence against TP							
(a) Defences under the contract	Yes	Yes	Yes	Yes	Yes	Yes	Yes

	Eire	France	Germany	Western Australia	Queensland	New Zealand	USA 2nd Restatement
5. Defence against TP (cont'd) (b) Set-offs against promisee	Yes, and not limited to set-offs arising out of the contract.					Yes, but limited to those arising out of the contract conferring the right.	Yes, but limited to those arising out of the contract conferring the right.
6. Variation and Cancellation	Yes, before TP *adopts* the contract.	Yes, before TP *accepts* the contract. Further, a promisee can *unilaterally* revoke the contract.	Revocability is determined by the contract and the circumstances surrounding it.	Yes, before TP *adopts* the contract.	Yes, before TP *accepts* the contract.	Yes, until TP has *materially altered* his position in reliance on the promise, or has obtained judgement thereupon.	Yes, until TP changes his position in reliance on the promise *or* brings suit on it *or* assents to it.
7. Rights of Suit for promisee		Promisee can demand performance. Cannot sue for loss suffered by TP, but can enforce a penalty under which promisor obliged to make payment in the event of non-execution.	Promisee can demand performance to TP.				Promisee cannot recover damages suffered by TP, but may be able to sue for specific performance.

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