CHAPTER - 4

RATIONALE AND AN APPRAISAL OF THE
COMMON LAW RULE

The case for the common law rule rests on a number of factors, First, although consideration has been provided for the promise, it has not been provided by the third party. Secondly, it is unjust that person could sue on a contract but not be sued upon the contract. Thirdly, if third parties could enforce contracts made for their benefit, the rights of the contracting parties to vary or terminate such contracts would be affected. Fourthly, it is undesirable for the promisor to be liable to two actions from both the promisor and the third party, and the privity rule limits the potential liability of a contracting party to a wide range of possible third claimants. The law Commission did not regard any of these explanations as convincing justifications of the rule. Those who favour the common law rule also point out that it is not absolute. The Courts and the legislature have created exceptions to avoid perceived injustice. It must also be remembered that the rule only precludes the third party from proceeding in contract. Where it is possible to base a claim on some other cause of action, for instance in tort or based on a property right, proceedings may

3 Privity  of Contract : Contracts for the Benefit of Third Parties, Law Com; C.P. No. 121 (1991), S 4.4; Law Com. No. 242 S 3.1.
succeed. Proceedings may also succeed if the Court can discern a collateral contract between the third party and the promisee under the main contract for the benefit of the third party.

4.1 AN APPRAISAL OF THE THIRD PARTY RULE

The considerable criticism of the principle that a third party cannot acquire rights under a contract has been discussed as follows. Its desirability as a matter of policy has been questioned by judges, law reform bodies, and commentators. Its pedigree has also been criticized on the ground that it was doubtful that the nineteenth century cases on which it is based in fact established its existence and that it was only a rule of procedure. It is said that it serves only to defeat the legitimate expectation of the parties and the third party, who often organize their affairs on the faith of the contract; that it undermines the social interest of the community in the security of bargains; and that it is commercially inconvenient. Above all it defeats the intentions of the parties to the contract.

Firstly the third party rule prevents effects being given to the intentions of the contracting parties. If remedy is denied to the third party

9 For difficulties in construction and insurance contracts, see Law Com. No. 242 (1996), 3.10.-3.27.
when the contracting parties intended it to be so, it frustrates their intentions. **Secondly**, it causes injustice to the third party who may have relied on the contract to regulate his affairs, and thus upsets the reasonable expectations of the third party to the benefit under the contract. **Thirdly** such a third party who suffers a loss cannot sue, and the promisee who has suffered no loss can. **Fourthly** therefore, the third party who suffers loss cannot claim compensation, and the promisee not having suffered any loss can claim nominal damages only. **Fifthly** even if the promisee were to obtain a satisfactory remedy, he may not be able to, or may not wish to sue.

Lastly the third party rule causes difficulties in commercial life, particularly where transactions and projects involve a 'network' of contracts allocating risks, responsibilities and liabilities between the parties.\(^\text{10}\) In the standard situation the person who has suffered the loss cannot sue, while the person who has suffered no loss can sue but may be able to obtain only nominal damages. Where the object of the contract is to benefit the third party, the effect of this is tantamount to ruling that the object of the contract is unenforceable.

**THIRD PARTY RULE CAUSES DIFFICULTIES IN COMMERCIAL LIFE**

The third party rule nowadays causes real difficulties in commercial life. There are two types of contract (i) constructions contracts and (ii) insurance contracts– to illustrate some of the difficulties caused by the

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rule\textsuperscript{11} discussed as follows.

\subsection*{4.1.1 CONSTRUCTION CONTRACTS}

Both simple construction contracts involving only an employer and a builder, and complex construction contracts involving several main contractors, many subcontractors and design professionals are affected by the third party rule. Simple construction contracts illustrate the difficulties which can arise when one contracting party agrees to pay for work to be done by another contracting party which will benefit a third party to the contract. Say, for example, a client contracts with a builder for work to be done on the home of an elderly relative. If the work is done defectively, it is only the client who has a contractual right to sue the builder for its failure to deliver the promised performance. On traditional principles, and subject to the decisions in \textit{Linden Gardens trust v. Lenesta Sludge Disposals Ltd.}\textsuperscript{12} and \textit{Darlington BC v. Wiltshier Northern Ltd.}\textsuperscript{13} the client can often only recover nominal damages, since he or she will have suffered no direct financial loss as a result of the builder's failure to perform. The elderly relative could not himself or herself sue for breach of contract, and the tort of negligence does not normally allow the recovery of pure economic loss.\textsuperscript{14} Therefore the elderly relative could not recover the cost of repairs in the tort of negligence and, if forced to move to alternative accommodation while the repairs were being carried out, could not recover

\textsuperscript{11} For practical difficulties in relation to shipping contracts (but see now the Carriage of Goods by Sea Act 1992), sale of goods contracts, contracts to pay money to a third party and contractual Licenses, see Consultation Paper No. 121, paras 4.8-4.11, 4.19-4.21, 4.23-4.24, 4.26.


\textsuperscript{13} [1995] 1 WLR 68.
consequent loss and expense either.

In complex construction projects, there will be a web of agreements between the participants in the project, allocating responsibilities and liabilities between the client (and sometimes its financiers), the main contractor, specialist sub-contractors and consultants (architects, engineers and surveyors). Most significant construction projects in the UK are carried out under one of three major contractual procurement routes,\(^{15}\) and so the documentation used is very often highly standardised.

The third party rule means that only the parties within each contractual relationship can sue other. The unfortunate result is that one cannot in the 'main' contracts simply extend the benefit of the architect's and engineer's duties of care and skill, and the contractor's duties to built according to the specifications, to subsequent purchases of or tenants of the development, or to funding institutions who might suffer loss as a result of the defective execution of the works. This cannot be achieved under the present third party rule without either joining the third party in question into the contract which constrains these obligation, which in the case of a subsequent purchaser or tenant is impractical, since their identity may be unknown at the of the duties in commencement of the works, or even for a long time afterwards, or executing a separate

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15 In 1987, 52% of work was undertaken on lump sum contracts with bills of quantities, whether for private or public clients, such as the Joint Contracts Tribunal Standard Form of Building Contract, 1980 edition ("JCT 80") or the JCT Intermediate Form of Contract, 1984 edition ("IFC 84"). 12% of work was carried out on design and build contracts, such as the JCT Standard Form of Building Contract with Contractor's Design, 1981 edition ("CD81"). 9% was carried out under management works contracts, such as the JCT Management Works Contract, 1987 edition ("MC 87"). The method of procurement will depend on factors such as the design route chosen for the project, the client's objectives and requirements, the funding arrangements chosen, and external factors such as economic risk and demographic trends: Ashworth, Contractual Procedures in the
document—a "collateral warranty"—extending the benefit question. Were it not for these collateral warranties, the third party rule would prevent contractual actions by subsequent owners of completed buildings against the architect, engineer, main contractor or subcontractor whose defective performance may have caused loss or damage to them.\textsuperscript{16}

In an effort to overcome the privity deficiency of the law of contract, attempts were earlier made by subsequent owners of defective premises to sue in tort, and the expansion of the categories of negligence following \textit{Hedley Byrne & Co. Vs. Heller & Partners Ltd.},\textsuperscript{17} and particularly \textit{Anns v. Merton London Borough Council},\textsuperscript{18} initially resulted in such claims being successful.\textsuperscript{19} However, the law is now set against the recovery in negligence of economic loss caused by defective construction. In \textit{D & F Estates Ltd. v. Church Commissioners for England},\textsuperscript{20} it was held that a builder was not liable in tort to a subsequent purchaser in respect of the cost of repair of defects to a building. The House of Lords then overruled \textit{Anns v. Merton LBC in Murphy v. Brentwood District Council}\textsuperscript{21} in holding that a local authority, which negligently failed to ensure that the builder complied with relevant by-laws and building regulations, owed no duty of care in tort as regards defects in the building causing pure economic loss; and, in a decision handed down on the same day, confirmed

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16  Similar problems apply when the third parties seeking rights of suit are tenants with full repairing leases, and who are therefore under a contractual obligation to the landlord of the building to maintain its fabric.
17  \cite{1964} AC 465.
18  \cite{1978} AC 728.
20  \cite{1989} AC 177.
21  \cite{1991} 1 AC 398.
}\end{footnotes}
the approach taken in the D & F Estates Ltd. case in relation to builders. As a result of these cases, a subsequent owner or purchaser now has little protection in tort.

A typical collateral warranty given by an architect, engineer or main contractor excludes consequential economic loss and limits the defendant’s liability, having regard to other claims of the warrantee, to a just and equitable proportion of the third party’s loss. The warranty will normally permit assignment by the finance house, purchaser or tenant without any consent of the warrantor being required. These collateral warranties are generally supported by separate nominal consideration or are made under deed and thus are not tied to consideration in the main contract. It is important to add that, where the benefit of the obligations undertaken by the warranty are assigned to sub-financiers or further purchasers or tenants down the line, this can give rise to further difficulties arising from the law of assignment. In particular, there is the difficulty as to whether an assignee can recover full damages, which was in issue in *Linden Gardens Trust Ltd. v. Lenesta Studge Disposals Ltd.* and *Darlington Borough Council v. Wiltshier Northern Ltd.* and which led to the application, and extension, of an exception to the normal rule on quantification of damages.

These reforms would enable contracting parties to avoid the need for collateral warranties by simply laying down third party rights in the main contract. Moreover, proposed reforms would enable the contracting parties

to mirror the terms in existing collateral warranties. Although this involves 'jumping ahead' to some details of our proposed reforms, it is worth explaining this latter point in some details. There is no reason why the architects', engineers' and contractors' liability to the third party could not be limited, as it presently is under collateral warranty agreements, so as to exclude consequential loss and so as to be limited, as it presently is under collateral warranty agreements, so as to exclude consequential loss and so as to be limited to a specified share or a just and equitable share of the third party's loss.\textsuperscript{25} As regards defences, a claim by a third party will be subject to defences and set-offs arising from, or in connection with, the contract and relevant to the particular contractual provision being enforced by the third party and which would have been available against the promisee. But this is a default rule only and the contracting parties can provide for a wider or a narrower sphere of operation for defences and set-offs, if they so wish. So the present position under collateral warranties, whereby the claim is subject to defences arising under the main contract, is, or can be, replicated. What about variation of the contract by the original contracting parties? A collateral warranty, once executed, may not be varied without the consent of the benefited third party purchaser, tenant or finance house. The Proposals are, on the face of it, more flexible in that the contracting parties can vary the contract without the third party's consent until the third party has relied on the contract or has

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\textsuperscript{23} \citeyear{1AC85}.
\textsuperscript{24} \citeyear{1WLR68}.
\textsuperscript{25} In contrast to limitations warranties, limitation clauses will not be subject to ss. 2(2) or 3 of the Unfair Contract Act 1977 where an action is brought by a third party under our proposed Act: see paras 13.9-13.13
\end{flushright}
accepted it. In practice, however, this ability to vary is not likely to be of any great advantage to the contracting parties because, assuming that the promisor could reasonably be expected to have foreseen that the third party would rely on the contract, they would only be certain that it was safe to vary or cancel the original contract if they first communicated with the third party to ensure that there has been no reliance. It should be stressed that when we refer to variation, we are referring to variation of the contract. The work in building contracts is commonly subject to variation and, if so, would obviously continue to be variable irrespective of the third party’s reliance or acceptance. A further advantage of the legislative reform, as against collateral warranty agreements, is that it would not be necessary to assign the benefit of a provision extending the contractor’s or architect’s duty of care to sub-financiers and other purchasers and tenants down the line, since these persons could simply be named as potential beneficiaries. Thus, the difficulties caused by quantification of damages in claims under assigned collateral warranty agreements would be entirely removed.

The main contact between the client and main contractor may also contain exclusion clauses limiting the liability of the main contractor for certain types of defective performance. The main contractor may have entered into these clauses on its own behalf and on behalf of subcontractors, in an effort to enable subcontractors to take advantage, in actions against them in the tort for negligence, of the limitations and exemptions contained in such clauses. As we have seen, the exception to
the third party rule, developed in **New Zealand Shipping Ltd. Vs. A.M. Satterthwaite & Co. Ltd.**,\(^{26}\) may not necessarily work in this context albeit that the courts have sometimes allowed third parties to take advantage of the exclusion clause by regarding it as negativing the duty of care that would otherwise have arisen.\(^{27}\) A reform of the privity rule would permit contractors and clients straight forwardly and uncontroversially to extend the benefit of exclusion clauses in their contract to employees, subcontractors and others.

Further problems may arise as regards payment obligations. At present, when a main contractor fails to pay a subcontractor for work performed, the subcontractor will have no right to sue the client directly for payment, although the client will be entitled to take the benefit of the subcontractor's work. It may be that the participants in a construction project might wish to provide for payment direct by the client to the subcontractor for work performed under a subcontract,\(^{28}\) and to give the subcontractor a corresponding right to sue the client for the agreed sum once the work is performed. Even if such a right were expressly provided for, the present third party rule would prevent such an express term from being enforceable by the subcontractor against the client, unless the subcontractor and client are in a contractual relationship.

Employers may make arrangements with contractors who are designed by both parties to benefit neighbours with regard to issues such

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28 JCT 80 (clauses 35.13.3-35.13.5) and Form NSC (Employer/ Nominated Subcontractor’s Agreement) 2a,
as noise, access and working hours. The intended recipients of these
benefits may be protected via the tort of nuisance but reform of the third
party rule would enable the parties to give the neighbours the right to
enforce the contract which gives them additional, and often significantly
better, protection than in tort.

The attention has also recently been drawn to the difficulties caused
by the third party rule in the offshore oil and gas industry, which provide
an excellent example of the anomalies and inconsistencies generated by the
rule in practice. It can be understand that for many years, major oil
companies and their advisers have attempted to minimize litigation arising
from drilling contracts in the North Sea. This has largely been achieved by
the use of cross indemnities between oil companies and contractors, which
to be effective, must not only benefit the parties to the contracts in
question but also all other companies in their respective groups, their
employees, agents, sub-contractors and co-licensees. This is because, for
example, it will often be unclear at the outset of a project which member of
a client company’s group will operate a platform and will thus be caused
loss by any failings on the part of the contractor. An indemnity should
therefore ideally benefit all companies likely to be affected. It is generally
impractical for more than a handful of the beneficiaries of the indemnities
given to be made parties to the contract. Moreover, careful drafting of the
indemnity is necessary to ensure that those made parties to the indemnity
can recover losses actually sustained by other group companies and

clause 6(1), create a duty on the part of the client to pay nominated subcontractors direct.
beneficiaries. At present therefore, the third party rule is circumvented by making the parties to the contract agents or trustees for the other beneficiaries. Some devices used have become even more complex than those commonly employed in the construction industry, with webs of mutual cross-indemnities, back to back indemnity agreements, and incorporation of all main contract provisions into sub-contracts. The contractors and employers should straightforwardly extend the benefit of indemnity and exemption clauses contained in a contract to other companies in a group, employees, sub-contractors and others.

4.1.2 INSURANCE CONTRACTS

There are several common situations where one party takes out an insurance policy for the benefit of another. The third party rule would prevent the third party enforcing the contract of insurance against the insurer. The inconvenience of this has led to a number of statutory inroads. For example, by section 11 of the Married Women’s Property Act 1882, a life insurance policy taken out 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 named in the policy. By section 148(7) of the Road Traffic Act 1988 a person covered by a liability insurance policy for motor accidents, even though taken out by someone else (for example, by a spouse or employer) is able to enforce that policy against the insurer. And under other legislation dealing, for example, with fire insurance and situations where the insured party becomes insolvent, third parties are given rights to enforce insurance contracts even though they are not expressly designated in them.
There are, however, still a number of insurance contracts where legislation has not intervened to give third party beneficiaries a right to enforce the contract against the insurer. For example, a life insurance policy taken out for the benefit of dependants other than spouses and children, for example a co-habitee or a parent or a parent or a stepchild, falls outside the **Married Women's Property Act 1882** and appears, therefore, not to be enforceable by those dependants. If a company takes out liability insurance covering the liability of its subsidiary company, and its contractors and sub-contractors, only the company itself would have the right to enforce the insurance contract.29

Again, if an employer takes out private health insurance, to cover medical expenses, on behalf of its employees, the employees would have no right to enforce the insurance contract so as to ensure reimbursement of expenses incurred.30 If in these circumstances the employer is insolvent or, because of a transfer of undertakings, has no interest in the contract, the employee has no legal standing to force the insurance company to pay in the event of a claim under the policy and the liquidator in the employer's insolvency may not wish to pursue such a claim. Even if the employer is solvent and wishes to sue, the employer may have difficulty in securing an adequate remedy as, in an action for damages, it can normally only recover its own loss which will usually be nil.31

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31 These types of situation are not within the strict ratio of Linden Garden Trust Ltd. v Lenesta Sludge Disposals Ltd. [1994] 1 AC 85 or Darlington Borough Council v. Wiltshire Northern Ltd. [1995] 1 WLR 68 (discussed above in paras 2.39-2.46). However they might appear to fall within the scope of these decisions, in that it was envisaged that the fruits of the contract would be enjoyed by a third party, and “it could be foreseen that damage caused by a breach would cause
In Australia, section 48 of the Contracts Act 1984 allows third parties to enforce insurance contracts where they are named as beneficiaries or as "covered by the policy". Nevertheless this reform proposals will enable an insurer and assured, by an express term, to confer enforceable rights on third parties (for example, employees): and contracts of insurance which purport to confer a benefit on an expressly designated third party will be enforceable by third party subject to this being contrary to the parties' intentions on a proper construction of the contract.

4.2 THE PRESENT LAW AND REFORM IN THIRD PARTY RULE

The abrogation of the third party rule by the Law Revision Committee in England, legislative reforms in New Zealand and in some jurisdictions in Australia, which have been discussed below.

4.2.1 THE BRITISH LAW REVISION COMMITTEE REPORT

In 1937, the Law Revision Committee, chaired by Lord Wright MR, presented its Sixth Interim Report.32 Among the topics addressed by the Committee in this Report was the common law’s rejection of a ius quaesitum tertio. It is recommended by the British Law Revision Committee. The Committee’s Report stated that England was almost alone among modern systems of law in its rigid adherence to the application of the third party rule, and that experience had demonstrated that the rule was apt to lead to hardship thus necessitating exceptions from it.33 The

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32 Law Revision Committee, Sixth Interim Report, para 41.
33 Law Revision Committee, Sixth Interim Report, para 41.
Committee regarded the trust exception, illustrated by the line of cases following **Tomlinson v. Gill**, as the most important, and said that, if this doctrine had been applied in all cases, it would be possible to say that English law did have a *ius quaesitum tertio*. However the application of the exception had been limited by other cases, and therefore "the law on this point is uncertain and confused. For the ordinary lawyer it is difficult to determine when a contract right 'may be conferred by way of property', in Viscount Haldane's phrase, and when it may not." The Report concluded that "there is a strong argument for attempting to frame a rule which will be more easily understandable". A further practical reason was that the enforcement of a *ius quaesitum tertio* by way of trust involved the addition of the trustee as a party to all legal proceedings to enforce the trust, which was wasteful and unnecessary, as the third party's position was more analogous to an assignee of a contractual right than to a beneficiary of a trust.

The Committee then went on to consider the circumstances in which
third party rights should arise, and considered that there should be three important limitations have been discussed.

Firstly, no third party right should be acquired unless given by the express terms of the contract. Secondly, the promisor should be able to raise any defences against the third party which he or she would have been able to raise against the promisee. Thirdly, the right of the promisor and promisee to vary or cancel the contract at any time should be preserved unless the third party had received notice of the agreement and had adopted it either expressly or by conduct. The Committee therefore recommended 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 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.

The Committee also recommended that the provisions of section 11 of the Married Women’s Property Act, 1882, should be extended to all life, endowment and education policies, in which a particular beneficiary is named.

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38 The Law Revision Committee was adamant that no third party right should be acquired by implication (eg. because the performance of the contract would benefit the third party), See Law Revision Committee, Sixth Interim Report, para 47.
39 Law Revision Committee, Sixth Interim Report, para 48.
40 Law Revision Committee, Sixth Interim Report, para 49. In its section on consideration, the Law Revision Committee included a recommendation that the rule that consideration must move from the promisee should be abolished: see para 37.
The Report of the Law Revision Committee was directly influential in promoting reform to the third party rule in Western Australia which, like Queensland, did not have a separate Law Reform Commission Report on the third party rule before introducing reform. However, its recommendations on the third party rule (and on the doctrine of consideration) have, of course, not been implemented in England.\(^{41}\)

**4.2.2 ABORPTION OF THIRD PARTY RULE IN ORDER COMMON LAW JURISDICTIONS**

(i). Western Australia

Section 11 of Western Australian Property Law Act 1969, in line with the proposal of the English Law Revision Committee, amended the third party rule by providing that: 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 enforceable by that person in his own name\(^ {42}\)

All defences which would have been available to the promisor had the third party been a party to the contract are available in an action by the third party,\(^ {43}\) and in any action on the contract by the third party, all parties to the contract must be joined.\(^ {44}\) Further, the legislation permits the enforcement of all terms of the contract against the third party which are "in the terms of the contract imposed on the [third party] for the benefit

\(^{41}\) For possible reasons for inaction, see J Beatson, 'Reforming the Law of Contracts for the Benefit of Third Parties- A Second Bite at the Cherry' (1992) 45(2) CLP 1, 14-15.


\(^{43}\) Western Australia Property Law Act 1969, s 11(2) (a).

\(^{44}\) Western Australia Property Law Act 1969, s 11(2) (b). This requirement was criticised by the New Zealand Contracts and Commercial Law Reform Committee, see para 4.6, below.
of the [promisor]”.\textsuperscript{45} The legislation also permits variation or cancellation of the contract by the contracting parties at any time until the third party adopts it either expressly or by conduct.\textsuperscript{46}

The New Zealand Contracts and Commercial Law Reform Committee\textsuperscript{47} made a number of criticisms of the Western Australian legislation: It does not appear to permit enforcement by third parties who are not in existence or ascertained at the time of formation of the contract;\textsuperscript{48} It seems to require express naming of the third party. It requires the joinder of each person named as a party to the contract in any proceedings commenced by the third party. It does not clearly express the necessity for the promisor and promisee to have intended to confer a legal right on the third party.

It should be noted that the Western Australian legislation does not provide for the situation where, instead of paying the third party, the promisor pays the promisee. If the third party is to be regarded as having an independent right under the contract, the fact that the promisor has performed in favour of the promisee should not necessarily eliminate the third party's right to performance. In Westralian Farmers Co-Operative Ltd. \textit{v.} Southern Meat Packers Ltd.\textsuperscript{49} the Supreme Court of Western Australia found that, where the plaintiff third party had established the

\textsuperscript{45} Western Australia Property Law Act 1969, s 11(2) (c).
\textsuperscript{46} Western Australia Property Law Act 1969, s 11(3).
\textsuperscript{48} We are not entirely convinced that this and the following point are accurate criticisms of the Western Australian legislation. The fact that the third party is "a person not named as a party" does not necessarily mean that it is only where the third party is named that he can enforce the contract.
existence of a contractual payment term in its favour, and the defendant claimed that it had already made payment to the original promisee, the plaintiff third party could nevertheless maintain its claim to payment.

(ii) Queensland

The third party rule was abrogated by statute in Queensland in 1974. **Section 55** of the *Queensland Property Law Act 1974* provides that. A promisor who, for a valuable consideration moving from the promisee, promises to do or to 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 the promise.\(^{50}\) Prior to acceptance, the promisor and promisee may vary or discharge the terms of the promise without the beneficiary's consent.\(^{51}\) After acceptance, the promisor's duty to perform in favour of and at the suit of the beneficiary becomes enforceable, and the promise may only be varied with the consent of the promisor, promisee and beneficiary.\(^{52}\) On acceptance, the beneficiary is bound to perform any acts that may be required of him by the terms of the promise.\(^{53}\) The section defines what constitutes an "acceptance" so as to render a promise enforceable by the beneficiary,\(^{54}\) and which "promises" will be capable of giving rise to rights in third party

\(^{50}\) Queensland Property Law Act 1974, s 55(1). The New Zealand Contracts and Commercial Law Reform Committee, *Privity of Contract* (1981) p. 52 regarded the Queensland legislation as "deficient in not providing that the duty may be created by deed as well as by simple contract"

\(^{51}\) Queensland Property Law Act 1974, ss 55(2).

\(^{52}\) Queensland Property Law Act 1974, ss 55(3)(a) and (d).

\(^{53}\) Queensland Property Law Act 1974, ss 55(3) (b).

\(^{54}\) Queensland Property Law Act 1974, ss 56(a): "acceptance means an assent by words or conduct communicated by or on behalf of the beneficiary to the promisor, or to some person authorized 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".
beneficiary.\textsuperscript{55} Unlike the Western Australian legislation, discussed above, the Queensland legislation does not require that the contract expressly purports to confer a benefit on the third party.\textsuperscript{56} And it imposes no obligation to join all parties in any action by the third party.\textsuperscript{57}

(iii) New Zealand

In 1981, the New Zealand Contracts and Commercial Law Reform Committee presented a Report on the third party rule, which amended draft legislation to implement the recommended reforms.\textsuperscript{58} The Report gave a brief account of the existing common law of New Zealand, which was virtually identical to that of England and Wales. The Report then considered developments in other jurisdictions, including the absence of a third party rule in most civilian systems\textsuperscript{59} and its abrogation, either by the courts or by statute, in the United States, Israel, Western Australia and Queensland.

The Committee considered arguments that the practical difficulties caused by the rule, and the devices adopted for avoiding its operation in particular circumstances, were insufficient to justify a fundamental change in the law, but refuted the contention that the intentions of the contracting

\textsuperscript{55} Queensland Property Law Act 1974, ss 55(6) (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”.

\textsuperscript{56} Although the promise must appear to be intended to confer a legal right enforceable by the third party: see note 29 above.

\textsuperscript{57} If criticisms (i) and (ii) in paragraph 4.6 above are accurate, the Queensland legislation also differs in that the beneficiary need not be named or in existence or identified at the time of the contract: see s 55(6) (b). See Ontario Law Reform Commission, Report on Amendment of the Law of Contract (1987) pp. 62-64; Manitoba Law Reform Commission, Privity of Contract (1993) Report No. 80 pp. 32-34.

\textsuperscript{58} New Zealand Contracts and Commercial Law Reform Committee, Privity of Contract (1981).

\textsuperscript{59} The Report, at para 3.1, considered the law of France, Germany South Africa, Denmark, Norway and Scotland.
parties could usually be the courts. The Report said:60

We are not convinced by such arguments. We have looked in vain for a solid basis of policy justifying the frustration of contractual intentions. We are left with a sense of irritation like that which, were suspect, motivated the majority of the Privy Council in *New Zealand Shipping Co. Ltd. v. Stterthwaite & Co. Ltd.*,61 to say, ‘to give the appellant the benefit of the exemption and limitations contained in the bill of lading is to give effect to the clear intentions of a commercial document.’ The case for reform is completed, in our opinion, by the observation of Lord Scarman (sometime Chairman of the English law Commission) in *Wooder Investment Development Ltd. v. Wimpey Construction (U.K) Limited.*62

The New Zealand Committee therefore recommended that a third party should be given a right to enforce a contract where a promise contained in a deed or contract confers, or purports to confer, a benefit on that third party.63 The New Zealand Committee's recommendations were substantially implemented in the New Zealand Contracts (Privity) Act 1982, although one of the changes in the 1982 Act, in contrast to the draft Contracts (Privity) Bill annexed to the Committee's Report, includes a requirement that the third party should be designated in the contract in order to obtain an enforceable right. The Act, in section 4, provides that 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

62 [1980] 1 WLR 277, 300-301. Lord Scarman's observations are set out above at para 2.64.
to a class, who is not a party to the deed contract the promisor shall be under an obligation, enforceable at the suit of that person, to perform that promise. Thus the section starts from the premise that all promises benefitting sufficiently designated third parties are to be enforceable at the suit of that third party. The section is not limited to express promises, and extends equally to implied promises. However the section goes on to provide that it does 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. Section 4 thus creates a reverse onus of proof in respect of the contracting parties' intention to create a legally enforceable obligation in favour of third party. It is up to them to establish that their promise was not intended to have this effect. The New Zealand Act therefore controls liability by the requirement that the third party be sufficiently designated in the contract and by resting liability on the intentions of the contracting parties to confer a right of enforceability (albeit under a reversed burden of proof).

The Act goes on to provide that promises benefitting third parties may not be varied or cancelled without the third party's consent once the third party has either (a) materially altered his position in reliance on the promise;\textsuperscript{64} (b) obtained judgment on the promise; or (c) obtained an arbitration award on the promise.\textsuperscript{65} However, where there is an express provision permitting variation in other circumstances, which is known to

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\textsuperscript{64} Or his position has been materially altered by the reliance of any other person on the promise.
\textsuperscript{65} New Zealand Contracts (Privity) Act 1982, s 5.
the third party, such variation is permitted. In 1993, the New Zealand Law Commission considered the operation of the Act, and concluded that most of the problems which had arisen in its operation concerned the scope of what became section 4, and particularly the requirement of designation. These caused difficulties particularly in connection with pre-incorporation contracts and contracts involving nominees. The New Zealand Law Commission examined the decisions under the Act, but recommended no changes to it.

(iv) United States

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

The New York Court of Appeals in Lawrence v. Fox 20 NY 268 (1859), it has become generally accepted that 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 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

66 New Zealand Contracts (Privity) Act 1982, s 6. For the New Zealand approach to defences,
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.

It became apparent that a number of third party beneficiaries did not fall within the "donee" and "creditor" categories, such that some courts simply disregarded the categorisation approach and allowed beneficiaries to recover who were neither creditors nor donees. 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: 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-the performance of the promise will satisfy an obligation of the promisee to pay money to the beneficiary; or the circumstances indicate that the promisee intends to give the beneficiary the benefit of the promised performance. An incidental beneficiary is a beneficiary who is not an

69 In a private construction context, subcontractors were neither donee for creditor beneficiaries: D Summers, 'Third Party Beneficiaries and the Restatement (Second) of Contracts' (1982) 67 Cornell L Rev 880, 884.
70 I bid. For an example of a third party taking the benefit of an exclusion clause as a third party beneficiary, see Carle & Montanari Inc. v. American Export Isbrandtsen Lines Inc 275 F Supp. 76 (1967).
71 Eg where B promises A to discharge a debt owed by A to C.
72 Eg where B promises A to make a gift C.
intended beneficiary.\textsuperscript{73}

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 the promise".\textsuperscript{74} The "intent to benefit" test has, in practice, failed to achieve consistent results,\textsuperscript{75} in particular in the field of public service contracts.\textsuperscript{76} 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?\textsuperscript{77} Some states have adopted requirement that the intent to benefit the third party be expressed within the contract. However, even in the states they have adopted this strict test of intent, the requirement has not been consistently applied.\textsuperscript{78}

\textbf{CONCLUSION}

The extent of the criticism and reform is itself a strong indication that privity is flowed, but most members of states of the European Union allow Third Parties to enforce contract. A reform of the third party rule is

\footnotesize{\textsuperscript{73} Eg where B promises A to built a structure which has the effect of enhancing the value of C's land.\textsuperscript{74} H Prince, 'Perfecting the Third Party Beneficiary Standing Rule under Section 302 of the Restatement (Second) of Contracts' (1984) 25 Boston College L Rev. 919, 979.\textsuperscript{75} 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 unmistakable" or "sufficiently immediate" : Prince, ibid, pp. 934-937.\textsuperscript{76} A Waters, "The Property in Promise: A Study of the Third Party Beneficiary Rule" (1985) 98 Harvard L Rev 1109, 1186-1188.\textsuperscript{77} In Beckman Cotton Company v. First National Bank of Atlanta 666 F 2d 181 (1982), 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.\textsuperscript{78} See H Prince, 'Perfecting the Third Party Beneficiary Standing Rule under Section 302 of the Restatement}
necessary. Contracting parties may not, under the present law, create provisions in their contract which are enforceable directly by a third party unless they can take advantage of one of the exceptions to the third party rule. Reform should be straightforwardly possible for contracting parties to confer on third parties the right to enforce the contract.

The rule of English law whereby a third party to a contract can not enforce, should be reformed so as to enable contracting parties to confer a right to enforce the contract on a third party. The right of third party to sue on a contract made for its benefit is recognised by the law of Scotland and the legal system of the United States. It has also been introduced by Statute in Several Commonwealth Countries. Contract (Rights of Third Parties) Act 1999 provides enforcement of contractual terms by third party. The UNIDROIT principles provide that a contract is binding upon the parties.