

WHEN DO THIRD PARTY RIGHTS ARISE UNDER THE CONTRACTS (RIGHTS OF THIRD PARTIES) ACT 1999 (UK)?

I. Introduction

There are two aspects to the common law doctrine of privity of contract. The first, that a contract cannot impose liabilities on a third party, is not very controversial. The second, that in general a contract can only confer rights on parties to the contract even if it is clearly the intention of the contracting parties to benefit a third party,¹ is highly controversial, and has been the subject of much judicial criticism.² The problems caused by the doctrine of privity of contract and judicial techniques to circumvent it are well documented in contract textbooks.³ There are three main techniques: One relies on actions by the third party on the promise itself by way of assignment, agency or trust; another depends on rights arising apart from the contract itself;⁴ and the third hinges on actions by the promisee to enforce the promise, or to recover damages for its breach, for the benefit of the third party.

Common law countries have been very slow to create any direct exceptions to the privity doctrine. The only notable judicial developments have occurred in Australia and Canada. The Australian High Court in *Trident General Insurance Co Ltd v McNiece Bros Pty Ltd*⁵ has allowed a third party to enforce a term in a contract, but in a situation where the third party would have been able to do so under legislation but for the fact that the relevant events occurred before the law took effect. It has not made any visible impact on Australian law since. The Canadian Supreme Court has allowed a third party to rely on an exclusion clause in *London Drugs Ltd v Kuehne & Nagel International Ltd*.⁶ The exception has since been extended to allow a third party to enforce a waiver of subrogation clause term in an insurance contract.⁷

1 *Tweddle v Atkinson* (1861) 1 B & S 393; 121 ER 762.

2 A catalogue of such criticism can be found in the judgment of Steyn LJ (as he then was) in *Darlington Borough Council v Wiltshier Northern Ltd* [1995] 1 WLR 68 (CA) 76–77. See also *The Mahkutai* [1996] AC 650 (PC HK) 663–665 (Lord Goff of Chieveley).

3 Eg, Andrew Phang (ed), *Cheshire, Fifoot and Furmston's Law of Contract* (2nd Singapore and Malaysian ed, 1998) 782–793. The arguments are usefully summarised in Law Com No 242, Cm 3329, 31 July 1996, Part III.

4 Eg, an action in tort: see *White v Jones* [1995] 2 AC 207, where a solicitor, having breached a contract with his client in failing to take steps to draw up a will before the client's death, was held liable in negligence to compensate disappointed beneficiaries for the amounts they would have obtained under the will, ie, as if the contract between the solicitor and the client had been performed. Other examples include collateral contracts, and deeds executed in favour of the third parties.

5 (1988) 165 CLR 107.

6 [1992] SCR 299.

7 *Fraser River-Pile & Dredge Ltd v Can-Dive Services Ltd* [1999] 3 SCR 108.

The most forceful argument in favour of a direct right of enforcement of third party rights is respect for the autonomy of the contracting parties.⁸ This was adopted as the primary basis for the reform of English law by the Law Commission for England and Wales in its report on *Privity of Contract: Contracts for the Benefit of Third Parties*.⁹ Subsequently, the Contracts (Rights of Third Parties) Act 1999, c 31,¹⁰ was enacted for England and Wales¹¹ by the United Kingdom Parliament, following substantially the recommendations of the Law Commission. While it left untouched the regime of liabilities imposed on third parties,¹² it opened up a whole new legal regime for third parties to enforce contracts directly, where the conditions of the legislation are satisfied. It has potentially wide-ranging effects on many typical contracts that affect third parties, including construction contracts, distribution contracts, and software licences.

The legislation has no direct relevance to Singapore law, which still follows the common law doctrine.¹³ However, it is indirectly relevant to Singapore in three ways. First, many international contracts are governed by English law, and the modified privity doctrine is now part of domestic English contract law.¹⁴ Secondly, in view of the fact that several other significant common law jurisdictions have already made legislative reforms of the common law privity doctrine,¹⁵ the English model is one possible model for Singapore to follow if it is considering reform in this area. It provides an interesting study of how the problem of privity can be approached, and how realistically it can be expected to solve the various problems

8 See Steyn LJ in *Darlington BC v Wiltshier Northern Ltd*, above, note 2, at 76.

9 Law Com No 242, Cm 3329, 31 July 1996, especially at para 1.1, 3.1.

10 The Act came into force on 11 November 1999, taking effect for all contracts (subject to English law) entered into on or after 11 May 2000. Contracts made in the interim may be subject to the statute if the contracting parties expressly opted to be subject to the Act. See section 10 of the Act.

11 Scottish law is different on the point.

12 Except to the extent that enforcement of the rights is subject to conditions in the contract.

13 See Andrew Phang, above, note 3, at 779–782.

14 The legislation is silent on the issue of choice of law, but its relevance to choice of law in Singapore is governed by Singapore conflicts principles. There can be little doubt that the legislation applies by way of the proper law of the contract. It cannot be argued that enforcement by a third party is a matter of procedure; the legislation confers substantive rights on third parties. It may be possible to design a contract governed by one law (say Singapore law), and a provision for the enforcement by a third party to be governed by English law by way of *depeçage*.

15 New Zealand: Contracts (Privity) Act 1982, s 4; Queensland: Queensland Property Law Act 1974, s 55; Western Australia: Western Australia Property Law Act 1969, s 11. The American Law Institute, *Restatement of Law (Second), Contracts (2d)*, section 302 provides that parties to a contract may confer enforceable rights on third parties. In civil law countries, third party beneficiaries may acquire rights under the contract: K Zweigert and H Kötz, *An Introduction to Comparative Law* (3rd ed, 1998), ch 34.

raised by the privity doctrine. Thirdly, the extent to which the statutory reform may affect common law developments related to the privity doctrine is of relevance to Singapore, because the English common law is still at least highly persuasive in Singapore.

II. The Contracts (Rights of Third Parties) Act

The purpose of the Contracts (Rights of Third Parties) Act was not to abrogate the doctrine of privity.¹⁶ Nor was it intended to affect the various techniques which the common law has devised around it.¹⁷ It was not intended to alter the rule that a contract cannot impose obligations on third parties. What it did was to create a broad statutory exception to the doctrine of privity, allowing the parties to a contract, in specified circumstances, to confer enforceable rights on a third party.

The key to the reform lies in the first three sub-paragraphs of section 1 of the Act. The rest of the statute contains provisions on the conditions of enforcement, variation and cancellation, and the circumstances under which relevant defences, set-off and counterclaims may be available to the promisor against the third party. The key provisions identify the circumstances in which the third party has the legal right to sue the promisor. It is the key that unlocks the rest of the provisions of the Act. If that threshold is not crossed, the entire Act is inapplicable. The key provisions of section 1 are set out below.

Right of third party to enforce contractual term.

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

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

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

16 Much less so the doctrine of consideration. The relationship between privity and consideration is a controversial one. The relationship is discussed in the Law Commission Report, above, note 9, Part VI, where it was acknowledged that the rule that consideration must move from the promisee was not necessarily clearly distinct from the rule that only a party to a contract can enforce it. However, insofar as there is a common law requirement for consideration to move from the third party to allow the third party to enforce the promise, the legislation, in conferring third party legal rights, must necessarily have amended the common law rule *pro tanto*: Law Commission Report, above, note 9, para 6.8, footnote 8.

17 Section 7(1) preserves the rights of the third party apart from the legislation, while section 4 preserves the rights of the promisee.

(2) Subsection (1)(b) does not apply if on a proper construction of the contract it appears that the parties did not intend the term to be enforceable by the third party.

(3) The third party must be expressly identified in the contract by name, as a member of a class or as answering a particular description but need not be in existence when the contract is entered into.

To summarise the effect of the above provisions, a third party may enforce a term in the contract, subject to further limitations and restrictions elsewhere in the statute, when two conditions are satisfied: (1) there must be sufficient *identification* of the third party in the contract; and (2) there must be *contractual intention* that the third party has the legal right to enforce the specific term. More specifically, third party rights arise where:

(1) the third party is expressly identified in the contract in one of three ways:

- (a) by name; **or**
- (b) as a member of a class; **or**
- (c) as answering a particular description;

and

(2) **either**

- (a) the contract expressly provides that the third party may sue on the term; **or**
- (b) the term purports to confer a benefit on the third party, **unless** on a proper construction of the contract the parties did not intend the third party to be able to sue.

This is the gateway to the enforcement of third party rights, and will likely be the legal battleground during the early stages of the implementation of the legislation. This article focuses on issues of interpretation and application of these key provisions. For brevity, unless otherwise indicated, the promisor, promisee and the putative third party will be referred to as *A*, *B* and *C* respectively when discussing scenarios.

III. Express identification of the third party

A. “*expressly*”

The requirement for the express identification appears straightforward. Section 1(3) requires the third party beneficiary to be “expressly

identified". This rules out an implied term identifying the third party who is to enforce the contract. In this respect, the legislative reform is more restrictive than the exception to privity created by the Canadian Supreme Court, where identification of third parties by implication is permissible.¹⁸ However, the English position is not as restrictive as it might at first sight appear. An express term does not have to be written down in an agreement. An express term may appear in a collateral contract, or the oral portion of a partly oral and partly written contract, or, if it was inadvertently left out of a written contract, it could be read in by construction or written into the contract by way of rectification.¹⁹

B. "identified" by "name", "class", or "description"

Section 1(3) requires the third party to be identified by name, class or description. The third party may not exist at the time of the contract. So, eg, children unborn at the time of contracting may be future beneficiaries of the contract.

One potential problem is the certainty of identification of the third party beneficiaries. Where the third parties are identified by name, difficulties are unlikely to arise. However, if, as is more likely to be the case, the third parties are identified by class or description, there may be difficulties in the level of certainty that is required of the term identifying them. The problem is less likely to arise in commercial contracts where third parties tend to be identified by a legal nexus (eg, employees, sub-contractors, sub-purchasers). The problem is more likely to arise in non-commercial contexts (eg, *A* promises *B* to pay *B*'s "relatives"). In principle, the normal rules of certainty of contractual terms should apply. The terms must be sufficiently certain at the time of contracting, but this does not necessarily mean that the identity of the third party must be ascertainable with certainty at the time of contracting. The right conferred on the third party is inextricably linked to the identity of the third party. But the right does not have to accrue at the time of contracting. What is required is that at the time the right to enforce the contract is alleged to

18 *London Drugs Ltd v Kuehne & Nagel International Ltd* [1992] 3 SCR 299, 450–452 (where the majority held that contracting parties had impliedly meant "warehousemen" where the exclusion clause had mentioned "warehouseman", thus identifying the warehouseman's employees as third party beneficiaries).

19 Eg, the reference to the third party was inserted by construction and rectification in the New Zealand case of *Rattrays Wholesale Ltd v Meredyth-Young & A'Court Ltd* [1989] 1 NZLR 83, discussed, below, text to footnote 27.

have accrued, the third party must be ascertainable with certainty.²⁰ How much certainty is required?²¹ The answer is likely to depend on the nature of the promisor's obligation. In most cases the only relevant consideration is whether, at the time the right of enforcement accrues, the third party is within the defined class or not. However, if the promisor's contractual obligation is to pay a fixed sum of money equally divided among members of a class of beneficiaries, then the definition of the class may need to be conceptually clear enough for a complete list to be drawn up.

Parties may not want to identify the third party outright in the contract, but may agree in the contract to a mechanism for the identification of the third party. The most common example is where *A* agrees with *B* to perform terms in the contract for the benefit of *B* or "*B*'s nominee". In principle, there seems to be no objection to such a designation of a third party. A contract does not fail for want of certainty if one of the parties has been given the unilateral right to make decisions affecting both parties.²² However, this method of appointing third parties to enforce the contract gave rise to grave difficulties in New Zealand, where the provision in the Contracts (Privity) Act 1982 (section 4) for the identification of the third party is similar in substance to the legislation in England and Wales. The New Zealand Act provides for the enforcement by a party not privy to the contract where the promise in the contract "confers, or purports to confer, a benefit on a person, designated by name, description, or reference to a class ... 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".

The first case to consider the interpretation of the New Zealand provision was *Coldicutt v Web & Keeys*, an unreported judgment of 1985,²³ where Hillyer J held that where a contract was made between *A* and *B* "or his nominee", *B*'s nominee was a person designated by description under

20 See also the Law Commission Report, above, note 9, paras 8.17, 8.18.

21 There is an analogy with the problems arising from issues of ascertainability of beneficiaries in the law of trusts, but the analogy can be misleading because the need for *prior* ascertainment of potential beneficiaries for the exercise of fiduciary or trust powers is often unnecessary in the enforcement of contracts. The analogy is useful to the extent that the test used depends on the obligations of the trustees. So the court must be able to draw up a complete list of persons who satisfy the criteria for fixed trusts: *IRC v Broadway Cottages Trust* [1955] Ch 20; *Re Poulton* [1987] 1 All ER 1068. But it is enough that the court can say in respect of a particular person whether or not he satisfies that criteria for fiduciary powers: *Re Gulbenkian* [1970] AC 508, and discretionary trusts: *McPhail v Doulton* [1971] AC 424.

22 *Lombard Tricity Finance Ltd v Paton* [1989] 1 All ER 918 (CA); *The Star Texas* [1993] 2 Lloyds' Rep 445 (CA).

23 HC, Whangarei, 17 May 1985, A50/84.

the Act. Subsequently, however, a narrower view was taken by the Court of Appeal in *Field v Fitton*.²⁴ *A* had contracted to sell land to *B* “or nominee”. *B* in turn entered into an agreement for consideration to nominate *C* under the former contract. *B* having failed to comply with certain conditions, *A* purported to cancel the contract. It was not disputed that *C* was entitled to lodge a caveat, and the only question was whether *A* could cancel the contract without the consent of *C*. Bisson J, delivering the judgment of the court, rejected *C*’s claim. He held that the nomination contract amounted to an assignment of *B*’s rights to *C*. However, this meant that *C* as assignee took subject to all equities, including *A*’s right to cancel against *B*. Counsel for *C* took up the separate argument that *C* was a third party to the original contract of sale under the Contracts (Privity) Act 1982. Bisson J rejected the submission for two reasons which are relevant to the discussion in this article.²⁵ (The second reason is discussed below²⁶). Bisson J stated that a bare reference to a nominee was not sufficient to identify the third party. He said (at 493–494):

“It is difficult to treat a bare nominee not designated by name, as a person identified by description or as being within a designated class of persons. The nominee could be anyone at all. In the context of s 4, designated means specified or identified so that if the nominee is not named, the word nominee in the contract should be qualified by the addition of a descriptive phrase or the addition of the particular class within which the nominee falls so as to specify or identify the nominee in the manner required by s 4.”

The issue arose again in *Karangahape Road International Village Ltd v Holloway*.²⁷ *A* had contracted to sell land to *B* “or nominee”. *B* nominated *C*. When *B* failed to settle the accounts on time, *A* purported to cancel the contract, and sold the land to another party. *C* then sought specific performance of the contract between *A* and *B*. Chilwell J followed the reasoning of Bisson J in *Field v Fitton* that a bare reference to a “nominee” is insufficient for identification; the phrase was “contingent and amorphous; there is no person specified or particularised.”²⁸

The pendulum appears, at least for the time being, to have swung back towards a more liberal construction. In *Ratrays Wholesale Ltd v Meredyth-Young & A’Court Ltd*,²⁹ *B* had subleased supermarket premises to *A*.

24 [1988] 1 NZLR 482.

25 The third reason was that even if the nominee had an enforceable right under the Act, he had failed to comply, or to procure compliance, with the conditions attached to the promise.

26 See below, text to footnote 55.

27 [1989] 1 NZLR 83.

28 *Ibid*, at 104.

29 [1997] 2 NZLR 363.

The lease contained a clause requiring that goods that were to be sold on the premises be bought from *D*, a related company of *B*. *C* was the lessor by assignment from *B*. *C* argued that *A* had promised to purchase goods from *D* or any company nominated by the lessor, and that *C* had nominated itself. *C* sued in both capacities of lessor and nominee. In respect of the privity issue, *C*'s argument³⁰ proceeded in two stages. First, *C* argued that the deed should be construed, or if necessary, rectified, to reflect the lessor's right to nominate a different company to supply goods to *A*. Secondly, *C* argued that it (as nominee) could enforce the promise under the Contracts (Privity) Act 1982. Tipping J found for *C* on the issues of construction and rectification. He also preferred the approach of Hillyer J in the *Coldicutt* case, and thought that an unduly narrow approach had been taken in *Field v Fitton* and *Karangahape*. He said that the purpose of the designation of the third party was to enable the promisor to know with certainty who could claim the benefit of the promise in the contract. The only requirement was that the person should be identifiable from the contract. There was no conceptual doubt as to whether a person was a nominee or not. He did not think that the fact that the nominee "could be anyone at all" was objectionable in any way. Tipping J refused to follow *Field v Fitton* on the basis that the statements on the enforcement of third party rights were *obiter*, the decision having turned on the valid cancellation of the original contract of sale. Accordingly, he allowed *C* to enforce the term.³¹

The Law Commission for England and Wales in its report supported the liberal interpretation.³² It is easy to see why. If the parties' intentions are clear enough such that the third party can be ascertainable at the time of enforcement of the contract, that intention should not be denied simply because the third party may be chosen from a large class of potential beneficiaries. There appears to be two concerns in the New Zealand authorities: (1) that the third party should be ascertainable at the time of the contract; and (2) that, as expressed by Wylie J in taking the narrow interpretation in the unreported High Court case of *McElwee v Beer*³³, the third party should not be chosen capriciously by one of the contracting

30 *C* also succeeded on other arguments not relevant to the discussion here.

31 Further indication of a more liberal attitude may be found in *New Zealand Dairy Board v New Zealand Co-operative Dairy Co Ltd* [1999] 2 NZLR 355, where Gallen J observed that the statute could apply where the third parties are not in existence at the time of the contract. This is inconsistent with the need to ascertain the parties at the time of contracting.

32 Law Commission Report, above, note 9, paras 8.3, 8.4. The Commission also cited, at para 8.4, the support of the New Zealand Law Commission in its *Contracts Statutes Review*, Report No 25 (1993), p 224.

33 HC Auckland, 19 February 1987, A 445/85, cited in Law Com Rep, above, note 9 at p 96 fn 3.

parties. On the first issue, it appears that Tipping J was prepared to test the certainty of identification with one contracting party's act of nomination in mind – until the nomination, it is impossible to ascertain the identity of the third party – whereas the court in *Field v Fitton* tested the ascertainability at the time of contracting. To this extent, Tipping J's approach is preferable in principle,³⁴ and the English position is in any event clear that the identity of the third party need not be ascertained until the accrual of the right, which may occur after the contract has been formed.³⁵ The second objection is difficult to understand. There is no limitation on assignment of contractual rights based on caprice. Further, the fact that *B* may make a nomination capriciously does not prevent *B* from enforcing the term against *A* to perform in favour of *C*. Moreover, *A* agreed to the term at the outset. *A* is not prejudiced.

IV. Intention to benefit the identified third party

The identification of the third party is only the threshold requirement for enforcement by the third party under the Contracts (Rights of Third Parties) Act. The third party must have been granted the right to enforce the contractual term. It must be shown that either the parties had (1) expressly conferred the right to sue on the third party,³⁶ or (2) that the term in the contract “purports to confer a benefit” on the third party, and there is nothing in the contract to show that the parties had not intended the third party to be able to sue. It was thought that a structured test of benefit in the second part would provide greater certainty than a roving search for an implied intention.³⁷

A. *Express provision for third party enforcement*

The first test is as much one of construction as the second. Contractual clauses conferring benefits on third parties may be construed as expressly conferring rights. The Law Commission Report considered that exclusion clauses drafted to cover third parties fell within the first test, because it was meaningless to confer the benefit of the exclusion clause on the third party unless it was also legally enforceable by the third party.³⁸ This analysis, as some commentators have pointed out, appears to shade into

34 See the discussion above on certainty of contractual terms, main text surrounding footnote 20.

35 This follows from the proviso that the third party need not be in existence at the time of the contract.

36 Section 1(1)(a).

37 A Burrows, “Reforming Privity of Contract: Law Commission Report No. 242” [1996] LMCLQ 467, 472.

38 Law Commission Report, above, note 9, para 7.18.

the second test of inferring contractual intention to confer enforcement rights.³⁹ However, the overlap of methodology is inevitable because of the nature of the exercise of construction of meaning from words. Nevertheless, a conceptual distinction can still be maintained: the first looks for the meaning of the words expressed in the terms, and the second looks for the meaning of the parties' intention beyond the meaning of those words.

Little difficulty is anticipated if there is an express term⁴⁰ that the third party can sue. The test of purporting to confer a benefit on the third party does not arise. Indeed, there is no requirement for the third party, expressly specified for the purpose of enforcement of a contractual right, to benefit from it.

B. Implied intention I: purporting to confer a benefit on the third party

It is the second test that is likely to be problematic in practice. It is necessary to show that the specific term sued upon purports to confer a benefit on the third party. So where there are different obligations contained in separate terms in a contract, the third party must prove his case in respect of each obligation separately. There is no requirement that such terms be express. The term purporting to confer a benefit on a third party may be an implied term.

The Act does not define the meaning of “purport to confer a benefit”. The ordinary meaning of “purport” is to “profess or claim by its tenor”.⁴¹ What a term “purports” to do must be a question of construction of contractual intention. According to the Law Commission Report, once it is shown that a term purports to confer a benefit on a third party, a rebuttable presumption arises that it is enforceable by the third party. It is then up to the promisor to resist the enforcement by showing that on a proper construction of the contract, the parties had not intended the third party to be able to sue.⁴²

The purpose of the requirement that the term purports to confer a benefit on the third party is to limit the presumption to cases where the benefit is conferred by the contract directly, and not incidentally.⁴³ Thus it is not

39 JN Adams, D Beyleveld and R Brownsword, “Privity of Contract – the Benefits and the Burdens of Law Reform” (1997) 60 MLR 238, 254 *et seq.*

40 The same considerations discussed above (Part III.A) in the context of express identification, apply to express conferment of enforceable rights.

41 Oxford English Dictionary (2nd ed, 1989).

42 Law Commission Report, above, note 9, para 7.17.

43 Burrows, above, note 37, at 473.

enough that the third party has factually or legally benefited. The term in question must purport to confer a benefit on the third party. It is a matter of construction. This requires the court to distinguish cases where the third party is intended by the parties to benefit from the specific term, from cases where the third party's identity is incidental to the term, or where the third party benefits incidentally from the performance of the term. In some cases this will be straightforward. For example, if *A* contracts to pay *B* \$500 when *C* reaches the age of majority, without more, the term purports to confer the benefit on *B* alone. If *A* contracts with *B* to cut a hedge separating *B*'s property from *C*'s, the contract will benefit *C*, but without more, it does not purport to benefit *C*.⁴⁴ In some cases it will be clear that the term purports to benefit a third party. For example, if *B* buys furniture from *A*, telling *A* that it is a gift to *C*, to be delivered to *C*'s home, without more, the relevant terms clearly purport to benefit *C*.

In other cases it may not be so clear whether a term purports to benefit the third party. A term that prima facie confers a benefit on a third party may turn out, on a proper construction, not to purport to be for that purpose. If *A* contracts with *B* to build on land belonging to *C*, prima facie *C* receives the benefit, but it may be that, on these facts alone, it could not be said that the contract purported to benefit *C*, for whether it was really for the benefit of *B* or *C* depends on the arrangement between *B* and *C*, and *A* may know nothing of the arrangement.⁴⁵

The judgment of the New Zealand Court of Appeal in *Malyon v New Zealand Trust Association*⁴⁶ is rather short, and the reasoning brief, but nevertheless the facts serve as an illustration. The subject matter was a deed of assignment of a lease, the parties to which were the assignor (described as the Vendor), the assignee (described as the Purchaser), the landlord (*C*) and the defendant, described as the guarantor (*A*). It contained, under the heading "Guarantor's Covenants with the Vendor" a clause that *A* had guaranteed payment to *C* by the Purchaser of all future rent and other moneys due under the lease. *C* sued *A* on the guarantee when the vendor failed to pay, under both common law and the Contracts (Privity) Act 1982. The common law claim failed on the basis that as a matter of construction the guarantor's undertaking was made to the vendor and not to *C*. Its purpose was to provide security to the assignor against an action by *C* for the rent should the assignee fail

44 See GH Treitel, *The Law of Contract* (10th ed, 1999) 601.

45 Ibid, at 602.

46 [1993] 1 NZLR 137.

to pay. The claim under the statute failed in the Court of Appeal for two reasons: first, the Act did not apply because *C* was not a third party to the agreement, and secondly, on the assumption that *C* was a third party, the proviso in section 4 created an insuperable barrier because the clause “is clearly *intended to confer direct benefit only on the vendor* and cannot be construed as evidencing an intention to create an obligation enforceable at the suit of the landlord.”⁴⁷ The court decided the case (on the assumption that *C* was a third party) on the lack of intention that *C* should have an enforceable right under the proviso, and it was silent on the question whether the main section itself had been satisfied, ie, whether the promise “purport[ed] to confer” a benefit on *C*. It would seem, however, that, based on the emphasised part of the statement quoted above, the term did not purport to benefit the third party.

The fact that the same factor can be used at both stages of the test reinforces the point that ultimately, the court is construing the contract and seeking an implied intention to confer a right on the third party. It remains to be seen to what extent the legislative test will be judicially interpreted to be loaded in favour of third party enforcement, as the Law Commission suggests.⁴⁸ Much will turn on the construction of the term in question and the contract as a whole.

C. *Implied intention II: parties’ intention to confer rights on the third party*

Where it is established that the term purports to benefit *C*, prima facie *C* can enforce the term.⁴⁹ It is up to *A* to resist the enforcement by *C*, by showing that by a proper construction of the contract *C* did not have enforceable rights.⁵⁰ There is little difficulty if *A* and *B* expressly state that the party has no right of enforcement; this would clearly rebut the presumption of enforceability.⁵¹ However, in many cases, the contract would be silent about the enforcement by the third party. What is the effect of this silence?

According to Professor Burrows, the Law Commissioner responsible for the Report leading to the legislative reform, the presumption in favour of enforcement by *C* is a “strong one”.⁵² He went so far as to say that

47 Ibid, at 140 (emphasis added).

48 Law Commission Report, above, note 9, para 7.18: “doubts as to the parties’ intentions will be resolved in the third party’s favour”.

49 Section 1(1)(b).

50 Section 1(2).

51 Law Commission Report, above, note 9, para 7.18.

52 Above, note 43, at 473.

normally it would be difficult to rebut such a presumption unless there is an express term negating the rights of *C*, or an express term inconsistent with the right of *C* to enforce the term, or there is a chain of contracts such that *C* has legal recourse against another party.⁵³ However, this view does not appear to be reflected in the Law Commission's draft bill, or in the Act.⁵⁴ For the rebuttal in section 1(2) is framed in terms of *A* and *B* not intending *C* to have enforcement rights, and not in terms of the parties intending *C* not to have enforcement rights.

Under New Zealand law, where similar statutory language is used in this respect, it would seem quite easy to reach the conclusion that *A* and *B* never intended to allow *C* to have enforcement rights. It was seen in *Field v Fitton*,⁵⁵ discussed above, that the New Zealand Court of Appeal did not think that a reference to a "nominee" without more could qualify as sufficient identification of a third party. The additional reason given by the court for refusing to allow *C* to enforce the contract was that on the construction of the contract, the bare reference to a third party without more did not manifest an intention to create an obligation enforceable by the third party:

"The second difficulty is that the proviso to s 4 is fatal to the first respondents as there is on the proper construction of this contract no intention to create an obligation on the appellants enforceable at the suit of the first respondents alone. The mere addition of the words "or nominee" without more, is not sufficient in this case ... on the proper construction of the agreement to impute an intention to the parties to create, in respect of the benefit to a named purchaser, an obligation on the part of the vendor enforceable at the suit of a bare nominee." ⁵⁶

This line of reasoning appears to be endorsed in the Law Commission Report, as an example of rebuttal of the prima facie right of enforcement.⁵⁷ This shows that the Law Commission clearly contemplated evidence of lack of intention, rather than negative intention, as possible rebuttal. On the other hand, the Law Commission appeared to take a stricter approach to the presumption in considering the application of its proposed legislation to the facts of *Beswick v Beswick*.⁵⁸ *B*, a merchant,

53 Ibid.

54 T Roe, "Contractual Intention under Section 1(1)(b) and 1(2) of the Contracts (Rights of Third Parties) Act 1999" (2000) 63 MLR 6.

55 [1988] 1 NZLR 482. See discussion above, main text to footnote 24.

56 Ibid, at 494. This reasoning was followed by Chilwell J in *Karangahape Road International Village Ltd v Holloway* [1989] 1 NZLR 83, 104-105.

57 Law Commission Report, above, note 9, para 8.4, footnote 4.

58 [1968] AC 58.

had transferred his business to his nephew (*A*) in return for, among other things, a promise to pay a weekly sum to the merchant's widow (*C*) after his death. The Law Commission said that, on these facts under its proposed legislation, the presumption that *C* could sue, as an expressly identified third party on whom a benefit had purportedly been conferred by *A*'s promise to pay, was unlikely to be rebuttable by absence of contractual intention on the facts.⁵⁹

It is likely that the silence of the parties is merely one of the factors to be considered in construing the contractual intention, and the weight to be given to it depends on all the circumstances of the case. One factor may be the degree of specificity with which the third party has been identified in the contract. For example, the more specific the identification of the third party, the more ready the court may be to infer an intention to confer enforceable rights. Thus, in *Beswick v Beswick*,⁶⁰ where the identity of *C* was specified from the beginning, it would be easy to infer that the parties intended *C* to have enforceable rights. In *Field v Fitton*,⁶¹ the third party was a bare nominee, who at the time of the contracting could be anyone at all. But the identification is highly specific because the nexus of nomination is very clear. However, the court appeared to be concerned with the state of affairs at the time of the contract,⁶² and influenced by the width of the class at that time. This is unlikely to have such a strong bearing on the issue under the English legislation.

The surrounding circumstances are also likely to be relevant. The Law Commission Report, in rejecting arguments from the construction industry to exempt it from the reform, considered that the industry understanding and practice of chain contracts could form a basis to rebut any presumption of enforceability, as part of the surrounding circumstances to construe the contractual intention.⁶³ This position is not without difficulty. One substantial reason why the parties are presumed not to intend the third parties named in the contract as recipients of services to have enforceable rights is that the third parties could not be given such rights under the common law. Carried to its logical conclusion, it means that if it is standard practice within an identifiable class of contracts for third parties to be named as beneficiaries of terms in the contract, the presumption may go the other way round – that there is no intention to allow the third party to sue unless something more is shown. This may

59 Law Commission Report, above, note 9, para 7.46. Treitel, above, note 44, at 602.

60 [1968] AC 58.

61 [1988] 1 NZLR 482.

62 See discussion above, main text to footnote 24, *et seq.*

63 Law Commission Report, above, note 9, para 7.18.

be an alternative explanation of the approach taken in *Field v Fitton*.⁶⁴ It appeared to be common conveyancing practice in New Zealand for the sale to be promised to a promisee or nominee,⁶⁵ leaving the promisee to enforce the promise in favour of the nominee if necessary. So in such a case, a term purporting to confer a benefit on the third party, in the absence of further indication of intention, may not be enough for the third party to acquire an enforceable right.

Professor Burrows has also suggested that one important indicator of the contractual intention is whether the third party has any legal recourse apart from the Act.⁶⁶ This would distinguish the chain contract situations, where there is normally a right of recourse, from one-off contractual situations, like *Beswick v Beswick*,⁶⁷ where it is unlikely that the third party has any recourse.

V. Uncertainty of application

The legislative test for third party enforceability based on the implied intention of the party is not a straightforward one. The result is that there is much work for the English courts to do to resolve the uncertainty surrounding the question of contractual construction in a newly created situation where contracting parties can confer rights on third parties. The main problem areas are specifically the meaning of “purporting to confer a benefit”, and the ascertainment of the contractual intention, or in its absence, to confer enforceable rights on the third party. The court’s role is to interpret the words of the statute in the light of the objectives of the statute. The discussion above is essentially premised on the acceptance of the approach recommended by the Law Commission. The courts may or may not follow the guidance provided in the Law Commission Report. The legislative reform has left much clarification to be done by judicial interpretation.

However, this should be viewed in the positive spirit of law reform. Construction of contractual intention is a business in which commercial courts have vast practical experience and honed specialised skills. No doubt opening up a new area for contractual intention to operate in will lead to some uncertainty in practice. But the statute allows the parties to state clearly that a third party has or does not have enforcement rights;

64 [1988] 1 NZLR 482.

65 Many of the cases on privity of contract arose in this context: *Lambly v Silk Pemberton Ltd* [1976] 2 NZLR 427; *Coldicutt v Keays* (HC Whangerei, A 50/84, 17 May 1985); *Field v Fitton* [1988] 1 NZLR 482; *Karangahape Road International Village Ltd v Holloway* [1989] 1 NZLR 83.

66 Above, note 37, at 473.

67 [1968] AC 58. This case itself was exceptional; see below: text to footnote 76.

this provides certainty in a carefully drafted contract. In between the two extremes, there are myriad instances in which it is practically impossible to provide any definitive legislative guidelines. Contractual intention provides the basis for both the new right and solution to such problems. The courts are well placed to resolve issues of contractual intention and to develop appropriate precedents to provide even greater certainty.

VI. Scope of the reform

It has been seen above that the reform does not affect the judicial techniques developed to circumvent problems of privity.⁶⁸ The test of enforceability, based on identification and intention of the parties, will not affect several classic problem areas of privity of contract.

It does not solve the problem of the disappointed beneficiary who is not party to a contract under which the obligation to draft appropriate wills is breached. In the *White v Jones*⁶⁹ situation, the lawyer (*A*) contracts with the testator (*B*) to draw up a will to benefit a putative beneficiary (*C*). Even if *C* is identified sufficiently in the contract, the contract is unlikely to be intended to confer any benefit on *C*. It is a contract to provide will drafting services to *B*. The contract only purports to confer a benefit on *B*, in order to enable *B* to confer benefits on *C*.⁷⁰ It does not purport to confer any benefit on *C* directly. Such cases will continue to be dealt with as a problem in tort law. Such facts were considered in the New Zealand Court of Appeal in *Gartside v Sheffield, Young & Ellis*.⁷¹ The Court held that a duty of care could be owed in tort. In respect of the Contracts (Privity) Act 1982, Cooke P observed that the contract between the solicitor and the testator would not by itself contain any promise conferring or purporting to confer a benefit on the putative beneficiary. There was no undertaking towards the third party: the “solicitor has not promised to confer a benefit on him”.⁷²

*Junior Books Ltd v Veitchi Co Ltd*⁷³ represents a typical construction situation involving third parties. A builder (*B*) had undertaken to construct a factory for the owner, the plaintiffs (*C*), under a contract which entitled *C* to nominate sub-contractors. *C* nominated *A* as flooring sub-contractors. The flooring work turned out to be defective. *A* was held liable in tort. Had the sub-contract named *C* expressly, it *might* have purported to

68 Above, text to note 4.

69 [1995] 2 AC 207.

70 Law Commission Report, above, note 9, paras 7.25, 7.36 and 7.48. Treitel, above, note 44, at 602.

71 [1983] NZLR 37.

72 Ibid, at 41–42.

73 [1983] 1 AC 520.

confer a benefit on *C*.⁷⁴ However, it is likely that on a proper interpretation of such contracts, the purpose of the contract was to regulate only the relations between *A* and *B*, and not intended to create any enforceable rights for *C*.⁷⁵

On the other hand, the situation typified by *Beswick v Beswick*⁷⁶ is likely to fall within the statutory framework. *B* had transferred his business to his nephew (*A*) in return for a promise to make regular payments to *B*'s widow after his death. The House of Lords held that *C* could sue *A* in her capacity as the executrix of *B*'s estate, but it was assumed throughout that, contrary to Lord Denning's opinion in the Court of Appeal,⁷⁷ *C* was prevented by the privity rule from suing in her own right. Under the statutory regime, the payment obligation purports to confer a benefit on *C* who is identified expressly, and *C* can enforce it unless it is shown that the contracting parties had not intended that *C* should be able to sue.

In some cases, *B* may be able to sue *A* for the benefit of *C*. *B* may be able to ask for specific performance of the promise directly.⁷⁸ Also, in a limited number of instances, *B* may be able to recover substantial damages for breach of contract in failing to confer the benefit, as specified in the contract, on *C*. The action by *B* to recover substantial damages is the subject of important recent judicial developments in English law.⁷⁹ These developments have not been rendered obsolete by the reforming legislation; in fact they are preserved in the Act.⁸⁰ Conversely, the ability to recover such damages does not make the legislative reform unnecessary, because *C* may not be able to compel *B* to sue *A*. Not every case where *B* seeks to recover such damages will fall within the parameters of the Contracts (Rights of Third Parties) Act.⁸¹ Moreover, the parties may, for tax or other reasons, prefer to structure their arrangements in such a way that *C* does not have any legal rights against *A* directly.

In *Linden Gardens Trust Ltd v Lenesta Sludge Disposals Ltd*,⁸² the simplified facts were that *A* contracted with *B* to work on a site owned by *B*, which *B* then sold to a third party, *C*. *A* breached its contract with *B*. *C* was not a party to the contract and could not sue. Ordinarily, *B* could only recover its own loss under its contract with *A*. The majority in the House of Lords, however, allowed *B* to sue to recover *C*'s losses

74 See discussion above, Part IV.B.

75 Law Commission Report, above, note 9, para 7.47. Treitel, above, note 44, at 602.

76 [1968] AC 58.

77 [1966] Ch 557.

78 Eg, *Beswick v Beswick* [1968] AC 58.

79 *Alfred McAlpine Construction Ltd v Panatown Ltd* [2000] 3 WLR 946 (HL).

80 Section 4.

81 Eg, the discussion of *Linden Gardens*, below.

82 [1994] 1 AC 85.

under the special common law rule that *B* could recover *C*'s loss or damage caused to property transferred by *B* to *C*, where *C* did not acquire any rights under contract, and it was foreseeable that *C* would not do so. It would appear that *C* would not have been able to sue under the Contracts (Rights of Third Parties) Act had the facts occurred after the Act came into effect. The mere possibility that the land may be transferred to another does not adequately identify any third party, nor does the contract purport to confer any benefits on any such party. In any event, a clause in the contract barring assignment of *B*'s rights in the contract would have indicated the parties' intention that third parties were not to have rights in the contract.

In two other recent cases where the question of damages had been considered, the parties had made explicit arrangements to attempt to get around the privity rule. In *Darlington Borough Council v Wiltshier (Northern) Ltd*,⁸³ the simplified facts were that *A* had entered into a contract with *B* to build on the land of *C*, and *B* had entered into a contract with *C* to assign the benefit of its contract with *A* to *C*. Additionally, *A* had directly undertaken by deed to pay *C* liquidated damages for delays in the construction. There were defects in the construction. The Court of Appeal allowed *C* to sue, as assignee of *B*, to recover losses suffered by *C*, based on an extension of the reasoning in the *Linden Gardens* case.⁸⁴ In *Alfred McAlpine Construction Ltd v Panatown Ltd*,⁸⁵ *B* had employed *A* as contractors to build an office block at a site owned, not by *B*, but their associated company, *C*, who were the actual developers. On the same day that the construction agreement was signed, *A* entered into a separate agreement by deed with *C* accepting limited liability for negligent construction. *B* alleged that the construction was defective and sought to recover damages from *A*. *C* could have sued *A* in its own right under the deed, but probably for strategic reasons⁸⁶ due to differences of terms under the construction contract and the deed, it was decided that *B* should take action under the construction agreement against *A*.

Since the parties clearly had in mind the legal interests of *C* at the outset, under the present regime, they would have been able to structure their

83 [1995] 1 WLR 68 (CA).

84 The original holding required the contractor to transfer property to the third party; in the *Darlington* case the contractor never had any proprietary interest in the land. An additional ground of the decision was that *B* held the benefit of the contract on constructive trust for *C*.

85 [2000] 3 WLR 946 (HL).

86 This probably had to do with the arbitration clause in the main contract which was absent from the deed, as well as the different standards of care undertaken in the two instruments.

arrangements better under the Contracts (Rights of Third Parties) Act. If the facts had arisen after the Act took effect and the parties had not expressly stated the position of *C* one way or the other, then whether the statute applies would have depended on, first, the express identification of the third party in the building contract, secondly, whether the term whereby the builder undertook the duty of care was purportedly for the benefit of the third party, and if so, whether the contractual intention was to give the third party the right to sue. Given the nature of the arrangements, it may be that the contracting parties had purported to confer on *C* the benefit of the right to sue *A* for defects, since both parties knew of the internal arrangements between *B* and *C*.⁸⁷ In the *Darlington* case, Steyn LJ observed that the parties had structured the transactions in such a way that it was contemplated that *A* would perform the building contract for the benefit of *C*, and that *C* would have been able to sue but for the privity rule.⁸⁸ If the facts were to be considered under the Contracts (Rights of Third Parties) Act, it may be that, assuming sufficient identification in the contract, the parties had purported to confer a benefit on *C*. Even so, the availability of legal recourse by *C* by way of the assignment or deed may have the effect that the contract is construed as a whole not to confer any enforceable rights on *C*.⁸⁹ The ability of *C* to take direct action on the building contract against *A* therefore depends on a number of contingencies, which may or may not be satisfied depending on the individual circumstances. Hence, in spite of the legislation, it is likely that the common law action by *B* to recover substantial damages from *A* will continue to be of practical significance.⁹⁰

87 It may be different if *A* had not been aware of the arrangements between *B* and *C*: Treitel, above, note 44, at 603.

88 Above, note 83, at 76.

89 It is admittedly somewhat incongruous to test the effect of the existence of the assignment or deed hypothetically under the Act – it was precisely because of the absence of the Act that those instruments were executed.

90 The ability of the promisee to recover substantial damages for the third party's loss is contingent upon the third party being unable to sue the promisor directly: *McAlpine v Panatown* [2000] 3 WLR 946. It follows that the ability of the third party to sue under the Act excludes the promisee's right to recover substantial damages on behalf of the third party. If the promisee has recovered such substantial damages from the promisor on the basis that the third party had no direct recourse under the Act, and the third party (provided he is not estopped by the previous judgment) subsequently proves that he has an enforceable right, the promisor is entitled to ask the court to reduce the amount of damages taking account of the sum already recovered by the promisee: section 5(a). In the converse situation, if the third party has already recovered damages by a direct action in prior proceedings, it is not legally possible for the promisee to recover any substantial damages for third party loss, so it was unnecessary for the statute to make any provision for this situation.

VII. Conclusion

The English legislative reform is not an abrogation of the common law privity rule. It is a broad exception to the rule based on the intention of the contracting parties to benefit ascertainable third parties. It provides a facilitative framework under which contracting parties can spell out enforceable rights for third parties. The basis of third party enforcement is the intention of the parties, so naturally it is possible to exclude the possibility of any third party rights by appropriately formulated words in the contract. Standard clauses of this type have been common since the enactment of the legislation. This practice seems to be based on caution arising from an untested legislation. The enforcement by third parties of contractual rights may prove useful in a number of situations, rendering other devices no longer necessary: for example, deed polls executed by one party to guarantee the liabilities of a company to a class of persons, eg, bond-holders; certain agency arrangements; trust arrangements where one party contracts as trustee of the benefit of the contract on behalf of third parties; and collateral contractual arrangements between the promisor and the third party intended to be benefited.

Nevertheless, the meaning of the key provisions allowing third parties to sue is likely to engender lawsuits in the near future as litigants test the limits of the application of the statute. The Act is not a comprehensive reform of the law of privity. It leaves the common law devices intact, and indeed it leaves many problem areas to continue to be resolved by common law techniques. So techniques like trust, agency, collateral contracts and others continue to be relevant. One important common law circumvention of the privity rule is the ability of the contracting party to recover for third party losses in certain circumstances. This has been the subject of recent important common law development. In England, these developments have not been superseded by the passage of the Contracts (Rights of Third Parties) Act, because the common law action survives the statute, and moreover it will not be in every case that the third party can sue directly. Further, it may be that in some cases the parties, for tax or other legal reasons, do not want the third parties to acquire any legal rights under the contract.

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