# PRIVITY OF CONTRACT

## INTRODUCTION

The main principle highlighted by this concept of Privity of Contract is regarding the rights of third parties in a contract. Thought the position in various countries is now similar, if not the same, it was not the same when the rule came into being. The most important questions to be considered were whether a third party could acquire rights, or incur obligations, to a contract to which he or she is not a party?

These questions were highly prevalent in England from 17th to 20th century. Under Common Law, the answer to these questions was no. It was developed by the end of 19th century that third parties were necessarily strangers to contract and hence could neither acquire the rights nor incur obligations upon any party to a contract to which they themselves were not a party. *"The doctrine of privity means that a contract cannot, as a general rule, confer rights or impose obligations arising under it on any person except the parties to it."* ***[ii]***

## WHAT IS MEANT BY PRIVITY OF CONTRACT?

If A makes a contract with B, he comes under a legal obligation to pay damages if he fails to keep his promise. The enforceability or liability as regards this contract lies firmly in the hands of A and B to the exclusion of others, this is the foundation of the doctrine of privity of contract.

The doctrine of privity of contract is that a contract cannot confer rights or impose those obligations arising under it, on any person except the parties to it. The term "parties" may seem simple enough but there are situations where it may become doubtful as to exactly who the parties are and resultantly, who, in the eyes of the law should be liable or should be compensated in event of inevitable breaches that may occur from time to time.

## HISTORY

Though the doctrine of privity was recognised and established in the case of ***Tweddle v. Atkinson*** ***[iii]***, its foundations had been laid by the English courts over the years, starting from as early as the end of 16th century. But in these cases, it can be seen that the Courts rather decided upon them by keeping in mind the so-called 'Interest Theory'. This theory basically meant that only he who had an interest in the promise could bring up an action before the court, or in the words of the Court, *"He that hath interest in the promise shall have the action"* ***[iv]***.

The first recorded case of such an instance was decided upon in 1599. This was the case of ***Levett*** **v.** ***Hawes*** ***[v]***. In this case, a father brought an action of assumpsit upon a promise made directly to him that marriage money would be paid to his son. The court was of the opinion that the action ought to have been brought by the son, *"for the promise is made to the son's use and the ordinary covenants of marriage are*

*with the father to stand seized to the son's use; and the use shall be changes and transferred to the son, as if it were a covenant with himself; and the damage of non-performance is thereof to the son."**[vi]***

***Rippon* v. *Norton*[vii]**which was decided in the year of 1602. In this case, the father of a child's assumpsit on the father of another child in order to stop the latter child from assaulting the former. But the objection made by the defendant party, which was relied upon the case of *Levett*v. *Hawes*[viii], was upheld by the court and it was held that *"…because there is no damage to the father by the battery to the son an action lies not for the father. And although it were objected that the father was at the charge for the curing the son of his wounds, yet, because it was a thing he was a thing he not compelled unto, it is no cause why he should maintain this action."*

Another important decision is that of ***Hadves*v. *Levit*[ix]**(1632). In this case, the bride's father (the defendant) had promised the groom's father (the plaintiff) that he would pay would pay 200 pounds to the plaintiff's son after the marriage had taken place and hence the plaintiff on this condition gave his consent for the marriage. But, after the marriage, the defendant failed to pay the required sum to the son which resulted in the plaintiff bringing and action in assumpsit. This claim was rejected by the Court of Common Pleas. Richardson, J. stated that the action should have been *"more properly"* brought by the son, for he was the person *"in whom the interest is".*

In ***Dutton* v. *Poole*[x]**a son promised his father that, in return for his father not selling a wood, he would pay 1000 pounds to his sister. The father refrained from selling the wood, but the son did not pay. It was held that the sister could sue, on the ground that the consideration and promise to the father may well have extended to her on account of the tie of blood between them.

## ESTABLISHMENT AND DEVELOPMENTS IN THE RULE

Though many cases were decided in the 17th century, the privity rule was still not established. It took a few more centuries for the rule to take its form as we know it. A study of a few cases decided in the 18th century and the 19th are essential in order to reach that establishment.

In ***Marchington* v. *Vernon*[xi]**, Buller J said that, independently of the rules prevailing in mercantile transactions, 13 if one person makes a promise to another for the benefit of a third, the third may maintain an action upon it.

In ***Carnegie* v. *Waugh*[xii]**, the tutors and curators of an infant, C, executed an agreement for a lease with A, for an annual rent to be paid to C. It was held that C could sue on the instrument, even though he was not a party to it.

In spite of these cases favouring actions by third party beneficiaries, it is not accurate to say that the third party rule was entirely a 19th century innovation. There were other 16th and 17th century cases where a third party was denied an action on the grounds that the promisee was the only person entitled to bring the action[xiii]. There were also cases where the reason given why the third party could not sue was because he was a stranger to the consideration, that is, he had given nothing in return for the promise[xiv]. These cases typically involved the following facts. B owed money to C. A would agree with B to pay C in return for B doing something for A, such as

working or conveying a house. A would not pay, and C would sue A. C would lose because he or she had given nothing for A's promise.

***Tweddle* v. *Atkinson*[xv]**: This is considered to be one of the most significant decisions which to the doctrine of privity. In this case, the plaintiff's father, and his prospective father-in-law, mutually agreed to pay sums of money to the plaintiff on marriage. The plaintiff duly married, but the father-in-law died before his portion of money had been paid. It was held that the plaintiff could not recover the money, even though the agreement had expressly provided that the plaintiff should have the right to sue on it. Wightman J said: *"It is now established that no stranger to the consideration can take advantage of a contract, although made for his benefit."*, whereas, Crompton J said that *"consideration must move from the promisee".*

The authority of *Tweddle v Atkinson*[xvi]was soon generally acknowledged. In ***Gandy v Gandy*[xvii]**, Bowen LJ said that, in spite of earlier cases to the contrary, *Tweddle v Atkinson*[xviii]had laid down "the true common law doctrine".

In ***Dunlop Pneumatic Tyre Co Ltd v Selfridge & Co Ltd.***[xix] the House of Lords accepted that it was a fundamental principle of English law that only a party to a contract who had provided consideration could sue on it.

In ***Drive Yourself Hire Co (London) Ltd v Strutt*[xx]**, Denning LJ said:

*"It is often said to be a fundamental principle of our law that only a person who is a party to a contract can sue on it. I wish to assert, as distinctly as I can, that the common law in its original setting knew no such principle. Indeed, it said quite the contrary. For the 200 years before 1861 it was settled law that, if a promise in a simple contract was made expressly for the benefit of a third person in such circumstances that it was intended to be enforceable by him, then the common law would enforce the promise at his instance, although he was not a party to the contract."*

Despite several attempts by Denning LJ to allow rights of suit by third party beneficiaries,[xxi] the House of Lords reaffirmed the general rule in ***Midland Silicones Ltd v Scruttons Ltd*[xxii]** Viscount Simonds said: *"*[*H]eterodoxy, or, as some might say, heresy, is not the more attractive because it is dignified by the name of reform. ...If the principle of jus quaesitumtertio is to be introduced into our law, it must be done by Parliament after a due consideration of its merits and demerits"*.

# EXCEPTIONS TO RULE OF PRIVITY

## Common Law Exceptions:

**A.) Trust:** Trust is a well-established exception to the rule of privity. This means that if A makes a promise to B for the benefit of C, C can enforce this promise if B has constituted himself trustee of A's promise for C[xxiii]. But this rule is subject to certain restrictions. A promisee can be held to be a trustee for a third party only if he has the **intention** to create a trust[xxiv] and this **intention** must be to benefit the particular third party and not third parties generally.

Also, the **intention** to benefit the third party must be irrevocable.[xxv] And a mere intention to confer a benefit is not enough, there must be an intention to create a trust. An intention to create a trust is clearly distinguishable from a mere intention to make a gift.[xxvi]

An Indian case relevant under this head is that of ***Rana Uma Nath Baksh Singh* v. *Jang Bahadur****[xxvii]*. In this case:

*U* was appointed by his father as his successor and was put in possession of his entire estate. In consideration, thereof *U* agreed with his father to pay a certain sum on money and to give a village to *J,* the illegitimate son of his father, on his attaining majority.

It was held that in the circumstances mentioned above a trust was created in favor of *J* for the specified amount and the village, Hence he was entitled to maintain the suit.

**B.) Covenants Concerning Land:** The law allows certain covenants (whether positive or restrictive) to run with land so as to benefit (or burden) people other than the original contracting parties. The relevant covenant may relate to freehold land or leasehold land. The law on covenants relating to leasehold land has recently been reformed by the Landlord and Tenant (Covenants) Act 1995.

The benefit and burden of covenants in a lease granted prior to 1996 would pass on an assignment of the lease or reversion so as to benefit or bind the assignee of the lease or the reversion, provided that the covenant "touched and concerned" the land.[xxviii]

**C.) Agency:** Agency is the relationship which exists between two persons, one of whom (the principal) expressly or impliedly consents that the other should act on his behalf, and the other of whom (the agent) similarly consents so to act or so acts.[xxix] Under this, the principal, i.e. the third party, may be benefited o burdened. The existence of the principal does not have to be known to the party with whom the agent is contracting. Also, an agent may be the agent of both the contracting parties. Thus insurance brokers are both agents of the insured and of the insurer.[xxx]

Although one can normally say that the principal is the real party to the contract concluded by his agent, agency can also be viewed as an exception to the privity doctrine as in that the principal, on the basis of a contract with a third party, that contract being concluded by his agent, is able to sue (and be sued) on it.

**D.) Tort of Negligence:** The tort of negligence can be viewed as an exception to the third party rule where the negligence in question constitutes the breach of a contract to which the plaintiff is not a party. For example, the classic case of negligence, ***Donoghue* v *Stevenson****[xxxi]*, established that where A supplies goods to B under a contract with B, A may owe a duty to C in respect of personal injury or damage to property caused by defects in those goods. But the right not to be injured or to have one's property damaged by another's negligence exists independently of any contractual undertaking by A. It is only in a very wide sense, therefore, that standard examples of the tort of negligence constitute exceptions to the third party

rule. Also, this rule goes into contradiction with that established by the case of ***Dunlop Pneumatic Tyres Co Ltd* v. *Selfridge Ltd*[xxxii]**where the pursuer could acquire no benefit under that contract because she was a third party to it. Yet, according to the principle laid down in ***Donoghue* v. *Stevenson*[xxxiii]**, the pursuer might recover against a manufacturer in respect of physical injuries suffered as a result of the manufacturer's negligence.

**E.) Assignment**: Except when personal considerations are at its foundation,[xxxiv] the benefit of a contract may be assigned (that is transferred) to a third party. The assignment is effected through a contract between the promisee under the main contract (that is, the assignor) and the third party (that is, the assignee). In addition to assignment by an act of the parties, there exists assignment by operation of law. The assent of the promisor is not necessary for an assignment. Assignment may therefore deprive promisors of their chosen contracting party, although safeguards are imposed to protect promisors.

In considering reform of the third party rule, assignment constitutes a particularly significant exception. For if, immediately after a contract for a third party's benefit is made, the promisee assigns his rights under it to that third party, the third party can enforce the contract and the promisee loses all right to enforce, vary or cancel the contract. There is a thin divide between (i) making a contract for the benefit of a third party; and (ii) making a contract for the benefit of a third party and, immediately thereafter, assigning that benefit to the third party (especially where the third party does not provide consideration). If an immediate assignment is valid, there can hardly be fundamental objections to allowing the third party to sue without an assignment. It also follows that in considering the details of reform it is instructive to consider the rules of assignment dealing with, for example, the defences and counterclaims available to the promisor (the principle is that an assignee takes "subject to equities"), and joinder of the original promisee (joinder of the assignor is sometimes necessary).[xxxv]

**F.) Vicarious Immunity**: The principle vicarious immunity is illustrated by the case of ***Elder, Dempster Ltd v Paterson Zochonis& Co Ltd.*[xxxvi]**. In this case, the House of Lords held that the owners of a vessel were entitled to rely on the limitations contained in a bill of lading issued pursuant to a contract between the cargo owners and the charterers of the vessel, when they (owners of the vessel) were sued by the cargo owners in respect of the damage caused by bad stowage.

Perhaps the most significant point is that some of their Lordships seemed to accept a principle of vicarious immunity, according to which a servant or agent who performs a contract is entitled to any immunity from liability which his employer or principal would have had. Hence, although the ship-owners may not have been privy to the contract of carriage (between shipper and charterer) they took possession of the goods on behalf of, and as agents for, the charterers and so could claim the same protection as their principals.

Although the principle of vicarious immunity was subsequently generally accepted by the lower courts, it did not survive the decision of the House of Lords (Lord

Denning dissenting) in ***Midland Silicones Ltd v Scruttons Ltd.****[xxxvii]*the defendant stevedores, engaged by the carrier, negligently damaged a drum containing chemicals. When the cargo-owners sued in tort, the stevedores unsuccessfully attempted to rely on a limitation clause contained in the bill of lading between the carriers and the cargo owners. The majority of the House of Lords confirmed English law's adherence to the privity of contract doctrine and was not prepared to hold that the principle of vicarious privity of contract doctrine and was not prepared to hold that the principle of vicarious immunity was the ratio of *Elder, Dempster*.[xxxviii]

**G.) Collateral Contract:** A contract between two parties may be accompanied by a collateral contract between one of them and a third party. A collateral contract may in effect allow a third party to enforce the main contract (between A and B). For instance, where C buys goods from B, there may be a collateral contract between C and the manufacturer in the form of a guarantee. Collateral contracts have been used as a means of rendering exclusion clauses enforceable by a third party; and are extensively used in the construction industry as a way of extending to subsequent owners or tenants the benefits of a builder's or architect's or engineer's contractual obligations. Strictly speaking, of course, a collateral contract is not an exception to the third party rule in that the 'third party' is a party to the collateral contract albeit not a party to the main contract.

In ***Shanklin Pier* v. *Detel****[xxxix]* the plaintiff had employed contractors to paint their pier, and instructed them to use a paint made by the defendants. This instruction was given in reliance on a representation made by the defendants to the plaintiffs that the paint would last seven years. It lasted for only 3 months. It was held that the defendants' representation gave rise to a collateral contract that the paint would last seven years.

**H.) Estoppel or Acknowledgement:** Where by the terms of a contract a party is required to make a payment to a third person and he acknowledges it to that third person, a binding obligation is thereby incurred towards him. Acknowledgment may be express or implied. This exception covers cases where the promisor by his conduct, acknowledgment, or otherwise, constitutes himself an agent of the third party. The case of ***Davaraja Urs* v. *Ram Krishnaiah****[xl]*is a relevant case under this head:

*A* sold his house to *B* under a registered sale deed and left a part of the sale price in his hands desiring him to pay this amount to *C*, his creditor. Subsequently *B* made part-payments to *c* informing him that they were out of the sale price left with him and that the balance would be remitted immediately. *B*, however, failed to remit the balance and *C* sued him for the same.

The suit was held to be maintainable. *"Though originally there was no privity of contract between B and C, B having subsequently acknowledged his liability, C was entitled to sue him for recovery of the amount."*

**I.) Marriage Settlement, Partition or Other Family Arrangements:** Where an agreement is made in any of the mentioned concerns and a provision is made for the benefit of a person, he may take advantage of that agreement although he is no party to it. In ***Rose Fernandez* v. *Joseph Gonsalves****[xli]*a girl's father entered into an

agreement for her marriage with the defendant, it was held that the girl after attaining majority could sue the defendant for damages for breach of the promise of marriage and the defendant could not take the plea that she was not a party to the agreement.
Another relevant case is that of ***Daroptiv. Jaspat Rai****[xlii]*:

*The defendant's wife left him because of his cruelty. He then executed an agreement with her father, promising him to treat her properly, and if he failed to do so, to pay her monthly maintenance and to provide her with a dwelling. Subsequently she was again ill-treated by the defendant and also driven out. She was held entitled to enforce the promise made by the defendant to her father.*

### Statutory Exceptions:

**A.) Life Insurance**: 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.

**B.) Fire Insurance:** Under section 83 of the Fire Prevention (Metropolis) Act 1774, where an insured house or building is destroyed by fire, the insurer may be required "upon the request of any person or persons interested" to lay out the insurance money for the restoration of the building. This means that a tenant can claim under its landlord's insurance, and a landlord under its tenant's insurance.[xliii]

**C.) Insurance by Persons with Limited Interest:** Any person who has an interest in the subject-matter of a policy of marine insurance can insure 'on behalf of and for the benefit of other persons interested as well as for his own benefit'[xliv] Also, where property is sold and suffers damage before the sale is completed, any insurance moneys to which the vendor is entitled in respect of the damage must be held for the purchaser and paid over on completion[xlv]. This has been upheld in various case laws[xlvi]

**D.) Motor Insurance:** Under section 148(7) of the Road Traffic Act 1988, a person issuing a policy under Section 145 of the Act shall be liable to indemnify the persons or classes of person specified in the policy in respect of any liability which the policy purports to cover in the cases of such persons.

**E.) Third Parties (Rights Against Insurers) Act 1930:** Section 1(1) this Act provides that the insured's right against the insurer shall, notwithstanding anything in any Act or rule of law to the contrary, vest in the third party to whom liability was incurred. This position also applies where the insured dies insolvent[xlvii].

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

## RULE OF PRIVITY IN OTHER COUNTRIES

When it comes to the rule of privity, the English Law is no alone in having it. Various other jurisdiction either have it or have adapted it. Some believe it to be very likely

that the introduction of the rule into English Law was accompanied by that in the French law as well, which took place in the early 19th century. Also, when the English Law explicitly, and without any ambiguity, reaffirmed the principle in ***Dunlop v Selfridge****[xlviii]*, this set led to be followed in a number of common law legal systems- for example, in both Canada[xlix] and Australia[l], a strict privity doctrine took root. Elsewhere, though particularly in the United States, a less strict approach had survived, with an explicit third party beneficiary rule being applied[li]. The same was true in Scotland[lii]. Also, in most of these jurisdictions, it has been experienced that it is remarkably difficult to maintain a strict line on privity and hence this doctrine is been criticized a lot, leading the paths to, either legislative relaxation in most of these jurisdictions, a well-known example of this being the **New Zealand Contracts (Privity) Act 1982**, or requiring the courts to address upon the need for reform in ahead-on fashion. A decision of the High Court of Australia ***Trident General Insurance Co Ltd* v. *McNiece Bros Pty Ltd****[liii]*and that of the Canadian Supreme Court ***London Drugs Ltd* v. *Kuehne and Nagel International Ltd****[liv]*are the two most significant cases in this aspect.

In the *Trident* case, the question was whether McNiece, a contractor employed by Blue Circle, could rely on an insurance policy written by Trident for Blue Circle. The policy was to cover Blue Circle and all its subsidiaries, contractors and sub-contractors involved in specified construction contracts. Although McNiece was within the category covered it was not directly in contract with Trident. Despite this lack of privity, the majority of the Hifh Court ruled in favour of McNiece. In the words of Toohey J[lv]:

*"When a rule of the common law harks back no further than the middle of the last century, when it has been the subject of constant criticism and when in its widest form, it lacks a sound foundation in jurisprudence and logic and further, when that rule has been so affected by exceptions or qualifications, I see nothing inimical to principled development in this Court now declaring the law to be otherwise in the circumstance of the present case."*

In the *London Drugs* case, the Canadian Supreme Court has followed the example of the *Trident* case by openly relaxing the privity doctrine in the *London Drugs* were as follows Pursuant to a warehousing contract, London Drugs delivered a transformer to Kuehne and Nagel for storage. Clause 11(b) of the contract provided:

*"The warehouseman's liability on any one package is limited to $40 and unless the holder has declared in writing a valuation in excess of $40 and paid the additional charge specified to cover warehouse liability."*

As in the *Trident* case, the central issue in *London Drugs* was whether the particular circumstances were appropriate ones in which to relax the privity doctrine. The majority had little doubt that the circumstances were eminently appropriate:

*"When all the circumstances of this case are taken into account, including the nature of the relationship between employees and their employer, the identity of interest with respect to contractual obligations, the fact that the appellant knew that employees would be involved in performing the contractual obligations, and the absence of a clear indication in the contract to the contrary the term 'warehouseman' in clause 11 (b) of the contract must be interpreted as meaning 'warehousemen'. As such, the respondents are not complete strangers to the limitation of liability clause. Rather, they are unexpressed or implicit third party beneficiaries with respect to this clause."*

## Examples of Legislative Relaxations:

**Western Australia:**

Section 11 of the 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 ona person who is not named as a party to the contract, the contract is…enforceable by that person in his own name…

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,[lvi] and in any action on the contract by the third party, all parties to the contract must be joined.[lvii] 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 of the [promisor]".[lviii] 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.[lix]

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 v Southern Meat Packers Ltd**[lx]***, the Supreme Court of Western Australia found that, where the plaintiff third party had established the 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.

**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 that promise.

Prior to acceptance, the promisor and promisee may vary or discharge the terms of the promise without the beneficiary's consent.[lxi] 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.[lxii] On acceptance, the beneficiary is bound to perform any acts that may be required of him by the terms of the promise.[lxiii] Defences that can normally be raised against an action to enforce a promissory duty can be raised by the promisor against the beneficiary.[lxiv]

**New Zealand:**

In 1981, the New Zealand Contracts and Commercial Law Reform Committee presented a Report on the third party rule, which appended draft legislation to implement the recommended reforms.[lxv] 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[lxvi] 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 parties could usually be achieved by the courts. The Report said:

*"We are not convinced by such arguments. We have looked in vain for a solid basis of policy justifying the frustration of contractual intentions…[W]e are left with a sense of irritation like that which, we suspect, motivated the majority of the Privy Council in New Zealand Shipping Co Ltd v Satterthwate & Co Ltd,**[lxvii]** to say, '…to give the appellant the benefit of the exemptions 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 observations of Lord Scarman (sometime Chairman of the English Law Commission) in Woodar Investment Development Ltd v Wimpey Construction (UK) Limited.**[lxviii]**"*

**United States of America:**

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

Since the decision of the New York Court of Appeals in ***Lawrence v Fox,***[lxix] it has become generally accepted that a third party is able to enforce a contractual obligation made for his benefit. However, the problem of defining what is meant by a third party beneficiary has never adequately been solved. Section 133 of the first Restatement of Contracts published in 1932 distinguished donee beneficiaries, creditor beneficiaries and incidental beneficiaries: only donee and creditor beneficiaries could enforce contracts made for their benefit. A person was a "donee beneficiary" if the purpose of the promisee was to make a gift to him, or to confer upon him a right not due from the promisee. A person was a "creditor beneficiary" if performance of the promise would satisfy an actual or asserted duty of the promisee to him. A person was an "incidental beneficiary" if the benefits to him were merely incidental to the performance of the promise.

**Canada:**

Two recent judgments of the Supreme Court of Canada have modified the law relating to privity: ***London Drugs Ltd v Kuehne & Nagel International Ltd****[lxx]*and ***Fraser River Pile & Dredge Ltd v Can-Dive Services Ltd****[lxxi]*. In the *Fraser River* case, a third party beneficiary sought to rely on a contractual provision so as to defend against an action brought by one of the contractual parties (the insurer). The court held that the third party beneficiary was entitled to rely on the waiver of subrogation clause whereby the insurer expressly waived any right of subrogation against the third party beneficiary. Iacobucci J emphasised that in appropriate circumstances the courts should not abdicate their judicial duty to decide on incremental changes to the common law which were necessary to address emerging needs and values in society.21 In the ***London Drugs Ltd*** case, employees of a warehouseman sought to rely on the limitation of liability clause in the contract between their employer and the client (the bailor) when the employees were sued by the bailor. The Supreme Court held that the privity rule could be relaxed where the parties to the contract had, expressly or by implication, intended the relevant provision to confer a benefit on the third parties (the employees), and the action taken out by the third parties came within the scope of the agreement between the initial parties. The employees fulfilled these two conditions, and thus could benefit from the limitation clause, despite the privity doctrine. The court recognised a limited exception to the doctrine in the circumstances of the case so as to conform to *"commercial reality and justice".*

**Hong Kong:**

The ***Trident*** case was considered in *B + B Construction Ltd* v *Sun Alliance and London Insurance Plc*,[lxxii]the facts of which were similar to those of the *Trident* case. The plaintiff brought an action against the defendant as the insurer for an indemnity. Since the defendant did not take the point that the plaintiff was not a party to the insurance contract, the Hong Kong Court of Appeal proceeded on the

footing that the plaintiff's claim, if otherwise good, was enforceable in the usual way. Hence, at issue was whether the scope of the indemnity extended to the plaintiff. Godfrey VP (with whom Ribeiro JA agreed) nonetheless stated incidentally:

*"[the court is] aware of the judicial abrogation of the rule effected in Australia by the decision of the High Court (split 4 to 3) in [the Trident case], a case the facts of which bear many similarities to our own. ...But here, in Hong Kong, the law remains as magisterially stated by Viscount Haldane LC in Dunlop Pneumatic Tyre Co Ltd v Selfridge & Co Ltd: '... only a person who is a party a contract can sue on it. Our law knows nothing of a jus quaesitumtertio...'* ***[lxxiii]*** *"*

The Privy Council in ***Re the Mahkutai*** ***[lxxiv]*** mentioned both the *Trident* case and the ***London Drugs Ltd*** case. Lord Goff of Chievely of the Privy Council stated in an *obiter dictum*:

*"the time may well come when, in an appropriate case, it will fall to be considered whether the courts should take what may legitimately be perceived to be the final, and perhaps inevitable, step in this development, and recognize in these cases a fully-fledged exception to the doctrine of privity of contract, thus escaping from all the technicalities with which courts are now faced in English law. It is not far from their Lordships' minds that, if the English courts were minded to take that step, they would be following in the footsteps of the Supreme Court of Canada (see [the London Drugs Ltd case]) and, in a different context, the High Court of Australia (see [the Trident case]).Their Lordships have given consideration to the question whether they should face up to this question in the present appeal. However, they have come to the conclusion that it would not be appropriate for them to do so, first, because they have not heard argument specifically directed towards this fundamental question, and second because, as will become clear in due course, they are satisfied that the appeal must in any event be dismissed."*

The Privy Council here raised the possibility of "a fully-fledged exception" to the privity doctrine. Nevertheless, as Godfrey VP reiterated in the *B + B* case, the privity doctrine is still part of the Hong Kong law.[lxxv]

# RULE OF PRIVITY AND INDIA

"*Doctrine of Privity*" is one of the most controversial doctrines under law of contracts, including that in the country of India. The debates are not just due to the lack of clarity in the statutes or dissenting judicial pronouncements but much of these

owe to the academic and judicial debates linked with the ground roots of this doctrine.

The debates and discussions on the Doctrine of Privity are relevant not only in daily life commercial contracts but also in the less frequent and comprehensive transactional contracts. It can be seen that practices such as imposing obligations on other party's affiliates, relatives and agents with respect to terms like restrictive covenants, non-compete and confidentiality obligations are quite common for the parties under a contract these days. Interest of such third parties secured by the contracting parties through which they have been benefited or burdened by the contract. No doubt there are volumes of cases in the books and journals in which such related third parties who are not parties to a contract have been allowed to sue upon it and their interest is secured against any breach by the counter party. But those cases are based on the view that such related third parties are claiming through a party to the contract, that it is in the position of a "*cestuique trust*"[lxxvi] or of a principal suing through an agent, that under the old procedure he/it could have filed a suit in equity, even if he/it could not have sued at common law. Such decisions are recognized as exceptions to a general principle that only parties to the contract can sue upon it. Hence the main question in consideration under this part of the study is to discover if it possible for these related parties to enforce their rights or secure their interest in as a third party.

**Section 2(d) in The Indian Contract Act, 1872:** When, at the desire of the promisor, the promisee or any other person has clone or abstained from doing, or does or abstains from doing, or promises to do or to abstain from doing, something, such Act or abstinence or promise is called a consideration for the promise.

One of the most notable features of Section 2(d) is that the act which is to constitute a consideration may be done by "the promisee or any other person". It means therefore, that as long as there is a consideration for a promise, it is immaterial who has furnished it. It may move from the promisee or, if the promisor has no objection, then from any other person. This is the principle as established by the English Courts in as early as 1677 in the case of ***Dutton* v. *Poole*** ***[lxxvii]***.

It has been already established in this study that the Doctrine of Privity as such was established in the case of ***Tweddle* v. *Atkinson*** ***[lxxviii]*** and that the principle laid down, or the law declared in it was affirmed in ***Dunlop Pneumatic Tyre Co. Ltd. v. Selfridge & Co. Ltd*** ***[lxxix]***.

The principle in ***Tweddle v Atkinson*** ***[lxxx]*** was based on two major grounds, firstly the third party was not privy to the contract and secondly, the consideration did not flow from the third party claiming under the contact. The two principles of privity and consideration have become tangled but are still distinct. Even though under Indian Contract Act, the definition of consideration is wider than in English law and the consideration can very well be given by a non-contracting party, yet the common law principle of Doctrine of Privity is generally accepted in India.

In India also there has been a great divergence in of opinion in the courts as to how far a stranger to contract can enforce it. There are many decided cases which declare that a contract cannot be enforced by a person who is not a party to the contract and

that the rule in ***Tweddle* v. *Atkinson*[lxxxi]**is very much applicable in India as well. The Privy Council in its decision in ***Jamna Das* v. *Ram Autar*[lxxxii]**extended this rule to India. In this case *A* borrowed ₹40,000 by executing a mortgage of her zamindari in favour of *B*. Subsequently she sold her property to C for ₹44,000 and allowed C, the purchaser, to retain ₹400,000 of the price in order to redeem the mortgage if he thought fit. B sued C for the recovery of the mortgage money, but he could not succeed because he was no party to the agreement between A and B.
Lord MacNaughtan, in his very short judgment, said that the undertaking to pay back the mortgagee was given by the defendant to the vendor. *"The mortgagee has no right to avail himself of that. He was no party to the sale. He was no party to the sale. The purchases entered into no contract with him, and the purchaser is not personally bound to pay this mortgage debt."*
This Doctrine of Privity, though accepted in many jurisdictions, has been subject to various reforms, each depending on the jurisdiction in question. In the words of Jenkins, CJ:

*"That Indian Contract Act is unlike the English Contract Act and the limits with which the doctrine of privity of contract operates in English law cannot with same vigour be applicable to Indian Contract Act"[lxxxiii].*

Time and again Indian judiciary has reiterated that the administration of justice should not be hampered by *Tweedle v Atkinson*[lxxxiv] and that in India, we are free from these trammels and are guided in matters of procedure by the rules of justice, equity and good conscience. The application of Doctrine of Privity has been appreciated by the Indian courts with the well –recognized exceptions like beneficiaries of a trust, family arrangement and marriage settlements, tort, collateral contracts, creation of charge or covenants running with land. The aforementioned are more or less the well- accepted and settled exceptions to the Doctrine of Privity. However these are not exhaustive and from time to time, number of exceptions against the Doctrine of Privity has been evolved and recognized by Indian judiciary and more than often quoted exception is that a person for whose benefit the contract is entered into can certainly sue as it is "beneficiary" in the contract.[lxxxv]
The Privy Council in ***Khwaja Muhammad Khan* v. *Hussaini Begum*[lxxxvi]**observed:
*"In India and among communities circumstanced as the Mohemmedans, among whom marriages are contracted for minors by parents and guardians it might occasion serious injustice if the common law doctrine was applied to agreements or arrangements entered into in connection with such contracts,"*

In ***Muniswami Naicker* v. *Vedachala Naicker*[lxxxvii]**, the Madras High Court held:

*"There is ample authority for he proposition that in this country, and indeed in a certain class of cases in England where a contract is made between 'A' and 'B' for the benefit of 'C', 'C' is entitled to sue the defaulting party. It is unnecessary to cite authorities, but the principle is firmly established for this country by the decision of the Privy Council in Khwaja Muhammad Khan v. Hussaini Begum[lxxxviii]."*

The Supreme Court has, by its decision in *M.C. Chacko v State of Travancore*[lxxxix], held that a person not a party to a contract cannot subject to certain well recognized exceptions, enforce the terms of the contract. The recognized exception mentioned in the quoted judgment is worded widely so as to cover the beneficiaries under the terms of the contract.

In this case, Shah AG. CJ endorsed the statement of Rankin CJ in *Krishna Lal Sahu* v. *Promila Bala Dasi*[xc], and after referring to the observations of Lord Haldane in ***Dunlop* v. *Selfridge***[xci]said:

*"The Judicial Committee applied that rule in Khwaja Muammad Khan v. Hussaini Begum*[xcii]*. In a later case, Jamna Das v. Ram Autar*[xciii]*, the Judicial Committee pointed out that the purchaser's contract to pay off a mortgage could not be enforced by a mortgagee who was not a party to the contract. It must be therefore taken as well-settled that except in the case of a beneficiary under a trust or in the case of a family arrangement, no right may be enforced by a person who is not a party to the contract…It is a settled law that a person not a party to a contract cannot enforce the terms of the contract."*

Views on the rights of third party beneficiaries have been laid down by other courts of the country. For instance in *Bh**ujendra Nath v. Sushamoyee Basu***[xciv], the division bench of the Calcutta High Court has held that a stranger to a contract which is to his benefit is entitled to enforce the agreement to his benefit. In ***Pandurang v. Vishwanath***[xcv], it has been held the person beneficially entitled under the contract can sue even though not a party to the contract itself.

In ***Khirod Behari Dutt v. Man Gobinda***[xcvi], Lord-Williams J said:

*"..Though ordinarily only a person who is a party to the contract can sue on it, where a contract is made for the benefit of a third person, there may be an equity in the third person to sue upon the contract."*

Hence it is clear that Indian judiciary has recognized "beneficiary" to the contract as an exception to the general rule of Doctrine of Privity. So the next question arises as to who may be treated as a "beneficiary" under a contract? Are there any criteria to be met to fall under the category of "beneficiary"? Whether affiliates, relatives and agents of the parties can be treated as "beneficiary" if their role is restricted to few terms like mentioned hereinabove?

# REFORMS IN THE RULE

This Third Party rule had been criticized widely over the number of years by various academics, law reform bodies and the most important to our studies, the judiciary. In this section we focus our attention on calls for reform made by the judiciary in past cases.

In ***Beswick v Beswick***,[xcvii] Lord Reid cited with approval the Law Revision Committee's proposals that when a contract by its express terms purports to confer a benefit directly on a third party, it should be enforceable by the third party in its own name. While implying that the way forward was by legislation, he stated that the House of Lords might find it necessary to deal with the matter if there was a further long period of Parliamentary procrastination.

In ***Woodar Investment Development Ltd v Wimpey Construction UK Ltd****[xcviii]*, Lord Salmon (dissenting) regarded the law concerning damages for loss suffered by third parties as most unsatisfactory and hoped that, unless it were altered by statute, the House of Lords would reconsider it.168 Lord Scarman expressed "regret that [the] House has not yet found the opportunity to reconsider the two rules which effectually prevent [the promisee] or [the third party] recovering that which [the promisor], for value, has agreed to provide."169 He reminded the House that twelve years had passed since Lord Reid in ***Beswick v Beswick****[xcix]* had called for are consideration of the rule, and hoped that all the cases which "stand guard over this unjust rule" might be reviewed.170 Lord Scarman concluded his judgment with an unequivocal call for reform:

*"[T]he crude proposition…that the state of English law is such that neither [the third party] for whom the benefit was intended nor [the promisee] who contracted for it can recover it, if the contract is terminated by [the promisor's]refusal to perform, calls for review: and now, not forty years on."*

In ***Swain v Law Society****[c]*, Lord Diplock referred to the general non-recognition of third party rights as *"an anachronistic shortcoming that has for many years been regarded as a reproach to English private law".*

In ***The Pioneer Container****[ci]* Lord Goff called into question the future of the rule, and in *White v Jones****[cii]*** his Lordship said, *"[O]ur law of contract is widely seen as deficient in the sense that it is perceived to be hampered by the presence of an unnecessary doctrine of consideration and (through a strict doctrine of privity of contract) stunted through a failure to recognise a jus quaesitumtertio".*

# CONTRACTS (RIGHT OF THIRD PARTIES) ACT 1999

This is one of the biggest reforms that took place when the rule of privity or, precisely, third party beneficiaries are considered. Five years after the publication of its provisional recommendations in favour of reforming the privity rule in English

Contract Law, the Law Commission confirmed its view and, indeed the view of a considerable body of judicial and academic options, as well as that of the vast majority of the Commission's consultees- that the privity rule was ripe for reform. In its central recommendation, the Commission proposed that the third parties (subject to being expressly identified) should have the *right* to enforce contractual provisions where either

- The contracting parties intend to confer such a right upon the third party (the so-called 'first-limb' of the test of enforceability)
- The contracting parties intend to confer a *benefit* on the third party (the so-called 'second limb' of the test of enforceability) –

-provided that the contracting parties do not also intend that the third party beneficiary should *not* have the right to enforce the contract.
The committee took a view that the relations between privity and consideration was largely unproblematic- the consideration requirement is relevant as to whether there is an enforceable bargain (a contract); the privity doctrine determines who is permitted to enforce the contract. However, in the Report, the Commission's reasoning ran along the following lines:

- The proposed right to enforce puts a third party beneficiary in a better position that the gratuitous promisee
- Neither the third party beneficiary nor the gratuitous promisee provides consideration; therefore
- The proposal must involve a relaxation of the consideration requirement.

The report, thus, signalled a decisive break from the orthodoxy of the privity doctrine which, in the earlier part of the century, was identified by Viscount Haldane LC as one of the fundamental principles of English contract law[ciii].

# CONCLUSION

Thus with the help of essential legislative actions and decisions in various countries, especially those of England and India, this study has established the very basis of the Doctrine of Privity.

The current relaxed requirements of modern contract law and non-conventional approach of the judiciary in relation to Doctrine of Privity have provided an avenue for redress to genuinely affected persons who the strict interpretation of Doctrine of Privity might have been deprived of rights as such. Under the current operation of the law, a stranger could be awarded damages if the infringement is proved. However the stranger should be included under the scope of "intended beneficiary" who has reciprocal obligations under the contract.[civ]

## Footnotes

[i] Infra n. 2
[ii]GH Treitel, The Law of Contract

[iii] 123 ER 762: I B&S 23: 30 LJ QB 218: 4 LT 468: 124 RR 610
[iv]*Corny and Curtis* v. *Collidon;* 1674 (1) Freem. K.B. 284
[v]Cro. Eliz. 654.
[vi]*Ibid*
[vii]Cro. Eliz. 849
[viii] Supra n. 4
[ix] (1632) Het. 176. This decision was supported, obiter, by Lord Mansfield in *Martyn* v. *Hind* (1776) 2 Cow p. 437, 443: ER 1174, 1177.
[x] (1678) 2 Lev 210; 83 ER 523
[xi](1797) 1 Bos& P 101, n (c); 126 ER 801, n (c)
[xii](1823) 1 LJ (OS) KB 89.
[xiii]*Jordan v Jordan* (1594) Cro Eliz 369; 78 ER 616 (C gave a warrant to B to arrest A for an alleged debt. A promised B that, in return for not arresting him, he would pay the debt. C failed in his action, on the ground, inter alia, that the promise had been made to B); *Taylor v Foster*(1600) Cro Eliz 776; 78 ER 1034 (A, in return for B marrying his daughter, agreed to pay to Can amount which B owed to C. In an action by B against A, it was held that B was the personto sue, being the promisee).
[xiv]*Bourne v Mason* (1669) 1 Ventr 6; 86 ER 5; *Crow v Rogers* (1724) 1 St 592; 93 ER 719; *Price vEaston* (1833) 4 B & Ad 433; 110 ER 518. Although in the former two cases, the reason why Cfailed was because he was a stranger to the consideration, *Price v Easton* contains seeds of moremodern doctrine: whereas Denman CJ said that no consideration for the promise moved fromC to A, Littledale J said that there was no privity between C and A.
[xv] Supra n. 3
[xvi]*Ibid*
[xvii](1885) 30 ChD 57, 69.
[xviii] Supra n. 3
[xix][1915] AC 847.
[xx][1954] 1 QB 250.
[xxi]*Smith and Snipes Hall Farm Ltd v River Douglas Catchment Board* [1949] 2 KB 500; *Drive Yourself Hire Co (London) Ltd v Strutt*[1954] 1 QB 250.
[xxii][1962] AC 446 (Lord Denning dissenting).
[xxiii]*Tomlinson* v. *Gill* (1756) Amb 330; *Lloyd's v. Harper* (1880) 16 Ch D 290; *Paul* v. *Constance* [977] 1 WLR 527.
[xxiv]*Swain* v. *Law Society* [1983] 1 AC 598; *Tito* v. *Waddell* (No 2) [1977] Ch 106
[xxv]*Re Sinclair's Life Policy* [1938] Ch 799; *Re Burgess' Business Policy* (1915) 113 LT 443; *Re Schebsman*[1944] Ch 83.
[xxvi]*Richards v Delbridge*(1874) LR 18 Eq 11; *Cleaver* v. *Mutual Reserve Fund Life Association* [1892] 1 QB 147, 152; *Re Foster* [1938] 3 All ER 357; *Green* v. *Russell* [1959] 1 QB 28.
[xxvii] AIR 1938 PC 245
[xxviii] By Law of Property Act 1925, s 78
[xxix]*Bowstead and Reynolds on Agency* (16th ed, 1996) para 1-001.

[xxx]*Toucheross& Co v Colin Bakr* [1992] 2 Lloyd's Rep 207; *Sin Yin Kwan v Eastern Insurance* [1994] 1 All ER 213.
[xxxi][1932] AC 562.
[xxxii] Supra n. 19
[xxxiii] Supra n.30
[xxxiv]Farrow v Wilson (1869) LR 4 CP 744
[xxxv]See *Chitty on Contracts* (27th ed, 1994), paras 19-002, 19-022-19-023.
[xxxvi] [1924] AC 522
[xxxvii][1962] AC 446
[xxxviii]Supra n. 35
[xxxix] [1951] 2 KB 854
[xl] AIR 1952 Mys 109
[xli] ILR (1924) 48 Bom 673: AIR 1925 Bom 97
[xlii] (1905) PR 171
[xliii]*Portavon Cinema Co* v. *Price & Century Insurance Co [1939] 4 All ER 601; Mark Rowlands Ltd* v. *Berni Inns Ltd* [1986] QB211; *Vural Ltd v Security Archives Ltd* (1989) 60 P & CR 258, 271-272;
[xliv] Marine Insurance Act 1906, s 14(2)
[xlv] Law of Property Act, 1925 s. 47
[xlvi]*Walters v Monarch Insurance Co* (1856) 5 E & B 870; *Hepburn v A Tomlinson (Hauliers) Ltd* [19660 AC 451; *Petrofina (UK) Ltd v. Magnaload Ltd.* [1984] QB 127; *Pan Atlantic Insurance Co Ltd v. Pine Top Insurance Co Ltd* [1988] 2 Lloyd's Rep. 505; *National Oilwell (UK) Ltd. V. Dac Offshore Ltd* [1933] 2 Lloyd's Rep. 582.
[xlvii] Section 1(2)
[xlviii] Supra n. 19
[xlix] See *e.g.Greenwood Shopping Plaza Ltd v. Beattie* (1980) 111 DLR (3d) 257
[l] See *e.g.Coulls v. Bagot's Executor and Trustee Co* [1967] ALR 385; *Wilson v Darling Island Stevedoing&Lighterage Co Ltd* (1956) 95 CLR 43
[li]*Lawrence v Fox* 20 NY 268 (1859), New York Court of Appeals Decision.
[lii]*Dundee Harbour Trustees v. Nicol*1915 SC (HL) 7, 13 per Lord Dunedin.
[liii] (1988) 165 CLR 107
[liv] [1993] 1 W WR 1
[lv] (1988) 165 CLR 107, 170-171
[lvi]Western Australia Property Law Act 1969, s 11(2)(a).
[lvii]Western Australia Property Law Act 1969, s 11(2)(b).
[lviii]Western Australia Property Law Act 1969, s 11(2)(c).
[lix]Western Australia Property Law Act 1969, s 11(3).
[lx][1981] WAR 241
[lxi]Queensland Property Law Act 1974, ss 55(2).
[lxii]Queensland Property Law Act 1974, s 55(3)(a) and (d).
[lxiii]Queensland Property Law Act 1974, s 55(3)(b).
[lxiv]Queensland Property Law Act 1974, s 55(4).

[lxv]New Zealand Contracts and Commercial Law Reform Committee, Privity of Contract (1981)
[lxvi] The Report, at para 3.1, considered the law of France, Germany, South Africa, Denmark,
Norway and Scotland.

[lxvii][1975] AC 154, 169.
[lxviii][1980] 1 WLR 277, 300-301
[lxix] Supra n. 47
[lxx](1992) 97 DLR (4th) 261
[lxxi][2000] 1 Lloyds Rep 199
[lxxii][2000] 2 HKC 295.
[lxxiii][1915] AC 847 at 853
[lxxiv][1996] 2 HKC 1.
[lxxv] THE LAW REFORM COMMISSION OF HONG KONG, REPORT,PRIVITY OF CONTRACT, September 2005
[lxxvi]Short for *cestui a que use le trust estcréé*, meaning 'the person for whose benefit anything is given in trust to another'.
[lxxvii](1677) 2 Lev 211
[lxxviii] Supra n.3
[lxxix]Supra n. 19
[lxxx] Supra n. 3
[lxxxi]*Ibid*
[lxxxii] (1911) 39 IA; 21 MLJ 1158
[lxxxiii]*DebnarayanDutt vs ChunilalGhose*, reported in (1914) ILR 41 Cal 137; approved and followed in *N DevarajeUrs v M Ramakrishniah* AIR 1952 Mys 109.
[lxxxiv] (1861) 1 B & S 393, [1861-73] All ER Rep 369, 124 RR 610
[lxxxv] TREATMENT OF "DOCTRINE OF PRIVITY" BY INDIAN JUDICIARY: Priyesh Sharma, Vaish Law Associates
[lxxxvi] (1910) 37 IA 152; 12 Bom LR 638
[lxxxvii] AIR 1928 Mad 23
[lxxxviii] Supra n. 80
[lxxxix]AIR 1970 SC 504
[xc] AIR 1928 Cal 518
[xci] Supra n. 19
[xcii] Supra n. 80
[xciii] Supra n. 76
[xciv]AIR 1936 Cal 66
[xcv]AIR 1939 Nag 20
[xcvi]AIR 1934 Cal 682
[xcvii][1968] AC 58, 72.
[xcviii][1980] 1 WLR 277.
[xcix] Supra n. 39
[c][1983] 1 AC 598, 611.

[ci][1994] 2 AC 324, 335.
[cii][1995] 2 AC 207.
[ciii]*Dunlop v Selfridge* [1915] AC 847, 653
[civ] Supra n. 85