

PRIVITY OF CONTRACT

1. THE DOCTRINE OF PRIVACY

“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.” (GH Treitel, *The Law of Contract*)

The common law reasoned that:

1. Only a promisee may enforce the promise meaning that if the third party is not a promisee he is not privy to the contract. See:

Dunlop Tyre Co v Selfridge [1915] AC 847 - The plaintiffs sold tyres to Dew & Co, wholesale distributors, on terms that Dew would obtain an undertaking from retailers that they should not sell below the plaintiffs' list price. Dew sold some of the tyres to the defendants, who retailed them below list price. The plaintiffs sought an injunction and damages. The action failed because although there was a contract between the defendants and Dew, the plaintiffs were not a party to it and “only a person who is a party to a contract can sue on it,” (per Lord Haldane).

2. There is the principle that consideration must move from the promisee. See:

Tweddle v Atkinson (1861) 1 B&S 393 - The fathers of a husband and wife agreed in writing that both should pay money to the husband, adding that the husband should have the power to sue them for the respective sums. The husband's claim against his wife's fathers' estate was dismissed, the court justifying the decision largely because no consideration moved from the husband.

The two principles of privity and consideration have become entwined but are still distinct.

2. EXCEPTIONS

If the doctrine of privity was inflexibly applied it would cause considerable injustice and inconvenience. Many exceptions to it have therefore been developed.

A) COLLATERAL CONTRACTS

A contract between two parties may be accompanied by a collateral contract between one of them and a third person relating to the same subjectmatter.

For example, in *Shanklin Pier v Detel Products* [1951] 2 KB 854, the plaintiffs had employed contractors to paint a pier. They told them to buy paint made by the defendants. The defendants had told them that the paint would last for seven years. It only lasted for three months. The court decided that the plaintiffs could sue the defendants on a collateral contract. They had provided consideration for the defendants' promise by entering into an agreement with the contractors, which entailed the purchase of the defendants' paint.

There must, however, be an intention to create a collateral contract before that contract can be formed

B) AGENCY

The concept of agency is an exception to the doctrine of privity in that an agent may contract on behalf of his principal with a third party and form a binding contract between the principal and third party.

For example, a third party may be able to take the benefit of an exclusion clause by proving that the party imposing the clause was acting as the agent of the third party, thereby bringing the third party into a direct contractual relationship with the plaintiff:

In *Scruttons Ltd v Midland Silicones Ltd* [1962] AC 446, a bill of lading limited the liability of a shipping company to \$500 per package. The defendant stevedores had contracted with the shipping company to unload the plaintiff's goods on the basis that they were to be covered by the exclusion clause in the bill of lading. The plaintiffs were ignorant of the contract between the shipping company and the stevedores. Owing to the stevedores negligence, the cargo was damaged and, when sued, they pleaded the limitation clause in the bill of lading. The House of Lords held that the stevedores could not rely on the clause as there was no privity of contract between the plaintiffs and defendants.

Lord Reid suggested that the stevedores could be brought into a contractual relationship with the owner of the goods through the agency of the carrier provided certain conditions were met: (1) that the bill of lading makes it clear that the stevedore is intended to be protected by the exclusion clauses therein. (2) that the bill of lading makes it clear that the carrier is contracting as agent for the stevedore. (3) the carrier must have authority from the stevedore to act as agent, or perhaps, later ratification by the stevedore would suffice. (4) consideration must move from the stevedore.

All of the above conditions were satisfied in *New Zealand Shipping v Satterthwaite (The Eurymedon)* [1975] AC 154.

C) TRUSTS

Equity developed a general exception to the doctrine of privity by use of the concept of trust. A trust is an equitable obligation to hold property on behalf of another.

The device was approved by the House of Lords in *Les Affreteurs Reunis v Leopold Walford* [1919] AC 801, where a broker (C) negotiated a charterparty by which the shipowner (A) promised the charterer (B) to pay the broker a commission. It was held that B was trustee of this promise for C, who could thus enforce it against A.

However, the trust device has fallen into disuse because of the strict requirements of constituting a trust and most particularly that there should be a specific intention on the part of the person declaring the trust that it should be a trust.

D) RESTRICTIVE COVENANTS

Restrictive covenants may, if certain conditions are satisfied, run with the land and bind purchasers of it to observe the covenants for the benefit of adjoining owners.

For example, in *Tulk v Moxhay* (1848) 2 Ph 774, the plaintiff who owned several houses in Leicester Square sold the garden in the centre to Elms, who covenanted that he would keep the gardens and railings in their present condition and continue to allow individuals to use the gardens. The land was sold to the defendants who knew of the restriction contained in the contract between the plaintiff and Elms. The defendant announced that he was going to build on the land, and the plaintiff, who still owned several adjacent houses, sought an injunction to restrain him from doing so. It was held that the covenant would be enforced in equity against all subsequent purchasers with notice.

This device was carried over into the law of contract by the Privy Council in *Lord Strathcona SS Co v Dominion Coal Co* [1926] AC 108, but Diplock J refused to follow the decision in *Port Line Ltd v Ben Line Steamers* [1958] 2

QB 146. Most recently, in *Law Debenture Trust Corp v Ural Caspian Oil Corp* [1993] 2 All ER 355, it was emphasised that the principle permitted no more than the grant of a negative injunction to restrain the person acquiring the property from doing acts which would be inconsistent with the performance of the contract by his predecessor and had never been used to impose upon a purchaser a positive duty to perform the covenants of his predecessor.

E) STATUTES

Certain exceptions to the doctrine of privity have been created by statute, including price maintenance agreements; and certain contracts of insurance enforceable in favour of third parties. For example, under s148(4) of the Road Traffic Act 1972, an injured party may recover compensation from an insurance company once he has obtained judgment against the insured person.

F) REMEDIES OF THE CONTRACTING PARTY

The question of the extent to which a contracting party may recover for loss sustained by a third party who is intended to benefit from the contract was raised in *Jackson v Horizon Holidays* [1975] 1 WLR 1468, where the plaintiff entered into a contract for himself and his family. The holiday provided failed to comply with the description given by the defendants in a number of respects. The plaintiff recovered damages and the defendants appealed against the amount. Lord Denning MR thought the amount awarded was excessive compensation for the plaintiff himself, but he upheld the award on the ground that the plaintiff had made a contract for the benefit of himself and his family, and that he could recover for their loss as well as for his own.

However, in *Woodar Investment Development v Wimpey Construction* [1980] 1 WLR 277, the House of Lords rejected the basis on which Lord Denning had arrived at his decision, and reaffirmed the view that a contracting party cannot recover damages for the loss sustained by the third party. Their Lordships did not dissent from the actual decision in *Jackson*, which they felt could be supported either because the damages were awarded for the plaintiff's own loss; or because booking family holidays or ordering meals in restaurants calls for special treatment.

3. ACADEMIC DEBATE ON THE DOCTRINE

GH Treitel, *The Law of Contract*, 9th ed, 1995, p588:

"The rule that no one except a party to a contract can be made liable under it is generally regarded as just and sensible. But the rule that no one except a party to a contract can enforce it may cause inconvenience where it prevents the person most interested in enforcing the contract from doing so. The many exceptions to the doctrine make it tolerable in practice, but they have provoked the question whether it would not be better further to modify the doctrine or to abolish it altogether."

4. REFORM

Proposals for legislative reform were made by the Law Revision Committee as long ago as 1937 (Cmnd. 5449) and further proposals were put forward for discussion by the Law Commission in 1991 (Paper No 121, 1991). In July 1996, the Law Commission published proposals in "*Privity of Contract; Contracts for the Benefit of Third Parties*" (Cmnd. 3329; Law Com No 242), which recommended that the law expressly provide for third parties to be able to enforce contracts (including taking advantage of exclusion/limitation clauses) in certain circumstances. These proposals for reform were acted upon.

The **Contracts (Rights of Third Parties) Act 1999** received Royal Assent on 11 November 1999. It reforms the common law rule of privity of contract. Section 1 provides that a third party may in his own right enforce a term of a contract if:

- (a) the contract expressly provides that he may, or
- (b) the term purports to confer a benefit on him (except where on a proper construction of the contract it appears that the parties did not intend the term to be enforceable by the third party).

There shall be available to the third party any remedy that would have been available to him in an action for breach of contract if he had been a party to the contract: s1(5).

See further, LCD press release 11 November 1999 and Gazette 1 December 1999.