

LLB ANSWERED

SAMPLE NOTES FROM OUR LLB *CORE GUIDE*:

Contract Law: Privity

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PRIVITY



KEY CONCEPTS

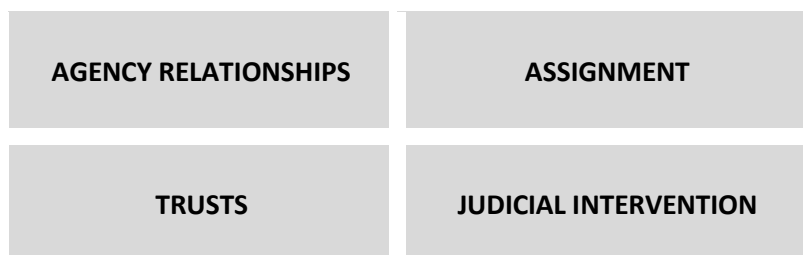
DOCTRINE OF PRIVITY

Under the common law:



AVOIDING THE DOCTRINE OF PRIVITY

The main common law exceptions are:



The main statutory exception is:



WHAT IS PRIVITY?

PRIVITY

“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.” Treitel, The Law of Contract.

Under the doctrine of privity:

A third party cannot	ACQUIRE RIGHTS UNDER	a contract to which they are not a party.
	BE LIABLE FOR	
	ENFORCE	

NOTE: the doctrine is closely connected to the principle that consideration must move from the promisee (see *Consideration chapter*). The leading cases on the classic doctrine are **Price v Easton**, **Tweddle v Atkinson** and **Dunlop Pneumatic Tyre Co Ltd v Selfridges & Co Ltd**.

WHO CAN SUE ON A CONTRACT?

Viscount Haldane LC made one of the classic statements on privity in **Dunlop v Selfridges**:

“ In the Law of England certain principles are fundamental. One is that only a person who is a party to a contract can sue on it. ”

The rule can be divided into two elements:

- 1) Who are the **parties** to the agreement; **and**
- 2) Has the claimant provided **consideration**?

THE AGREEMENT COMPONENT

Establishing the parties to a contract is usually straightforward. Confusion can arise where one party is acting as agent for another. Whether the person who took part in the negotiations was acting as an agent or as principal with the **intention to be a party** to the contract is a question of fact.

In some circumstances it may be disputed whether the beneficiary entered into the contract as a **party** to the agreement or merely as someone **interested** under the agreement.

COLLATERAL CONTRACTS

A collateral contract is a subsidiary contract which relies upon another contract for its existence.

Consider the following examples:

<p><i>Shanklin Pier v Detel Products Ltd</i></p>	<p>Shanklin Pier (SP) employed contractors to paint a pier. It instructed the contractors to buy the paint from Detel Products Ltd (DP), which they did. SP had relied on a statement from DP that the paint would last 7 years. The paint only lasted 3 months and it was held that there was a collateral contract between SP and DP that the paint would last 7 years.</p>
<p><i>Charnock v Liverpool Corp</i></p>	<p>A damaged car was repaired by a garage under a contract with the owner's insurers. It was held that there was a collateral contract between the garage and the owner, with an implied term that the garage would do the repairs in a reasonable time, not the eight weeks taken. The owner had provided consideration by leaving the car with the garage to be repaired.</p>

The same principle applies where a person buys goods from a retailer and is given a manufacturer's guarantee. Here, the main contract is between the retailer and the customer, but the guarantee is a collateral contract between the customer and manufacturer.

NOTE: legislation for the protection of consumers may also apply in this situation.

Where is the consideration in collateral contracts?

- In ***Shanklin Pier*** the consideration was in the instruction given to the claimant's contractors to use the specific paint.
- In guarantee cases the consideration is the purchase of the goods from the retailer.
- In cheque guarantee or credit card cases, the consideration is the supply of goods by the retailer to the customer, and the discount allowed by the retailer to the issuer of the card.

MULTIPLE PARTY CONTRACTS

<p><i>Clarke v Earl of Dunraven</i></p>	<p>There was a collision during a race which was organised by a yacht club, Clarke's yacht sank. Dunraven had a contract with the yacht club but not with the owners of other boats. The House of Lords held Dunraven had effectively entered into an obligation with the owners of all the yachts who were competing in the race, holding each liable to the other for any damage caused by a breach of club rules.</p>
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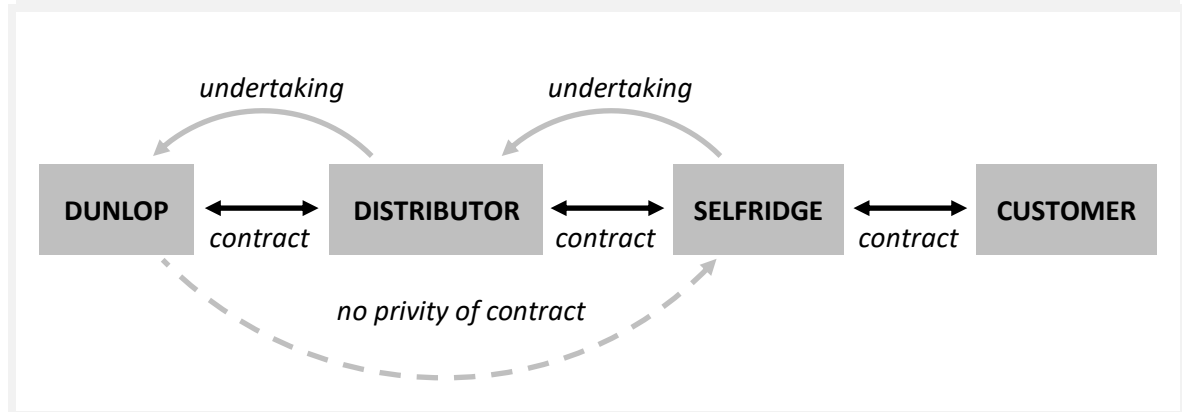
THE CONSIDERATION COMPONENT

As discussed above in the Consideration chapter, consideration must move from the promisee i.e. a claimant can only sue on a contract if the claimant has provided consideration.

KEY CASE: *Dunlop Pneumatic Tyre Co v Selfridge & Co Ltd*

Facts: Dunlop sold tyres to a distributor on the terms that they would not resell at a price lower than Dunlop's price list and would obtain undertakings from any trade customers not to do so. The distributor sold the tyres to Selfridge who sold them on at less than the agreed price in breach of their undertaking to the distributor. Dunlop sued Selfridge.

Held: Dunlop could not sue on the contract between Selfridge and the distributor, as Dunlop was not a party to the contract and had provided no consideration (*see diagram below*).



See also *Tweddle v Atkinson* in the Consideration chapter.

JUSTIFICATIONS FOR THE PRIVACY RULE

Several key arguments have historically been put forward to justify the doctrine of privity:

- The doctrine rests on the principle of **mutuality**: it would be unfair to allow a person to sue on a contract to which they are not a party. In *Tweddle v Atkinson* it was argued that “it would be a monstrous proposition to say that a person was a party to the contract for the purpose of suing upon it for his own advantage, and not a party to it for the purpose of being sued.”
- It is undesirable for third-party rights to be created by contract, since that would restrict the freedom of the parties to amend or rescind their agreement (*Re Schebsman*).

ARGUMENTS AGAINST THE PRIVACY RULE

There are several arguments for avoiding the rule that only parties who are parties to the contract can enforce it:

- The doctrine of privity is arguably outdated given developments in other areas of law:
 - As estoppel has gained prominence, the concept of reliance can allow parties to obtain relief even if no consideration has been given; and
 - The doctrine of consideration has itself been weakened by the establishment of various judicial and statutory exceptions to the rule.
- If a person makes a contract for the benefit of a third party, not only would the doctrine of privity prevent the third party beneficiary from enforcing breaches of the contract, the party

making the contract would also be unlikely to be entitled to more than nominal damages for any breach, as they would have suffered no loss.

- Many commercial contracts involve multiple interlinked contracts, each with multiple parties. Preventing third parties who are benefited by a contract from enforcing the agreement can sometimes defeat the intentions of the parties to the contract.

EXAM TIP: if you plan to answer an essay question of privity, you should familiarise yourself with the historic arguments for and against the doctrine. Justifications for reform have been considered by numerous Law Commission reports, as well as the Law Revision Committee in 1937. Try reading the Law Commission’s 1996 report, “*Privity of Contract: Contracts for the benefit of Third Parties*”.

Consider **Steyn LJ**’s statement in *Darlington Borough Council v Wiltshier Northern Ltd*:

“ The case for recognising a contract for the benefit of a third party is simple and straightforward. The autonomy of the will of the parties should be respected. **The law of contract should give effect to the reasonable expectations of contracting parties.** Principle certainly requires that a burden should not be imposed on a third party without his consent. But **there is no doctrinal, logical or policy reason why the law should deny effectiveness to a contract for the benefit a third party where that is the expressed intention of the parties.** Moreover, often the parties, and particularly third parties, organise their affairs on the faith of the contract. **They rely on the contract. It is therefore unjust to deny effectiveness to such a contract.** ”

METHODS OF AVOIDING THE DOCTRINE OF PRIVACY

COMMON LAW AVOIDANCE OF PRIVACY RULE

<p>AGENCY RELATIONSHIPS</p>	<p>In agency relationships, the agent contracts with a third party on behalf of the principal. It is the principal who can enforce the contract and be sued upon it.</p> <p>This is arguably not a true exception to the privity rules, as the agent is not actually a party to the contract – they merely negotiate on behalf of the principal.</p>
<p>ASSIGNMENT</p>	<p>A party may assign their contractual rights to a third party. In such a case the third party is able to sue under the contract, despite not being a party to the original agreement. This is subject to strict equitable rules.</p> <p>NOTE: it is not possible to assign the burden under a contract.</p>

TRUSTS	<p>The doctrine of privity does not apply to trusts. It is therefore possible for a party to a contract to use this principle to circumvent the privity requirement by declaring themselves trustee of the benefit of the contract, with a third party as the beneficiary.</p> <p>A contractual right is a “chose in action”, and thus may be subject to a trust just like any other form of property. The third-party beneficiary would gain an equitable interest in the contractual right and be able to enforce it in the courts, despite not being party to the agreement.</p>
COLLATERAL CONTRACTS	Collateral contracts are a further common law method of avoiding the doctrine of privity (<i>see above for more detail</i>).
JUDICIAL INTERVENTION	<p>There have been various judicial attempts to circumvent the strict requirements of privity.</p> <p>In Jackson v Horizon Holidays, Denning ruled that, after experiencing a bad holiday, a man was able to recover not only for his own losses, but for those of his family as well, despite the fact that the contract for the holiday was made only with the man.</p> <p>In Woodar v Wimpey it was suggested that such holiday contracts might make up part of a limited group of contracts exempt from the doctrine of privity (along with situations such as hiring a taxi or ordering food for a group).</p> <p><i>Further precedent is in Linden Gardens Trust v Lenesta Sludge Disposals; St. Martins Property Corp. v McAlpine; Beswick v Beswick; The Albazero, Alfred McAlpine Construction Ltd v Panatown Ltd</i> and the recent case of First Abu Dhabi Bank v BP Oil where the Court of Appeal followed the other cases with reluctance and called for the Supreme Court to reconsider this area of law.</p>

STATUTORY AVOIDANCE OF PRIVACY RULE

There are various specific statutory exclusions to the doctrine of privity. Below are some examples:

s. 11 Married Women’s Property Act 1882	Enables wives to claim under their husbands’ life assurance policies.
s.136 Law of Property Act 1925	Allows contractual rights to be assigned to a third party.
s. 148(7) Road Traffic Act 1988	Requires road users to have third party insurance, which third parties can use if they suffer loss as a result of the driver’s negligence.
Contracts (Rights of Third Parties) Act 1999	By far the most significant exception to the privity rule (<i>see next page for more details</i>).

CONTRACTS (RIGHTS OF THIRD PARTIES) ACT 1999 (“C(RTP)A”)

There was a long history of judicial dissatisfaction with the doctrine of privity in the lead up to the passing of the C(RTP)A. For example, in *Beswick v Beswick* Lord Scarman commented that:

“*If the opportunity arises, I hope the House will reconsider **Tweddle v Atkinson** and the other cases which stand guard over this unjust rule.*”

However, the courts recognised the problems with judicial reform, and the Law Commission recommended reform through legislation. Reform eventually came in the form of the C(RTP)A, but the scope of the reform is limited:

- The Act **does not allow the enforcement of burdens** imposed on third parties;
- The Act **deals only with enforcement of benefits by third parties** entered into after 11 May 2000 (the C(RTP)A came into force on 11 November 1999); and
- Even where the Act does apply, it is **not every third party who can enforce a contractual provision** – the test of enforceability in s. 1 of Act must be satisfied. However, the common law exceptions will continue to apply, so the common law and statute work together.

The Law Commission recommended that the privity doctrine be reformed by legislation to “*enable contracting parties to confer a right to enforce the contract on a third party*”, i.e. the right to enforce the **remedies for breach of contract** that would have been available had the third party been a contracting party.

The basic right is contained in s. 1(1) and provides that a person who is not a party to a contract may enforce a term of the contract in their own right if the **test of enforceability is satisfied**, even when the third party beneficiary is unaware of the contract at the time it was made (*Chudley v Clydesdale Bank*).

It is not intended that strangers should be able to enforce contractual provisions. **Only third parties who were intended to benefit under the relevant term of the contract** can enforce such contracts. **NOTE:** parties are able to expressly exclude the C(RTP)A from applying to a contract.

TEST OF ENFORCEABILITY

There are **two ways** in which a third party may satisfy the test of enforceability and be able to enforce contractual terms under the C(RTP)A:

s.1(1)(a) “The contract expressly provides that [the third party] may” enforce the provision; **or**

s.1(1)(b) “The term purports to confer a benefit” on that third party.

NOTE: s. 1(1)(b) will 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 (s. 1(2)). Under s. 1(3): the third party “**must be expressly identified in the contract by name, as a member of a class or as answering to a particular description,**” although the third party need not be in existence at the time contract is

made. (Reference to a client account amounted to an express identification of the class (*Chudley v Clydesdale Bank*)).

Examples from case law:

<i>The Swedish Club</i>	The Claimant sought to recover commission payable to them by underwriters and cargo-owners from the club. It was held that such a payment was not covered by s. 1(1)(b) , as it was merely payment of a commission to an agent.
<i>Nisshin Shipping Co Ltd v Cleaves & Co Ltd</i>	Cleaves had negotiated a number of time-charters under which commission was payable. Nisshin refused to pay on the basis that the contract had been repudiated. It was held that Cleaves could recover payment under s. 1(1)(b) . The clause purported to confer a benefit on Cleaves and there was nothing to indicate that the parties did not intend Cleaves to have a right to enforce.
<i>Avraamides v Colwill</i>	Avraamides (A) employed Colwill (C) to refurbish A's bathroom. C's performance was defective, and C would have been liable for damages, but C had sold the relevant business to a third party (B). B had taken on C's liabilities under the agreement. It was held that since A was not expressly identified in the contract between C and B, s. 1(1) did not apply and therefore A could not recover from B.

VARYING A CONTRACT UNDER THE C(RTP)A

The parties to a contract are **not** able to remove a purported benefit granted to a third party if:

s. 2(1)(a)	the third party has communicated their assent to the term to the promisor;
s. 2(1)(b)	the promisor is aware that the third party has relied on the term; or
s. 2(1)(c)	the promisor can reasonably be expected to have foreseen that the third party would rely on the term and the third party has in fact relied on it.

FURTHER READING

Law Commission Report No. 242, 1996. *Privity of Contracts: Contracts for the benefit of third parties*, Cm 3329.

Treitel, G., 2002. The battle over privity. In G. Treitel (ed). 2002 *Some Landmarks of Twentieth Century Contract Law*. Oxford: Clarendon Press.

ANSWERING A PROBLEM QUESTION ON PRIVITY

STEP 1:	Briefly set out the potential claim(s) in the scenario. State that the issue is with privity of contract.
STEP 2:	Define the doctrine of privity.
STEP 3:	Does privity of contract exist between C and the potential defendant? Is C a party to the agreement? Has C provided consideration?
STEP 4:	If C does not have privity, is there a relevant common law or statutory exception to the doctrine? Set out all potentially relevant exceptions and analyse whether the requirements have been met. Remember to consider whether the C(RTP)A applies.
STEP 5:	Conclude by identifying which mechanism C can use to bring a claim. If the doctrine of privity will prevent a claim, is there anything which could have been done differently which would have enabled C to make a claim, for example including an express provision in the contract allowing C to enforce the contract?

ANSWERING AN ESSAY QUESTION ON PRIVITY

EXAMPLE QUESTION:

“Despite the attempts to avoid the rule of privity, the doctrine still causes injustice.” Critically discuss.

STEP 1: Introduction:

Set up your argument, briefly outlining the key points of discussion. State whether you agree with the statement.

STEP 2: Define Privity:

Set out the law on privity, referring to the key case law (*Dunlop; Tweddle* etc.).

STEP 3: Consider the criticisms of the doctrine of privity:

Consider the criticisms that have been made of the doctrine of privity, both in case law and academic commentary. Explain how the doctrine can cause *“injustice”*, for example by preventing a party from benefiting from a contract in the way intended by the original contracting parties. Refer to relevant case law.

STEP 4:**Consider the exceptions to the doctrine. To what extent have these mitigated the negative effects of the doctrine?**

Consider the different exceptions to the doctrine in both common law and statute. Do they reduce the “injustices” you have identified in STEP 3? Is there a risk that they could create their own injustices in some circumstances?

For example, some of the common law exceptions have a narrow scope and could lead to unpredictable outcomes in some cases. This arguably undermines legal certainty, preventing parties from knowing in advance what the legal consequences of their actions will be.

Consider the effect of the **C(RTP)A**. To what extent has it removed the injustices of the doctrine of privity? Consider the limits of the act – it does not apply in all situations and can be excluded by the parties.

The **C(RTP)A** subverts the general requirement that consideration is needed to enforce a contract and enables a third party to enforce an agreement even if they have offered nothing in return. Is this just? Remember that the act is designed to give effect to the intentions of the contracting parties and only applies if the test for enforceability has been satisfied.

STEP 5:**Consider the justifications for the doctrine of privity:**

Do not be afraid to challenge the premise of the question. Do you in fact agree that the doctrine causes injustice? Consider the various justifications for the doctrine.

STEP 6:**Conclusion:**

Summarise your argument and conclude as to how far you agree / disagree with statement.