Introduction

'The rule of privity can produce the bizarre result that the third party who suffers a loss cannot sue, while the contracting party who can sue has not suffered a loss and thus may only be entitled to nominal damages.'

This quotation from the Law Reform Commission's report on Privity of Contract and Third Party Rights highlights the negative effects of the doctrine of privity and asserts the need for change in this complex and unbalanced area of law. But before we enter into a discussion on law reform it is important to outline and define the rule, discuss its genesis and justify why it has existed for so long.

In the middle of the nineteenth century the common law judges reached a decisive conclusion upon the scope of a contract. No one, they declared, may be entitled to or bound by the terms of a contract to which he is not an original party.[1] The doctrine in effect answers the question, who may sue under a contract? Privity can be compared to the law on remoteness of damages in that both prescribe the range of harms to which a breaching party may be held liable. The origins of the doctrine lie in the famous English case *Price v Easton*[2]. The facts of the case are as follows; X had made a promise to Easton, the defendant, to carry out certain work, for which Price, the plaintiff, would in turn be paid £19 by Easton. The problem was Easton never paid. As a result of this Price attempted to sue Easton. He lost. This was because his case fell foul of the doctrine of privity. As Price was a mere third party to the contract he had no right to sue on it. This ruling seems unfair *prima facie* and, indeed, perhaps, it is a draconian measure to refuse a third party his damages and allow one of the parties in a contract the ability to avoid his contractual obligations. But we will park any discussion on justification or fairness of the doctrine for now until we have fully explored its development.

A contract is private to its parties. Collins says that: 'all contracts resemble a marriage insofar as no third party can claim the right to share the intimate relations established between the spouses'[3]. The decisive case in the doctrine's development was *Tweddle v Atkinson*[4], in consideration of an intended marriage between the plaintiff and the daughter of William Guy, a contract was made between Guy and the plaintiff's father, whereby each promised to pay the plaintiff a sum of money. Guy failed to do so and the plaintiff sued his executors. The action was dismissed, Wightman J said: 'It is now established that no stranger to the consideration can take advantage of a contract, although made for his benefit.'[5] This rule is based on the fact that because the third party does not offer any consideration he cannot be considered a party to the contract. This ruling emphasised the English identification of contract and bargain.

The doctrine finds its modern position in the complex case of *Dunlop v Selfridge*[6] , Dew & Co. bought a number of tyres from the plaintiffs. The contract contained two terms, the first; was that Dew & Co. would not resell the tyres at an undervalue and secondly, that if he were to sell them on to a trade buyer that he would impose the same price clause on the buyer. Dew & Co. sold the tyres to

[1] Price v Easton (1883) 110 ER 518
[2] Ibid
[3] Collins, The Law of Contract (LexisNexis, 2003) 314
[4] (1861) 1 B & s393
[5] Ibid at 397-398
[6] (1915) AC 847

Selfridge, who agreed to observe the restrictions and to pay Messrs Dunlop the sum of £5 for each tyre sold in breach of this agreement. Selfridge supplied tyres to two of their own customers below the listed price. Dunlop sued Selfridge but failed. This appears harsh on the initial facts because both contracts contained a clause that Selfridge eventually broke. But no contractual nexus could be drawn between Dunlop and Selfridge. Selfridge was not a party to the first contract between Dunlop and Dew & Co., nor was Dunlop privy to the contract between Dew & Co. and Selfridge; therefore Selfridge could not be sued. Selfridge had slipped through the cracks of privity. Viscount Haldine LC famously said: 'My Lords, in the law of England certain principles are fundamental. One is that only a person who is party to a contract can sue on it. Our law knows nothing of a *jus quesitum tertio* arising by way of contract.' The Irish case of *Murphy v Bower*[7] backs up the English position in our jurisdiction.

The Rationale behind Privity

When we look at the above cases it can be easy to feel that the doctrine of privity of contract is harsh and unnecessary, allowing parties to a contract to avoid their obligations and leave intended third party benefactors out in the cold so to speak with no option for remedy. But the justifications behind the rule are valid, the first rule is the 'floodgates' argument. The rule of privity protects society from the potential outcome that anybody could potentially enforce any contract regardless of whether or not they had any actual involvement in its creation. If this were allowed to happen we could begin to see contracts where parties could be held liable to an unlimited number of third parties. The second justification for the doctrine of privity is that: no one except a party to a contract can acquire rights under it; and no one except a party can be subjected to liabilities under it, this justification is rooted in contractual autonomy. It is also noteworthy that parties to a contract should be free to alter or modify their contract without requiring the permission of a third party.

These reasons do not take into account the inconvenience that can result from its practical operation. Mason CJ made a compelling argument against privity in the famous Australian case *Trident General Insurance Co. Ltd v Mc Niece Proprietary Ltd*[8] believing it possible to balance the right to contractual freedom with the rights of third parties: 'The entitlement of the third party to enforce the provision in his favour can be subordinated to the right of the contracting party to rescind or modify the contract, in which event the third party would lose his rights except insofar as he relied on the promise to his detriment.' In a nutshell he believed a hierarchy of rights is preferable to total non-recognition of third party rights. Finally there is also what might be called an equitable justification for the doctrine. It might be asked why a person who has contributed nothing to the contract has the privilege of enforcing it. As the doctrine of consideration shows, the law will not enforce gratuitous contracts. In addition, the doctrine of privity prevents an imbalance of rights between contractual parties and third parties: why should a third party be permitted the benefit of suing on a contract when he cannot in turn be sued? In *Tweddle*, Crompton J observed that: 'It would be a monstrous proposition to say that a person was a party to the contract for the purposes of suing upon it for his own advantage and not a party to it for the purpose of being sued.'

[7] (1868) IR 2 CL 506
[8] [1988] 165 CLR 107

The Problems with Privity

Some judges have described privity as 'a blot on our law and most unjust'[9] and as 'an anachronistic shortcoming'.[10] The main area in which privity runs into a lot of problems is in the reality of commercial transactions. Oftentimes parties enter into contracts for the benefit of third parties. What has become abundantly clear is that, if the contract is breached the third party will fail in any attempt to sue and will lose out on any benefits he may have once had entitlement to. He therefore must rely on the goodwill of the non-breaching party to sue the breaching party as no order exists which can compel the non-breaching party to do so. Inefficient, complicated chains of contract claims can arise. If the non-breaching party is willing to sue he cannot sue for the benefits that the third party stood to gain, only the, usually minimal, loss that he himself suffered from the breach.

Alternatively to suing for damages the third party may be able to persuade the non-breaching to sue for specific performance – an order compelling the breaching party to carry out his side of the bargain. A significant case in this area is *Beswick v Beswick*[11], a widow wanted to sue on a contract between her deceased husband and his nephew. The Court held that if she sued her nephew in her personal capacity she would lose. She was, however, able to sue as administratrix of her late husband's estate in *his* personal capacity forcing the nephew to carry out his obligations by specific performance. The problem with this form of remedy is that it is at the judge's discretion to decide whether or not to grant the order. In instances of complexity he may decide against granting such an order.

The end result is that, as *Price* and *Dunlop* show, the doctrine of privity can allow a party to sidestep his obligations unpunished, even where the other party has performed his end of the bargain in good faith. It can cause a situation where a third party may be fully aware of the existence of the contract and spends money in expectation of its completion but ends up disappointed and out of pocket. Lastly, *Tweddle* illustrates the possibility that the doctrine can frustrate a party's intentions. For example Tweddle's father-in-law wanted to give him money but was hampered. The defaulting party can simply ignore his contractual obligations to the third party. This final point answers the argument made in favour of the doctrine of privity that it safeguards the party's autonomy. The Courts are not ignorant of these arguments. In *Darlington Borough Council v Wiltshere Northern Ltd*[12] Lord Steyn said:

'...there is no doctrinal, logical or policy reason why the law should deny effectiveness to a contract for the benefit of 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. It is therefore unjust to deny effectiveness to such a contract.'

The Exceptions to Privity

The rule that a third party cannot sue on a contract to which he is not party was never absolute. The law has always recognised some exceptions to, or qualifications of, the rule. The source of these

[9] Forster v Silvermere Golf and Equestrian Centre [1981] 125 Sol Jo 397
[10] Swain v Law Society [1983] 1 AC 598
[11] [1968] AC 58
[12] [1994] ABC.L.R

exceptions is to be found at common law and in various statutes. The principal exceptions are as follows:

1. **Tort of Negligence**- The duty of care is a useful tool for side-stepping the doctrine of privity. In *Wall v Hegarty*[13]. The High Court found that a beneficiary of an invalid will could sue the solicitor who negligently drew it up.
2. **Family Holiday**- This could be referred to as 'quasi-agency' where one party is booking for a group, he can sue for damages suffered by the group, claims for 'his loss of amenity' due to failure of his group to get agreed benefits. Although the plaintiff can keep the money the third party can recover that money from him by legal action if he declines to hand it over.[14]
3. **Constructive Trusts**- A trust is an equitable obligation to hold money, property or a chose in action on behalf of another party. The party who holds his rights under the contract on trust for the third party is called the trustee. The third party for whose benefit those rights are held is called the beneficiary. Rights under a contract can become the subject of a trust where the trustee so provides in the main contract. Developed in *Tomlinson v Gill*[15]
4. **Agency** – An agent is a person who enters into a contract on behalf of another person called a principal. Even though the contract is 'private' to the agent and the other party, the principal has rights and obligations under that contract as if he had made that contract himself.
5. **Collateral Contracts**- It is possible that a court may analyse a privity scenario in terms of two contracts: the main contract between the original parties and a separate contract between one of the parties and the third party beneficiary. The second, collateral contract will contain that clause in the main contract upon which the third party seeks to rely.
6. **Statutory Exceptions**- The Oireachtas has created a number of *ad hoc* statutory exceptions to the doctrine of privity.

Options for Reform

The Law Reform Commission's 2006 Consultation Paper on Privity of Contract and Third Party Rights[16] suggested that legislative reform would be preferable to judicial reform as the doctrine of precedent is too slow a process. It creates a situation where judges must wait for an appropriate case which raises all the relevant issues before they can create reform[17]. Reforming legislation has already been created in England and Wales, in the form of the Contracts (Rights of Third Parties) Act 1999. Similar reforms also have taken place in Canada, New Zealand, Australia and Singapore. However the commission recommended that legislative reform of the privity rule should not constrain judicial development of third party rights.[18] The Canadian case of *Fraser River Pile and Dredge Ltd v Can Dive Services Ltd*[19] could be seen as one of the earlier examples of a call for legislative reform rather than judicial reform, Iabocucci J said: 'In appropriate circumstances, courts should not abdicate their judicial duty to decide on

[13] [1989] ILRM 124
[14] Jackson v Horizon Holidays [1975] WLR 1468
[15] [1756] Amb 330
[16] LRC CP40-2006
[17] Consultation Paper, paragraph 2.93
[18] Consultation Paper, paragraph 2.73
[19] [1999] 3 SCR 108

incremental changes to the common law necessary to address emerging needs and values in society.'

The Commission has ruled out two things in its recommendations, the first being, an abolition of the rule and the creation of new statutory exceptions. Clarity in the form of detailed legislation is needed to remedy the complexity of the current law and provide guidance for judges. The Commission also takes the view that further statutory exceptions will only lead to further confusion in the area.

A test of enforceability based on the parties to the contract is one of the main recommendations. Two requirements would need to be satisfied if a third party were to be able to enforce a contract. First, it must be shown that the parties to the contract had the intention of benefiting the third party through the contract or one of its terms. This intention will be evidenced by naming the third party or through him being described. Second, the beneficial contract or term was intended to be enforceable by him in his own name. The type of intention required is important. It is a dual test of intention: if the third party was merely intended to benefiting from the contract he will not have any rights. He must also have been intended to be able to sue on it. The test of intention is objective. The intention to create legal relations applied to direct contracting parties is the standard this is set at. Third, the privity rule would apply unless the parties specifically contracted otherwise. The fourth, important, observation is that the parties' freedom of contract is protected by the focus on intention; their contract will remain private to them and unassailable by the State or by third parties unless they expressly decide to relinquish the shield of the privity doctrine. Once the first element of the dual intention test is satisfied, it will be presumed that the second element has been satisfied. This presumption would be rebuttable and generally speaking, parties who do not wish to confer a right of enforcement on a third party should state so clearly in their contractual document.

Conclusion

The doctrine of privity is a feature in our law that, despite its many flaws, is a necessary one to prevent indeterminate liability being imposed on contracting parties. The current position of the rule in our jurisdiction appears to be coming to its end. The Law Reform Commission's report and the legislative reforms seen in other countries along with judicial unrest seems to have placed the writing firmly on the wall for the end of privity as we know it. Change is clearly needed. The Oireachtas can no longer stand idly by and allow the slow process of judicial law reform to occur, or not at all as the case may be. The Law Reform Commission's report should be adhered to and steps taken to bring about the creation of a new privity bill. It is important, though, that the individual's right to contractual autonomy and freedom to enter a contract without fear of being sued from an unintended third party be protected.

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