CHAPTER SIX

Comparative Study on Selected Countries

I. Introduction

Chapters 4 and 5 explained the various common law mechanisms and their limitations to override the privity doctrine. This chapter undertakes a comparative study on the legal position in selected countries in relation to the position of a third party in a contract made for his benefit. The countries selected for discussion are England, New Zealand, Australia and the United States as well as the Principles of European Contract Law which is applicable to members of the European Union. The reasons for the selection of these respective countries are stated in Chapter 1 Part VI. The reform of the privity doctrine in these countries allows third parties to enforce a contract intended for their benefit. The purpose of this comparative study is to determine the preferred model for reform of the doctrine in Malaysia.

To achieve the above, this chapter first examines the benefits of a comprehensive legislative reform to the doctrine compared with judicial reform which is limited in a number of aspects. Comprehensive legislative reform was undertaken in England, New Zealand and some states in Australia (Western Australia, Queensland and Northern Territory). Particularly, this discussion focuses on how this method of reform can prevent or reduce the problems of judicial reform of the doctrine. Secondly, this chapter lays out and analyses the individual strengths and weaknesses of the various rules of the statutory reform, the Principles of European Contract Law and the Restatement (Second) of

Contracts in the United States. The judicial decisions relating to these reforms and Restatement are assessed to determine the difficulties, if any created by these reforms.

II. Benefits of Comprehensive Statutory Reform

Parliament is the proper avenue to undertake reform of the law. Firstly, Parliament's role is to make and revise the law when the need arises for the benefit of the public. The law made by members of Parliament, arguably, receives the required level of legitimacy as they are the chosen representatives of the public. By contrast, judicial reform is only undertaken by a few judges sitting in the highest court. Thus, judges may exercise restraint in making vast changes to the law for fear of usurping the role of the Parliament.

Secondly, reform of the privity doctrine requires a number of policy choices to be made in relation to the scope of reform, the contracting parties' right to vary the contract made, the exclusion of certain types of contracts from the reform and other relevant matters. The power to decide on policy matters is within the realm of the Parliament's legislative powers.

Thirdly, the process of statutory reform allows a more detailed consideration on the benefits as well as any undesired consequences of the proposed reform. For a statutory reform, the existing position of the law will be considered by a Law Commission comprising of experts in the particular field. The Law Commission has sufficient time to deliberate on all aspects involved in relation to the proposed reform. Invitation is also opened to the public for suggestions and comments on the proposed reform. This guarantees that a better and

workable solution is recommended to the Parliament. As a result, chances of success of the reform are higher.

By contrast, judicial reform may not be as successful as legislative reform due to the inherent nature of the judicial process of resolution of disputes. In deciding disputes, judges are concerned mainly with the issue arising from the facts of the particular case only. For other issues which are not in dispute, judges only provide obiter remarks or leave the matters to be dealt with in subsequent cases. Thus, it is difficult to reach a complete overhaul of the reform to the privity doctrine at one time.[1]

Besides, the doctrine of judicial precedent is also a major hindrance to judicial reform. According to this doctrine, lower courts are bound by decisions of higher courts. Once a rule is entrenched by the highest court, the only way to change the rule is either through statutory intervention or where the highest court reverses its own previous decision. However, judicial reconsideration of a particular rule is hard to come by. Litigants may not appeal against the decision of the trial judge or the Court of Appeal or they may have settled their dispute outside court. Hence, it may be difficult for the highest court to correct unsuitable rules that have been decided in previous decisions.[2]

The difficulty of self-correction by judges is further aggravated by the fact that the ability of judges to tackle a particular issue depends very much on the arguments put forward by

[1] Judicial creation of exceptions to the privity doctrine in *Trident General Insurance Co. Ltd.* v *McNiece Bros Pty Ltd* [1988] 165 CLR 107 and *London Drugs Ltd.* v *Kuehne & Nagel International Ltd* [1992] 3 SCR 299 leaves many aspects unsettled as discussed in Chapter 5 Part III(E) and Chapter 5 Part IV(A)(3).
[2] This is further elaborated by Schauer, Frederick, "Do Cases Make Bad Law?" 73 (2006) *U Chi L Rev* 883-918, at 908-911.

legal counsels. This is put succinctly by Steyn LJ in *Darlington Borough Council* v *Wiltshier Northern Ltd* where it was stated that:

> But that requires the door to be opened by the House of Lords reviewing the major cases which are thought to have entrenched the rule of privity of contract. Unfortunately, there will be few opportunities for the House to do so. After all, by and large, courts of law in our system are the hostages of the arguments deployed by counsel. And counsel for Darlington, the third party, made it clear that he will not directly challenge the privity rule if this matter should go to the House of Lords.[3]

Undertaking statutory reform also avoids the dangers posed by firstly, swings of judicial attitude[4] and secondly, differing judgments in a major decision.[5] As a result of the malleable judicial attitude, there is lack of clear guideline provided for judges in subsequent cases and this leads to uncertainty in the law.

It is submitted that some of the problems created by the process of judicial resolution also exist in a statutory reform as reliance is placed on judges to construe and give effect to the statutory rules. However, if proper and sufficient guideline is provided by the Parliament, these problems will be minimised. Judges are not burdened with the need to deal with the creation and expansion of the exception to the doctrine but only on application of rules devised by the Parliament. Hence, a comprehensive statutory reform will result in greater certainty and clarity compared to judicial development of the law. This will also reduce litigation costs borne by litigating parties.

---

[3] [1995] 1 WLR 68, at 77-78.

[4] A good illustration is the different judicial attitude displayed in relation to third party's reliance on exclusion clauses as discussed in Chapter 5. In *Elder, Dempster & Co* v *Paterson, Zochonis & Co* [1924] AC 522, judges were willing to introduce the doctrine of vicarious immunity which was popular for some time before it was rejected in *Scruttons Ltd* v *Midland Silicones* [1962] AC 446.

[5] For example, in *Trident General Insurance Co. Ltd.* v *McNiece Bros Pty Ltd* [1988] 165 CLR 107, there was no unanimous decision by the High Court.

Legislative reform also prevents litigants from suffering the retrospective effects of judicial changes to the law. Usually, the public is given ample notice before a new Act takes effect. This ensures that the public is aware of the new changes and arrange their affairs accordingly. Particularly, the parties involved in commercial activities can adjust their risk to suit their business needs.

III. Legal Position in Selected Countries

Discussion on each of the statutory reform, Principles of European Contract Law and the Restatement (Second) of Contract is divided into the following areas:

(a) Enforceability test

(b) Rescission or variation of third party's right

(c) Defences and set-off

(d) Miscellaneous

Area (a), (b) and (c) are chosen as they are the core areas behind any reform to create third party rights. Area (d) is to discuss the remaining rules which fall outside the core areas but are still relevant in reforming the doctrine of privity. For (a), discussion focuses on the requirements that a third party has to satisfy in order to enforce the benefit made in his favour. This includes discussion on the requirement relating to the identification and the existence of the third party at the time the contract is created. For (b), discussion focuses on the right of the contracting parties to vary or rescind the benefit intended for the third party. For (c), the defences and set-off available to the defendant in a legal action brought by the third party are examined. For (d), discussion includes other matters relating to the

enforcement of contract by the third party. The extent of comprehensiveness of the legal reform in the selected countries differs from one to another. If the particular country does not have certain provisions compared to other countries, such omission of the provisions will not be mentioned unless it is relevant to do so.

A. England

In England, the Contracts (Rights of Third Parties) Act 1999 (hereinafter referred to as '1999 Act (E&W)') was enacted to reform the doctrine of privity. Some preliminary points are explained before proceeding further into the discussion on the 1999 Act (E&W). Firstly, the 1999 Act (E&W) applies to written contracts and oral contracts provided there is a term benefiting the expressly identified third party. Any third party who seeks to rely on the 1999 Act (E&W) to enforce a contract will be bound by conditions stipulated in the contract for the enjoyment of the benefit.[6] Accordingly, a third party is bound by the exclusion or limitation of liability by the promisor. The 1999 Act (E&W) also applies to exclusion or limitation clauses intended to benefit third parties.[7] The third party is deemed to be a party to the contract only for the purposes of the 1999 Act (E&W) and no other Acts.[8]

[6] Section 1(4) which provides that:

> This section does not confer a right on a third party to enforce a term of the contract otherwise than subject to and in accordance with any other relevant terms of the contract.

[7] Section 1(6). In *Precis (521) plc* v *William M Mercer Ltd* [2005] EWCA Civ 114, the Court of Appeal allowed a third party to a contract to rely on the exclusion clause found in the contract.

[8] Section 7(4).

1. Enforceability Test

Section 1(3) provides that any third party who seeks to claim the benefit of any terms of the contract must show that he is expressly identified by name, falls within a class or answers to the description provided in the contract. The identification of the third party must be such that it supports the fact that the particular term of the contract purports to benefit him.[9] The courts cannot imply terms into the contract to make references to the third party.[10] At first sight, this may exclude many deserving third parties in domestic contracts where the promisee fails to expressly refer to the third party in the contract. However, such concern is allayed as express terms can be incorporated into the contract if both the contracting parties know that the contract is made for the benefit of a third party at the time the contract is created.[11] The third party does not need to be in existence at the time the contract is created but he must be ascertained at the time the performance of the contract is due or in case of an exclusion clause, at the time the promisor incurs liability.[12]

Section 1(1) provides two enforceability tests.[13] Firstly, s.1(1)(a) requires an express term in the contract stating that the third party is entitled to enforce the contract. No imputation

---

[9] Peel, Edwin, *Treitel - The Law of Contract*, 12th Edition, (Sweet & Maxwell, 2007) (hereinafter referred to as '*Law of Contract*'), at 695-696.

[10] *Avraamides* v *Colwill* [2006] EWCA Civ 1533. This case also shows that if a generic term such as 'customers' is used in the contract, it is more difficult to prove that the 1999 Act (E&W) applies as s.1(3) requires identification of the third party. This is so as generic terms may apply to a large number of unidentified claimants.

[11] As an illustration, a mother brings her son to a computer shop to buy him a laptop. The sales assistant is aware of this fact. If a contract is concluded between the mother and the shop, arguably, the son is entitled to enforce the contract if the laptop is defective as an express term of the contract will be that the laptop is bought for the son even though this may not be expressly stated in the bill or invoice of the sale concluded. The same opinion is also shared by Yeo Tiong Min, "When do Third Party Rights Arise under the Contracts (Rights of Third Parties) Act 1999 (UK)?" (2001) 13 *SAcLJ* 34-53, at 38.

[12] Section 1(3).

[13] Section 1(1) provides that:

> Subject to the provisions of this Act, a person who is not a party to a contract (a "third party") may in his own right enforce a term of the contract if -
> (a) the contract expressly provides that he may, or

is allowed as to whether the third party is intended to be given such right. The third party is not required to be the ultimate recipient of the benefit of the contract. For example, the third party may act as an agent or trustee for the benefit of others. In this situation, he is entitled to enforce the contract if this is expressly stated in the contract.

It is most likely that the third party's claim to rely on an exclusion clause falls under s.1(1)(a). The only purpose to include a third party in an exclusion clause is to enable him to seek protection under the clause. This is akin to stating expressly that the third party can enforce the exclusion clause.[14] In the absence of an express term allowing the third party to sue, s.1(1)(b) states that it must be shown that the term which he seeks to enforce 'purports to confer a benefit to him'. If this is proven, a rebuttable presumption that the third party is entitled to sue on the contract is raised. Section 1(2) provides that the presumption is rebutted if the contracting parties do not intend the third party to enforce the particular term. The promisor bears the burden of proof to rebut the presumption.[15]

The inclusion of s.1(1)(b) is to ensure that more situations involving contracts made for the benefit of third parties can fall within the 1999 Act (E&W). This is to cater for situations where the contracting parties fail to expressly state that the third party is entitled to enforce the contract. This may happen where legal advice on the 1999 Act (E&W) is not available to them.

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

[14] Treitel (*Law of Contract*), at 692, states that Himalaya clauses will fall under s.1(1)(a). Thus, it is arguable that third parties' reliance on exclusion or limitation clauses which expressly intended to include them should fall under s.1(1)(a).

[15] Merkin, Robert, ed., *Privity of Contract: The Impact of the Contracts (Right of Third Parties) Act 1999*, (LLP, London, 2000) (hereinafter referred to as 'Merkin'), at para 5.27.

According to Burrows,[16] the phrase 'purports to confer a benefit' to the third party means that the contracting parties intend to provide the benefit of the performance of the contract 'directly' to the third party. As an illustration, a contract to make a will does not purport to confer a benefit to the third party.[17] The purpose of the contract between the testator and the solicitor is to provide a benefit to the testator only, that is to enable him to make a will. The benefit to the third party is a consequence of the performance of obligation of the solicitor to the testator. Here, no performance is due to the third party or involving his property.[18]

In determining whether the presumption is rebutted,[19] the court will construe the whole contract to ascertain the contracting parties' intention. The promisor can also refer to the surrounding circumstances of the making of the contract.[20] It seems that s.1(2) requires an objective construction of the parties' intention due to the phrase "it appears" as found in the subsection. It has been argued that the use of an objective test carries the risk that judges' decision may be inconsistent with the actual intention of the contracting parties.[21] But this

[16] Burrows, Andrew, "Reforming Privity of Contract: Law Commission Report No. 242" (1996) *LMCLQ* 467-486, at 473. The learned author was a member of the Law Commission of England responsible for making recommendations to reform the privity doctrine.

[17] The beneficiary in *White* v *Jones* [1995] 2 AC207 will be excluded from relying on the 1999 Act (E&W).

[18] This view which was adopted by Burrows and the Law Commission has been subject to criticism as seen in Adams, J.N., Deryck Beyleveld and Roger Brownsword, "Privity of Contract – the Benefits and the Burdens of Law Reform" (1997) 60 *MLR* 238–264, at 250 and Stevens, Robert, "The Contracts (Rights of Third Parties) Act 1999 (2004)" 120 *LQR* 292–323, at 306-307. The criticism highlighted by these academics is that this view may lead to difficulty in applying s.1(1)(b) in practice as there will bound to be borderline cases where the distinction between a situation in *White* v *Jones* and a contract purported to benefit third party is not so clear-cut.

[19] Burrows states that the presumption created by s.1(1)(b) is a 'strong one'; Burrows (1996) *LMCLQ* 467-486, at 473. This means that it is difficult for the promisor to rebut this presumption.

[20] If the words used by the contracting parties are sufficiently clear, judges may be reluctant to take into account the surrounding circumstances to determine the actual meaning intended by them. To do so may be unfair to the third party who construes the contract at face value. It is also most probably that he is not aware of the surrounding circumstances when the contract is concluded; per Saville LJ in *National Bank of Sharjah* v *Dellborg* (unreported), relied on by Roe in his article "Contractual Intention under Section 1(1)(b) and 1(2) of the Contracts (Rights of Third Parties) Act 1999" *MLR* 63 (2000) 887–894, at 891.

[21] Stevens (2004) 120 *LQR* 292–323, at 294-295 and Chan, Wai Meng, "Contracts (Rights of Third Parties) Act 1999 – Legislative Reform of the Doctrine of Privity in the United Kingdom" (2001) *JMCL* 137-159, at 146. Chan added that the third party may be given rights of enforcement despite the fact that the contracting parties never contemplate to do so at the time the contract is created.

approach can be justified as it is consistent with the general principles of construction of contract where judges will construe a contract objectively.

There are two situations where this presumption can be rebutted.[22] Firstly, a third party is not entitled to enforce the contract if the contractual terms exclude third party rights or are inconsistent with his right to enforce the contract. Secondly, the third party is not entitled to rely on the 1999 Act (E&W) if he has entered into a chain of contracts providing him with recourse for the promisor's breach of contract. Thus, the presumption can be easily rebutted in relation to construction contracts as the creation of chain contracts is a popular practice in this industry.[23] The concern arising from the use of chain contracts to rebut the presumption in s.1(2) is that it illustrates that the test used to rebut the presumption differs from one class of third parties to another.[24] Judges may be more stringent in applying the 1999 Act (E&W) to commercial contracts where the agreement is drafted by legal professionals compared to a domestic agreement drafted without such assistance. For commercial contracts, the contracting parties would have been advised by legal professionals as to the effects of the 1999 Act (E&W). If they intend the Act to be applicable they would have made it clear in their contract. As such, the use of chain contracts negates the contracting parties' intention to rely on the 1999 Act (E&W) to create third party rights.[25]

---

[22] Burrows (1996) *LMCLQ* 467-486, at 473.

[23] As such, the plaintiff in *Junior Book* v *Veitchi* [1983] 1 AC 520 will not be entitled to any rights under the 1999 Act (E&W); Law Reform Commission's Report No 242, *Privity of Contract: Contracts for the Benefit of Third Parties* (1996) (hereinafter referred to as 'LCR'), at para 7.38.

[24] Adams, J.N., Deryck Beyleveld and Roger Brownsword, "Privity of Contract – the Benefits and the Burdens of Law Reform" (1997) 60 *MLR* 238–264, at 253.

[25] In *Laemthong International Lines Co Ltd* v *Artis*, it was held by both the High Court, [2005] 1 Lloyd's Rep 100, and the Court of Appeal [2005] 2 All ER (Comm) 167 that the presumption in s.1(1)(b) will only be defeated by chain contracts if these contracts are very "well-known and provide a commercial background of practice to contracts which are unlikely to cut across the legal framework customarily employed" at para 53 and 54 of [2005] 2 All ER (Comm) 167. As such, judges will not easily rebut the presumption merely because there is a chain of contracts. On the facts of *Laemthong International*, the presumption was not rebutted by a

Section 1(1) uses the phrase 'enforce a term' rather than 'enforce a contract'. If a third party attempts to enforce more than one term in the contract, he must show separately that each of the terms purports to benefit him.[26] This may appear to be burdensome on the third party. But this requirement is consistent with the basis of reform, to respect the contracting parties' intention. There may be situations where the contract is complex and deal with many issues, some which do not concern the third party. In these situations, the contracting parties may not wish the third party to be able to enforce the whole contract.

The application of s.1 has been discussed, clarified and applied in *Nisshin Shipping Co Ltd* v *Cleaves & Co Ltd.*[27] In this case, Cleaves (chartering brokers) negotiated nine time charters on behalf of Nisshin. Each charterparty contained a clause provided payment of commission to Cleaves and an arbitration clause. There was a dispute between the parties as to Cleaves' entitlement of commission. Cleaves sought to refer the matter to arbitration. This was challenged by Nisshin on the ground that Cleaves was not a party to the time charter. Thus, it could not rely on the arbitration clause in the contract to claim for payment of commission.

It was held by Colman J that in determining whether s.1(1)(b) applies, it must be first considered whether there is an intention to confer the benefit to the third party. If the answer is in the affirmative, the court must then look at whether this presumption is rebutted on the basis that the contracting parties do not intend the third party to have enforceable rights. If the contract is neutral on this matter, the presumption is not rebutted.

---

chain of letter of indemnities as these contracts had a number of different forms and there are many disputes as to the terms of these contracts between the contracting parties. Thus, each contract of indemnity must be construed on its own.

[26] McMillan, Catherine, "A Birthday Present for Lord Denning: The Contracts (Rights of Third Parties) Act 1999" (2000) 63 *MLR* 721–738, at 724.

[27] [2004] 1 All ER (Comm) 481.

On the facts of this case, s.1(1)(b) applied to the commission clause as the clause benefitted Cleaves who was expressly identified to receive payment of commission. Since there were no provisions in the contract which excluded Cleaves' right, the presumption was not rebutted. It was also held that Cleaves was entitled to refer the matter to arbitration. Although the arbitration clause did not expressly mention that Cleaves was entitled to the benefit of the arbitration clause, this conclusion was reached by applying s.8(1) which is discussed later in this chapter at Part III(A)(4).

The application of s.1(1)(b) is further discussed in *Prudential Assurance Co Ltd* v *Ayres*.[28] In this case, Prudential (plaintiff) granted an underlease to Ayres (defendants) which was later assigned to A&G. Ayres covenanted with Prudential that it would guarantee payment of rent and other charges by A&G. On the same day where the lease was assigned by Ayres to A&G, Prudential entered into a Supplemental Deed to the underlease with A&G.[29] A&G went into bankruptcy and failed to pay rent and other charges due under the lease. Prudential sued Ayres for the amount owed by A&G. Ayres argued that the effect of Clause 2.1 of the Supplemental Deed was to prevent Prudential from recovering a greater sum from Ayres than it could recover from A&G. The High Court held that Ayres was entitled to rely on the 1999 Act (E&W) to enforce the Supplemental Deed. Lindsay J adopted a liberal interpretation of s.1(1)(b). The learned judge held that this section was satisfied if on a true construction of the term in question it had the effect of conferring a benefit on the

[28] [2007] All ER 43.

[29] This supplemental deed contained the following clause:

> 2.1 The liability of the Tenant under the Lease and all documents ancillary to or supplemental to the lease and the liability of the Tenant under any authorised guarantee agreement given in connection with any assignment of the Lease shall be limited to the Partnership (including, but not limited to all its assets, income and accounts) and such liability shall not extend to the personal assets of individual partners (present, past or future) therein. Consequently, any recovery by the Landlord against the Tenant **or any previous tenant under the Lease for any such default shall be limited to assets of the Partnership and shall not extend to the personal assets of any individual partners therein other than the capital and current accounts of such partners in the Partnership.** (emphasis added)

third party. There is no requirement that the benefit to the third party should be the predominant purpose or intent behind the term or that the applicability of s.1(1)(b) is denied if a benefit is conferred on someone other than the third party.

Lindsay J's decision was reversed by the Court of Appeal.[30] Moore-Bick LJ took a different construction of Clause 2.1 of the Supplemental Deed. His Lordship held that it was unlikely that Prudential and Ayres intended to limit Ayres' liability and that there was a drafting error of Clause 2.1 and reworded the clause.[31] As a result, the clause no longer benefits any third party. However, Moore-Bick LJ did not disapprove of Lindsay J's approach on the application of the 1999 Act (E&W). But in this case, the Supplemental Deed was not construed to benefit Ayres as it did not contain any express provisions that the contracting parties (Prudential & A&G) intended to allow Ayres to limit their liability by enforcing Clause 2.1. Due to the fact that the parties had different agreements to protect their own position, if Clause 2.1 was really intended to benefit Ayres, the contracting parties would have expressly stated so or make Ayres a party to the Supplemental Deed.[32] This case illustrates that in situations involving a number of different parties and complex arrangements, third parties are only entitled to rely on the 1999 Act (E&W) if this is clearly expressed in the contract.

[30] Reported as [2008] EWCA Civ 52.
[31] According to Moore Bick LJ, at para 35 (*Prudential* - CA), Clause 2.1 should read as "Consequently, any recovery by the Landlord or any previous tenant under the Lease against the Tenant for any such default shall be limited to assets of the Partnership and shall not extend to the personal assets of any individual partners therein other than the capital and current accounts of such partners in the Partnership."
[32] At para 34 (*Prudential* - CA).

2. Rescission or Variation of Third Party's Right

The contracting parties are allowed to rescind or vary the benefit intended for the third party. However, this power is limited by s.2(1).[33] If the third party's right under the contract crystallises[34] according to any of the events stipulated in s.2(1), the contracting parties cannot 'by agreement' rescind or vary the contract to the prejudice of the third party. It must be noted that due to the phrase 'by agreement', the fetter of power in s.2 will not cover situations (i) where any of the contracting parties exercises his right to rescind the contract (for example, where one of the parties has misrepresented to the other) or (ii) where the contract is revoked due to operation of law such (for example, where the contract is frustrated).[35] In these situations, the contracting parties can exercise their right to rescind the contract even after the third party's right has crystallised. The fetter of power in s.2 will also not apply to a situation where the promisee retains the right to choose among the third parties as to whom is to receive the benefit.[36]

---

[33] Section 2(1) provides that:

> Subject to the provisions of this section, where a third party has a right under section 1 to enforce a term of the contract, the parties to the contract may not, by agreement, rescind the contract, or vary it in such a way as to extinguish or alter his entitlement under that right, without his consent if -
> (a) the third party has communicated his assent to the term to the promisor,
> (b) the promisor is aware that the third party has relied on the term, or
> (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.

[34] If more than one third party is involved, each of them will have to satisfy the crystallisation test on its own to prevent the contracting parties from varying the contract; LCR, at para 9.43.

[35] Andrews, Neil, "Strangers to Justice No Longer: The Reversal of the Privity Rule under the Contracts (Rights of Third Parties) Act 1999" (2001) 60 *C.L.J.* 353–381, at 364.

[36] Treitel (*Law of Contract*), at 700.

The three crystallisation tests offered by s.2(1) are as follows:

(a) Third party has communicated his assent to promisor

The third party must let the promisor know that he has accepted the benefit provided in the contract.[37] Assent can be by conduct or words.[38] The postal rule will not be applicable if letter of acceptance is sent by the third party to the promisor.[39] Nonetheless, it is not clarified in the 1999 Act (E&W) whether communication is considered to be made when the letter reaches the promisor or when he actually reads the letter.[40] Although it is not difficult to satisfy this crystallisation test, it may be prejudicial to the third party who is not aware of the provisions of the 1999 Act (E&W). He may fail to communicate his assent to the promisor before the benefit is revoked or varied.

(b) Promisor is aware that third party has relied on the term

To amount to reliance, there must be some acts done by the third party as a result of the promise that he will receive a benefit.[41] No material reliance is required. Trivial acts of reliance are sufficient to trigger the crystallisation process.[42] It may not be difficult to prove acts of reliance unless the third party has not done anything in anticipating the benefit.

[37] In *Precis (521) plc* v *William M Mercer Ltd* [2005] EWCA Civ 114, Arden LJ rejected the appellant's counsel's argument that acceptance had to be made within a reasonable time as this argument is inconsistent with the words found in s.2(1)(a) 1999 Act (E&W).
[38] Section 2(2)(a).
[39] Section 2(2)(b).
[40] Beale, H.G., ed., *Chitty on Contracts*, 29th Edition, 2 vols., (Sweet & Maxwell, London, 2004), at para 18:095.
[41] LCR, at para 9.19.
[42] LCR, at para 9.31. All that is important is the fact that expectation has been engendered in the third party that he will be entitled to the benefit.

However, the promisor may not be aware of the reliance if he has no dealing with the third party before he renders performance to the latter.

(c) Promisor can reasonably be expected to have foreseen that third party would rely on the term and third party had in fact relied on it

In view of the fact that there are situations where the promisor is not aware of the third party's reliance, s.2(1)(c) provides that crystallisation will occur if the promisor can reasonably foresee reliance by the third party. This is determined objectively. The promisor is not required to expect the exact form of reliance by the third party. It is sufficient if he can foresee some form of reliance by the third party.[43] This test although beneficial to the third party, has caused concern to the promisor as this may be the easiest crystallisation test to be satisfied. Dean comments that the contracting parties' power to vary the contract "is going to be of little practical use".[44] To ensure that the third party's right has not crystallised under s.2(1)(c), the promisor must check whether there is any reliance by the third party before he agrees with the promisee to vary the contract. Once he checks with the third party, he will either realise that the latter has relied on the contract or accepts the benefit there and then.

The need to check with the third party can be burdensome and inconvenient to the promisor. Moreover, there may be situations where he needs to first check with the promisee. For example, the promisor may not know whether the third party is aware that a contract is made for his benefit. He has to check with the promisee to determine whether

[43] Andrews (2001) 60 *C.L.J*. 353–381, at 367.
[44] Dean, Meryll, "Removing a Blot on the Landscape – The Reform of the Doctrine of Privity" (2000) *JBL* 143–152, at 150.

the third party is informed of the benefit. If the third party has no such knowledge, the crystallisation test will not be satisfied and there is no necessity to check with him.

Once any of the above crystallisation tests applies, the contracting parties can only vary the third party's right with his consent. Nonetheless, the 1999 Act (E&W) allows the courts to dispense the requirement of obtaining such consent if any of the following are satisfied:

(a) The consent of the third party cannot be obtained as his whereabouts are unknown,[45]

(b) The third party is mentally incapable of giving his consent,[46] or

(c) It cannot be reasonably ascertained whether or not the third party has in fact relied on the term.[47]

Judges can impose conditions on the contracting parties as they deem fit in granting the order to dispense with the third party's consent.[48]

In light of the possibility that third party rights can crystallise easily, the contracting parties may prefer to exclude the application of s.2(1) or modify the crystallisation tests as set out in s.2(1). These are allowed by the 1999 Act (E&W).[49] However, the 1999 Act (E&W) is silent as to whether the contracting parties can provide for unilateral revocation of the benefit.[50] If this is allowed, the next query is whether such revocation can be effected after the crystallisation of the third party's right. Arguably, such revocation falls outside the

[45] Section 2(4)(a).
[46] Section 2(4)(b)
[47] Section 2(5).
[48] Section 2(6). This includes an order of compensation to the third party by either or both of the contracting parties; Treitel (*Law of Contract*), at 701.
[49] Section 2(3)(a) and (b).
[50] Merkin, at para 5.77, opines that s.2(3) should be construed to allow the contracting parties to provide for unilateral revocation.

limits of s.2(1) which applies only where there is an agreement to rescind the contract. Accordingly, unilateral revocation is valid irrespective of whether the third party's right has crystallised or otherwise.[51]

The contracting parties can also include a term stating that the term benefiting the third party is unalterable. The variation of this term is similar to the rules which govern the variation of other terms of the contract benefiting third parties. This means that this term can only be varied before the third party's right crystallises.[52]

Accordingly, the third party's rights are very precarious as his rights are subject to the agreement of the contracting parties. McMillan provides one example where unfairness could arise from allowing the contracting parties to exclude the operation of s.2(1) where the third party is not aware of this fact.[53] In this example, C enters into contract 1 with B who undertakes to provide daily nursing care to C. Subsequently, B realises that he cannot provide this care. B contracts with A, by contract 2, to provide the care to C who agrees to such arrangement. In contract 2, A reserves the right to vary or rescind this contract without C's consent. C, by contract 3, discharges B's obligations to perform contract 1 for the consideration of B having entered into contract 2. C cannot complain if A varies contract 2 to C's detriment.

In MacMillan's example, it can be argued that C should look at the contents of contract 2 before discharging contract 1. However, it may not be realistic to expect C to do so unless

[51] The same conclusion is reached by Chan (2001) *JMCL* 137-159, at 150.
[52] LCR, at para 9.46.
[53] McMillan (2000) 63 *MLR* 721–738, at 728. The order of creation of the contracts begins with contract 1, contract 2 and contract 3.

he knows or is advised as to the possible detrimental consequences that he would face as a result of his failure to read contract 2. Even if contract 1 is not discharged, there will be a circuity of legal actions. C will sue B for breach of contract 1 and B in turn will sue A for breach of contract 2. C will be in the most disadvantageous position if B is insolvent.

3. Defences and Set-Off

The defences and set-off that the promisor can utilise in an action brought by the third party are provided in s.3. The 'defences' intended to be covered by s.3 are matters affecting the existence, validity and enforceability of the contract or the term benefiting the third party.[54] This includes matters which make the contract void, voidable or matters leading to the discharge of contract such as frustration or breach of condition. 'Defences' are not intended to cover procedural restrictions to the promisee's claim or bar to remedies which can be acquired by the promisee.[55]

(i) Defences and Set-Off Available against Promisee

According to s.3(2) 1999 Act (E&W), the promisor is entitled to rely on any defences or set-off any matter which (i) 'arises in connection of the contract and is relevant to the term' benefiting the third party and (ii) 'would have been available to him by way of defence or set-off if the proceedings had been brought by the promisee.' For example, if the promisee has misrepresented to the promisor, the latter can rely on this ground to rescind the contract.

[54] LCR, at para 10.2.
[55] LCR, at para 10.2.

Stevens raises two difficulties with s.3(2).[56] The first difficulty in relation to the scope of s.3(2) is due to the limitation that any defences relied on by the promisor must be "relevant to the term". He provides the following example:

> A needs three cows. He agrees to buy Daisy, Ermintrude and Flo in a single contract from B for £1,000 each. The purchase price for Flo is to be paid to C and it is intended that this should be enforceable by C. After the sale A discovers that B has misrepresented that Daisy is a one year old when in fact she is five years old.[57]

If A rescinds the contract, it is questionable whether he can rely on B's misrepresentation as a defence in a legal action brought by C to recover the purchase price for Flo. If this matter is looked at strictly, the misrepresentation is not relevant to the term benefiting C. Accordingly, A would not be able to rely on this defence against C. This conclusion is strange and it is most likely that judges will decide that the defence or set-off is relevant to the term. It is submitted that this should be the approach taken by judges as the third party's right flows from the contract. This forms the link between the defence and the term. If the contract is voidable and is rescinded, the third party should not be able to assert his right under the contract. To do so will elevate his right above that of the promisee who is the one providing the benefit to him.

The second difficulty stems from the lack of guidance as to the types of defences which are covered by s.3. For example, any claim for the remedy of specific performance can be defeated if the promisee does not come to courts with "clean hands". The conundrum posed is whether this amounts to a defence or merely a restriction on the promisee's right of

[56] Stevens, (2004) 120 *LQR* 292–323, at 311.
[57] Stevens, (2004) 120 *LQR* 292–323, at 311.

enforcement, so that it will be outside the scope of s.3.[58] From the tenor of the Law Commission Report, the restrictions on the promisee's right to claim remedies for breach of contract do not affect the third party's right. The Law Commission's view is acceptable as there may be circumstances where the third party, without any knowledge of the misconduct of the promisee, relies on the term and incurs losses.

Section 3(3) states that the promisor is also entitled to rely on any defences or set-off which is not connected to the term benefiting the third party if this is expressly provided for in the contract and which would have been available to him if he is sued by the promisee. Section 3(5) allows the contracting parties to exclude any defences or set-off which are available to the promisor by virtue of s.3(2).[59]

(ii) Defences, Set-Off and Counterclaims against Third Party Only

Section 3(4) provides that the promisor is also entitled to the defences, counterclaim or set-off which would be available if the third party had been a party to the contract. For example, if the third party has misrepresented to the promisor to induce the promisor to enter into a contract for his benefit, the promisor is entitled to rely on this misrepresentation as a defence. However, any set-off or counterclaim against the third party cannot exceed the value of the benefit to the third party under the contract.[60]

[58] Stevens (2004) 120 *LQR* 292–323, at 311.
[59] Chan (2001) *JMCL* 137-159, at 152-153 comments that it is illogical to allow contracting parties to contract out of s.3(2) because this gives the impression that third parties enjoy rights under a void contract. This places them in a better position than the promisee. With respect, if the contract is void, the third party is not entitled to any rights as the contract is of no effect. However, s.3(2) is wide enough to cover defences which do not make the contract void. In these instances, the contracting parties are given the discretion whether to exclude these defences in a dispute brought by the third party against the promisor.
[60] Merkin, at para 5.103.

Section 3(5) allows any defences, set-off or counterclaims available to the promisor under s.3(4) to be expressly excluded in the contract.

(iii) Defences Applicable where Third Party is Enforcing Exclusion or Limitation Clauses

In relation to exclusion or limitation clauses, the third party will only be protected under the 1999 Act (E&W) if he is entitled to rely on these clauses had he been a party to the contract.[61] As such, the third party will not be able to rely on the exclusion clause if the contract is invalid or if the promisor is entitled to set aside the contract.

(iv) Defences and Set-Off of Promisee against Third Party

The 1999 Act (E&W) is silent as to the defences and set-offs that are available to the promisee against the third party. As such, it is arguable that the promisor is not entitled to rely on these defences and set-offs in a legal action brought by the third party. It is uncertain as to whether express provisions in the contract allowing the promisor to rely on these defences and set-offs are effective to assist the promisor.

[61] Section 3(6).

4. Miscellaneous

There are a number of other matters arising from the operation of the 1999 Act (E&W).

(i) Remedies

Section 1(5) provides that the third party is entitled to all the remedies available in an "action for breach of contract".[62] According to Merkin, the phrase "action for breach of contract" is significant in three aspects.[63] Firstly, the third party is not entitled to terminate the contract on the ground of the promisor's repudiation of the contract. Secondly, the third party is not entitled to any restitutionary claim on the contract. Thirdly, in assessing the damages suffered by the third party, the ordinary rules of remoteness and mitigation of damages apply.

The third party's right is separate and independent from the promisee's right to claim remedies for breach of contract. Thus, the third party is claiming for his own loss due to the promisor's breach of contract. He is entitled to claim for any reliance or expectation loss that he suffered.[64] Stevens highlights the possible anomaly in allowing the third party to claim expectation losses and provides an example to illustrate his point.[65] Suppose B agrees to sell his car to A for £5,000. The payment is to be made to C. Delivery and payment to take place the following week. In breach of contract, A repudiates the deal. Since C is treated as a party to a contract, he should be placed in the position had the contract been

[62] These include damages, specific performance and injunction. In relation to the remedies of specific performance or injunction, the fact that the third party is a volunteer will not prevent judges to grant these remedies.
[63] LCR, at para 5.49.
[64] LCR, at para 9.33 and Andrews (2001) 60 *C.L.J.* 353–381, at 360.
[65] (2004) 120 *LQR* 292–323, at 301.

performed in assessing the amount of damages. Accordingly, he is able to claim £5,000 from A. This is an absurd result as if the same contract involves only A and B, B is only entitled to the difference between the market value at the time of breach of contract and the contract price for the car.

Judges facing these situations must provide additional guidelines to ensure that the promisor is not unduly prejudiced by the operation of the 1999 Act (E&W). For instance, Burrows states that in determining the amount of damages to be awarded to the third party, it is most likely that courts will take into account the position of the promisor and the promisee where relevant.[66] This ensures that no injustice is done to the promisor. This is particularly true in situations of unexecuted contracts such as the example provided by Stevens. In Stevens' example, the courts will consider the amount of 'saved cost of performance' of the promisee as a result of the promisor's breach of contract in determining the amount of damages to be granted to the third party.[67]

(ii) Procedural Requirements

There is no requirement that the promisee must be joined in a legal action brought by the third party. However, a joinder can be ordered by the courts in situations where the promisor seeks to rely on defences or set-off available against the promisee. The priority of legal action between the promisee and the third party is also not specified in the 1999 Act (E&W).

---

[66] Burrows, Andrew, *Understanding the Law of Obligations: Essays on Contract, Tort & Restitution*, (Hart Publishing, Oxford, 1998) (hereinafter referred to as (*Contract, Tort & Restitution'*), at 230.

[67] *Contract, Tort & Restitution,* at 230. Thus, if the promisee has not paid the full purchase price for the car (relying on Stevens' example), the third party should not be entitled to recover the full value of the car.

(iii) Promisee's Right and Avoidance of Double Liability

Section 4 provides that the promisee's rights under the contract remain unaffected. The promisee can sue the promisor for the losses that he suffers as a result of the breach of contract and bring any restitutionary claim where relevant. Claim for damages under the 'narrow ground' or the 'broad ground' in *Panatown* is allowed.[68] As both the third party and the promisee are entitled to sue the promisor, concern arises as to whether the promisor will be subject to double liability. Section 5 specifically deals with this problem. Section 5 does not allow any overlapping of damages to be recovered from the promisor. If the promisee has sued and recovered losses suffered by the third party or the expenses that he incurs in making good the breach, the courts will reduce the amount of damages payable to the third party in his (third party) legal action against the promisor.

Concern arises whether the third party is protected from the losses he suffers since he is not the party suing and receiving the damages. If the promisee's recovery of damages is on the 'narrow ground', the third party is protected as the promisee is required to account the damages to the third party. The same cannot be said in relation to recovery of damages on the 'broad ground'. It remains unsettled as to whether the promisee has to account the damages to the third party since the damages are to compensate the promisee's loss of performance interest of the contract.

[68] The 'narrow ground' and the 'broad ground' are discussed in Chapter 4 Part IV. The 'narrow ground' is developed by judges to allow recovery of third party losses whereas the 'broad ground' is a liberal application of the principles governing damages to allow the promisee to recover damages for cost of repair or diminution of value to properties belonging to third parties.

The 1999 Act (E&W) is silent as to the situation where the third party sues the promisor before the promisee. In this situation, it is submitted that if the third party has been compensated for his losses, the promisee will only be entitled to nominal damages. This conclusion is reached as the purpose of the contract (to benefit the third party) has been achieved. However, if the promisee suffers any losses of his own due to the breach of contract, he can recover these losses from the promisor.

(iv) Arbitration

According to s.8(1),[69] if the contract contains an arbitration agreement, the third party will be considered to be a party to the arbitration agreement if his right to enforce the contract under s.1 is subject to it. This provision is based on a "conditional benefit" approach that is if the third party wishes to enjoy a benefit of the contract, he has to take it subject to the conditions of the contract. In *Nisshin Shipping Co Ltd* v *Cleaves & Co Ltd,*[70] Colman J held that s.8(1) will apply if on a proper construction, the arbitration agreement is wide enough to cover the dispute on the performance of the 'substantive term'[71] between the promisor and the promisee. As such, in *Nisshin*, since the arbitration agreements between the promisor and the promisee covered dispute as to payment of commission, the broker was entitled to refer the matter to arbitration. Section 8(2) allows a third party who does not fall

[69] Both s.8(1) and (2) have been extensively discussed in Ambrose, Clare, "When Can a Third Party Enforce an Arbitration Clause?" (2001) *JBL* 415–432.
[70] [2004] 1 All ER (Comm) 481.
[71] The phrase 'substantive term' is found in s.8(1) and it means the term benefiting the third party which is enforceable by him under s.1.

within s.8(1) to assert his right to have recourse to arbitration and will be treated as a party to the arbitration agreement.[72]

(v) Exclusion of Certain Types of Contracts

The 1999 Act (E&W) excludes its application to the following contracts:

(a) Contracts on bill of exchange, promissory note or other negotiable instrument,[73]

(b) Contracts covered by s.14 Companies Act 1985,[74]

(c) Third parties are not allowed to enforce terms found in employment contracts or worker's contract in a legal action brought against the employee or worker,[75]

(d) Contracts of carriage of goods by sea,[76] and

(e) Contracts of carriage of goods by rail or road or for the carriage of cargo by air, which is subject to "appropriate international transport convention"[77]

In relation to contracts of carriage of goods, the 1999 Act (E&W) applies to exemption or limitation clauses found in these contracts.[78]

---

[72] According to the Explanatory Notes to Contracts (Rights of Third Parties) Act 1999, s.8(2) applies to a situation where the third party is given a unilateral right to arbitrate a dispute other than one concerning the third party under s.1.
[73] Section 6(1).
[74] Section 6(2).
[75] Section 6(3).
[76] Section 6(5)(a).
[77] Section 6(5)(b).
[78] Section 6(5).

(vi) Preservation of Existing Mechanisms Circumventing Doctrine of Privity

Section 7(1) preserves the existing common law mechanisms that provide a right or remedy to the third party. The existence of such right at common law will not defeat the third party's right to rely on the 1999 Act (E&W).[79] The third party is given an option to decide the avenue which he wishes to utilise to enforce the contract. The common law mechanisms remain an important source for third parties to enforce contracts made for their benefit as the entitlement under the 1999 Act (E&W) can be easily excluded by the contracting parties. Moreover, the Law Commission had emphasised a number of times in its report that judges are not prevented from developing the law where the third party's claim does not fall under the statutory reform.[80]

(vii) Position of Joint Promisee

The Law Commission recommended for joint promisees to be excluded from the coverage of the 1999 Act (E&W).[81] Yet, the Act is silent on this matter prompting arguments that joint promisees are entitled to rely on it.[82] No difficulties may be posed in practice. If the plaintiff can prove that he is a joint promisee, there is no necessity to rely on the 1999 Act (E&W). His rights as a joint promisee are equivalent to the rights of a contracting party. Such rights are stronger than the third party's right because it cannot be altered without his

[79] *Nisshin Shipping Co Ltd* v *Cleaves & Co Ltd* [2004] 1 All ER (Comm) 481.
[80] LCR, at para 5.10–5.11 and 12.1. Phang, Boon Leong, "On Justification and Method in Law Reform – The Contracts (Rights of Third Parties) Act 1999" (2002) 18 *JCL* 32-51, at 49-50 opines that this is the "most practical approach to adopt" due to the need to preserve flexibility in the law so that the law is able to deal with the different factual matrix that goes to the courts.
[81] LCR, at para 6.10 and Clause 8 of the draft bill of the 1999 Act (E&W).
[82] Stevens (2004) 120 *LQR* 292–323, at 314 and Merkin, at para 5.55.

consent from the time the contract is created and there is no necessity to prove whether s.1(1)(a) or s.1(1)(b) applies.

B. New Zealand

The Contracts (Privity) Act 1982 (hereinafter referred to as '1982 Act (NZ)') was enacted as a result of the recommendations made by the New Zealand Contracts and Commercial Law Reform Committee in Report on Privity of Contract (1981). The 1982 Act (NZ) expressly states that its application extends to oral and implied contracts.[83] It also covers enforcement of exclusion and limitation clauses.[84] The third party is known as the beneficiary. There is no section which stipulates that the beneficiary is subject to the terms and conditions attaching to the benefit.

1. Enforceability Test

The enforceability test of the 1982 Act (NZ) found in s.4[85] is similar to the test found in s.1(1)(b) and s.1(2) in the 1999 Act (E&W). Similarly, the contracting parties can expressly exclude the application of the 1982 Act (NZ).

[83] Section 2.
[84] Section 2.
[85] Section 4 provides that:

> Where a promise contained in a deed or contract confers, or purports to confer, a benefit on a person, designated by name, description, or reference to a class, who is not a party to the deed or contract (whether or not the person is in existence at the time when the deed or contract is made), the promisor shall be under an obligation, enforceable at the suit of that person, to perform that promise: Provided that this section shall not apply to a promise which, on the proper construction of the deed or contract, is not intended to create, in respect of the benefit, an obligation enforceable at the suit of that person.

The principles in relation to the designation and existence of the beneficiary are similar to the 1999 Act (E&W) as well. The meaning and scope of these principles have received judicial consideration in a number of cases. In *Cross* v *Aurora,*[86] Wyllie J stated that "Designation is a strong word, a positive word, and means something more than a mere contemplation or possibility."[87] In *Field* v *Fitton*,[88] it was held that the third party must be 'defined with sufficient particularity'. The case of *Rattray Wholesale Ltd* v *Meredyth-Young & A Court Ltd*[89] requires that in situations where designation is by description, the identity of the third party must be 'described with precision in the contract'.

The strength of the protection granted to a beneficiary is dependent on the approach taken by judges in applying the enforceability test in s.4. This is evidenced by the differences in the judicial approach in determining the application of the 1982 Act (NZ) to a nominated person under the contract who is not privy to it.[90]

---

[86] (1989) 4 NZCLC 64, 909 at 64, 913.

[87] This had been referred in a number of cases such as *Oceanic Foods Ltd* v *Owens Security Ltd* [1996] NZDCR LEXIS 116, at 19 (according to the pagination provided by *Lexis.com Research System*) and *Kevdu* v *Ko HC* [2007] NZHC 224, at para 28.

[88] [1988] 1 NZLR 482, at 493.

[89] [1997] 2 NZLR 365, at 383.

[90] In *Coldicutt* v *Keeys* (High Court, Whangarei, A 50/84, 17 May 1985), it was held that a nominee was a person identified and designated by description and accordingly could rely on s.4 to enforce the contract. However, the court came to a different conclusion in *Field* v *Fitton* which was followed in the subsequent case of *Karangahape Road International Village Ltd* v *Holloway* [1989] 1 NZLR 83. The courts in these two cases decided that designation requires a person or a group of persons to be specified or particularised. The mere inclusion of the word 'nominee' without more was not a sufficient designation of a third party since no person is specified or particularised, anyone could be nominated to take a benefit under the contract. However, in a more recent case of *Rattray Wholesale Ltd* v *Meredyth-Young & A Court Ltd*, the trial judge commented that the approach taken in *Field* and *Karangahape* was "unduly restrictive" and did not reflect the purpose behind the 1982 Act (NZ) which was intended to be a remedial statute. The learned judge thus, decided that a nominee can rely on s.4 since there must be a reason as to why the contracting parties include the word 'nominee' in the contract. It is most likely that the contracting parties intend that the nominee to take over the rights of one of the contracting party, at 381-383. Recent judicial decisions adopted the approach taken in *Rattray* where a nominee was held to be entitled to enforce a contract based on s.4 as seen in *Cornerstone Group Ltd* v *Edison Ltd* [2006] NZHC 1135 and *Pragma Holdings* v *Great South 507 Ltd* [2006] NZHC 977. This approach was favoured by the Law Commission in England as seen in LCR, at para 8.4.

The stricter approach adopted by judges in relation to s.4 in the late 1980's and early 1990's has led Roe to comment that the presumption created by s.4 in favour of the beneficiary may not be very strong.[91] Support for such comment is found in the cases of *Malyon* v *New Zealand Methodist Trust Association*[92] and *Karangahape Road International Village Ltd* v *Holloway.* In these cases, the failure of the contracting parties to provide an express right for the third party to enforce the contract despite the fact that it was easy for them to do so negated the intention to confer a benefit to the latter. If this approach is followed, it will be easy to rebut the presumption in s.4. However, in light of recent decisions, it is submitted that as a whole, judges adopt a liberal application of s.4. This can be seen in Tipping J's decision in *Rattrays* where it was held that:

> The Contracts (Privity) Act was intended to be a remedial enactment substantially doing away with a rule which for many years had itself been regarded as unnecessarily restrictive.
>
> Section 4 should be given such fair, large and liberal interpretation as will best ensure its remedial purpose.[93]

Tipping J's approach was adopted by the Court of Appeal in *Ballance Agri-Nutrients (Kapuni) Ltd* v *The Gama Foundation*[94] and followed by the High Court in *Pragma Holdings* v *Great South 507 Ltd*.[95] A liberal approach is also seen in *Kevdu* v *Ko HC* where it was held that the word 'you'[96] as found in the contract sufficiently identified the third party. This decision was achieved by looking at the knowledge of the contracting parties at

---

[91] Roe, (2000) 63 *MLR* 887–894, at 892.
[92] [1993] 1 NZLR 137.
[93] At 382 (*Rattrays*).
[94] [2006] 2 NZLR, at para 122. It was held that in this case that the third party was sufficiently designated by description through the use of the phrase 'permitted assigns'.
[95] In fact, in this case it was held that the third party was entitled to bring a claim of misrepresentation under the 1982 Act (NZ).
[96] The word 'you' was used in the agreement to indicate the position of the party who benefits from the contract.

the time that the contract was made. All the parties involved knew that the third party was the recipient of the benefit and was the one responsible to perform the obligations of the contract.

A term purporting to confer a benefit to the third party can be implied. In *Pacific Software Technology* v *Perry Group Ltd*,[97] a dispute arose as to whether the party (Perry Group) commissioning a new database programme was entitled to its copyright. The Court of Appeal observed that to give full weight to the position of the commissioning party and to give the commission business efficacy, it is necessary and appropriate to imply a non-revocable license for Perry Group to utilise the database and further a term that such license enures **for the benefit of any successor or assignor of Perry Group**[98] (emphasis added).

2. Rescission or Variation of Beneficiary's Right

Section 5 provides that subject to s.6 and s.7, the contracting parties can vary or discharge the benefit given to the beneficiary until the benefit crystallises. When this happens, any modification to the benefit can only be made with the beneficiary's consent. The circumstances stipulated in s.5 which lead to crystallisation are as follow:

(a) The position of a beneficiary has been materially altered by the reliance of that beneficiary or any other person on the promise (whether or not that beneficiary or that other person has knowledge of the precise terms of the promise); or

(b) A beneficiary has obtained against the promisor judgment upon the promise; or

(c) A beneficiary has obtained against the promisor the award of an arbitrator upon a submission relating to the promise.

[97] [2004] 1 NZLR 164.

[98] In *Pragma*, the trial judge referred to *Burrows, Finn & Todd Law of Contract*, 2nd Edition (2002) which states that a promise in the contract may be made by implication if there is an intention to confer a benefit to the third party, relying on *New Zealand Guardian Trust Co Ltd* v *Peat Marwick* (1991) 5 NZCLC 67.

The most significant circumstance is (a). Such alteration of the beneficiary's position can be due to an act or omission in reliance on the promise by the beneficiary or another person. The meaning of 'material alteration' was not defined in the 1982 Act (NZ). Newman presumes that 'material alteration' covers 'alteration of position to one's detriment'.[99] There is no requirement that the contracting parties must be aware of the reliance nor is it necessary for them to have reasonably expected that reliance would occur. As such, it is not advisable for the contracting parties to vary or discharge the promise before checking whether the beneficiary has relied on the promise.

It can be argued that the crystallisation tests in s.5(b) and (c) are redundant. If the beneficiary brings legal proceedings against the promisor, arguably, he has materially altered his position in terms of the legal cost incurred.[100] Otherwise, it will be unfair to the beneficiary if the contracting parties vary or discharge the benefit after the legal action has started but before judgment is obtained.

In a situation where the beneficiary's right under the promise has crystallised under s.5(1)(a) or where it is unclear whether this has occurred, s.7(1) allows the promisor or the promisee to apply to court to dispense with the requirement of obtaining consent of the beneficiary to vary or discharge the promise.[101] Courts may grant an order waiving the requirement of consent if it is 'just and practicable' to do so. In granting such order, the court may impose any conditions as it thinks fit.

---

[99] Newman, R.H, "The Doctrine of Privity of Contract: The Common Law and the Contracts (Privity) Act 1982" (1983) 4 *AULR* 339–360, at 350. The author gives an example of a beneficiary who in reliance of a promise to be given an annuity on retirement, fails to renew a life insurance policy and it lapses.

[100] However, it is opined by Pearson, G D, in "Privity of Contract: Proposed Reform in New Zealand" (1983) *Otago L Rev* 316-341, at 333 that such interpretation is not possible as it will make s.5(b) and (c) redundant.

[101] This may apply in a situation where the performance of the contract become more onerous due to certain changes on the position of the contracting parties; Wilson, L., "Contract and Benefits for Third Parties" (1987) 11 *Syd L Rev* 230-258, at 255.

If the beneficiary or any other person has incurred losses in reliance on the promise, the court may order the promisor to pay a sum of compensation to the beneficiary as the court deems just.[102] The compensation usually reflects the reliance loss suffered by the beneficiary in relying on the promise unless justice requires compensation to reflect the expectation loss of the beneficiary to be awarded.[103] There are no apparent difficulties with the application of s.7 from decided cases.[104]

Section 6[105] provides two situations where the benefit acquired under s.4 can be varied or discharged. Section 6(a) merely states the obvious that the benefit can be varied or discharged if the contracting parties and the beneficiary agree to do so.

Section 6(b) allows the contracting parties to include a term in the contract to the effect that any one or both of them can discharge or vary the promise without the beneficiary's consent (this term is hereinafter referred to as 'special term'). To exercise these rights, the contracting parties have to satisfy four requirements. Firstly, s.6(b)(i) states that the special term must be included in the contract at the time the promise is made. A literal reading of s.6(b)(i) suggests that the contracting parties cannot alter the contract subsequently to include this term. This may be unduly restrictive as the contracting parties cannot change

---

[102] Section 7(2).

[103] Rogers in Finn, Ed., *Essays on Contract*, (The Law Book Co. Ltd, 1987) (hereinafter referred to as 'Finn'), at 101, referring to Professor Coote's work found in [1984] *Recent Law* 107, at 114.

[104] Section 7(a) was applied in *New Zealand Dairy Board* v *New Zealand Co-operative Dairy Co Ltd* [1999] 2 NZLR 355. In this case, it was held that the court could approve the cancellation of benefit on behalf of future and unascertained beneficiaries who might have been entitled to the benefit under the contract.

[105] Section 6 provides that:

> (a) By agreement between the parties to the deed or contract and the beneficiary; or
> (b) By any party or parties to the deed or contract if -
> (i) The deed or contract contained, when the promise was made, an express provision to that effect; and
> (ii) The provision is known to the beneficiary (whether or not the beneficiary has knowledge of the precise terms of the provision); and
> (iii) The beneficiary had not materially altered his position in reliance on the promise before the provision became known to him; and
> (iv) The variation or discharge is in accordance with the provision.

their mind after the contract is made to include this term. It is submitted that they should be entitled to do so provided the beneficiary's right has not crystallised under s.5. Secondly, s.6(b)(ii) requires the beneficiary to know of the existence of the special term. It is not necessary for him to know the precise details of this term. Thirdly, s.6(b)(iii) provides that the variation or discharge is only allowed if the beneficiary has not materially altered his position in relying on the promise before he becomes aware of the special term. Any reliance by the beneficiary after he knows of this term will not take away the contracting parties' right to discharge or vary the promise. Fourthly, s.6(b)(iv) states that the variation or revocation must be made in accordance to the provisions of the special term.

There are some difficulties with the application of s.6(b). It imposes a duty on the promisor or promisee to inform the beneficiary of the existence of the term reserving their right to vary or discharge the contract without the beneficiary's consent. Problems may ensue if the beneficiary denies knowledge of the existence of such term after being informed.[106] This may lead to evidential difficulties. To strike a balance between the rights of the various parties, Newman comments that both actual and constructive notice of the beneficiary's knowledge of the term can be relied on to prove s.6(b)(ii).[107] Section 6(b)(iii) only requires material alteration of the beneficiary's position in reliance of the promise. Applied literally, the contracting parties may still be entitled to discharge the promise if a person other than the beneficiary has relied on the promise and alters the beneficiary's position. Newman suggested that s.6(b)(iii) should be interpreted to include the 'beneficiary or any other person's reliance on the promise'.[108] This will be consistent with s.5(1)(a) which allows for

[106] Newman (1983) 4 *AULR* 339–360, at 352.
[107] Newman (1983) 4 *AULR* 339–360, at 352.
[108] Newman (1983) 4 *AULR* 339–360, at 353.

material alteration of the beneficiary's position by another person. However, Newman's suggestion may not be possible in light of the clear wording of s.6(b)(iii).[109]

In sum, although s.6(b) allows the contracting parties to enjoy their contractual freedom to vary or discharge the contract without the beneficiary's consent, practically, it may be difficult to do so due to the requirements laid down in this section.

3. Defences and Set-Off

Section 9(2)(a) allows the promisor to plead any defences, set-off and counterclaim which will be available to him if the beneficiary is a party to the contract. Section 9(2)(b) covers the defences, set-off and counterclaims which will be available in a legal action brought by the promisee. Nonetheless, such defences, set-off and counterclaim will only be allowed if they arise out of or in connection with the contract which include the promise to benefit the third party.[110] Section 9(4) provides that the beneficiary shall not be liable under any counterclaim raised by the promisor unless he proceeds with the legal action after being aware of the counterclaim. However, his liability under the counterclaim cannot exceed the value of the benefit provided to the beneficiary. The 1982 Act (NZ) is silent as to whether the contracting parties can exclude or include the defences and set-off applicable to the promisor as stated in s.9(2) in a legal action brought by the beneficiary.

---

[109] The New Zealand Law Reform Committee had proposed an amendment of s.6(b)(iii) to include alteration of the beneficiary's position by another person; NZLR R25, at para 77 as referred to by Barton, George, "The Effect of the Contract Statutes in New Zealand" [2000] *JCL LEXIS* 18, at 56 (according to the pagination offered by *Lexis.com Research System*. However, such recommendation is yet to be acted upon by the New Zealand Parliament.

[110] Section 9(3).

4. Miscellaneous

The provision[111] governing the beneficiary's entitlement to remedies for breach of contract by the promisor is similar to the 1999 Act (E&W). Section 14(1) expressly preserves the beneficiary's right against the promisor, which exists under any other statute or common law. Pre-incorporation contracts are excluded from the application of the 1982 Act (NZ).[112]

C. Australia

Legal reform on the doctrine of privity has taken place in some of the states in Australia such as Western Australia, Queensland and Northern Territory. These reforms took place at different times. The changes that have taken place in these states are discussed in turn.

1. Western Australia

Reform took place in the enactment of s.11(2) Property Law Act 1969[113] (hereinafter referred to as 'PLA 1969 (WA)'). This reform adopted the recommendation made by the English Law Reform Commission in 1937. Section 11(2) is silent as to the enforceability of oral contracts. The benefit to the third party must be expressly provided in the contract. This requirement has led to opinions that this section is limited to written contracts.[114] Nonetheless, this point remains debatable as express terms also arises from oral contracts

[111] Section 8.
[112] Section 182(5) Companies Act 1993.
[113] Section 11(2) provides that:

> Except in the case of a conveyance or other instrument to which subsection (1) of this section applies, where a contract expressly in its terms purports to confer a benefit directly on a person who is not named as a party to the contract, the contract is subject to subsection (3) of this section, enforceable by that person in his own name.

[114] Vroegop, J, "The New Zealand Contracts (Privity) Act 1982" (1984) 58 *ALJ* 5- 7, at 6.

and therefore s.11(2) applies equally to an oral contract. The third party is bound by the conditions stipulated in the contract made in favour of the promisor if he wishes to assert his right over the benefit in the contract.[115] Section 11(2) is also silent as to whether it applies to exclusion and limitation clauses.[116]

(i) Enforceability Test

According to s.11(2), there must be an express term in the contract which purports to provide a 'direct benefit' to the third party. Such term must contain words which are sufficiently clear to indicate that the third party is to receive the benefit under the contract.[117] The scope of express and direct benefit has yet to receive a full discussion of the courts. Implied terms are excluded and the courts are not allowed to consider surrounding circumstances in deciding whether the third party is entitled to enforce the contract. Section 11(2) may pose problems to laymen trying to benefit a third party. If they are not sufficiently careful and tedious in choosing the words to be used in drafting the contract, the third party may not fall within s.11(2).

Due to the fact that benefit is confined to 'a person who is not named as a party to the contract', arguably, the third party must be in existence and identified at the time the

[115] Section 11(2)(c).
[116] Benefit is not defined by section 11(2). However, Rogers in Finn, at 96 opined that s.11(2) should be construed benevolently so to include exclusion and limitation clauses.
[117] In *Jones* v *Barlett* [2000] 176 ALR 137, the son (third party to a lease agreement) failed in his attempt to rely on s.11(2) to sue the lessor for the injuries he suffered. The High Court rejected his claim as there was nothing in the contract which conferred a benefit to him.

contract is created.[118] Query also arises as to whether s.11(2) can be used to confer benefit to a class of persons or to those who fulfil the description provided in the contract.[119]

One successful case that has relied on s.11(2) is *Westralian Farmers Co-op. Ltd* v. *Southern Meat Packers Ltd*.[120] In this case, the Co-operative (agent), on behalf of Mr and Mrs King (owners), sold 36 head of cattle belonging to the latter to Southern (buyer). The buyer paid the purchase price directly to the owners despite the fact there was a clause[121] in the contract of sale which stipulated that the purchase price was to be paid to the agent. In fact, the agent had credited the purchase price minus commission into the owners' bank account. The agent then took an action against the buyer to recover the full purchase price. It was held that s.11(2) was applicable as the clause in question conferred a direct benefit to the agent and the buyer had to pay the purchase price to the agent.

(ii) Rescission and Variation of Third Party's Right

Section 11(3) provides that the third party loses the right to enforce a contract if it is cancelled or modified by the mutual consent of the contracting parties unless the contract prohibits such cancellation or modification. Nonetheless, the contracting parties' loses the right to cancel or modify the contract if the third party has adopted the contract either expressly or impliedly by conduct. Section 11(2) does not provide any definition of

[118] Vroegop (1984) 58 *ALJ* 5-7, at 6. In *Jones* v *Barlett,* the son relied on a clause in the lease agreement between his parents and the landlord which stated that the premises were to be used as "a private dwelling to be occupied by not more than THREE persons". Gleeson CJ at 145, stated that this clause did not benefit the son as his parents could invite anybody besides him to occupy the premises. This was because the clause did not sufficiently identify him as the third person to occupy the premises.

[119] Longo, J., "Privity and the Property Law Act: Westralian Farmers Co-Operative Ltd. v Southern Meat Packers Ltd (1983) 15 *UWALR* 411-417, at 416.

[120] [1981] WAR 241. Section 11(2) was also applied in *Toal* v *Aquarius Platinum Ltd* (2004) FCA 550. In *Toal*, the contract concerned expressly conferred the benefit to the third party.

[121] The clause stipulated that "To enable the agents to protect themselves as del credere agents in the sale the full purchase price shall be payable by the buyer and be recoverable by the agents alone."

'adoption'. This is regretted as it leaves ambiguity in determining whether the third party's right has crystallised. A number of possibilities have been identified as to the meaning of 'adoption' in this context. 'Adoption' may be similar to acceptance or reliance.[122]

In *Westralian Farmers*, Burt C.J stated that 'adoption' in this case had taken place when the agent credited the bank account of the owners with the sale price less commission.[123] It was not stated on the facts whether any notification of this fact was given to the owner or buyer. The learned judge did not emphasise on the need to give such notice to the contracting parties. Accordingly, it is arguable that the contracting parties need not be informed that the third party has adopted the contract. This position is not settled and awaits further clarification from the courts.

(iii) Defences

Section 11(2)(a) provides that the promisor, in the course of an action brought by the third party is entitled to rely on all the defences which would be available to him if the third party is a party to the contract.[124]

(iv) Miscellaneous

Section 11(2)(b) requires each party to the contract to be joined as a party to the legal action brought by the third party against the promisor.[125] The objective behind this rule is to

[122] LCR, at para 9.17.
[123] This was merely obiter dicta as this issue was not relevant in *Westralian Farmers* as there was no cancellation or modification of the contract by the contracting parties.
[124] Rogers in Finn, at 93 states that this will include defences of illegality, fraud, undue influence or mistake.

avoid double recovery by the promisee and the third party. However, whether this is actually achieved in practice is doubtful as seen in *Westralian Farmers.* Despite the fact that the promisee (owners) had received the purchase price and was joined to the legal action, the courts still held that the promisor (buyer) had to pay the purchase price to the third party (agent). This was unfair to the buyer who was required to pay the price twice, once to the owners and another to the third party. In fact, the unfairness to the buyer in this case can be avoided had the judges required the owners to account to the third party the sum paid to them by the buyer.[126]

There are no provisions dealing with the promisee's rights, the third party's remedies, the preservation of the existing exceptions to the doctrine of privity and the exclusion of certain contracts from s.11(2). Anyhow, it can be assumed that the remedies are similar to the remedies for breach of contract and that the existing common law methods to circumvent the doctrine of privity are preserved.[127]

---

[125] In *Jones* v *Bartlett*, Gaudron J, at 151, held that one of the reasons behind the failure of the son to rely on s.11(2) was that he did not join his parents to his legal action against the landlord. Similarly, in *JWH Pty Ltd* v *Kimpura Pty Ltd* [2004] WASC 39, it was held that the third party could not rely on s.11(2) as not all parties to the deed were joined as parties to the action.

[126] Siopis, A, Note, (1983) 57 *ALJ* 640–642, at 641–642.

[127] Judges continue to discuss the applicability of other statutory exceptions and the common law mechanisms to circumvent the doctrine of privity if s.11(2) is not applicable such as seen in *Jones* v *Bartlett*.

2. Queensland

The statutory reform in Queensland is found in s.55 Property Law Act 1974[128] (hereinafter referred to as 'PLA 1974 (Qld)'). Section 55 applies to both express and oral promises.[129] The beneficiary is bound by the terms of contract attaching to the benefit intended for him.[130] It is not entirely clear whether s.55 covers enforcement of exclusion and limitation clauses.[131]

(i) Enforceability Test

Section 55(1)[132] provides that a promisor who accepts 'valuable consideration' from the promisee to provide benefit to the beneficiary owes a duty to the beneficiary to perform his promise upon the beneficiary's acceptance. The requirement of 'valuable consideration' to be provided by the promisee may be inconsistent with the general principles of contract law where judges are willing to accept nominal benefit or detriment as sufficient consideration. In these situations, even if the contract is intended to benefit the third party, s.55(1) may not apply as no 'valuable consideration' moves from the promisee. The possible danger of this

[128] This reform is recommended by the Queensland Law Reform Commission through the Report on a Property Law Bill, QLRC 16. The statutory reform undertaken in Northern Territory through the enactment of s.56 Law of Property Act 2000 (hereinafter referred to as 'LPA 2000 (NT)') is largely similar to the reform taken in Queensland. As such, there will be no discussion on the position in Northern Territory unless it is necessary to do so.

[129] Section 55(6)(c). On the contrary, in Northern Territory, the statutory reform is limited to promises in writing only; s.56(6) LPA 2000 (NT). Arguably, this is too restrictive as there are contracts made for the benefit of third parties which are not in writing or partly in writing and partly orally made.

[130] Section 55(3)(b). The promisor is entitled to remedies if the beneficiary fails to fulfill the conditions stipulated in the promise; s.55(3)(c). The equivalent in Northern Territory are s.56(3)(b) and (c) LPA 2000 (NT).

[131] Section 55(1) only provides for a promise "to do or refrain from doing an act or acts for the benefit of the third party". A liberal construction of this section should be adopted so that enforcement of exclusion and limitation clauses is covered.

[132] Section 55(1) provides that:

> A promisor who, for valuable consideration moving from the promisee, promises to do or 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.

requirement is that not all contracts made for the benefit of the third party will be covered by s.55(1).

The beneficiary does not need to be in existence at the time the promise is created.[133] He only needs to be identified and in existence at the time of the acceptance of the promise. Rogers suggested that the courts will look at surrounding circumstances in determining the persons who are intended to benefit from the promise.[134]

Section 55(1) adopts a dual intention test in determining whether the beneficiary is entitled to enforce the promise. It requires the beneficiary to show that (i) there is a term stating that the promise is made for his benefit and (ii) the 'promise creates or **appears to** be intended to create a duty enforceable by a beneficiary' (emphasis added).[135] As such, the enforceability test can be satisfied either based on a subjective or objective standard in determining the contracting parties' intention.

The enforceability test in s.55(1) poses a number of difficulties. It is not clear as to how the third party is going to prove such intention. Particularly, it is debatable whether the courts can assess the surrounding circumstances in determining the contracting parties' intention. Wilson[136] opines that judges should be limited to the four corners of the contract in determining this matter. In the absence of an express statement stating the third party can sue, the courts would have to infer such intention from the contract. It is submitted that there is nothing in s.55 which prohibits the courts from looking at the surrounding

[133] Section 55(6)(b). The equivalent in Northern Territory is s.56(6) LPA 2001 (NT).
[134] Rogers in Finn, at 97.
[135] Section 55(6)(c)(ii).
[136] Wilson, L., "Contract and Benefits for Third Parties" (1987) 11 *Syd L Rev* 230-258, at 253.

circumstances in resolving any dispute concerning the application of s.55. To ensure that the contracting parties' intention is given effect too and a just result is achieved, judges should look at the surrounding circumstances at the time the promise is created.[137]

A beneficiary's entitlement to sue only arises if he has accepted the promise.[138] The principles in relation to the requirement of acceptance under s.55(1) is largely similar to the crystallisation test found in s.2(1)(a) 1999 Act (E&W). However, unlike the 1999 Act (E&W), s.55(6)(a) expressly requires communication to be made within the time stated in the promise. In the absence of such term, acceptance must be made within a reasonable time.[139] It may be difficult for the beneficiary to decide what amounts to reasonable time. In this situation, the beneficiary is advised to notify the promisor as soon as he learns about the promise.[140] If there is a term in the contract stipulating the duration in which acceptance must be communicated to the promisor, it may be disadvantageous to a beneficiary who does not know about the existence of this term. He may miss the opportunity to inform the promisor of his acceptance. There is no duty on the part of the contracting parties to inform the beneficiary of the existence of such term.

---

[137] Considerations that can be taken into account include the relationship between the promisee and the third party, any statement made by the promisee or promisor to the third party after the contract is entered into.

[138] Section 55(6)(a) provides that:

> "acceptance" means an assent by word or conduct communicated by or on behalf of the beneficiary to the promisor, or to some person authorised on his behalf, in the manner (if any), and within the time, specified in the promise or, if no time is specified within a reasonable time of the promise coming to the notice of the beneficiary.

The equivalent in Northern Territory is s.56(6) LPA 2000 (NT).

[139] In *Re Davies* [1989] 1 Qd R 48, the third party failed to invoke the application of s.55 as it did not accept the benefit within reasonable time. In *Hyatt Australia Limited* v *LTCB Australia Limited* [1996] 1 Qd R 260, it was held by the Court of Appeal that reasonable time will start to run against the third party the moment he is aware of the benefit intended for him in the contract.

[140] By contrast, the 1999 Act (E&W) does not place any time limit on the communication of acceptance by the third party.

Since communication can be addressed to the promisor's agent, it is advantageous to the beneficiary if the promisee is regarded as the promisor's agent. Any notice of acceptance given by the beneficiary to the promisee will be sufficient to bind the promisor. However, courts may not agree with this approach unless there are facts to support the finding that the promisee is acting as the promisor's agent in the latter's dealing with the beneficiary. This is to prevent any dilution of the legal principles in relation to creation of agency.

McPherson JA in *Hyatt Australia Limited* v *LTCB Australia Limited,*[141] a decision of the Queensland Court of Appeal, observed that it may be possible for the beneficiary to give 'anticipatory acceptance' of the benefit in a contract which he knows is going to be created in his favour. McPherson JA stated that allowing 'anticipatory acceptance' will not be problematic. If the contracting parties no longer wish to benefit the beneficiary, they can refrain from creating the contract as the beneficiary is only equipped with enforcement rights if the contract is created. It is submitted that it is not advisable to allow for 'anticipatory acceptance' as such allowance is inconsistent with the reading of s.55(1) which arguably, presupposes a contract to be created before any acceptance is given by the beneficiary.[142] If 'anticipatory acceptance' is allowed, the contracting parties will lose the right to vary or rescind the contract once it is created. It is unlikely that the contracting parties to intend to lose their rights to rescind or vary the contract so easily. Additional

[141] At 264 (*Hyatt*). This observation was agreed by the remaining judges in *Hyatt* and by the Supreme Court of Queensland in *Cousins Securities Pty Ltd* v *CEC Group Limited* [2006] QSC 30**7.** In *Hyatt,* the third party applied an interlocutory injunction by arguing that its right to do so arising from a contract made for its benefit. The Court of Appeal held in favour of the third party.

[142] By contrast, McPherson JA, in *Hyatt* at 264, opined that the use of the word 'acceptance' in s.55(1) did not necessarily exclude 'anticipatory acceptance'.

uncertainties are created as questions will arise as to when 'anticipatory acceptance' can be invoked successfully by the beneficiary.[143]

Section 55 received judicial discussion in *Harris* v *Northern Sandblasting*.[144] This case shows judicial divergence on the scope and application of s.55. In *Harris*, a nine year old girl (the respondent) was seriously injured in the premises rented by her parents due to the negligence of the landlord's (appellant) electrical contractor. In the Queensland Court of Appeal, McPherson JA stated that there was a common law warranty owed by the landlord that the premises let were fit for human habitation. However, since the respondent was not a party to the tenancy agreement, she had to rely on s.55 to enforce the warranty. The learned judge opined that:

> **It is perhaps not quite impossible to force the common law warranty implied in the case of a furnished letting into a form which would fit s.55(3)(b) of that Act.** The difficulty is, however, that acceptance by the beneficiary is a prerequisite to the acquisition and enforcement by a third party of rights under that provision; and, although "acceptance" is defined widely in s.55(6)(a), **there is here naturally no evidence that the nine year old plaintiff ever knew of or accepted any promise comprised in the implied warranty, or that she ever authorised her parents to accept it on her behalf.** (emphasis added)[145]

Accordingly, the respondent's claim on s.55 failed as it could not be proven that she had accepted the benefit of the tenancy agreement.

---

[143] Questions may arise concerning the duration where the 'anticipatory acceptance' can be given before the contract is created and whether 'anticipatory acceptance' is effective if the contract created differs in some aspects from the original agreement that the beneficiary has in mind at the time of acceptance.
[144] [1995] QCA 413. The High Court decision was reported as *Northern Sandblasting Pty Ltd* v *Harris* [1997] 146 ALR 572. The respondent succeeded in her claim by relying on the law of tort.
[145] At 8-9 according to the pagination provided by Supreme Court of Queensland Library.

In the High Court, Brennan CJ[146] stated that the duty owed by the landlord to the tenant is found in the Property Law Act 1974 and the Residential Tenancies Act 1975. This duty is contractual in nature. The respondent could not enforce this duty as she was not a tenant under the tenancy agreement. Brennan CJ rejected the respondent's claim that s.55 applied to this case. The learned judge held that s.55 requires the promisor to do an act to benefit the beneficiary and the latter's identity must be ascertainable from the contract. Clearly, the respondent could not fulfill these requirements as no reference was made about her in the tenancy agreement. Similarly, Gummow J rejected the argument on s.55 as the tenancy agreement did not fall within the purview of this section.[147] By contrast, Kirby J, whom Gaudron J[148] agreed with, held that s.55 was applicable in this case. Kirby J went further than McPherson JA in the Court of Appeal in applying s.55. The learned judge held that:

> But where, as here, the tenancy agreement between the appellant and the respondent's parents as tenants **was obviously for her benefit**, the purpose of s 55 of the Property Law Act extended to securing to her the entitlement to enforce the duties owed by the landlord to her parents as tenants. All that was required was her "acceptance" of her status as a beneficiary. **By the Property Law Act, she could do this by "conduct" communicated to the landlord. The landlord knew that she had entered into possession of the demised premises with her parents.** By s 55 of the Property Law Act, the difficulties of her enforcement of the obligations owed by the landlord to her parents as tenants were therefore overcome. (emphasis added)[149]

There are two approaches that can be discerned from *Harris*. Brennan CJ and Gummow J were clearly of the view that s.55 applies to situations where the benefit is expressly provided in the contract for the third party. The other approach by Kirby J, Gaudron J and McPherson JA holds that the promise to benefit the third party under s.55 can be implied.

---

[146] At 579 (*Harris*-High Court).
[147] At 621 (*Harris*-High Court).
[148] At 606 (*Harris*-High Court).
[149] At 644-645 (*Harris*-High Court). Dawson J and Toohey J agreed with Gummov J's judgment on this matter at 590 and 593 (*Harris*-High Court) respectively.

The scope of acceptance was also expanded by Kirby J in *Harris.* Acceptance is allowed as long as the promisor is aware that the third party is enjoying the benefit. It was not necessary for the beneficiary to be aware that he is accepting the benefit. With due respect, the decision of McPherson JA in relation to the interpretation on the requirement of acceptance is more in line with the definition of 'acceptance' in s.55(6)(a).

Speedy Gantry Hire Pty Ltd v *Preston Erection Pty Ltd*[150] is another case which illustrates that the court give a liberal interpretation to s.55. It must be noted that s.55 was discussed by Emmett J in this case as an alternative to his main reasoning of his judgment. In this case, Speedy Gantry (SG) alleged that a promise was made between the inventor of a patent (Nielson) and Richards. In return of Richard's waiver of the fees for the engineering services that he provided to Nielson in inventing a patent, Nielson promised to transfer the ownership of the invention to a company formed by them (SG, the beneficiary) via an assignment of the patent. The promise was alleged to be made in a discussion between Nielson and Richards prior to the incorporation of SG. The issue which was relevant for discussion here was whether SG could rely on s.55 to claim the benefit of the promise. The problem faced by SG was that there was no evidence to support its contention that an express promise to transfer the ownership of the patent to it had been created.

Emmett J viewed that s.55 can be satisfied by an 'implied promise'.[151] On the facts, the learned judge found that there was a valid contract between Neilson and Richard as to the formation of the company to exploit the patent, their contribution to the company and the benefits that they enjoyed from the company. Accordingly, a term to the effect that Neilson

[150] 40 IPR 543 obtained from *Lexis.com Research System*.
[151] At 12 (*Speedy*), according to the pagination provided by *Lexis.com Research System.*

promised to transfer the ownership of the patent to SG was implied as it was necessary to give business efficacy to the contract.

It is submitted that the division of opinion by Australian judges in relation to the scope of s.55 is due to the fact that the section is not very clear as to whether it can apply to an implied promise.

(ii) Rescission or Variation of Beneficiary's Right

Section 55(2)[152] states that the contracting parties can vary or discharge the promise without obtaining the beneficiary's consent. However, once the beneficiary accepts the promise, any variation or revocation of the promise can only be made if the contracting parties and the beneficiary consent to such a change.[153]

(iii) Defences and Set-Off

Section 55(4)[154] provides that the promisor is entitled to rely on the defences and any matter which will render the promise to be void, voidable or unenforceable if the promisee is the one bringing the legal action.

[152] The equivalent in Northern Territory is s.56(2) LPA 2000 (NT).
[153] Section 55(3)(d). The equivalent in Northern Territory is s.56(3)(d) LPA 2000 (NT).
[154] The equivalent in Northern Territory is s.56(4) LPA 2000 (NT).

(iv) Miscellaneous

The beneficiary is entitled to remedies such as damages, injunction and specific performance in enforcing the promise.[155] Section 55(7)[156] expressly preserves the rights of the beneficiary arising from other principles of the law.

D. Principles of European Contract Law

The Principles of European Contract Law (hereinafter referred to as 'PECL')[157] contains a body of rules relating to formation of contract, performance and non-performance of contract, remedies for breach of contract, authority of agent and other rules representing the contract law of the European Union. It was introduced in stages. Part I and II was introduced in 1995 and Part III was introduced in1999. According to Art 1:101(2), PECL applies when the contracting parties have incorporated it into their contract. Art 1:106(1) states that the PECL should be interpreted and developed in accordance with its purposes. The considerations to be taken into account include 'the need to promote good faith and fair dealing, certainty in contractual relationship and uniformity of application'.[158]

Art 6:110(1)[159] allows a third party to enforce a contract made for his benefit. Art 6:110 does not clearly state whether it applies to written contracts only[160] and whether it applies

[155] Section 55(3)(a). The equivalent in Northern Territory is s.56(3)(a) LPA 2000 (NT).
[156] The equivalent in Northern Territory is s.56(7) LPA 2000 (NT).
[157] The PECL was drawn up by an independent body of experts from each of the member states of the European Union in a project organised by the European Commission.
[158] Art 1:106(1).
[159] Art 6:110(1) provides that:

> A third party may require performance of a contractual obligation when its right to do so has been expressly agreed upon between the promisor and the promisee, or when such agreement is to be

to enforcement of exclusion and limitation clauses. A literal reading of Art 6:110 suggests that it does not apply to exclusion or limitation clauses.[161] Art 6:110 also does not state whether the third party is bound by the terms and conditions of the contract attaching to the benefit. However, in light of the guidance provided in Art 1:106(1), arguably, the PECL should be interpreted liberally to give effect to the purpose behind Art 6:110 that is to avoid additional transactions in achieving the contracting parties' intention.[162] Thus, it can be contended that Art 6:110 covers enforcement of exclusion and limitation clauses. Art 1:102(2)[163] allows contracting parties to expressly exclude or vary the legal effects of Art 6:110.

1. Enforceability Test

The enforceability test in Art 6:110(1) requires the existence of an agreement that the third party can demand the performance of the contract intended for him. This agreement can be created expressly or inferred from surrounding circumstances at the time the contract is created. There are two instances which trigger the operation of the enforceability test. Firstly, the test is satisfied if the contract is such that the promisor promises to perform the obligation to the third party on demand by the latter.[164] Secondly, the test is satisfied if the

---

inferred from the purpose of the contract or the circumstances of the case. The third party need not be identified at the time the agreement is concluded.

[160] Arguably, the PECL is only expected to deal with written contracts. Most contracts involved will be commercial contracts which are usually in writing.

[161] Lando does not discuss the application of this Article to exclusion or limitation clauses in Ole and Hugh Beale, eds., *Principles of European Contract Law Part I & II*, (Kluwer Law International, Netherlands, 2000) (hereinafter referred to as 'Lando')

[162] Lando, at 318.

[163] To protect the contracting parties' freedom of contract, Art 1:102(2) allows them to exclude the application of any of the Articles of PECL or to vary and modify the effect of the rules unless expressly prohibited by PECL.

[164] Illust. 1 provided in Lando, at 319 which states: "P opens a bank account in his own name and pays regularly € 800 per month to the account. The bank promises to pay this sum to P's son B on B's demand. B may claim performance."

third party is the person who knows when to make the claim specified in the contract and the amount to be claimed from the promisor.[165]

Art 6:110(1) states that the third party does not need to be identified at the time the contract is created. The exact identity of the third party may be made known or determined after the contract is created. Arguably, Art 6:110(1) allows situations where the contracting parties are not decided as to which third party they wish to benefit and reserve the right to designate the person who is entitled to receive the benefit later. However, Art 6:110 does not mention that the third party must be in existence at the time the contract is created. It is submitted that a broad interpretation of the PECL would waive such requirement.

2. Rescission or Variation of Third Party's Right

Art 6.110(3) provides that the promisee can unilaterally deprive the third party from his benefit by notifying the promisor.[166] On the contrary, arguably, if the promisor intends to do the same, this must be done with the promisee's consent.

The promisee's right to revoke the benefit is lost in two situations. Firstly, Art 6:110(3)(a) states that the promisee cannot revoke the benefit if he has informed the third party that the benefit has been made irrevocable. At first sight, it may be questionable as to how often the promisee will make such statement to the third party. As such, this crystallisation test may not be useful to the third party. However, Lando has given a liberal interpretation to Art

[165] Illust. 2 provided in Lando, at 319 which states: "The landlord L gives P permission to erect high voltage lines over a quarry which is worked by T, his tenant. P promised L to pay an indemnity for damage done to T's property. T has direct claim against P when damage is done."

[166] This is different from the general rule that the contract made can only be altered or revoked with the mutual consent of both the contracting parties.

6:110(3)(a). According to Lando, Art 6:110(3)(a) applies if the promisee informs the third party that the promisor has promised to perform the obligation in favour of the third party or that the latter can now demand performance from the promisor.[167] Secondly, the third party's right crystallises if he communicates his acceptance either to the promisor or promisee. The third party's acceptance of the benefit will only be valid if he is informed of the benefit by the promisee or the promisor.[168]

The third party's acceptance can be implied through his conduct in relying on the promise as long as he makes known this fact to the promisor or promisee.[169] He does not need to expressly state that he accepts the benefit. The rule that communication of acceptance can be made to either of the contracting parties is beneficial to the third party. It is easier for his rights under the contract to crystallise as it is most likely that he keeps in touch with either one of the contracting parties.

3. Defences and Set-Off

There are no specific provisions governing defences and set-off in relation to contracts made for the benefit of third parties.

[167] At 321 (Lando).
[168] At 320 (Lando).
[169] Illust. 8, as provided in Lando, at 321.

4. Miscellaneous

The third party can renounce the benefit intended for his enjoyment. If he does so, he will be treated as if he is not entitled to the right from the very beginning.[170] The promisee is equally entitled to enforce the contract.[171] The promisor is taken to have duly performed his obligation under the contract by rendering the performance to the third party.[172]

E. United States

The courts in the United States recognised the ability of contracting parties to create enforceable rights in favour of third parties beginning with *Lawrence* v *Fox*.[173] Originally, this third party beneficiary rule was not universally accepted in all the states. Acceptance of this rule gradually occured with the adoption of the Restatement of Contracts introduced by the American Law Institute which makes provisions for the entitlement of third parties to enforce a contract. The third party beneficiary rule is currently governed by s.302 to s.315 of the Restatement (Second) of Contracts 1981 (hereinafter referred to as 'Restatement').[174] Under the Restatement, the third party to a contract is known as the beneficiary.[175] Only intended beneficiaries are entitled to rights under the contract made. Incidental beneficiaries are not allowed to enforce the contracts.[176] The Restatement allows contracts made for the

[170] Art 6.110(2). The rules relating to giving of notice are found in Art 1:303. According to Art 1:303(1), notice can be given by any means, writing or otherwise. It is only effective when it reaches the addressee; Art 1:303(2).
[171] Lando, at 319.
[172] Lando, at 319.
[173] 20 N.Y. 268 (New York Court of Appeals).
[174] This replaces s.133 Restatement (First) of Contracts 1932. The United States Restatement is not a statute. It is an influential but non-binding statement of the law.
[175] This is defined in s.2 as referring to a person other than the promisee who will be benefited by the performance of the contract.
[176] Section 315.

benefit of third parties to be expressly or orally made.[177] The Restatement covers enforcement of exclusion and limitation clauses by the beneficiary.[178] The beneficiary may be bound by the conditions or terms attaching to the benefit.[179]

1. Enforceability Test

The enforceability test to differentiate between intended and incidental beneficiaries is found in s.302.[180] If the enforceability test is satisfied, the promisor owes a duty to the beneficiary to perform the promise.[181] Section 302(1) clearly states that the parties to the contract have the freedom to decide whether the beneficiary is allowed to enforce their contract. They can expressly agree to include or exclude the beneficiary's right to sue the promisor for breach of duty to perform the contract. If no indication is provided on this matter, in accordance to s.302(1), the beneficiary is able to enforce the contract if he can satisfy the 'intent to benefit test', a two-stage test.

Firstly, the beneficiary must prove that by giving him the right to sue gives effect to the contracting parties' intention. Secondly, he must prove that he falls within subsection

---

[177] This is so as Illust. 1 to s.2 which explains the meaning of a promise gives an example of an oral promise.
[178] *Carle & Montanari, Inc.* v *American Export Isbrandtsen*, Inc 275 F. Supp. 76; 1967 U.S. Dist. LEXIS 9078.
[179] Comment *c* to s.309. If the beneficiary accepts the benefit subject to terms and conditions attaching to the benefit, he will be bound. See also s.309(4).
[180] Section 302 provides that:

> (1) Unless otherwise agreed between promisor and promisee, a beneficiary of a promise is an intended beneficiary if recognition of a right to performance in the beneficiary is appropriate to effectuate the intention of the parties and either
>
> (a) the performance of the promise will satisfy an obligation of the promisee to pay money to the beneficiary; or
>
> (b) the circumstances indicate that the promisee intends to give the beneficiary the benefit of the promised performance.
>
> (2) An incidental beneficiary is a beneficiary who is not an intended beneficiary.

[181] Section 304. In relation to contracts with a government or governmental agency, in determining whether the beneficiary is entitled to enforce the contract, further requirements as found in s.313 have to be satisfied.

s.302(1)(a) or (1)(b). This depends on the beneficiary's position, whether he is a creditor beneficiary[182] or a donee beneficiary.[183] This distinction between creditors and donees in the Restatement (First) of Contracts 1932 is maintained partly in the Restatement (Second) of Contracts.

To satisfy the enforceability test, there must be a clear and definite intention of the contracting parties to benefit the beneficiary. It is not necessary to prove that they intend the beneficiary to be able to enforce the contract.[184] The intention to benefit the beneficiary does not have to be expressly stated in the contract. It can be implied from the other terms of the contract or the surrounding circumstances at the time the contract is created.[185] The courts use an objective test in determining the contracting parties' intention.

A number of academics have written on the interpretive problems created by s.302.[186] Firstly, s.302 does not provide much guidance as to how the 'intent to benefit test' is proven. A point by Eisenberg is as follows:

---

[182] The creditor beneficiary will fall under subsection (1)(a). *Tilva L. Souza v Westlands Water District*, 135 Cal. App. 4th 879 defined creditor beneficiary as 'a party to whom a promisee owes a pre-existing duty which the promisee intends to discharge by means of a promisor's performance.' at 894. The decision of *Kmart Corporation* v *Balfour Beatty, Inc* 994 F. Supp. 634; 1998 U.S. Dist. LEXIS 1840, at 893 showed that it is easier to prove an intention to benefit the beneficiary in situations involving promises to pay the debts of the promisee.

[183] The donee beneficiary will fall under subsection (1)(b). This was defined in *Tilva L.Souza,* at 893 as 'a party to whom a promisee intends to make a gift'.

[184] *Schuerman* v *United States* 30 Fed. Cl. 420 and *Montana* v *United States* 124F.3d 1269 (Fed. Cir. 1997).

[185] *Guy* v *Liederbach* 459 A.2d 744 (1983); *Limbach Company* v *City of Philadelphia* 905 A.2d 567; *Mary K. Sullivan* v *Grass Catcher, Inc* 1999 Me. Upper. LEXIS 311; *Elmet Technologies, Inc* v *Advanced Technologies Systems, Inc* 2007 U.S. Dist. LEXIS 349; *Cordero Mining Company* v *United States Fidelity and Guarantee Insurance Company* 2003 WY 48; 67 P.3d 616; *Scarpitti* v *Weborg* 530 Pa. 366; 609 A.2d 147; *Stacy L. Burks* v *Federal Insurance Company* 2005 PA Super 297; 883 A.2d 1086.

[186] Summers, David M., "Third Party Beneficiaries and the Restatement (Second) of Contracts" (1982) 67 *Corn LR* 880–899; Prince, Harry G., "Perfecting the Third Party Beneficiary Standing Rule Under Section 302 of the Restatement (Second) of Contracts" (1984) 25 *Bost CLR* 919-997; Eisenberg, Melvin A., "Third-Parties Beneficiaries" (1992) 92 *Col LR* 1358–1430; Paglin, Orna S., "Criteria for Recognition of Third Party Beneficiaries' Rights" (1989) 24 *New Eng L Rev;*. 63-113 Powers, Jean Fleming, "Expanded Liability and the Intent Requirement in Third Party Beneficiary Contracts" (1993) *Utah L Rev* 67-147 and Curry, Jason, "No Appropriate Beneficiary Left Behind: How to Refine Texas Third Party Beneficiary Law to Include All Appropriate Intended Beneficiaries" (2007) 40 *Tex Tech L Rev* 183-224.

> How is it to be determined, as an objective matter why in some contracts whose performance will benefit a third party, the benefit is objectively "intended" within the meaning of the test, while other contracts whose performance will benefit a third party, the benefit is not so "intended"?[187]

The cases decided on s.302 shows that more than one approach is taken in determining the entitlement of a beneficiary to enforce the contract.[188] The lack of guideline in s.302 also gives rise to the need of judges to add further requirements to the enforceability test.[189]

Secondly, the wording of s.302 leads to confusion as to whose intention should be paramount in deciding whether the beneficiary should be given the right to enforce the contract. The first requirement as stated in the introductory clause of s.302 indicates that the intention of both parties to the contract is to be assessed but s.302(1)(b) only focuses on the promisee's intention to benefit the beneficiary.[190] Section 302(1)(b) can be justified on the basis that it is usually the promisee who intends to benefit the beneficiary. The promisor is usually a stranger to the beneficiary who is requested by the promisee in return of consideration to provide the benefit to the beneficiary.

---

[187] (1992) 92 *Col LR* 1358–1430, at 1379. Although the quotation is found in the discussion of the problems related to s.133 Restatement (First) of Contracts but Eisenberg, at 1383 argues that similar problems exist in relation to s.302.

[188] Some judges adopt a stricter test while some adopt a more liberal test in applying s.302. For example, there are cases which require the intention to benefit the third party to be expressly stated in the contract; *Sheldon Whitehouse* v *New England Ecological Development, Inc* 1999 R.I. Super. LEXIS 154; *Rhode Island Department of Corrections* v *ADP Marshall, Inc* 2004 R.I. Super. LEXIS 66 and *Fen X. Chen* v *Sreet Beat Sportswear, Inc* 226 F. Supp. 2d 355. On the contrary, some cases allowed for such intention to be implied. See n 185. In fact, in *Beckman Cotton Company* v *First National Bank of Atlanta* 666 F.2d 181, the third party was entitled to enforce the letter of credit despite the fact that he was not referred to in the contract.

[189] Some of the considerations that the courts take into account include whether performance of the contract amount to a direct benefit to the third party (*Manor* v *United States* 2003 331 F.3d 891; *Castle* v *United States* 2002 301 F.3d 1328 and *Glass* v *United States* 258 F.3d 1349. In *Glass*, at 1354, the United States Court of Appeals for the Federal Circuit held that their previous decision in *Montana* v *United States*, at 1354, is consistent with this requirement. In addition, the purposes and motives of the contracting parties in entering the contract will also be considered; *Cordero Mining Company* v *United States Fidelity and Guarantee Insurance Company*.

[190] Most of the cases require both the contracting parties to intend to benefit the third party such as *Cordero* and *Wakefield* v *Santa Clara County Sheriff's Department* 2004 Cal. App. Unpub. LEXIS 4509.

The difference between the introductory clause and s.302(1)(b) can be reconciled. For the promisee, it must be shown that he intends to benefit the beneficiary. By contrast, for the promisor, it is only required to prove that he realises that the promisee intends to benefit the third party and assents to this fact.[191] The promisor's assent assimilates with the promisee's intention to become the contracting parties' intention to benefit the beneficiary.

Besides, s.302(1)(b) appears to be redundant[192] as it overlaps with the requirement in the introductory clause. If it can be proven that both the contracting parties intend to benefit the beneficiary (required by introductory clause), this must mean that the promisee intends to benefit the beneficiary. Accordingly, the second requirement under s.302(1)(b) is also satisfied.

It is also submitted that the different treatment given to creditors and donees under s.302 is unnecessary.[193] Be it contracts to benefit creditors or donees, the underlying basis of allowing the beneficiary to enforce the contract is the same that is to give effect to the contracting parties' intention. Thus, a similar enforceability test can be used for contracts benefiting creditors or donee.

The third interpretive difficulty stems from Comment *d* to s.302 which provides that the beneficiary is an intended beneficiary if he "would be reasonable in relying on the promise as manifesting an intention to confer a right on him". Actual reliance is not necessary due

[191] This is the approach adopted in *Kmart Corporation* v *Balfour Beatty, Inc* and by Summers (1982) 67 *Corn LR* 880–899, at 897. Prince, (1984) 25 *Bost CLR* 919-997, at 981 opines that the promisor's intention to benefit the beneficiary is proven if the promisor is aware of the promisee's intention.

[192] Summers, (1982) 67 *Corn LR* 880-899, at 897.

[193] At present, the enforceability test involving creditor and donee beneficiaries is slightly different as mentioned earlier. For creditor beneficiaries, s.302(1)(a) requires that performance of the promise to benefit a beneficiary is to satisfy an obligation to pay money owed by the promisee to the beneficiary. This is different from s.302(1)(b) which only requires the promisee to intend to benefit the beneficiary.

to the phrase 'would be reasonable'. Section 302 does not provide guidance on the application of Comment *d*. Uncertainty arises as to whether Comment *d* must be satisfied in all situations or it is an alternative test that judges can rely on if they think fit to do so.[194]

The existence of the reliance test may overtake the function of the 'intent to benefit test'. At first sight, these two tests seem different. Yet, the importance of Comment *d* can be played down by adopting the principle that reliance would only be reasonable if the beneficiary should be allowed to enforce the contract.[195] Whether he is allowed to enforce the contract will depend on the contracting parties' intention to be determined according to s.302(1). Seen in this light, Comment *d* can assimilate itself into the two-stage test of s.302(1). Despite such reconciliation, the existence of Comment *d* adds unnecessary complexities to the application of s.302.

For a beneficiary to fall under s.302(1), it is not necessary for him to be identified at the time the contract is made[196] as long as the contract provides sufficiently clear guidance on the determination of the beneficiary's identity when the time for performance of the contract arrives.[197] Nonetheless, the Restatement is silent as to whether the beneficiary must be in existence at the time the contract is created. A liberal interpretation of the Restatement would have waived this requirement.

---

[194] In *Montana* v *United States*, it was held that one method to ascertain the intention to benefit the third party is to rely on the reliance test provided in Comment *d*. However, in *Cordero Mining Company* v *United States Fidelity and Guarantee Insurance Company*, at 622, the Supreme Court of Wyoming held that the focus of s.302 is the intention of the contracting parties rather than reliance by the beneficiary.

[195] Eisenberg, (1992) 92 *Col LR* 1358-1430, at 1384. Wilson (1987) 11 *Syd. Law Review* 230–258, at 249-250, also opines that the decisive factor in applying Comment *d* is still the intention of the contracting parties.

[196] Section 308.

[197] This means that the beneficiary is entitled to protection if he falls within the class clearly intended by the contracting parties to receive the benefit; *Commercial Insurance Company of Newark, New Jersey* v *Pacific-Peru Construction Corp*, 558 F.2d 948; *Montana* v *United States*, 124F.3d 1269 (Fed. Cir. 1997) and *Fireman's Fund Insurance Company* v *Allen Grass*, 1997 U.S. Dist. LEXIS 7518.

2. Rescission or Variation of Beneficiary's Right

According to s.311(1), the contracting parties can agree to exclude their power to discharge or vary the duty owed to the beneficiary. A term of contract to this effect can be expressly or impliedly provided in the contract.[198] As a consequence, any subsequent discharge or variation of the duty to the beneficiary is ineffective. Section 311(1) does not state clearly whether the contracting parties can discharge a term stating that the duty to the beneficiary is irrevocable. Arguably, they should be entitled to do so before the beneficiary's right crystallises according to s.311(3).[199]

If the contract does not limit the contracting parties' power to discharge or vary the duty, it can be so discharged or varied by their subsequent agreement.[200] The power to discharge or vary the duty is terminated if one of the three events (crystallisation tests) stipulated in s.311(3) occurs before the beneficiary is notified of the modification or discharge. The contracting parties have to inform the beneficiary of their change of intention as soon as possible to prevent the crystallisation of the beneficiary's right after they decide to discharge or vary the duty but before the beneficiary is notified of the variation. However, it is not necessary to inform him if he is not aware that a contract has been made for his benefit.[201]

---

[198] Comment *b* to s.311.

[199] Section 311(3) provides that:

> Such a power [to modify or discharge] terminates when the beneficiary, before he receives notification of the discharge or modification, materially changes his position in justifiable reliance on the promise or brings suit on it or manifests assent to it at the request of the promisor or promisee.

[200] Section 311(2).

[201] This is the interpretation obtained from reading Illust. 6,7 and 8 of s.311.

Section 311 does not state whether the contracting parties can modify or replace the crystallisation test found in s.311(3) or whether they can include a term in their contract allowing them to discharge or vary the beneficiary's duty without his consent.

The three crystallisation tests are as follows:

(a) Material change in beneficiary's position

The beneficiary's right crystallises if there is a material change in his position in justifiable reliance of the promise. Comment *g* to s.311 presumes that an intended beneficiary's reliance is justifiable. This can be rebutted by contrary indication. It does not matter whether the beneficiary learns of the promise to benefit him from the promisee, promisor or any other person. However, no guidance is provided as to what amounts to 'material change' of position.

(b) Beneficiary brings a suit to enforce the promise

The contracting parties lose the power to discharge or modify the duty if the beneficiary has taken steps to enforce the promise.

(c) Beneficiary manifests his assent as requested by promisor or promisee

The assent given by the beneficiary must be given in the manner as stipulated by the promisor or promisee, if any.[202] If there is no request by either the promisor or promisee, any assent by the beneficiary will not crystallise his right. However, it can be contended that the existence of such request can be proven easily due to Illustration 10 to s.311 which provides that:

> B contracts with A to pay C $ 200 which A owes C, and A notifies C of the contract by mail. C mails a letter to A assenting to the contract before receiving notification of a rescission by A and B. The rescission is ineffective against C.

In Illustration 10, the mere notification of the benefit to C is sufficient to amount to a request of assent by A.

Turning back to the discussion of s.311, in the event of an ineffective variation of the duty owed to the beneficiary, s.311(4) allows him to recover any consideration accepted by the promisee in discharge or variation of the duty. At the same time, the beneficiary is also entitled to sue the promisor but the promisor's duty is discharged to the extent of the amount of the consideration paid to the promisee.

[202] Comment *h* to s.311.

3. Defences and Set-Off

Section 309(1) provides that if the contract made to benefit the beneficiary is void or unenforceable, he is not entitled to any rights under the contract. According to s.309(2),[203] the promisor may also rely on the defences which he is entitled to if the claim is brought by the promisee instead of the beneficiary.[204] The promisee's breach of contract which is not connected to the beneficiary's right under the contract does not affect the beneficiary.[205] In such situation, the promisor cannot rely on the promisee's breach of contract to defend himself in a claim brought by the beneficiary. However, the contracting parties can provide in the contract that the duty to the beneficiary is not affected by any breach of contract by the promisee. Accordingly, the beneficiary is entitled to enforce the duty owed to him irrespective of the promisee's breach of contract.

According to s.309(3),[206] the promisor is not allowed to raise any defences which falls outside s.309(1) and (2)[207] against the beneficiary unless the defences are provided in the contract.[208]

---

[203] Section 309(2) provides that:

> If a contract ceases to be binding in whole or in part because of impracticability, public policy, nonoccurrence of a condition, or present or prospective failure of performance, the right of any beneficiary is to that extent discharged or modified.

[204] For example, the promisor can defend his non-performance by stating that the promisee has failed to perform his part of the obligation.

[205] Comment *b* to s.309.

[206] Section 309(3) is subject to s.312 which provides that an erroneous belief of the contracting parties of the duty owed to the intended beneficiary will relieve the promisor from his duty to the beneficiary. The existence of such mistake is determined by the rules of making contracts voidable for mistake.

[207] This restriction includes any defences or counterclaim which a promisee can raise against the third party; Comment *c* to s.309.

[208] Comment *c* to s.309 explains that since "the beneficiary's right is direct, not merely derivative, and claims and defenses of the promisor against the promisee arising out of separate transactions do not affect the beneficiary's right except in accordance with the terms of the contract." This justification behind s.309(3) has been criticised by Eisenberg (1992) 92 *Col LR* 1358-1430 at 1426-1427 on two grounds,. Firstly, the beneficiary's right is derivative of the promisee's rights. Secondly, the promisee's purpose to benefit the beneficiary may be due to contractual dealings with the beneficiary. As such, the promisee may not intend to create an 'unconditional promise' to benefit the beneficiary. This means that the promisee will not intend to benefit the beneficiary if the latter breaches the contract with the promisee, is dishonest or misrepresents crucial facts to the promisee in procuring the contract made for his benefit.

4. Miscellaneous

(i) Remedies

A beneficiary of a gift promise is entitled to all remedies for breach of contract.[209] Remedies of a creditor beneficiary are found in s.310(1) which provides that he can bring a legal action against the promisor or the promisee to recover the debt.

(ii) Promisee's Rights and Avoidance of Double Liability

Section 305(1) provides that the promisor owes a duty to the promisee to perform the contract. The promisee can sue the promisor for any breach of contract.[210] However, the promisee cannot recover damages suffered by the beneficiary. In situations where the promisee suffers nominal damages only, the appropriate remedy to be granted is specific performance.

In order to prevent double liability, Comment *b* to s.305 provides that a single payment by the promisor discharges his liability to the promisee and the beneficiary. However, if both the promisee and the beneficiary's losses do not overlap, then the promisor is liable to both. Furthermore, the court may protect the promisor from double liability by requiring a joinder of the beneficiary and the promisee in a legal action against the promisor.[211]

---

[209] Comment *d* to s.304.
[210] Comment *b* to s.307.
[211] Illust. 4 to s.305 stipulates that:

> A owes C $ 100. For consideration B promises A to pay the debt to C. On B's breach A may obtain a judgment for $ 100 against B. But the court may protect B against double payment by permitting joinder of C, by an order that money collected by A is to be applied to reduce A's debt to C, by giving

(iii) Beneficiary's Disclaimer of Benefit

The beneficiary can disclaim any benefit provided to him in a contract if he has not assented to it within a reasonable time after he learns about it.[212]

IV. Comparative Study of Legal Position in Selected Countries

This part analyses the similarities and the differences between the various statutory reforms discussed in Part III of this chapter on the following aspects:

(a) Principles determining third parties' entitlement to enforce a contract

(b) Rescission and variation of third party's right

(c) Defences and set-off

(d) Miscellaneous

A. Principles Determining Third Party's Entitlement to Enforce a Contract

This part examines the (i) different enforceability tests adopted in different countries, (ii) principles guiding the identification and existence of third parties and (iii) comments on (i) and (ii).

B credit on the judgment for payments to C which reduce A's obligation, or by enjoining enforcement of the judgment to the extent of such payment.

[212] Section 306.

1. Enforceability Test

Despite the fact that different enforceability tests are adopted by the various countries, the basis of the tests is similar that is to respect the contracting parties' intention. Accordingly, each of the countries allows contracting parties to exclude third party rights. The 1999 Act (E&W) provides two tests in determining whether the third party can enforce the contract. The first test requires the contracting parties to expressly state that the third party can enforce the contract.[213] The PECL bears similarity with this test as Article 6.110(1) stipulates that there must be an agreement of the contracting parties allowing the third party to require performance under the contract. However, the PECL differs from the 1999 Act (E&W) in two aspects. Firstly, the scope of PECL is wider as its enforceability test is satisfied as long as the third party is given the right to demand the promisor to perform the contract. It is not necessary to prove the existence of an agreement to allow the third party to enforce the contract. Secondly, the agreement to allow the third party to require performance of the contract can be inferred from surrounding circumstances.

The second test under the 1999 Act (E&W) requires the contract to purport to benefit the third party.[214] If this requirement can be satisfied, a rebuttable presumption that the third party is entitled to enforce the contract is created. This presumption can be rebutted if the promisor can prove that the contracting parties do not intend the third party to enforce the contract. The 1982 Act (NZ) adopts this test as well. The concept of 'rebuttable presumption' is not used in Australia (Western Australia, Queensland and Northern Territory), PECL and the United States.

[213] Section 1(2)(a) 1999 Act (E&W).
[214] Section 1(2)(b) 1999 Act (E&W).

The position in Western Australia seems to represent the strictest enforceability test. According to s.11(2) PLA 1969 (WA), the contract must expressly 'purports to confer a **benefit directly to the third party'** (emphasis added). The words used in s.55(1) PLA 1974 (Qld) are not as strong as it merely states 'for the benefit of a beneficiary' without referring to the requirement that such benefit must be conferred on the beneficiary directly.[215]

The position in Queensland is special as it is the only jurisdiction which requires 'valuable consideration' to move from the promisee to the promisor. Moreover, the duty owed by the promisor only arises upon the beneficiary's acceptance. In relation to other countries, the duty owed to the third party arises the moment the contract is created.

The enforceability test adopted in the United States is also unique as it divides the category of third parties into two groups, namely, creditor beneficiary and donee beneficiary and uses concepts such as intended beneficiaries and incidental beneficiaries. The position in the United States represents the most liberal enforceability test. The 'intent to benefit' test used does not require the contracting parties to intend the third party to enforce the contract. Hence, it is not surprising that the third party beneficiary rule in the United States has been applied in situations which fall within the traditional boundary of the law of tort.[216] In addition, there is no requirement that the courts in determining this issue are bound by the four corners of the contract. The courts are entitled to look at surrounding circumstances to

[215] It must be noted that in Queensland, it must be shown that it appears that the promise is intended to be enforceable by the third party; s.55(6)(c)(ii) PLA 1974 (Qld).

[216] In *Guy* v *Liederbach* 459 A.2d 744 (1983), the Pennsylvania Supreme Court allowed a named beneficiary under a will to sue the attorney who was alleged to have failed to properly draft the will. By contrast, as seen above in England and New Zealand, a similar claim of a beneficiary under a will falls outside the scope of statutory reform of the doctrine of privity. Furthermore, in the United States, the third party beneficiary principle has been utilised as a vehicle in welfare law for individuals to enforce contracts made by the government to benefit the society.

determine the contracting parties' intention. There are cases where the third party was held to be entitled to enforce the contract even though the contract made no reference about him.

Besides the position in the United States, the PECL, arguably the 1982 Act (NZ) and the PLA 1974 (Qld) allow surrounding circumstances to be taken into account in determining the contracting parties' intention to benefit a third party. A term benefiting third party can be implied. By contrast, in England and Western Australia, it must be expressly stated in the contract that the benefit must be intended for the third party. The courts are not entitled to imply terms from the surrounding circumstances.

2. Identification and Existence of Third Party

The 1999 Act (E&W) which is identical to the 1982 Act (NZ) on this matter provides the clearest principles. The third party must be expressly identified either by name, as a member of a class or as answering a particular description provided in the contract. The third party does not need to be in existence at the time the contract is created.[217] The position is similar in Queensland and arguably, United States. The PECL is silent on this matter. In Western Australia, the words used in s.11(2) seems to require the third party to be in existence at the time the contract is created.

3. Comment

Overall, the enforceability test in the 1999 Act (E&W) is the best test. If the contracting parties expressly allow the third party to enforce the contract, the third party's rights are

[217] Section 1(3) 1999Act (E&W).

guaranteed unlike the position in the 1982 Act (NZ) where a rebuttable presumption is raised. It is redundant to raise a rebuttable presumption in this situation. The presumption will not be rebutted since the contracting parties' intention is shown clearly through the term allowing the third party to sue.

In other situations where it is not very clear as to whether the contracting parties intend the third party to enforce the contract, it is better to utilise the concept of rebuttable presumption. This strikes a proper balance between the rights of the contracting parties and the third party. The presumption relieves the third party of the burden to prove that the contracting parties intend to allow him to sue. At the same time, the presumption allows the contracting parties, namely the promisor an opportunity to prove that the they do not intend to create any third party rights.

Judges should be allowed to take into account the relevant surrounding circumstances at the time the contract is created in deciding the contracting parties' intention in situations where there is ambiguity in the terms of the contract.[218] Reform of the privity doctrine should not extend to implied terms that the contract purports to benefit the third party. There may be a risk that such implied terms are inconsistent with the contracting parties' intention. Since reform is the exception rather than the general rule, it is reasonable to adopt a more cautious approach. In addition, the provisions in the 1999 Act (E&W) in relation to the enforceability test and identification of the third parties are clearer, sufficiently detailed and more straightforward compared to the other statutory reforms especially the Restatement and the PLA 1969 (WA).

[218] This should be done in accordance with the general principles of construction of contract.

B. Rescission and Variation of Third Party's Right

The discussion on the rescission and variation of a third party right's will be made in relation to the five matters below:

(i) Power to grant an irrevocable right to third party

(ii) Various crystallisation tests

(iii) Exclusion, replacement and modification of crystallisation tests

(iv) Judicial intervention entitling contracting parties to vary contract after crystallisation of third party's right without his consent

(v) Comment

1. Power to Grant an Irrevocable Right to Third Party

The 1999 Act (E&W), the Restatement, PLA 1969 (WA) and arguably the PECL allow the contracting parties to include a term in their contract stating that the benefit to the third party is irrevocable.

2. Various Crystallisation Tests

The 1999 Act (E&W), 1982 Act (NZ) and the Restatement provide three crystallisation tests. The PECL has two crystallisation tests while the Australian statutory reforms contain only one crystallisation test. PECL is the only jurisdiction which states that the promisee may by notice to the promisor rescind or alter the third party's right of performance before crystallisation of the latter's rights. The 1982 Act (NZ) expressly allows either the

contracting parties to do so provided this is stated in the contract. The other statutory reforms expressly require mutual consent.[219]

The following are the types of crystallisation tests applicable in the selected countries examined in Part III of this chapter.

(i) Acceptance

In England, the third party's right crystallises if he has communicated his acceptance to the promisor or the latter's agent. Communication of acceptance to the promisee only is insufficient. The only other statutory reform which adopts a similar test is the PLA 1974 (Qld). By contrast, in the PECL, the promisee loses his right to alter or rescind the benefit if either the promisor or himself receives notice of acceptance from the third party. The third party has an option as to whether he wishes to inform the promisee or the promisor. This differs from the 1999 Act (E&W) and PLA 1974 (Qld).

The Restatement provides that the beneficiary's right crystallises where he communicates his assent to the promisee or promisor at the request of either one of them. In order to invoke this crystallisation test, one of the contracting parties must make a request for acceptance to be communicated by the beneficiary to either one of them. There is no such requirement in the 1999 Act (E&W), PLA 1974 (Qld) and PECL.

[219] Merkin, at para 5.77 argues that unilateral revocation is allowed under the 1999 Act (E&W) if this is expressly provided for in the contract.

(ii) Reliance

In the 1999 Act (E&W), the third party's right crystallises if he has relied on the promise to the promisor's knowledge. Alternatively, his right crystallises if the promisor can reasonably expect that he will rely on the promise and such reliance actually occurs. Trivial acts can amount to reliance. The reliance test used in New Zealand and United States differs from the one adopted in England in two aspects. Firstly, the 1982 Act (NZ) and the Restatement do not require the promisor or even the promisee to be aware of the third party's reliance. Secondly, under the 1982 Act (NZ) and the Restatement, the beneficiary must show that there is material change in his position in reliance on the promise. The Restatement has an additional requirement. The beneficiary's reliance must be justifiable. The 1982 Act (NZ) is the only jurisdiction which expressly allows reliance by another person other than the beneficiary.

(iii) Adoption

Only the PLA 1969 (WA) applies adoption as the crystallisation test. Section 11(3) PLA 1969 (WA) provides that the third party's right crystallises if he adopts the promise. Yet, s.11(3) does not provide additional details as to how this test is satisfied. As a result, this test does not achieve the certainty and clarity achieved in the other statutory reforms.

(iv) Third Party Brings a Legal Action

Crystallisation of the beneficiary's right occurs if he takes steps to enforce the promise. This test is only found in the Restatement.

(v) Third Party Obtains Judgment or Arbitration Award

The beneficiary's right will crystallise if he obtains a court judgement or an award of the arbitrator in relation to the breach of promise by the promisor. Only the 1982 Act (NZ) contains this test.

(vi) Promisee Informs Third Party that Right is Irrevocable

Crystallisation of the third party's right occurs if the promisee informs the third party that the right has been made irrevocable. This second crystallisation test in the PECL also stands out on its own as it is not found in other countries.

3. Exclusion, Replacement and Modification of Crystallisation Tests

The 1999 Act (E&W),[220] the 1982 Act (NZ) [221] and the PECL[222] allow the crystallisation tests as stipulated in the respective Act and Principles to be excluded. Contracting parties can replace and modify the crystallisation test in accordance to their intention. The 1999 Act (E&W), the 1982 Act (NZ) and the PECL allow contracting parties to include a term in the contract stating that they can rescind or vary the promise without the third party's consent after crystallisation. The position under the 1999 Act (E&W) and the PECL are similar and more liberal compared to the 1982 Act (NZ). Under the 1999 Act (E&W) and PECL, a term reserving the contracting parties' right to rescind or vary the promise without the third party's consent will be upheld without additional requirements to be satisfied. On

[220] Section 2(3)(a) and (b) 1999 Act (E&W).
[221] Section 6 1982 Act (NZ).
[222] Article 1:102(2) PECL.

the contrary, s.6 of the 1982 Act (NZ) only gives effect to such crystallisation test provided the relevant requirements under this section are fulfilled.[223]

There is no express provision allowing the contracting parties to exclude, replace or modify the crystallisation tests in United States and Australia.

4. Judicial Intervention Allowing Contracting Parties to Vary Contract after Crystallisation of Third Party's Right without His Consent

Only the 1999 Act (E&W) and the 1982 Act (NZ) have express provisions dealing with this matter. The scope of the 1982 Act (NZ) on this issue is wider than the 1999 Act (E&W). According to s.7 of the 1982 Act (NZ), an application can be made to the court by any of the contracting parties to dispense with the need to obtain the beneficiary's consent to vary the contract. By contrast, s.2(4) of the 1999 Act (E&W) requires both the promisor and the promisee to make similar application to the court.

In New Zealand, courts will grant an order authorising the discharge or variation of the contract if it is 'just and practicable' to do so. For the 1999 Act (E&W), courts will only grant such order if the application falls within the limited grounds as found in s.2(4) and s.2(5). If the beneficiary or any other person has suffered any losses in reliance of the contract, the 1982 Act (NZ) allows courts to order the promisor to compensate the beneficiary if it is just to do so. By comparison, similar results can be achieved in the 1999 Act (E&W) as courts can impose conditions to the order allowing variation of the contract.

[223] The requirements are listed above in Part II(B)(2).

5. Comment

It is submitted that since the basis of reforming the doctrine of privity is to give effect to the contracting parties' intention, they should be allowed to exclude, replace or modify the crystallisation tests. They are also entitled to provide that the benefit conferred on the third party is unalterable or irrevocable. The crystallisation tests found in the 1999 Act (E&W) are preferred compared to the crystallisation tests of the other statutory reforms. It is too restrictive to provide only one crystallisation test as seen in the PLA 1969 (WA) and the PLA 1974 (Qld).

The crystallisation tests which require the beneficiary to take steps to bring a legal action against the promisor or obtain a court judgment or award of an arbitrator are redundant. If these two crystallisation tests are satisfied, this shows that the beneficiary has accepted the benefit or has relied on the promise. It is unnecessary to include additional tests.[224]

In relation to the reliance test, it is not recommended that one should accept reliance by others besides the third party to satisfy this test. This reliance may fall outside the expectation of the contracting parties. It is also burdensome and unreasonable to expect the contracting parties to check with persons besides the beneficiary as to whether any reliance has been incurred.[225]

At first sight, inconsistency arises between the crystallisation tests found in the 1999 Act (E&W) and the justification behind the taking away of the contracting parties' power to

[224] LCR, at para 9.22.
[225] LCR, at para 9.35.

revoke or vary the contract. Chapter 2 explained that it is justifiable to give priority to third party's right if he suffers actual loss or would suffer actual loss as a result of the revocation or variation of the contract. However, it is submitted that applying the crystallisation tests found in the 1999 Act (E&W), crystallisation can occur without the third party having to suffer or would suffer any losses.[226] The Law Commission provided justifications for these crystallisation tests. For the acceptance test, if the third party accepts the benefit, an analogy to a bilateral contract is drawn.[227] The contracting parties' right to rescind or vary the benefit is terminated as a legitimate expectation is created in the third party who is now considered to be a promisee in a bilateral contract.

The justification for the reliance test is problematic. The Law Commission allowed trivial acts of reliance to crystallise the third party's right following the development of the doctrine of promissory estoppel where mere reliance is sufficient to invoke this doctrine.[228] This analogy between the third party's right and estoppel is misplaced in circumstances involving gift contracts to the third party. The emphasis in relation to estoppel is unconscionability. It is difficult to argue that it is unconscionable for the promisee to revoke a gift contract where all that the third party suffers is mere loss of expectation of the benefit.

The possible inconsistency between the crystallisation tests found in the 1999 Act (E&W) and the justification behind trumping the intention of the contracting parties can be

[226] For eg., in a gift contract, the third party merely loses an expectation of the gift to be provided to him if the contract is revoked. However, if he communicates his acceptance to the promisor, the contracting parties' right to revoke the benefit is lost even though he suffers no actual loss.
[227] LCR, at para 9.16.
[228] LCR, at para 9.34.

reconciled. There are many reasons why the promisee creates a contract to benefit a third party. These reasons can be broadly divided into three categories.

(a) The contract is created to discharge a legal obligation owed by the promisee to the third party.

(b) The contract is a gift to the third party

(c) The relationship between the promisee and the third party necessitates the promisee to include an exclusion or limitation clause to protect the third party. For example, the third party is an agent, sub-contractor or employee of the promisee in carrying out the duties owed by the promisee to the promisor.

For category (a) and (c), the third party would suffer a loss if the benefit is rescinded or revoked. For category (a), although the third party can sue the promisee in the event that the contract is revoked, this leads to circuity of legal action. For category (c), if the exclusion or limitation clause is revoked, the third party will be liable in an action brought by the promisor. Accordingly, the crystallisation test adopted should not be too difficult to be satisfied. However, the crystallisation test also applies to category (b), where the third party may suffer an expectation loss only. In these situations, the justification allowing the third party's right to crystallise easily seems to be lacking.

It is difficult to impose a more burdensome crystallisation test for situations involving category (b) as there may be instances where the third party does indeed suffer or would suffer actual losses if the benefit is rescinded or varied. Moreover, having different crystallisation tests for different situations complicates the law.

To ensure that the contracting parties' interest is protected in situations where the third party suffers expectation loss only,[229] judges should be given discretion to waive the need to obtain the third party's consent in an application by any of the contracting parties. Hence, s.7 of the 1982 Act (NZ) is the better approach compared to s.2(4) of the 1999 Act (E&W) in striking a sufficient balance between the contracting parties' rights and the third parties. It is submitted that judges should exercise their discretion sparingly and only in situations where it is necessary to do so. The conduct of the third party will be one of the main considerations taken into account by the judges.

In determining the amount of money to be awarded to the third party if the contracting parties rescind or vary the benefit intended for him without his consent, there may be situations where it is unfair to make the promisor solely liable for his losses. This is due to the fact that as the promisee may be the party who initiates the revocation of the benefit. In these situations, the best solution is to provide discretion to judges to determine the proper order making both the promisee and the promisor liable to the third party. This is allowed under the 1999 Act (E&W).

Different emphasis is placed on the importance of the position of the promisor and the promisee in relation to the operation of the crystallisation tests. An examination of the PECL shows that the promisee's position is more important than the promisor. The promisee can unilaterally rescind or vary the promise and his notice to the third party that the promise is made irrevocable crystallises the third party's right. By contrast, the promisor's position is emphasised in the 1999 Act (E&W) and 1974 Act (Qld). Only the

[229] The discretion given to judges to waive the third party's consent is also useful in situations where it is no longer fair to provide the benefit to the third party. In these circumstances, if the third party suffers a loss, an order can be made against the promisor, promisee or both to compensate the third party.

promisor is involved in the crystallisation tests. The legal position in Western Australia and United States is neutral in this matter.

The promisor's position is emphasised because he is the one who is obligated to perform the contract. He would want to know whether his obligation under the contract can still be rescinded or varied. The emphasis on the promisor's position may also give a longer time for the contracting parties to decide whether to rescind or vary the benefit. If the third party's right crystallises the moment acceptance is communicated to the promisee or if the promisee is aware that the third party has relied on the term or can reasonably expect that the third party will rely on the term, crystallisation may occur much earlier in situations where the promisee informs the third party about the intended benefit immediately after the contract is concluded.

The crystallisation tests of the 1999 Act (E&W) may create unfairness in certain circumstances as highlighted by McMillan.[230] There is no duty to inform the third party as to whether the promise is made irrevocable, whether the right can be varied or discharged without the third party's consent, whether they have replaced the crystallisation tests of the 1999 Act (E&W) with their own tests and the subsequent revocation of any of the earlier mentioned terms.

To counter the possible problems highlighted in the preceding paragraph, a stricter test on the contracting parties' right to rescind or vary the contract can be imposed as seen in s.6

[230] As discussed in this chapter at Part III(A)(2). Andrews (2001) 60 *C.L.J*. 353–381, at 368 also expresses surprise that there is no need to inform the third party that the contracting parties has expressly reserved the right to rescind or vary the contract without his consent.

1982 Act (NZ).[231] Contracting parties may not find a stricter test on their right to vary or rescind the benefit attractive. As a result, they may exclude the application of the rules allowing a third party to enforce a contract or may put in a term stating that the benefit of the third party can be varied or discharged without his consent. Therefore, a stricter test will only catch contracting parties who are not familiar with the provisions of the statutory reform. As such, the position in the 1999 Act (E&W) remains the better option. Any possible unfairness arising from the application of the 1999 Act (E&W) should be dealt with by relying on the common law principles as discussed in Chapters 4 and 5.

C. Defences and Set-Offs

The PECL does not contain any provisions governing this matter. The position in Western Australia and Queensland is more restrictive compared to the remaining jurisdictions. In Western Australia, the promisor is entitled to the defences which would be available to him if the third party is a party to the contract.[232] In Queensland, the promisor is entitled to any defences or arguments which will render the contract to be void, voidable or unenforceable.[233]

The position in England and New Zealand is largely similar whereby the promisor is entitled to the defences and set-offs which are available to him if the promisee is the one suing him or had the third party been a party to the contract. However, the 1999 Act

[231] The Hong Kong Law Commission, in its Consultation Paper entitled *Privity of Contract* (2005) (hereinafter referred to as 'HKLC'), at para 4.67 recommended that the contracting parties can add a term to the contract before crystallisation occur allowing them to vary or rescind the contract after crystallisation of the third party's right. But they must inform the third party of the inclusion of the term before his right crystallises. Notice published in the press is sufficient.
[232] Section 11(2)(a) PLA 1969 (WA).
[233] Section 55(4) PLA 1974 (Qld) which is interpreted by the HKLC, at para 4.88, to be subject to the provisions of the contract.

(E&W) differs from the 1982 Act (NZ) in two aspects. Firstly, the 1999 Act (E&W) allows contracting parties to expressly include any defences and set-off against the promisee arising from the contract which is not connected to the benefit provided to the third party[234] or exclude any defences, set-off and counterclaims which would be available to the promisor under the Act.[235] The 1982 Act (NZ) is silent on this matter. Secondly, unlike the 1982 Act (NZ), the 1999 Act (E&W) excludes counterclaims between the promisor and the promisee.

The position under the Restatement[236] is similar to the 1999 Act (E&W) and 1982 Act (NZ). However, the Restatement is unique s.309(3) suggests that the contracting parties can expressly provide in their contract that the promisor can rely on any defences which is not covered by s.309. This includes those defences available to the promisee in a legal action against the third party.[237] The rest of the statutory reforms do not have any provisions similar to s.309(3).

Comment

The preferred position in relation to defences and set-offs is found in the 1999 Act (E&W). Its wordings are less complicated compared to the 1982 Act (NZ) and the Restatement and its scope is broader than the PLA 1969 (WA) and PLA 1974 (Qld). However, the absence of any mention of the defences which the promisee is entitled to in relation to the third party is lamentable. The possible justification behind such position is that the law will

[234] Section 3(3) 1999 Act (E&W).
[235] Section 3(5) 1999 Act (E&W).
[236] Section 309(1) and (2) Restatement.
[237] An example would be the misrepresentation by the third party to the promisee in inducing a contract to be made with the promisor for his benefit.

become unclear and complicated if defences from another dealing (contractual or otherwise) between the promisee and the third party are considered in a dispute revolving a separate contract between the promisor and the promisee. Moreover, there may not be many incidents where such defences are relevant to the claim made by the third party against the promisor. But in situations where such defences are relevant,[238] the contracting parties should be entitled to state in their contract that the promisor is entitled to rely on these defences in a claim brought by the third party.

D. Miscellaneous

The 1999 Act (E&W) uses the word 'term' of the contract which benefits the third party in its enforceability test. On the contrary, the other statutory reforms use the word 'contract', 'promise' or 'agreement' which benefits the third party. The difference is that in the 1999 Act (E&W), if there are two terms which benefit the third party, he has to prove that each term purports to benefit him. By contrast, if the same situation occurs in other countries, the third party only has to prove that the contract benefits him. It is not necessary to prove that each term benefits him.

It can be contended that the reforms of the doctrine of privity undertaken in various countries cover both written and oral contracts except the position in Northern Territory which only apply to written contracts and arguably, the PECL. However, the 1982 Act (NZ) is unique as its definition of 'contract' includes implied contracts. The same cannot be

[238] For eg., B purchased goods from C in contract 1. B entered into a contract 2 with A whereby A is bound to pay a sum of money to C to pay off B's debt to C. If the goods purchased from C turn out to be defective, it is unfair for C to claim the purchase price from A. As such, A should be entitled to rely on B's defence under contract 1 in a legal action brought by C to enforce Contract 2.

said with certainty in relation to the legal position in Queensland, United States and PECL. The 1999 Act (E&W) and PLA 1969 (WA) do not apply to implied contracts.

Only the 1999 Act (E&W) provides specifically for the exclusion of certain types of contracts and has provisions dealing with arbitration agreements.

With regards to exclusion and limitation clauses, the 1999 Act (E&W), 1982 Act (NZ) and the Restatement expressly provide coverage for these clauses. The PECL and the PLA 1969 (WA) are silent on this issue. PLA 1974 (Qld) is not very clear on this matter. The 1999 Act (E&W), PLA 1969 (WA) and PLA 1974 (Qld) and the Restatement state that the third party is bound by any conditions and any other terms attached to the enjoyment of the benefit. The PECL and the 1982 Act (NZ) do not have any specific provisions governing this matter.

Only the PLA 1969 (WA) requires a joinder of the promisee and the third party in bringing a legal action against the promisor for breach of contract.

The 1999 Act (E&W), 1982 Act (NZ) and the PLA 1974 (Qld) expressly preserve the application of the existing common law devices to avoid the doctrine of privity. Comment *f* to s.302 Restatement reserves the trust and agency mechanisms. Although the PLA 1969 (WA) does not expressly provide for this issue, the common law mechanisms continue to apply in relation to third party claims. In relation to the promisee's right and avoidance of double liability, only the 1999 Act (E&W) and the Restatement expressly deal with this matter.

Comment

The 1999 Act (E&W) which covers both written and oral contracts is commendable. Although most of the commercial contracts are usually in writing, gift contracts are usually made orally or partly in oral form and partly in writing. Implied contracts should not be included as it serves to confuse the application of the enforceability test. Terms benefiting the third party from an implied contract are equally implied. This is inconsistent with the enforceability test which requires the contract to make express reference on the benefit granted to the third party. There is also a danger where the tool of implied contract is used to achieve justice irrespective of the contracting parties' intention. It is not necessary to include a procedural requirement such as a joinder of the third party and the promisee. However, judges should be given discretion to order such joinder where relevant. For clarity purposes, the 1999 Act (E&W) is a good example as it provides specific provisions preserving the common law devices to the doctrine of privity, the promisee's rights and avoidance of double liability to the promisor.

V. Conclusion

From the discussion in this chapter, reform of the privity doctrine involves many issues and choices of policy to be adopted on the scope of third party rights and the situations in which the reform should apply. Therefore, legislative reform is the better choice compared to judicial reform as seen in Part II of this chapter.

An examination of the judicial decisions applying the statutory reform shows that there are no major difficulties arising from the operation of the legislative reform in England. The

New Zealand position experienced a swing in the judicial mood as to the generosity of judges in applying the 1982 Act (NZ). Section 55 PLA 1974 (Qld) illustrates room for disagreement as to the scope of this section. The position in Western Australia is also less satisfactory, particularly, looking at the outcome of *Westralian Farmers*. In the United States, the majority of the cases illustrate the problem on the scope and application of the 'intent to benefit test' stated in s.302 of the Restatement.

A comparative study on the legal positions in the selected countries shows that they share a similar basis on allowing a third party to enforce a contract that is to respect the contracting parties' intention. The law must provide the contracting parties with the power to grant and shape enforceable third party rights that are consistent with their intention. None of the selected countries abolished the doctrine of privity. Instead, a general exception is created to cater for contracts made for the benefit of third parties. However, in fulfilling the purpose of reform of the privity doctrine, the selected countries have adopted different rules (in form and in substance) from one another. These differences are found in relation to the scope of reform, the crystallisation tests and the types of defences available to the promisor. Overall, the 1999 Act (E&W) is a much improved effort compared to the reform taken earlier in New Zealand, Western Australia and Queensland. The 1999 Act (E&W) is the preferable model for reform. However, there remain some minor weaknesses in the 1999 Act (E&W) where the 1982 Act (NZ) and the Restatement offer better principles in dealing with specific issues of reform of the doctrine.[239]

[239] The weaknesses are on the judicial intervention to waive the need to obtain third party's consent to vary or rescind the contract and the promisor entitlement's to rely on the defences that a promisee can raise against the third party.

It is also observed that with the exception of the Restatement,[240] very little is provided by the statutory reforms on the relationship between the promisee and the third party. Particularly, the legal positions do not state about the existence of any duty owed by the promisee to the third party on the performance of the contract. No mention is made on the promisee's duty not to revoke the benefit or accept consideration for an agreement to do so. It is arguable that it is not necessary to provide elaborate provisions for promisee's duty. If the promisee and the third party create a contract for the former to provide benefit to the latter, it is understood that the third party can sue the promisee for breach of contract if the stipulated benefit is not provided. Even in situations where there is no such contractual relationship between the promisee and the third party, the doctrine of estoppel can apply to redress any injustices caused as a result of the revocation of the benefit. Otherwise, there is no justification to allow the third party to sue the promisee if the contract is not performed.

There are three further difficulties that could arise from reform of the doctrine. Firstly, statutory reform may not be able to deal with all the possible situations dealing with contracts made for the benefit of third parties. The contracting parties are free to exclude the third party's right to enforce the contract.[241] This problem is particularly acute in relation to standard form contracts which may exclude the application of the statutory reform. As a consequence, the 'legal black hole'[242] remains open.

[240] Section 310 applies to beneficiaries of promises to pay the promisee's debt. It states that if the beneficiary has an enforceable claim against the promisee, the former can choose to sue either the promisor or the promisee in enforcing the promise. Comment *c* to s.310 provides that the promisee is not allowed to compete with the beneficiary for the assets of the promisor. Section 311(4) allows the beneficiary to claim from the promisee, any consideration received from the promisor for discharging the duty owed by the promisor to the beneficiary.

[241] The contract is still considered to be a contract made for the benefit of a third party although he is not given any rights of enforcement as the performance of the contract is intended to benefit him.

[242] The 'legal black hole' refers to situations where losses suffered by third parties are not recoverable from the promisor either by the promisee or the third parties.

Secondly, the contracting parties may be trapped by the technicalities of the legislation which they are not aware of. There may be situations where the express terms of the contract do not indicate clearly whether they intend to allow the third party to have enforceable rights over the contract. They may not be aware as to when they will lose their right to rescind or vary the benefit intended for the third party or the limitations on the defences which a promisor can plead in an action brought by the third party.

Thirdly, there may be situations where the third party is prejudiced by the operation of the statutory rules. This may happen in situations where he is not aware on the vulnerability of his rights due to the contracting parties' rights to vary or rescind his right and the defences against him which has been incorporated into the contract.

To address these difficulties, educational efforts and advocacy programs must be carried out to publicise the changes made to the privity doctrine so that the contracting parties are aware of their legal position. The public must be encouraged to draft their contract clearly. The common law mechanisms will be utilised to prevent any injustice which occurs. In situations where the third party's right is excluded, the promisee's remedies for breach of contract are important tools to ensure that the objective of the contract made is fulfilled. In situations where the third party suffers a detriment due to his reliance on the contract without knowledge that his rights could be rescinded or varied easily, the doctrine of promissory estoppel should be utilised whenever possible.