

## **Third Party Rights on the Way**

### **December 2012**

At the end of October, the Department of Justice ("DoJ") published a working draft of the Contracts (Rights of Third Parties) Bill (the "Bill").

The Bill, when enacted, will reform the doctrine of privity of contract and allow third parties who are not a party to a contract, to sue to enforce contractual terms, subject to the intention of the contracting parties.

The effect of the Bill would bring Hong Kong in line with legislative reforms that have taken place in other common law jurisdictions over the last 15 years, notably England, New Zealand, Singapore and parts of Australia. The reform of the doctrine of privity of contract has been under study in Hong Kong for a decade and the current Bill adopts all of the recommendations resulting from the Law Reform Commission's ("LRC") 2005 *Report on Privity of Contract*.

#### **Criticism of the doctrine of privity of contract**

The doctrine of privity, also known as the "third party rule", holds that a contract cannot confer rights or impose obligations on any persons other than the parties to a contract. This has two aspects:

- (1) a person cannot acquire and enforce rights under a contract to which he is not a party; and
- (2) a person who is not a party to a contract cannot be made liable under it.

While the second aspect is generally regarded as just and sensible, the first aspect can lead to unfairness and has been subject to much criticism.

Various everyday examples of such injustice have been provided by the LRC. A simple example would be where "A" and "B" enter into an agreement for "A" to pay money to "C" and "A" defaults. "C" cannot sue "A" as he is not a party to the agreement. "B" cannot sue "A" because he has not suffered any damage<sup>1</sup>.

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<sup>1</sup> The Court may be able to prevent injustice to "C" if "B" is prepared to sue "A" for specific performance. Other legal principles have also developed to allow the effect of allowing third parties to enforce rights under different circumstances. However, despite the various common law and legislative inroads to circumvent the doctrine, the Law Reform Commission has now recommended reform of the doctrine by a comprehensive, systematic and coherent legislative scheme.

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#### **Impact**

The current Bill allows contracting parties the freedom to choose whether to adhere to the doctrine of privity and provides for parties to contract out of the new statutory provisions.

In anticipation of the new law, businesses should consider whether to review and revise their standard terms and conditions to include boilerplate clauses to that effect.

The public consultation on the Bill will close on 31 December 2012. We will continue to monitor and provide updates on developments.

DoJ Consultation Paper:

<http://www.doj.gov.hk/eng/public/pdf/2012/consulte.pdf>

LRC Report:

<http://www.hkreform.gov.hk/en/publications/rprivity.htm>

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