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TRANSFERRED LOSS: A BLACK HOLE IN ENGLISH LAW OF CONTRACT?

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"Hominem unius libri timeo"

I fear the man of a single book

St Thomas Aquinas

Part I - Introduction

I.1 – Foreword

The issue of transferred loss has received little attention under the common law (if not also under the civil law). In fact, even the concept of transferred loss is somewhat alien to the common law and can be said to have been inspired by *drittschadensliquidation* – a German concept.

The concept of *drittschadensliquidation* emerged in earlier Germany, being presented as result of the short comings of a very strict tort law system, while the concept of transferred loss emerges as result of the short comings of a very strict law of contract. In both cases, facts and judicial decisions preceded most doctrinal elaboration on the subject. In face of a reality for which the preexisting legal regime gave insufficient (unsatisfactory) answers, the courts forged new answers.

Such answers came up most notably in sets of cases, of particular fields. Nowadays, it is still unclear whether there is a general principle of *drittschadensliquidation* or if *drittschadensliquidation* has resulted in exceptions to be applied only in such cases. To a certain extent, in relation to transferred loss, the XX century may represent for English law of contract what the XIX century represented for German Law.

In English law, although transferred loss has received few attention by scholars and case law hasn’t often referred to it; the legal reality it intends to describe and the cases to which it may apply are overwhelming. Transferred loss may or may not be a legal regime, but it certainly is a reality, as we shall see. As such, one must not ignore such reality and one must seek which answers does the legal system provide.

In fact, transferred loss is a matter of defining which concepts are to be used, from which angle should the law be interpreted and how should the acts of parties interact with law. Although transferred loss has often not been fully studied under English law, it is unquestionable that such reality exists and there must be a legal answer for it (whether satisfactory or not).

The issue is how we frame the question to be answered. We may take the angle of the existing legal regimes and from that on seek to which cases it may apply. Or, we may take the angle of existing cases and situations and from that on see which legal solutions may apply. Both are viable, both provide answers – and supposedly should provide the same answer.

In this paper we do not claim at start the existence of a transferred loss principle (a general principle of law or comprehensive legal regime), nor do we develop our research from any specific legal regime to the cases to which it may apply. On the contrary, we take a specific problem, we bring down the issues it raises and then we focus on identifying the most important judicial decisions. In doing so, one must always take into account that law is not an exact science.

As such, this paper doesn't import the concept of *drittschadensliquidation*. What this paper does is to take transferred loss (as defined infra) as an operative concept. And to the extent that such concept describes a set of cases that globally refer to a common problem that is, therefore, considered under a common heading: transferred loss. This paper does not intend to import the solutions of German law, nor to appraise its virtues. What we take as starting point is a problem defined in a similar way to the one how it was identified in Germany.

That said, one must not ignore that we are partially within the realm of one of the most essential paradigms in the English law of contract: privity – the multisecular foundation from which the binding force of contracts is legally derived. As such, most common law scholars have considered this issue merely from the angle of privity: what is privity, to which extent is privity applicable and, eventually, what are its shortcomings. For those who do not relinquish privity as a quasi sacred quintessential flawless foundation of contract law, then alternatives (and complements) to current contractual liability seem pointless – as they would imply a shortcoming of privity.

The latter excluded the admissibility of contracts with protective effects towards third parties – as we shall see infra. The exclusion of such contractual alternative, reinforcing the orthodoxy of privity, strengthened the acuteness of this issue. The problem of transferred loss could be partially answered by contracts with protective effects towards third parties, a theory that is gaining consistency in civil law countries.

In the absence of such contractual alternative, what are we left with? An unsolved problem? A persistent orthodoxy? Or the emergence of new paradigms?

From an unsolved transferred loss problem…
… can a transferred loss principle emerge?

I.2 – The problem

On both common law and civil law systems there is a distinction between contractual and tort law liability. On the one hand, contract law provides redress mechanisms under which creditors may claim compensation for the damages caused by the debtors' default. On the other hand, tort law provides redress mechanisms under which one may claim compensation for damages caused by others irrespectively of contract. Each legal system then adjusts and provides specific criteria.

The distinction between both relies on the special relation that exists between debtor and creditor, a relation that is created by one's will, namely, through contract. As such, many legal orders create better conditions for the creditor to recover in contract damages caused by the debtor's default, than for any one to recover in tort from damages caused by others.

This (at least) two millennia old paradigm, takes into account the distinction between the commitment of the debtor / the confidence it creates on the creditor and the damages created without such personal commitment / confidence. The problem emerges when applying this model to cases in which there is commitment / confidence (created by acts of one's will), which is breached, but whose damage is caused to a party to which no primary obligation is owed. When there is a contract, the contract is breached, but the damages of such breach are caused to a third party, how should the paradigm be applied?

The traditional answer is to consider that the scope of contract law only applies between creditor and debtor of primary obligations, because only in such case there is the special relation (most times of a contractual nature) prescribed by law. As such, outside of the aforementioned scope, only tort law could be applied.

What if there was an indirect contractual relation between all parties? What if in spite of the absence of a proper debtor-creditor relationship between who causes the damage and who suffers it, there was still personal commitment / confidence? What if a damage is excluded from the contractual scope precisely by another contract with a different party?

All this questions have traditionally received negative answers, because of how privity in common law and the primacy of contract in civil law were upheld. This strict interpretation had as a starting point the argument that a contract creating an obligation could not be affected by third parties: its performance or default relied merely on the parties; its default could only harm the creditor.

Facts have superseded the longstanding legal theories. Let's imagine: A has a contract with B; A has a contract with C. The default by B may make it impossible for A to fulfill its contractual obligations to C. The default by B may cause no harm to A. The default by B, may cause the default by A, which may cause significant damages to C.

In this situation, under contract law we may find ourselves in the following paradigm: B defaults its obligations and such default causes damages; A cannot claim compensation because A had no damages[1]; C has damages but cannot claim compensation because C isn't a party to the contract. There is dissociation between the right to claim compensation and the actual loss, that enables to claim such compensation – this is the essence of transferred loss.

It should be noted that such dissociation isn't necessarily regarded as problematic. Atiyah, although not addressing specifically the transferred loss issue, strongly criticizes the developments of legal compensation mechanisms, considering that "*[t]he legal system is helping to create a 'blame culture' in which people have a strong financial incentive to blame others for loss or death or injury*"[2]. In fact, the remarks Atiyah addresses in relation to personal injuries can be equally applicable to transferred loss:

> "*How fair is the system? The answer is that the system is about as fair as a lottery. In fact it is not too much to say that it is a lottery, a lottery by law. It is*

[1] We are taking, as a starting point, a non-nominal concept of damages.
[2] (Atiyah, 1997)

almost a matter of chance whether you can obtain damages (...); it is almost a matter of chance who will pay them; it is almost a matter of chance how much you will get." (Atiyah, 1997)

I.3 – An at least two-millennia old debate

The main concepts regarding the contractual rights of third parties – known in English law as the privity doctrine – were already known to roman lawyers. Under roman law such concepts were known as *res inter alios acta, neque nocere, neque prodesse potest* (the acts between others may not harm nor benefit further ones), *alteri stipulari nemo potest*[3] (no one may agree in lieu of another) and *per extraneam personam nihil adquiri posse* (nothing shall be acquired through an extraneous person)[4].

Alteri stipulari nemo potest, as prescribed by the Justinian's Institutes, meant it was not possible to *stipulate* in favor of a third party. Although the verbal contract of stipulation (*stipulari*) was a specific contract under roman law, this principle may have been applicable to any contract in favor of an absent beneficiary[5]. Two exceptions were known: the cases when the stipulator had a monetary interest in the performance for the third party (e.g., the payment to the stipulators creditors) and when a penalty clause was established. In both cases the stipulator would acquire a right and would be allowed to judicially claim such right. No one but the stipulator in the aforementioned cases could claim contractual rights. Exceptional cases in which the third party has the right to enforce contractual performance can even be found in the Corpus Iuris.

An analysis of such roman law concepts, despite of their importance to the development of civil law, shall not be carried on in this paper. What is important to retain is that privity-like doctrines already existed in ancient roman law and that such concepts were later developed in the ius commune – with some limited exception towards third parties having been recognized.

[3] Also quoted as *stipulari alteri nemo potest*
[4] (Hallebeek & Dondorp, 2008)
[5] (Hallebeek & Dondorp, 2008)

I.4 – The German perspective: drittschadensliquidation

I.4.1 – The German concept of *drittschadensliquidation*

D*rittschadensliquidation* was construed as a judge-made concept under which the creditor might claim in contract for the loss of a third party, to whom the creditor's loss had been transferred. It is still controversial if such concept is to be considered as a legal doctrine (applicable in general to cases of loss' transfer) or as an heading for specific judicially recognized exceptions (applicable only in analogous circumstances to prototypical cases).

There is a long standing legal debate on the theoretical basis of *drittschadensliquidation*. To a certain extent, such debate amounts to the debate in English law regarding the several grounds on which transferred loss could be considered (narrow versus broad grounds), which we shall see infra.

In fact, German courts had accepted *drittschadensliquidation*, considering it to derive parties' will – and, as such, recognized it has an implied term in some existing contracts. Therefore, for German courts *drittschadensliquidation* arose from the parties' agreement[6].

Nonetheless, later the BGH (the supreme German court) came to realize that this implied term approach, requiring the courts to establish that parties' intention (or what would have been the parties' intention if they had foreseen the issue) was in favor of *drittschadensliquidation*, was somewhat problematic. The BGH concluded that such couldn't be easily undertaken as the ground for *drittschadensliquidation*, since the parties intention tends to be to protect themselves. The BGH concluded in 1963[7] that such an approach amounted to fiction.

[6] RGZ 170, 246; endorsed in BGHZ 15, 224
[7] BGHZ 40,91

Afterwards, the German courts adopted an objective approach under which, departing from the parties' will criteria, there could be *drittschadensliquidation* only if:

i) "*All the damage due to the harmfull conduct of the obligor is suffered by the third party*";

ii) "*The claimant would have suffered [it] if the protected interest had been vested in him*"[8].

The legal ground for such *approach* was the "*special legal relations between the creditor under the contract and the beneficiary of the protected interest [which] cause[s] the interest to be 'shifted' on to the third party, so that as a matter of law the damage is done to him, and not to the creditor.*[9]"[10]

This approach leads to a clearer distinction between *drittschadensliquidation* and *Verträge mit Schutzwirkung für Dritte* (contracts with protective effects towards third parties). The first encompasses only the loss which was transferred, in as much as the promise would have suffered loss himself/herself, unless it had been transferred to the third party. The protected interest is the same, though it shifts from the promisee to the third party. On the contrary, *Verträge mit Schutzwirkung für Dritte* encompasses an enlargement of the interests contractually protected, simultaneously serving as a ground for promisee and third party to claim compensation.

Still, taking the novel legal ground, *drittschadensliquidation* wasn't contained in the contractual domain. German courts finally accepted that such *drittschadensliquidation* ought also be recognized in tort law. Thus, *drittschadensliquidation* became the concept/doctrine under which one might judicially claim from another (either in contract or in tort) the loss of a third party, provided the former could bring the claim if he had himself suffered the loss and provided that the loss had been transferred to the third party.

[8] Quotations from BGHZ 40, 91, case num. 71, translated by Markesinis, B., & Unberath, H. (2002)
[9] Quotations from BGHZ 51, 91, case num 61, translated by Markesinis, B., & Unberath, H. (2002)
[10] Even such reasoning was not uniformely welcomed in following judicial decisions. See for instance BGH NJW 1977, 2208.

In parallel, the scope of the doctrine had yet to be defined. D*rittschadensliquidation,* as a judicially devised concept, was gradually (though not uniformly) applied to cases put forward before the courts. These cases unsurprisingly occurred more often on a set of cases in specific fields of law (in which either due to the nature of business practices or due to specific legal agreements, the transfer of loss took place more often, or even in which such transfer of loss appeared more often as unjust).

German courts have recognized *drittschadensliquidation* namely in three sets of cases: indirect representation, transfer of risk, and taking care of another's goods. Indirect representation stands for the cases in which a contract in concluded on the account of a third party. Transfer of risk encompasses the cases in which risk and property are not transferred simultaneously. Taking care of another's goods describes cases in which one possesses the goods of another, looking after such goods.

Would *drittschadensliquidation* be an exception only applicable in the judicially recognized domains or would it be a general concept? The question remains unsolved.

I.4.2 – Relation between the German and English concepts

The German concept of *drittschadensliquidation* is often quoted in the transferred loss debate in English law. In fact, transferred loss is conceived as resulting from the importation of such German concept, to the point that *drittschadensliquidation* is translated to English as *transferred loss*.

Although these concepts are clearly close, transferred loss isn't (or wouldn't be) a mere translation or importation of a German concept. Despite the fact that English reasoning in this field has been enriched by the German judicial and doctrinal elaboration on the subject, an even if both systems arrive at similar solutions, their eventual specificities must not be overlooked.

Two reasons for such eventual specificities may be immediately perceived: Firstly, there is an historical *acquis* of English legal thinking that could not be discarded and to which such *novel* concept ought to be adapted; that is to say that transferred loss wouldn't emerge in English law in a conceptual void. Secondly, we are dealing with concepts meant to solve what is now understood as a *lacunae* or as a legal injustice, but this two legal systems are different from one another and may not present the same challenges. Another unveiled reason may exist, as we shall see infra: the concept of transferred loss may have also roots in medieval English law.

Still, considering the above mentioned reasons, understanding *drittschadensliquidation* is nonetheless essential for understanding the transferred loss debate in English law.

I.5 – The Privity doctrine

I.5.1 – The doctrine in general

The doctrine of privity of contract now stands as an essential pillar of the English law of contract. Privity is the doctrine by which no one may benefit from or be bound by a contract to which he / she is not a party to. Thus, Privity stands as the legal main ground for discarding (i) contractual liability outside a very strict scope *inter partes* and (ii) novel legal reasonings regarding liability – such as, contracts with protective effects towards third parties and transferred loss.

The novel doctrines put forward in English law, namely transferred loss, attempt to breach the strictness imposed by a long standing understanding of privity. Though, the doctrine of privity has long prevailed (and still endures) in the English law of contract and is nowadays regarded as an essential principle of contract law, it has not always been so.

In fact, the clear establishment of the doctrine of privity can be traced back just to the XIX century. And, what now may seem a revolutionary breakthrough in contract law (a reshaping of privity in order to accommodate third parties interests) can be found in case law prior to the establishment of such doctrine. So, unlike what we are led to believe, such novel concepts are not so unknown to contract law – instead they precede the clear strict establishment of privity in English law.

The decisive case towards the establishment of privity was *Tweddle v. Atkinson* (1861). In such case, in consideration of an intended marriage, the father of the soon-to-be wife entered into a contract with the father of the soon-to-be husband, whereby each promised to pay the soon-to-be husband a sum of money. The soon-to-be husband, not having received such sum, sued his executors. Yet, the action was dismissed.

Justice Wightman said:

> "***Some of the old decisions appear to support the proposition that a stranger to the consideration of a contract may maintain an action upon it****, if he stands in such a near relationship to the party from whom the consideration proceeds, that he may be considered a party to the consideration … But there is no modern case in which the proposition has been supported.* ***On the contrary, it is now established that no stranger to the consideration can take advantage of a contract, although made for his benefit****.*" (emphasis added)

The doctrine of privity, as construed by the House of Lords, is a reflection of the general assumption that "*contract, as a juristic concept, is the intimate if not the exclusive relationship between the parties who have made it*"[11]. This intimateness was taken to such a conceptual degree that prevented third parties from judicially claiming any benefits from a contract, even when the parties clearly intended to confer such benefits upon them . This raises the issue of when should one be a considered as a party to a contract, which shall be dealt latter.

The Law Revision Committee proposed substantial reform of the doctrine as early as 1937, in its Sixth Interim Report[12]. Yet, only in the cases *Woodar Investment Development Ltd v. Wimpey Construction Ltd* (1980) and *Darlington Borough Council v. Wiltshier* (1995) opinions (though the minority) forcefully urged for privity to be reconsidered. In 1999 the privity doctrine was finally reshaped through the Contract (Rights of Third Parties) Act[13].

In the meanwhile, the High Court of Australia in the case *Trident General Insurance Co Lts v. McNiece Bros Pty Ltd* (1988), rejected the doctrine of privity . Followed by the Supreme Court of Canada in the case *London Drugs Ltd v. Kuehne and Nagel International Ltd* (1993).

[11] (Cheshire, Fifoot, & Furmston, 2001, pag 573)
[12] (Committee, 1937, Cmd. 5449)
[13] Act in force at Royal Assent (11.11.1999)

I.5.2 – Reasons for the doctrine

There has been a vast debate over the grounds on which the doctrine of privity is based. On the one hand, it is clear that no one except a party can be subjected to liabilities under it, as otherwise contractual obligations would be imposed without one's consent, unduly restraining one's contractual freedom. On the other hand, it is not so clear why no one except a party to a contract can acquire rights under it.

Steyn LJ has expressed that there is no "*doctrinal, logical or policy reason*"[14] justifying it. Furthermore, according to Treitel's Law of Contract:

> "*The rule that a third party cannot acquire rights under a contract can scarcely be justified by saying that a contract is, or gives rise, to a personal relationship, affecting only the parties to it; for this is rather a restatement of the rule than a reason for its existence*" [15].

With all due respect, the personal relationship is first and foremost a matter of fact: the contract is concluded between the parties. In addition, as recognized in Treitel's Law of Contract, by recognizing third parties rights in contract, the contract is no longer limited to the parties. In light of third party rights it would be hard to conceive that the parties alone could still amend or cancel a contract, altering or voiding another one's right. Yet, from another point of view, each party as *dominus* of the contract should master the rights and obligations therein through agreement with his/her counter-parties.

In parallel to this debate, it should be noted that the English system does not give the right to enforce a gratuitous promise (in light of consideration), third parties may be comparable to gratuitous promisees.

In the end, despite the several studies on the scope and effects of privity, English law lacks an in-depth analysis on the rational that underlies such doctrine.

[14] (Darlington Borough Council v. Wiltshier, 1995)
[15] (Peel, 2007, p. 622)

I.5.3 - Qualifications to the doctrine

Qualifications to the doctrine of privity can be traced back to the eighteenth century, when privity itself wasn't clearly established. As such, modern law empowers to a certain extent ancient legal regimes that predate the establishment of privity and are now regarded as qualifications to such doctrine.

a) The agency reasoning

The doctrine of the undisclosed principle is one of the qualifications to the privity doctrine and has been questioned for being contrary to its principles[16]. In a contract made by two parties, a third party may intervene *in lieu* of one the parties provided he/she can establish the party was acting as his or hers agent.

Agency is the relationship through which one acts as the representative of another. As such,

> "*The essential characteristic of an agent is that is invested with a legal power to alter his principal's legal relations with third parties; the principal is under a correlative liability to have his legal relations altered*"[17]

The aforementioned legal power can result from express appointment, estoppel, ratification, necessity or can be presumed in the case of cohabitation. The underlining agency contract is one of the special contracts of English law.

Whenever an agent performs a contract with another party under agency, privity is established between the agent's principal and the other party. In those circumstances, the contract is enforceable by the principle (and exceptionally also by the agent when so provided). All this derives from the fact that the agent acts in representation of the principal. Often difficulties arise in establishing whether someone acted as an agent (agency doesn't require to be expressly invoked) or as an independent contractor. Such

[16] Lectures in Legal History
[17] Dowrick 17 MLR. Reynolds 94LQR 225

difficulties are most common when someone acts as an intermediary: the intermediary can perform a contract as an agent, but can also perform independent contracts.

The issue of undisclosed principle is raised when the other party in unaware that the contract was concluded with someone's agent. It has long been established that in such case the contract in enforceable either by or against both the agent and the principal (*Sims v Bond* [1833] and *Saxon v Blake* [1861])

b) The law of property in general

Difficulties in bringing together the doctrine of privity with the needs and concepts of the law of property also predate even the clear establishment of the former. In fact, by the XVI century it had been recognized that there were contracts that create rights of property that cannot be kept within contractual bonds (leases for instance)[18]. No doubt that in such cases there is privity between the parties themselves, but if either transfers his interest to a stranger then the benefits and burdens ought to be equally transferred.

Modern case law acknowledged such qualification most notably in *Smith and Snipes Hall Farm Ltd v River Douglas Catchment Board* [1949]. In such case, the owners of land had commissioned improvements in the land and their maintenance for all times of the work when completed. In 1940 one of the land owners sold her land to a third party, later the third party leased the land to another. Could the new land owner and the third party which had leased the land enforce the contract? The Court of Appeal answered in the affirmative, though both plaintiffs were strangers to the contract. The ground for such decision was the fact that the contract was intended to benefit anyone to whom the land might be transferred and to whom the defendants were liable.

c) The law of property act

The Law of Property Act 1925 provides under Section 56(1) that:

[18] Spencer's case (1583)

"*A person may take an immediate or other interest in land or other property, or the benefit of any condition, right of entry, covenant or agreement over or respecting land or other property, although he may not be named as a party to the conveyance or other instrument*."

And, under Section 205(1):

"*'Property' includes any thing in action, and any interest in real or personal property*"

According to various Lord Denning's obiter dictums[19], the above quoted section of the Law of Property Act abrogated the doctrine of privity in the case of contracts related to property (property under section 205(1) of the aforementioned). Lord Denning's interpretation was repealed by the House of Lords in *Beswick v Beswick* [1968].

Peter Beswick sold his business to his nephew in consideration that he would pay him £6,10 per week and after his death he would pay his widow £5 per week. After Peter Beswick's death his nephew refused to pay Peter's widow. She sued him both as administratrix of Peter's estate and in her personal capacity. The Court of Appeal unanimously recognized her *locus standi* as administratrix, while only Lord Denning and Lord Justice Danckwerts were in favor of recognizing her *locus standi* additionally in her personal capacity under Section 56(1) of the Law of Property Act 1925.

The Defendant appealed to the House of Lords, which up hold that the widow only had *locus standi* as administratrix. The House of Lords decided so, despite admitting that the language of Section 56(1) was broad enough for it to be construed in order to support the conclusions of Lord Denning and Lord Justice Danckwerts. This was so because their lordships considered that in an act devoted to real property the parliament didn't intend to inadvertedly revolutionize the law of contract. As such, the purpose of the Law of Property Act 1925 was merely to consolidate the enactments relating to conveyancing and the law of property in England and Wales[20].

[19] (Cheshire, Fifoot, & Furmston, 2001, pag 507, note 20)
[20] (Treitel, 2003, pag 30) (Cheshire, Fifoot, & Furmston, 2001, pag 507)

d) Doctrine of constructive trust

Qualifications on the privity doctrine were more reluctantly accepted in common law outside the fields of property and commercial law. Yet, a possible answer had been found in equity by the eighteenth century. In *Tomlinson v Gill* [1756], Lord Hardwicke facing a case in which A promised B to pay a sum of money to C, found - as *obiter dictum* - that it would be possible to regard B as a trustee for C of the benefit of the contract. Only by 1817 a case was decided taking such constructive trust as *ratio decidendi*: *Gregory and Parker v Williams* [1817].

Taking into account that the doctrine of constructive trust was developed within equity, one must seek how it was observed following the Judicature Act 1873[21]. In *Lloyd's v Harper* [1880], Lush LJ referred:

> "*I consider it to be an established rule of law that where a contract is made with A for the benefit of B, A can sue on the contract for the benefit of B and recover all that B could have recovered if the contract had been made with B himself.*"

Though this could erroneously be interpreted as simply putting forward the doctrine of privity, it is cited by Lord Birkenhead in *Les Affréteurs Réunis v Walford* [1919] as admitting this doctrine of constructive trust. It should be noted that the doctrine of constructive trust wasn't even taken into consideration inbetween those two cases in *Dunlop v Selfridge* [1915], while the facts could call upon constructive trust.

The case law that followed, though not repealing the doctrine of constructive trust, reveals judicial reluctance in recognizing the existence of trusts in such circumstances. According to Du Parq LJ in *Re Schebsman, Official Receiver v Cargo Superintendents (London) Ltd and Schebsman* [1944], there isn't any trust "*unless an intention to create a trust is clearly to be collected from the language used and the circumstances of the case*". Or, as additionally explained by Romer LJ in *Green v Russell* [1959], *"[a]n*

[21]The debate over the substantive effects (if any) of the Judicature Act 1873 is to be found outside the scope of this paper. (Webb & Akkouh, 2008, pag 9) (Birks, 1996) (Burrows, 2002)

intention to provide benefits for someone else and to pay for them does not in itself give rise to a trusteeship".

Thus, over time law as evolved and the scope of the constructive trust's doctrine has been fairly restricted to cases in which the parties specifically intended to create a trust. Therefore, the ground on which *Gregory and Parker v Williams* was decided back in 1817 is no longer valid in English law, as when someone enters into a contract for the benefit of another it no longer amounts to a constructive trust.

I.5.4 – The Contract (Rights of Third Parties) Acts

The Contract (Rights of Third Parties) Act 1999, legally empowering the views expressed the 1996 Law Commission Report[22] [23], confers rights on third parties which have the nature of a statutory exception.

The initial proposal for reform put forward by the Law Commission was enacted as statutory law (with minor refinements), without having been substantially further enhanced. This means that the re-shaping of the privity doctrine was rather limited and - as result of that – instead of a substantial reform of the general rule, the aforementioned statutory exception emerged.

As Treitel[24] points out, the The Contract (Rights of Third Parties) Act's effects are mainly limited in two ways:

a) Several transferred loss cases are outside the scope of the statutory exception to the privity doctrine;
b) The statutory exception is itself subject to several exceptions.

In the end, as the Commission acknowledged:

[22] (Law Commission Report N.º 242 (1996))
[23] Preceded by the 6th Interim Report of the Law Revision Committee (1937)
[24] (Peel, 2007, pag 615)

> "*it is important to emphasise that, while our proposed reform will give some third parties the right to enforce contracts, there will remain many contracts where a third party stands to benefit and yet will not have a right of enforceability. Our proposed statute carves out a general and wide-ranging exception to the third party rule, but it leaves the rule intact for cases not covered by the statute*".

In the end, the act acknowledges a strictly defined recognition of contracts with for the benefit of third parties, excluding cases in which third parties are affected without being owned a contractual obligation[25].

[25] For more on The Contract (Rights of Third Parties) Act 1999, see chapters II.2.2 and II.2.3

Part II - Alternatives to Transferred Loss

II.1 – Tort claims

According to Street, "*[l]aw of Tort defines the obligations imposed on one member of society to his or her fellows and provides compensation and other remedies for harms caused by breach of such obligations*" (Murhpy, Brazier, & Street, 2003). Under English Law, there is a closed system of nominate torts – in contrast with the general clauses of some continental systems. As such, there is a set of torts.

First and foremost, regarding this field of English Law and the definition put forward by Street, one might question: are we dealing with a Law of Tort or a Law of Torts? This apparently irrelevant question steams from an essential theoretical question: is there a common core that unites the different torts under a single institute?

Underpinning such definition there is a distinction between, on the one hand tort law and criminal law, and, on the other hand, tort law and contract law. The distinction between Tort, Criminal and Contract Law can be drawn from several viewpoints and encompasses the differences regarding who owes the obligation, to whom the obligation is owed, the nature of the obligation, the reactions prescribed by law to its breaches and the functions it serves.

There is no clear-cut disjunctive distinction between the operative fields of each type of responsibility. In many circumstances, the same facts may accommodate various types of liability. A crime or a tort can be committed through a contract or through the same facts that constitute its breach. On some cases this leads to an overlap of responsibility of different types. This leads to an array of issues, namely, which, if any, takes precedence over the others and to what extent may reparation may claimed under which in such case. On others, one type of responsibility may complement the shortcomings of another. The purpose of this section to explore to what extent may tort law provide an answer to the contract law short comings regarding transferred loss.

As just mentioned, under English law, each tort has its own scope and conditions. Therefore, a separate inquiry must me developed regarding each tort that may be relevant to the issue. For the sake of clarity and synthesis our analysis shall be limited to the broadest tort available in English law: negligence.

II.1.1 – General overview of the tort of Negligence

The tort of negligence occupies a central position in the English law of torts. Gradual recognition that, in some cases, compensation should be awarded for damages caused by carelessness led to the development of the tort of negligence. Yet, negligence didn't emerge as a separate tort until the XIX century and was only clearly defined by a XX century leading case. Three XIX century cases emerge as foundational cases in such process: *Vaughan v Menlove* (1837), *Winterbottom v Wright* (1842) and *Heaven v Pender* (1883).

In the first of the aforementioned, *Vaughan v Menlove*, the reasonable person test was put forward, establishing what would be a feature of the tort of negligence:

> "*[W]hether the Defendant had acted honestly and bona fide to the best of his own judgment (...) would leave so vague a line as to afford no rule at all (...) [Since the judgment of the individual is] as variable as the length of the foot of each (...) we ought rather to adhere to* ***the rule which requires in all cases a regard to caution such as a man of ordinary prudence would observe***." (Emphasis added).

Once having defined the view point from which diligence ought to be evaluated, the scope of duties (to which such test was to be applied) was sill uncertain. So, in *Winterbottom v Wright*, the plaintiff sought recovery as a third party, based on the breach of a defendant's duty under a contract. The Court decided that the right to recover for a breach of contract is confined to those who enter into such contract, under privity. Later, in *Heaven v Pender*, Brett MR recognized that individuals may claim the existence of a duty of care (it may be added: despite being third parties to contracts and irrespective of such contracts):

> "*[W]henever one person is by circumstances placed in such a position with regard to another* ***that everyone of ordinary sense who did think would at once recognize that if he did not use ordinary care and skill in his own conduct with regard to those circumstances he would cause danger or injury*** *to the person or property of the other****, a duty arises to use ordinary care and skill to avoid such danger***". Brett MR Speech obiter dictum (Emphasis added)

The answer given in *Heaven v Pender* developed into the "neighboring principle" as set forward by Lord Atkin in *Donoghue v Stevenson* [1932]:

> *"There must be, and is, some general conception of relations giving rise to a duty of care, of which the particular cases found in the books are but instances. (...) The rule that you are to love your neighbour becomes in law you must not injure your neighbour; and the lawyer's question: Who is my neighbour? receives a restricted reply.* ***You must take reasonable care to avoid acts or omissions which you can reasonably foresee would be likely to injure your neighbour****. Who, then, in law, is my neighbour? The answer seems to be -* ***persons who are so closely and directly affected by my act that I ought reasonably to have them in contemplation as being so affected when I am directing my mind to the acts or omissions*** *that are called in question . . . a manufacturer of products, which he sells in such a form as to show that he intends them to reach the ultimate consumer in the form in which they left him with no reasonable possibility of intermediate examination, and with knowledge that the absence of reasonable care in the preparation or putting up of products will result in an injury to the consumer's life or property, owes a duty to the consumer to take that reasonable care." Lord Atkin speech (Emphasis added)*

The above quoted was paramount in the establishing in English Law the tortious principle of a general duty of care. The reasoning supporting such principle derives not only from *Heaven v Pender* but more importantly from US case law - most notably *MacPherson v. Buick Motor Co. [1916]*.

The neighboring principle has its roots in the Christian principle of loving your neighbor, as prescribed in James 2:8 ("*If ye fulfil the royal law according to the scripture, Thou shalt love thy neighbour as thyself, ye do well*") and Leviticus chapter 19 ("*love one's neighbor as oneself*").

It should be noted however that – despite being a landmark – such reasoning by Lord Atkin constituted merely *obiter dictum* and according to Street "*it is probable that Lord Atkin never intended it to be an exact comprehensive statement of law*"[26]. The *ratio decidendi* of the case is somewhat more limited by focusing on the recognition of a duty from the manufacturer of goods to the eventual users of those goods. What is certain, however, is that it demonstrated that the tort of negligence was capable of further expansion. As Lord Macmillan aptly put it "*categories of negligence are never closed*", that is, courts are to recognize the existence of duties even when no precedent establishes such duty.

Therefore, three notes should be taken: i) the nineteenth century and initial twentieth century development of the tort of negligence lead to the development of a general duty of care in England and in the US; ii) both achieved a certain judicial recognition, though no precedent could be said to exist in English law; iii) there was a clear gradual broadening of the tort of negligence.

Yet, the broadening of the tort of negligence wasn't a continuous uniform process. In fact, on other cases the courts refused to acknowledge duties on which the tort of negligence could be based (or the existence of a general duty applicable to the case). For instance, *Langbrook Properties Lta v Surrey County [1969]* and *Midland Bank v Bargrove Property Services [1991]* could be quoted.

[26] (Murhpy, Brazier, & Street, 2003, pag 178) (Haseldine v CA Daw & Son Ltd, 1941)

Still, by 1970 the courts embraced the aforementioned Lord Atkin's *obiter dictum*. In *Home Office v Dorset Yacht Co Ltd [1970]*, Lord Reid stated:

> "*The time has come when we can and should say that it [Lord Atkin's neighbour principle] ought to apply unless there is some justification or valid explanation for its exclusion*".

The rule as such was best synthesized in *Anns v Merton London Borough Council* (1978) by Lord Wilberforce:

> "*[T]he position has now been reached that in order to establish that a duty of care arises in a particular situation**, it is not necessary to bring the facts of that situation within those of previous situations in which a duty of care has been held to exist**. Rather the question has been approached in two stages. First, one has to ask whether, as between the alleged wrongdoer and the person who suffered damage there is **a sufficient relationship of proximity or neighbourhood** such that, in the reasonable contemplation of the former, carelessness on his part may be likely to cause damage to the latter, in which case a prima facie duty of care arises. Secondly, if the first question is answered affirmatively, it is **necessary to consider whether there are any considerations which ought to negative, or to reduce or limit the scope of the duty** of the class of person to whom it is owed or the damages to which a breach of it may give rise*". Emphasis added.

The expansionary progression of the scope of the duty(ies) of care was reversed by 1985, most notably after the *Governors of the Peabody Donation Fund v Sir Lindsay Parkinson & Co Ltd [1985*] case. In this case the Court, through the speech of Lord Keith, regarding the broadening of the duties under the tort of negligence, stated "*It is material to take into consideration whether it is just and reasonable that it should be so*".

As such, initially a duty was said to exist whenever there was a relationship of proximity or neighbourhood (derived from the reasonable contemplation from one that his careness would cause loss to the other.) Afterwards, a two stage test was developed: firstly one should assert there is proximity, secondly when there is proximity a presumption is raised for the existence of the corresponding duty (and may be rebutted provided that there is a valid justification, namely of public policy). The 1985 decision established the opposite rule: a duty doesn't exist, unless there is a valid justification. One may say that the presumption was reversed.

Ultimately, in *Stovin v Wise* [1996][27], the Court through Lord Hoffmann's speech considers:

> "*The trend of authorities has been to discourage the assumption that anyone who suffers loss is* prima facie *entitled to compensation from a person (preferably insured or a public authority) whose act or omission can be said to have caused it. The default position is that he is not.*"

In as so much, the tort of negligence has evolved through a number of periods: the establishment of a tort of negligence, the establishment of a duty of care and the containment of the duty of care.

II.1.2 – Towards *neminem laedere* ?

The tort of negligence has been broadened to such an extent that the question "Has English Law Become more French than French?" – posed by Malcom Clark – could be imported into this domain. In fact, one may question: Does the tort of negligence represent a step closer to the *neminem laedere* principle (which inspired the French general liability clause under article 1382 of the Civil Code)?

[27] See also Murphy v Brentwood District Council (1991), which expressly considered Anns v Merton London Borough Council not in accordance with the Law.

This even closer relationship between the different liability systems is best described by Sacco (Piezzorusso & alli, 1992) in an anecdotal style:

> *"[For the Frenchman] compensation is certainly due,* because every act *whatever of man which causes damage to others imposes an obligation for compensation on the person because of whom the damage has been caused."*
> *"The German does not agree. It is not possible that every culpable act should bind you legally. The obligation arises from the culpable, illegal injury of the absolute right of the victim. (...)"*
> *"The Englishman does not understand this doctrine of absolute rights. Responsibility operates when you commit one of the specific wrongs laid down by law (...)".*
> *"[In the end,]* ***the empirical solutions are largely uniform****. The French judge, when condemning takes inspiration from* tout fait quelconque *and when absolving resorts to the doctrine of* les causes de justification*. The German judge, when condemning, always finds a paragraph in the code that legalizes the sanction, and when absolving recalls without any problem the lawfulness of acts not prohibited.* ***In England ever wider applications of the tort of negligence allow to neutralize the typicalness of actions based on responsibility* ex delicto**." (Emphasis added)

II.1.3 – Have intentional torts become obsolete?

The vast majority of the judicial decisions under English law awarding damages are based on the Tort of Negligence. This may lead to the aforesaid question: "have intentional torts become obsolete?" The question derives from the broadening of the Tort of Negligence.

If the Tort of Negligence were to become the English equivalent to the *neminem laedere* principle (as addressed supra), then such tort would encompass the actions causing damages in general. In such case, actions causing damages in general would fall within the scope of negligence and some would also – at the same time - fall within the scope of other specific torts (namely the intentional torts). Under those circumstances, the tort of negligence would prevail and render all others obsolete in as much as it would be easier to claim compensation under negligence.

First and foremost, the tort of negligence did not become the English equivalent to the *neminem laedere* principle. Two main aspects apparently restrain negligence from becoming so: i) the concept of proximity; ii) the need for justification in terms of public policy. Yet, the main reason for not becoming so is the judges' will, as expressed in *Stovin v Wise* [1996] (quoted above). In fact, both proximity and public policy are grey areas, undetermined concepts, which need to be fulfilled through judicial interpretation. This means that proximity and public policy could be interpreted as to generate a *neminem laedere* principle, but they are not. In particular a judge, when determining what public policy is (or should be), can argue that the adequate public policy is *neminem laedere* or can argue the opposite. In the end, judges are making the law along the way and are making public policy themselves (rather then interpreting or applying a public policy set forward through the political institutions).

Secondly, it must be strengthened that plaintiffs have more often invoked negligence since on intentional torts an additional element must be proven: intention. The importance of intention in the so-called intentional torts (contrary to what may seem) is a somewhat recent evolution of the law. As Street aptly states: "*Early common layers were not especially interested in the mental state of the defendant. They were satisfied to ask whether the defendant had directly inflicted on the claimant the harm complained of.*" This understanding of early common lawyers was most notably repelled in *Fowler v Lanning* [1959] (clarified by *Letang v Cooper* [1965]). Still, it was not without difficulty that such concept of "intention" was developed. On the one hand it was clear that when the defendant had wished to inflict the damage upon the plaintiff we were within the scope of "intention". And it was equally clear that purely involuntary acts were outside its scope. While, on the other hand, the issue of voluntary acts with unwanted results wasn't of simple answer.

Thirdly, while the torts of negligence evolved into a unified tort of negligence, the intentional torts remained distinct, with separate scopes and without systematically covering the field of intentionally caused damages.

Fourthly, the way English tort law evolved lead to a paradox: intentionally caused damages may be within the scope of the tort of negligence. An intentional action can be under the proximity and public policy restraints of negligence. And, it should be noted that while intentional torts require intention, the tort of negligence doesn't require negligence itself – an intentional act can be found to be within its scope. In fact, the tort of negligence started has a residual category and it is now the most used tort. In extremis, an intentional action can be within the scope of the tort of negligence but do not correspond to any of the set intentional torts.

Fifth, the statistical data stating that most tort law actions are based on the tort of negligence can be explained by one last feature. The fact that the law regarding the tort of negligence is far more unclear than the law regarding intentional torts may also cause greater litigation regarding the former. Such statistical data shows which cases appear more before the courts, but doesn't tell us which ones enable more damages recovery in every day life.

II.1.4 – Pure economic loss in the Tort of Negligence

The distinctive character of pure economic loss, even within the realm of the tort of negligence has been pointed out – creating a special legal regime. The distinction was most notably stated by Lord Bridge in *Caparo Industries plc v Dickman* [1990]:

> "*One of the most important distinctions always to be observed lies in the law's essentially different approach to the different kinds of damage which one party may have suffered in consequence of the acts or omissions of another. It is one thing to owe a duty to avoid causing injury to the person or property of others. It is quite another to avoid causing others to suffer purely economic loss.*"

The issue raised is: when is there a duty to safeguard against pure economic loss? The restrictiveness courts imposed on the tort of negligence is of particular importance in this field. By 1985, Lord Fraser stated in *The Mineral Transporter* case that "*some limit or control mechanism has to be imposed on the liability of a wrongdoer towards those who have suffered economic damage as a consequence of his negligence*".

The most notable decision in respect for pure economic loss was rendered as early as 1964. In *Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1964], Lord Morris of Borth-Y-Gest holds that:

> "***I consider that it follows and that it should now be regarded as settled that if someone possessed of a special skill undertakes, quite irrespective of contract, to apply that skill for the assistance of another person who relies upon such skill, a duty of care will arise****. The fact that the service is to be given by means of or by the instrumentality of words can make no difference. Furthermore, if in a sphere in which a person is so placed that others could reasonably rely upon his judgment or his skill or upon his ability to make careful inquiry, a person takes it upon himself to give information or advice to, or allows his information or advice to be passed on to, another person who, as he knows or should know, will place reliance upon it, then a duty of care will arise.*" (Emphasis added)

As is clear from the above quoted speech by Lord Morris of Borth-Y-Gest, in that case the court not just recognized the duty to avoid careless statements by those who posses special skills and apply such skills by given statements to assist others – that is to say, the court not just recognized a duty of care in issuing professional opinions. Indeed, the court acknowledged a broad duty of care in special skill undertakings in relation to those in whose assistance the undertaking was conducted and whom relied on such undertaking – that is to say, the court acknowledged a broad duty of care in professional activities for those at whom they were directed.

Following *Hedley Byrne & Co Ltd v Heller & Partners Ltd* [1964] the way for extending the tort of negligence to pure economic loss had been paved as above mentioned. Still, such extension only received subsequent judicial recognition in *White v Jones* [1995] – which became the milestone of the extension of the so called Hedley Byrne principle, more than 30 years after the Hedley Byrne case itself.

White v Jones has the following factual background: Mr White asked Mr Jones (a solicitor) to draft his will. When he initially did so, Mr White and his daughters were upset with each other. As a result, Mr White asked Mr Jones to cut them out of the will. Before Mr White's death, he and his daughters resolved the pending issues between. Subsequently, Mr White asked Mr Jones to reinstate them in his will, awarding tem £9000. Until his death, Mr Jones didn't follow Mr White's last instruction.

Could the daughters recover from Mr Jones?

Several issues could be raised. First of all, in relation to pure economic loss, one may ask: was there any loss? Is it really a loss? Can someone lose something even before acquiring it? The answer relies in contemplating what was lost. The £9000 weren't theirs, so they couldn't be lost. Yet, there was an expectation to acquire the £9000 and the loss is the non-fulfillment of such expectation.

This leads us to the second question: Should every expectation be protected under the law, namely under tortious law? The answer is in the negative, otherwise there would be liability towards an indefinite number of people, for an indefinite type of actions, amounting to an indefinite compensation. On the one hand, there are cases in which simple expectations shouldn't be protected; on the other hand, there are cases in which it would be extremely unjust not to protect. In this case, Lord Goff refers to the "*impulse to do practical justice*". Yet, "*justice*" as a subjective concept would hardly become a reliable legal criterion. Thus, according to Lord Goff, "*there is a lacuna in the law, in the sense that practical justice requires that the disappointed beneficiary should have a remedy against the testator's solicitor in circumstances in which neither the testator nor his estate has in law suffered a loss*".

Lorenz, referring to similar factual circumstances, considered "*this is a situation which comes very close to the cases of 'transferred loss', the only difference being that the damage due to the solicitor's negligence could never have been caused to the testator or to his executor*"[28] (Professor Lorenz in Essays in Memory of Professor F H Lawson p 90).

The solution adopted rests in Lord Goff's speech:

> "*In my opinion, therefore, your Lordships' House should in cases such as these extend to the intended beneficiary a remedy under the Hedley Byrne principle by holding that the assumption of responsibility by the solicitor towards his client should be held in law to extend to the intended beneficiary who (as the solicitor can reasonably foresee) may, as a result of the solicitor's negligence, be deprived of his intended legacy in circumstances in which neither the testator nor his estate will have a remedy against the solicitor.*"

Several teachings can be extracted from *White v Jones*, namely:

a) the existence of a contract on the matter (between the defendant and a third party – the testator) didn't prevent the applicability of tort law remedies; that is, the privity of contract doesn't exclude tortious liability;

b) a duty in tort can arise (irrespectively of contract) when there is a special relationship between the parties;

c) a special relationship, within this context, arises when the defendant assumes responsibility for performing a particular task knowing and accepting others' economic welfare depends on the careful execution of the task[29]

[28] (Merkin & alli, 1986, pag 90)
[29] It should be noted that reliance is not an essential condition for a relationship to arise.

The extension of the Hedley Byrne principle was latter consolidated in Williams v Natural Life Health Foods Ltd [1998]. Lord Steyn in his speech (unanimously uphold) synthesized the law as follows:

> "*The extended Hedley Byrne principle is the rationalisation or technique adopted by English law to provide a remedy for the recovery of damages in respect of economic loss caused by the negligent performance of services. Secondly, it was established that once a case is identified as falling within the extended Hedley Byrne principle, there is no need to embark on any further inquiry whether it is "fair, just and reasonable" to impose liability for economic loss. Thirdly, and applying Hedley Byrne, it was made clear that "reliance upon [the assumption of responsibility] by the other party will be necessary to establish a cause of action (because otherwise the negligence will have no causative effect)." Fourthly, it was held that the existence of a contractual duty of care between the parties does not preclude the concurrence of a tort duty in the same respect.*"

The somewhat complementary role of the tort of negligence, expanding to overcome the shortcomings of contract law and of other specific torts, was to become even clearer in *Kapfunde v Abbey National plc* [1999]. In this case, an employee made an inaccurate reference in relation to his employer, which caused the latter damages. Though the tort of defamation is clearly established, it requires malice to be proven – which is extremely difficult. As such, redress was obtained through the tort of negligence, most notably the Hedley Byrne principle.

Still, the Hedley Byrne principle - through its formulation - leaved outside its scope many cases of economic loss. To a great extent, it is a matter of public policy to define how far should recovery be allowed. With the Hedley Byrne principle the possibility to recover damages was extended when there was a special relationship and within a strict causality link. Was this enough to address adequately the economic loss issue under the tort of negligence?

Apart from Hedley Byrne, the House of Lords was called adjudge the applicability of the Anns v Merton London Borough Council doctrine (the duty of care test refered supra) to cases of pure economic loss. Most notably, in Murphy v Brentwood District Council (1991), Lord Keith of Kinkel considered:

> "*It being recognised that the nature of the loss held to be recoverable in Anns was pure economic loss, the next point for examination is whether the avoidance of loss of that nature fell within the scope of any duty of care owed to the plaintiffs by the local authority. On the basis of the law as it stood at the time of the decision the answer to that question must be in the negative. The right to recover for pure economic loss, not flowing from physical injury, did not then extend beyond the situation where the Joss had been sustained through reliance on negligent mis-statements, as in Hedley Byrne."*

Whether Anns v Merton London Borough Council was or not a pure economic loss is a complex debate, though it is clear that it no longer remains the standart for establishing the existence of a duty of care both for physical and pure economic loss. In addition, the proximity requirement is judicially interpreted far more strictly in cases of pure economic loss. The above quoted Lord Keith's speech limits proximity in cases of pure economic loss to the Hedley Byrne principle.

Lord Keith's view excessive strictness is correct by Lord … speech in the same case. Lord – although generally concurring Lord Keith's speech considers:

> "*There may, of course, be situations where, even in the absence of contract, there is a special relationship of proximity (...) which is sufficiently akin to contract to introduce the element of reliance so that the scope of the duty of care (...) is wide enough to embrace purely economic loss. The decision in Junior Books Ltd v. Veitchi Co. Ltd. [1983] 1 A.C. 520 can, I believe, only be understood on this basis*."

II.1.5 – Tort of Negligence: an answer to transferred loss?

Despite the major steps that English courts have taken to encompass pure economic loss, the tort of negligence's scope is still unclear[30]. No specific rules have been recognized in Tort Law regarding transferred loss.

Yet, specific transferred loss cases may eventually be adressed under the tort of negligence within the liability for negligent misstatements[31], the liability for negligent performance of a service[32], the liability for negligence in case of defects in buildings and products[33] and liability for relational economic loss arising from damage to a third party's property[34] .

In Markesinis and Deakins Tort Law[35] it is stated that the Contracts (Rights of Third Parties) Act 1999 and the *Panatown*[36] case may cause a further reshapment of tort law. Such reshapment could provide new answers in the field of transferred loss. Tort and Contract law are two complementary system, so changes in one may be followed by changes in the other. Deakin, Johnson, & Markesinis in expecting *Panatown* to produce changes in Tort law are expecting transferred loss to be also equated in Tort law, as happened in Germany[37].

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[30] (Deakin, Johnson, & Markesinis, 2008, pags 157-198)
[31] (Hedley Byrne & Co Ltd v Heller & Partners Ltd, 1964)
[32] (Henderson v Merrett Syndicates Ltd, 1994)
[33] (Murphy v Brentwood District Council, 1991)
[34] (Leigh and Sillavan Ltd v Aliakmon Shipping Co Ltd , 1986) (Owners of cargo lately laden on board the ship or vessel "Starsin" and others v. Owners and/or demise charterers of the ship or vessel "Starsin", 2003)
[35] (Deakin, Johnson, & Markesinis, 2008, pag 198)
[36] (Alfred McAlpine Construction Lta v Panatown Ltd, 1998)
[37] See chapter I.4

II.2 – Third party's contract claims

II.2.1 – The types of third party's contract claims

Third party's contract claims could represent a solution to the transferred loss problem, provided that the cases in which such problem arises could be within the scope of admissible third party's contract claims. Under this heading, two types of third party's contract claims will be considered: the contract for the benefit of a third party and the contract with protective effects towards third parties.

The contract for the benefit of a third party is one by which the contractors create a primary obligation owed to a third party; while contract with protective effect is one by which the contractors create a secondary obligation owed to a third party. In the former, the third party is the recipient of the obligation owed. In the latter, the third party is the recipient of protective duties, becoming part of the relationship without being owed any primary obligation, but being able to rely on its adequate performance.

II.2.2 – The contract for the benefit of a third party

The concept of contract for the benefit of a third party was long debated both in civil and common law jurisdictions. In civil law the contract for the benefit of a third party was largely implemented in the XIX century codification. While in English law the contract for the benefit of a third party only definitely emerged through the Contract (Rights of Third Parties) Act of 1999.

As mentioned supra, the late acceptance of the contract for the benefit of a third party in English law as due to the rigid interpretation of the privity doctrine, while civil law departed earlier from the Roman law principle *res inter alios acta nec nocet nec prodest* (a matter between others does not arm nor benefit) - since a matter between others may now benefit provided certain conditions are met.
Still, as addressed supra in relation to the qualifications to the doctrine of privity, several legal constructions over time have been tried to overcome the rigid

interpretation of the privity doctrine. For their importance, the agency reasoning, the constructive tort and section 56(1) of the Law of Property Act 1925 must once again be mentioned.

Nowadays in English law, the conditions for third party claims in contract are established under section 1 of the Contract (Rights of Third Parties) Act: i) the contract expressly provides that the third party may enforce a term of the contract; or ii) the term purports to confer a benefit to the third party, unless if on a proper construction of the contract it appears that the parties did not intend the term to be enforceable by the third party.

As such, when the terms of a contract don't expressly provide their enforceability by a third party, the enforceability test under section 1, designed by the Law Commission, provides that: i) when it is shown that the contract "purports to confer a benefit" a presumption of third party enforceability is raised; ii) such presumption may be rebutted taking into account the apparent intention of the parties on a proper construction of the contract. Still, according to the Law Comission, "express designation by name, class or description is a necessary but not a sufficient condition for raising the rebuttable presumption"[38] [39].

Hence, many cases which would fall into the category of transferred loss are excluded from the scope of the Contract (Rights of Third Parties) Act. In addition, paragraph 6 provides that contracts from a number of fields are excluded from the scope of section 1, namely those related to promissory notes, employment and goods' carriage.

In the cases emerging within the scope of the Contract (Rights of Third Parties) Act, there is now legal ground to prevent the situation in which the person who had suffered the loss could not sue, while the person who had suffered no loss could sue. Yet,

[38] (Law Commission Report N.º 242 (1996), para. 7.18)

[39] The Law Comission's reports relevance in interpreting statutory law as been recognised in Pepper v Hart [1993]

transferred loss doesn't only emerge when the parties intend to confer a benefit to a third party and most certainly doesn't only emerge within the enforceability test.

II.2.3 – The contract with protective effects towards third parties

The acceptance of the contract with protective effects towards third parties would represent an alternative for recovery. In relation to such contracts three main issues should be taken into consideration: i) the concept of such contracts; ii) the scope of contracts with protective effects towards third parties is much broader than that of transferred loss; iii) the restrictive approach to contracts for the benefit of a third party has deep impacts in the admissibility of contracts with protective effects towards third parties.

The concept of contract with protective effects towards third parties has its roots in a BGH (German Supreme Court) decision of April 25th, 1956. In such case, a machine was sold to a factory. Such machine was dangerous and one of the factory employees was injured. Such employee directly sued the machine manufacturer. The Court considered that when selling such machine the parties were aware that the machine was going to be used by third parties and extended the benefit of the contractual protective duties to them. Larenz considers this to have been a major step in the fields of protective duties and good-faith[40]. According to Kannowski, German case law has been inconsistent by deriving such protective effects either from an objective duty of good faith, either from the interpretation of the parties will[41].

A major distinction must be draw between contracts with protective effects towards third parties and transferred loss. The first protect the third party' own interest, while the second only protects the interest that was transferred from one of the contract's party to the third party. This type of contract subjects the obligor to a greater liability, encompassing the liability of the party and of the third party in their specific interests. On the contrary, transferred loss is aimed at cases in which the obligor is subject to

[40] (Larenz, 2002)

[41] (Kannowski)

liability for the party's interest, which was later transferred – so conceptually there is no greater liability, simply transferred liability.

The recognition of contracts with protective effects towards third parties would provide an answer to most transferred loss cases, is as much as the interest that had been transferred to the third party could be protected. However, the strict legal framework in which the contract for the benefit of a third party was accepted, renders the acceptability of contracts with protective effects towards third parties extremely unlikely. The case for contracts with protective effects towards third parties would be extremely difficult to uphold since in such case no primary obligation is owed to the parties.

III - Transferred loss in English law

III.1 – Early developments

III.1.1 – Early developments in the XVIII and XIX centuries

One of the fields in which the transferred loss problem arose was transportation, namely regarding the liability of carriers. In fact, the law of carriage of goods had soon to deal with the issue of transferred loss because the series of interrelated contracts often existing.

Firstly, it should be noted that the nature of carrier's liability was highly debated. The common carriers' liability had been held either as *ex contractu* or *ex delicto*. And, often courts would adjudicate on the matter without establishing any distinction whatsoever.

In this context the *Davis and Jordan v James* [1770] case emerged. In such case, consignors sued the common carrier for not delivering the goods. Naturally, the common carrier objected by claiming that the action had to be brought by the consignee. Yet, the court considered that the action had been properly brought since the agreement had been made between the plaintiff and the defendant – and the former were to pay to the latter. By considering that the action had been properly brought, the court departed from the proposition according to which property and contract had to coincide. This means that in the *Davis and Jordan v James* case the contract alone provided basis for liability. Another case, *Moore v. Wilson* – though poorly reported – seems to be based on similar grounds. In the end, in both cases, the consignor was allowed recovery although he was not the owner of the goods.

Though many conceptual issues were not expressly addressed in those judgments, there are two underlying considerations: 1) there was *ex contractu* liability of common carriers, 2) a different concept of loss was taken into account.

Both cases were later addressed in *Dawes v Peck*. In this case the court – purporting a strict interpretation - considered those judgments had been based on "special" or "particular" agreements between the parties, because there was a warranty to safely carry the goods.

Afterwards, the transferred loss problem was yet given another conceptual framework in *Joseph v Knox* [1813]. Lord Ellenborough rendered the following speech:

> "*There is a privity of contract established between these parties by means of the bill of lading. That states that the goods were shipped by the plaintiffs, and that the freight for them was paid by the plaintiffs in London. To the plaintiffs, therefore, from whom the consideration moves, and to whom the promise is made, the defendant is liable for the non-delivery of the goods. After such a bill of lading has been signed by his agent, he cannot say to the shippers they have no interest in the goods, and are not damnified by his breach of contract. I think the plaintiffs are entitled to recover the value of the goods, and they will hold the sum recovered as trustees for the real owner*."

The set of cases quoted above from the XVIII and XIX centuries are based on various legal doctrines regarding transferred loss which are still under debate. The Davis and Jordan v James (1770), Moore v. Wilson and Joseph v Knox (1813) cases, though providing answers to the transferred loss problem, were not part of a uniform precedent. On the contrary, such cases can be regarded truly as exceptions to the standard legal answer.

III.1.2 – A judicial landmark in the XIX century

In considering the early developments of transferred loss, a Scottish case deserves even greater attention because of how it inspired later judgments: the *Dunlop v. Lambert* (1839) case. Dunlop shipped a puncheon of whisky deliverable to Mr Robson[42].

[42] The first puncheon was destroyed during the shipment due to bad weather and a second puncheon was shipped at no cost.

The first issue dealt was the contract between seller and buyer. As Lord Cottenham LC asserted, the general rule was that delivery to the carrier amounted to delivery to the consignee, unless there was a particular[43] contract between consignor and consignee.

The second issue dealt was the contract between consignor and carrier. In this domain, in order to allow the carrier to be liable, the rule in *Dunlop v Lambert* emerged:

> "*These authorities, therefore, my Lords, established these propositions: that although, generally speaking, where there is a delivery to a carrier to deliver to a consignee,the consignee is the proper person to bring the action against the carrier if they should be lost; yet the consignor may have a right to sue if he made a special contract with the carrier (...) which special contract supersedes the necessity of showing ownership in the goods; and by authority of Davis v James (5 Burr 2680), and the last case of Joseph v Knox (3 Camp 320), that the consignor is enabled to maintain an action, though the goods may the goods of the consignee*".

III.1.3 – A statutory landmark in the XIX century

The uncertainty relating to the judicial precedent in the English law in this matter led to the Bills of Lading Act 1855. Section 1 of the Act provides that:

> "*Every consignee of goods named in a bill of lading and every endorsee of a bill of lading of a bill of lading to whom the property in the goods therein mentioned shall pass, upon or by reason of such consignment or endorsement, shall have transferred and vested in him all rights of suit, and be subject to the same liabilities in respect of such goods, as if the contract contained in the bill of lading had been made with himself.*"

[43] The precise wording of Lord Cottenham's speech was "*special contract*". Nonetheless, the expression "*special contract*" has a different specific technical sense, so it should not be used. (Unberath, 2003, pag 106)

This section became the governing rule in this matter – upon which the case law was rewritten. The bill – in providing remedy in cases of third party loss (not all, but most) – ruptures with the standard understanding of privity. Consequently, such rupture also departs from compromise solutions as the reasoning adopted in *Joseph v Knox (1813)*.

Paradoxically, the Bill that was enacted as a solution to the shortcomings of privity, was later crystallized with its own shortcomings[44].

[44] Adewale A. Olawoyin considers it a phanton to the current law in Nigeria. (Olawoyin, 2004)

III.2 – The Albazero principle

In *Albacruz (Cargo Owners) v Albazero (Owners)* [1977], commonly known as *The Albazero* [1977] the House of Lords acknowledged a small revolution in the field of transferred loss.

The plaintiffs time chartered the Albacruz ship to transport crude oil in bulk. The crude oil had been bought by the plaintiffs FOB[45] and had been sold CIF[46]. As such, under CIF, the plaintiffs delivered when the goods were shipped – so it was for the buyer to bear the risk of loss or of damage to the goods.

The Albacruz ship sank and the cargo was completely lost. A bill of lading had been issued to them as shippers in respect of the cargo pursuant to the charterparty and was endorsed to the buyers the day before the ship sank.

The plaintiffs sued arguing there was a breach of the charterparty. Consequently, the defendants claimed the property of the cargo had passed to the CIF buyers, so the plaintiffs had suffered no loss. Additionally, the buyers could no longer bring themselves an action under the bill of lading since it was already time-barred.

III.2.1 – The Court of Appeal

a) The issue of property

[45] FOB stands for "Free On Board", which means "*that the seller delivers when the goods pass the ship's rail at the named port of shipment. This means that the buyer has to bear all costs and risks of loss of or damage to the goods from that point. The FOB term requires the seller to clear the goods for export. This term can be used only for sea or inland waterway transport. If the parties do not intend to deliver the goods across the ship's rail, the FCA term should be used*". (ICC, 2010)

[46] CIF stands for "Cost, Insurance and freight", which means "*that the seller delivers when the goods pass the ship's rail in the port of shipment. The seller must pay the cost and freight necessary to bring the goods to the named port of destination BUT the risk of loss of or damage to the goods, as well as any additional costs due to events occurring after the time of delivery, are transferred from the seller to the buyer. However, in CIF the seller also has to procure marine insurance against the buyer's risk of loss of or damage to the goods during the carriage. Consequently, the seller contracts for insurance and pays the insurance premium. The buyer should note that under the CIF term the seller in required to obtain insurance only on minimum cover. Should the buyer wish to have the protection of greater cover, he would either need to agree as much expressly with the seller or to make his own extra insurance arrangements. The CIF term requires the seller to clear the goods for export. This term can be used only for sea and inland waterway transport*". (ICC, 2010b)

The court reminded that normally under a CIF contract, the property is only transferred when both the shipping documents are received and the price has been paid. The purpose of which is to secure the payment of the goods.

Since the Court found that in this case the buyer and the seller were associated companies, it wouldn't have been necessary for the seller (the current plaintiff) to reserve the right of disposal to secure payment of the price. Therefore, both property and risk were transferred from the seller to the buyer the day before the ship sank, through the endorsement of the bill of lading, irrespectively of payment.

b) The consignor's right to recover damages

More surprisingly, Brandon J and later the Court of Appeal, concluded that existing case law could be construed has to allow the consignor's right to recover damages even when it no longer has any proprietary interest in the goods.

In fact, nineteenth century case law had acknowledged that the consignor could have the right to recover substantial damages despite lacking proprietary interest, provided a "*special contract*" between the consignor and the carrier could be construed[47]. Brandon J and the Court of Appeal were calling upon, and eventually extending, *Dunlop v Lambert*[48].

The Court of Appeal's judgment was influenced, according to Ormrod LJ's speech, by the fact that not to consider the Dunlop v Lambert rule applicable would allow the defendants to "*escape liability on what on the facts of this case is the merest technicality*".

III.2.2 – The House Of Lords

[47] Compare with *Mead v South Eastern Railway Co (1870)*
[48] (Dunlop v. Lambert, 1839)

a) Rationalization of the “*special contract*”

The House of Lords, adhering to Lord Diplock’s speech, further developed and rationalized the grounds on which the lower courts had concluded that the consignor might be allowed to recover damages irrespectively of any proprietary interest in the goods.

It is understood from Lord Diplock’s speech that the concept of “special contract” ought to be abandoned as it remained a vestige with procedural connotations of the long abolished forms of action. As such the concept of “special contract” should give place to the intention of the parties to allow recovery for damages on behalf of a third party.

In Lord Diplock’s own words:

> “*The only way in which I find it possible to rationalize the rule in Dunlop v Lambert so that it may fit into the pattern of English law is to treat it as an application of the principle, accepted also in relation to policies of insurance upon goods, that in a commercial contract concerning goods where it is in the contemplation of the parties that the proprietary interest in the goods may be transferred from one owner to another after the contract has been entered into and before the breach which causes loss or damage to the goods, an original party to the contract, if such be the intention of them both, is to be treated in law as having entered into the* ***contract for the benefit of all persons who have or may acquire an interest in the goods before they are lost or damaged, and is entitled to recover by way of damages for breach of contract the actual loss sustained by those for whose benefit the contract in entered into***.” (Emphasis added).

b) Direct third party rights

Taking into consideration that such *contract for the benefit of all persons* emerged from the intention of the parties, Lord Diplock also concluded that there was no sensible business reason for the transporter to accept liability for the same damage to both the consignor and the consignee. In as much, "*where there are two contracts with the carrier covering the same carriage and under one of them there is privity of contract between the person who actually sustains the loss and the carrier*".

Furthermore, under the reasoning of Lord Diplock, a consignor's right to recover damages couldn't be construed as to surpass the time-bar prescribed by the Bills of Lading Act 1855 – which prevented the consignee himself from recovering damages.

III.3 – Panatown: A new beginning

III.3.1 – Precedents in construction law

In the twentieth century a series of cases in the field of construction law have questioned the scope of the Albazero principle, paving the way for *Alfred McAlpine Construction Lta v Panatown Ltd*. The following cases are of special importance to understanding the evolution of transferred loss in English Law: *Linden Gardens Trust Ltd* [1992], *St Martins Property Corporation Ltd v Sir Robert McAlpine Ltd* [1992], *Darlington BC v Wiltshier Northern Ltd* [1995].

a) Linden Gardens and St Martins cases

This two cases were heard together by the House of Lords. In the first (Linden Gardens[49]) the property was transferred after the breach of the contract in relation to such property. In the second (St Martins[50]), the property was transferred before the breach of the contract in relation to such property.

In St Martins the original contracting party judicially claimed compensation. Two alternative conceptual paths to recovery emerged: the so called “narrow ground” and the so called “broad ground”.

According to Lord Griffiths, applying the “broad ground” of recovery, the plaintiffy could recover because it had sustained the loss the itself. The “broad ground” of recovery became the doctrine according to which, in case of default of contractual obligations, the contracting party suffers a nominal loss in the value of the non-performed obligation – even though no proprietary interest was damaged. As such, under the “broad ground” of recovery, loss isn’t the value of the unperformed benefit, but the value of the performance itself. As a result, even though the contract brings a

[49] (Linden Gardens Trust Ltd, 1992)
[50] (St Martins Property Corporation Ltd v Sir Robert McAlpine Ltd, 1992)

benefit to a third party, in case of default there is a loss to the contracting party, as what it paid for wasn't performed.

On the contrary, Lord Brown-Wilkinson, Lord Keith and Lord Bridge of Harwhich, applying the "narrow ground", awarded compensation to the contracting party, though recognizing it had suffered no loss. As derives from the leading speech by Lord Brown-Wilkinson, the court followed the Albazero principle:

> "*[I]t could be foreseen that damages caused by a breach would cause loss to a latter owner and not merely to the original contracting party (...) McAlpine [the defendant] had specifically contracted that the rights under the building contract could not without McAlpine's consent be transferred to third parties who became owners or occupiers and might suffer loss. In such case, it seems to me proper, as in the case of the carriage of goods by land, to treat the parties as having entered into the contract on the footing that Corporation [the plaintiff] would be entitled to enforce contractual rights for the benefit of those who suffered from defective performance but who, under the terms of the contract, could not acquire any right to hold Mc Alpine liable for the breach.*"[51]

The above quote does indeed comprise an application of the Albazero principle in as much as it takes the intention of the parties as the ground to allow a contracting party to recover third party loss. Still, it should be noted that it includes a reference to foreseeablility, which was never explicitly referred in Lord Diplock's speech in Albazero (where the concept of "contemplation" was applied instead).

Furthermore, it is open for debate if such contract could in fact be derived from the intention of the parties or if I was simply the legal mechanism chosen by the Law Lords to fill a black hole and correct injustice. When a party to a contract restricts the assignment of rights to third parties is intention may very well be to limit its own liability, which would be contrary to allowing the other contracting party to claim the losses of others. In fact, under Lord Brown-Wilkinson speech it appears that an the intention to allow recovery for third parties (the intention to enter into a contract "for

[51] (St Martins Property Corporation Ltd v Sir Robert McAlpine Ltd, 1992)

the benefit" of third parties) derives from the foreseeability of third party loss – as if a presumption were raised.

As such, one must take into account that Lord Brown-Wilkinson reasoning was inspired from the fact that, if it weren't for the Albazero principle:

> "*neither of the plaintiffs has any right to substantial damages; [the current owner] has incurred damages (...) but has no cause of action; [the former owner] has a cause of action but has suffered no loss. If this is right, in the words of my noble and learned friend, Lord Keith of Kinkel (...) 'the claim to damages would disappear (...) into some legal black hole, so that the wrongdoer escaped scot-free.*"[52]

b) Darlington BC v Wiltshier Northern Ltd

A town council entered into a contract with a finance company, according to which the latter would arrange for a recreational center to be built in Darlington and the former would pay the sums falling under the building contract. In addition, a deed was entered into by the three parties (town council, finance company and construction company), giving the council direct contractual rights against the construction company for failure to complete the construction on time.

After the construction had been completed, the council filled an action against the construction company for defective building, due to bad workmanship. Two separate conceptual paths for recovery were considered by the House of Lords: constructive trust and the Albazero principle.

Dillon LJ considered that the finance company was a constructive trustee for the council of the benefit of any rights under or for the breach of the building contract – being, as such, analogous to Lloyd's v Harper. The other members of the high court found it difficult to accept Dillon LJ's reasoning in this case because in parallel to such contract

52 (St Martins Property Corporation Ltd v Sir Robert McAlpine Ltd, 1992)

there was a tripartite deed. Thus, it can be argued that if the finance company was acting as a trustee, then there would be no need for the council to take directly part in the deed.

As a result, the Law Lords turned to the following question: can the Dunlop v Lambert rule, as rationalized in the Albazero principle and eventually extended through St Martins be applicable in this case? Another difficulty rose in answering this question. It this case no contractual or proprietary rights had shifted between the contracting party and the relevant third party. The contracting party never had a proprietary interest in the construction which had been developed. In answering the question, the House of Lords concluded that the foreseeablity test had been met (it was obvious that the building was being constructed for the benefit of the council) and the lack of proprietary interest from the out set wasn’t a compelling objection. According to Steyn LJ this would be a limited and conservative extension of the Albazero principle.

c) Bovis

The facts of this case, according to Staughton LJ, constitute “*a tangled web of complications*”. The site owners employed developers to carry out a large residential development. The owners and developers are associated companies. The developers entered into construction management agreements with the managers, by which the latter would supervise the development. The developers contracted a loan from a syndicate of banks, though a finance company acting as agent. The developer’s rights were assigned to the finance company. In due time, shire had been repaid and the rights were reassigned to the developers.

The managers filled an action against the developers, claiming the payment of fees and disbursements. The developers counterclaimed for breach of contract, delay and causing increased expense.

Did the developers suffer any loss despite the delay and increased expense? On the one hand, the developers did not have any proprietary interest in the land. On the other hand, the developers were reimbursed under the contract with the land owners of theirs costs. Even if considering the developers had suffered loss, could the developers recover damages when at the time of breach the cause of action was assigned to the finance company and the finance company had suffered no loss?

Millett LJ solved the problem of an "*apparent separation of loss and remedy*"[53] through the application of agency law principles. According to such analogy, the damages were hold on trust for the "*principals*".

III.3.2 – The Panatown case

a) The facts

UIPL owned a land where it intended to develop a building. For tax reasons, Panatown (a company from the same group) employed McAlpine to develop such building. Panatown received the funds for the construction from the parent company and its main obligation was to enter into a building contract with a construction company (McAlpine). In addition, McAlpine entered into a Duty of Care Deed with UIPL, under which the building owner acquired a direct remedy against the construction company for failure to exercise reasonable skill and care under the building contract.

After McAlpine completed the construction, the building was found to be defective and required significant repair work, Panatown filled an action claiming compensation for breaches of the building contract by McAlpine, due to defective work and delay.

b) The Court of Appeal

Several key legal issues were discussed in Panatown. First and foremost it was questioned if a general rule under which the plaintiff could only claim his/hers own loss did really exist. The plaintiff quoted Mr Wallace and Prof Treitel[54], interpreting their words as denying such general rule. Lord Millett, accompanied by every other lordship

53 (Unberath, 2003, pag 202)
54 (Unberath, 2003, pag 207)

except Lord Goff[55], considered such general rule to be "*self-evident*". As Cairns LJ had referred in The Albazero, it is "*so fundamental to our law that nobody in this case has thought it necessary to cite authority for it*"[56].

Evans LJ speech reaffirms the general rule that third parties losses cannot be recovered, except if the parties to the contract so intended. As such, parties could agree to enhance the scope of contractually protected interests. It is a contractual approach to the narrow ground.

c) The House of Lords

The House of Lords took the opportunity to depart from the apparently intention based contract-approach of The Albazero and St Martins. As Lord Clyde expressed:

> "*In my view it is preferable to regard it as a solution imposed by the law and not as arising from the supposed intention of the parties, who may in reality not have applied their minds to the point.*"

In addition, Lord Clyde also accepted (*obiter dictum*) that foreseeability or contemplation of third party loss were unnecessary and, even more clearly, the narrow ground was irrespective of foreseeability. Lord Clyde's view was welcomed by Lord Jauncey and Lord Browne-Wilkinson only in as much as foreseeability or contemplation of third party loss still needed to be established.

In his speech, Lord Clyde, properly identified *Panatown* as a transferred loss case:

> "*What is there propounded is, as was noticed by my noble and learned friend Lord Goff of Chieveley in White v Jones [1995] 2 AC 207, 267, a case of transferred loss. This is not a situation where the loss that of the promise. It is a loss suffered by the third party but transferred to the promise who is then*

[55] Lord Goff criticises a too rigid interpretation of the principle and professes a solution to the transferred loss issue which is overall consistent with such general rule (the broad ground).

[56] (Albacruz (Cargo Owners) v Albazero (Owners), 1977)

accountable to the third party (...) The promise is deemed to have suffered the loss so that it is he and not the third party who is able to pursue the remedy in damages".[57]

III.3.3 – After Panatown

Following Panatown, English Courts have faced other cases in which the transferred loss issue has been put forward. Among such cases, two are most notably worth mentioning: the *John Harris Partnership v Groveworld* [1999] and the *And So to Bed v Dixon* [2000] case.

Regarding the first case, one may conclude from the decision by Judge Thornton that Panatown's reasoning is applicable to all services contracts[58]. More surprisingly, Judge Thorton considers – as obiter dicta – that "*Groveworld [the promisee] as an equitable obligation to pursue JRH [the obligor] for the loss caused to Frogmore [the third party] by JRH [the obligor] and a duty to account to Frogmore [the third party] for any recovery*". Accordingly, in cases of transferred loss, there would be not only a right to claim such third party loss, but an obligation to claim such loss[59]. It should be highlighted that such statement can hardly be regarded as a persuasive precedent, taking into consideration it is *obiter dicta* and was rendered by a lower court.

The second case is a remainder that law's evolution is a dialectic process. In the *And So to Bed v Dixon,* David Donaldson QC makes use of the intention based approach applied by Evans LJ in the Court of Appeal in Panatown, departing from the House of Lords' objective approach. Furthermore, David Donaldson QC provides a clear reminder that:

"*There are numerous situations in which C may foresseably suffer loss in consequence of the breach by B og his contract with A without C having a cause*

[57] (Alfred McAlpine Construction Lta v Panatown Ltd, 1998)
[58] (Jackson & Sutherland)
[59] (Unberath, 2003, pag 218)

of action against B, and it cannot be in every such case that even in a rational and coherent legal system it will be requisite that A should recover damages encompassing C's loss."[60]

[60] (And So to Bed v Dixon, 2000)

IV - From fragmentation to a general principle

IV.1 – Fragmentation of transferred loss

Transferred loss issues have not only been raised within several fields of law, but have been considered under different conceptual frameworks. On the one hand, transferred loss issues have arisen most notably in Transportation Law and Construction Law. On the other hand, the array of judicial answers to transferred loss includes considering there is no remedy, the so-called narrow ground and the so-called broad ground.

Not limited to transportation and construction law, transferred loss cases can also be identified in sale of goods cases (often related to transportation law cases), tenancy cases, services cases, among others. The specificity of transportation law (to be more precise, the carriage of goods) has been addressed *supra*, taking into account for instance the Bills of Lading Act 1855. The specificity of construction law lies frequently in existing collaterals. The specificity of tenancy cases is greatly summoned by policy reasons.

Therefore, not only in light of the fragmentation which is proper to a case-by-case precedent-forming judicial system, but also in light of such specificities, judicial answers to transferred loss have not been uniform.

Unberath[61] interprets tenancy cases, sale of goods cases and carriage of goods cases as having – within their own specificities – to have contributed to the broad road approach; while new developments in construction law have taken the narrow road. As we shall see infra, despite fragmentation, both approaches (broad and narrow) pave the way for a uniform answer.

[61] (Unberath, 2003, pag 36-51)

IV.2 – An apparent exception?

As we have seen, transferred loss initially appears as opposed to the doctrine of privity, eventually constituting an exception to such doctrine. On the one hand, privity is based on the assumption that, as a matter of fact, no one but the parties to a contract can benefit from its performance and suffer loss from its non-performance. On the other hand, the transferred loss debate is based on an apparently opposed assumption: the lack of performance of a contract may have effects outside the strict scope of the parties.

A question must be answered: When and why does the lack of performance affect third parties?

Firstly: the third party may simply rely on the performance, without any contractual relation to any of the parties to the main contract, which could still eventually indirectly contribute to its own undertakings, thus having an expectation. In such case, the lack of performance of the main contract may remotely contribute to a loss of the third party.

Secondly: the third party may have a contractual relation with one of the parties to the main contract, both contracts with related subject matters, thus having an indirect contractual relation. In such case, the lack of performance of the main contract could determine a loss of the third party.

The doctrine of privity is often presented as preventing compensation in both circumstances. As under a contract only the promisee could claim compensation and compensation could only be claimed for one’s loss, then the loss of third parties could not be compensated (except where it could fall within tort law). The main policy argument for so is the flood-gate argument: If compensation were to be allowed regarding third party loss, then contractual parties would face unlimited liability, for an unlimited time, towards an unlimited number of people.

In addition to specific qualifications to the privaty doctrine, two general paths (inspired from the recent developments of German law) have been: contracts with protective effects towards third parties or transferred loss (subdivided in two paths, narrow and broad).

The path of contracts with protective effects towards third parties could provide an answer to third party loss, both in cases of simple expectations and of indirect contractual relations – provided the third parties interest ought to be protected (being difficult to ascribe objective criteria in determining when should such protection be awarded). As we have seen, this path would be contrary to a recent development of the English law of contract: the Contracts (Rights of Third Parties) Acts 1999

The path of transferred loss is a common heading for several doctrinal solutions to a more specific problem: when a third party was harmed in an interest that had been transferred from the promisee, is as much as if the interest handn't been transferred, the loss would have been suffered by the promisee.

A legal answer to the third party loss issue is seen as contrary to legal principles and to legal policy mostly because it would imply an exponential increase of contractual liability, beyond the parties will, beyond the strict contractual scope and with unforeseen results. A legal answer to the transferred loss issue (which is a specific concept within the broader third party loss) may be considered as needed in light of the very same principles and policy, because otherwise contractual parties could be exempt from liability.

As such, instead of regarding transferred loss as opposed to privity, transferred loss may be understood as fulfilling the demands of privity. The doctrine of privity oughtn't be merely considered from the view point that third party cannot claim benefit (or compensation for non-performance) from the contract. By accepting the assertion that the performance or non-performance or defective performance of a contract is a matter between the parties only and third parties cannot claim compensation under a contract between others, then privity should also demand for liability to arise between the parties

– irrespectively of it having been transferred to third parties. If not, under privity, third party's acts would be considered in order to relieve the contractual party's liability, while the same acts would be discard to recognize the very same loss caused to a different subject.

This issue is at the heart of the distinction between the narrow and the broad road. The narrow road envisages a new principle (or an exception to privity, depending on its different formulations), while, the broad road makes use of a wide interpretation of privity itself. Generraly,under the broad road, the obligor is liable to the promissee for the cost of attaining the expected performance – irrespectively of the interests bearer.

In the end, is transferred loss truly an exception to the privity doctrine? No definite answer can be given for one simple reason: the several solutions put forward for the transferred loss problem lack a common core in this matter.

IV.3 – The building of a general principle

IV.3.1 – The narrow road and the Albazero principle

As we have seen, the narrow road is the ground for recovery that was authoritatively recognized in the Albazero case (though its routes can be traced back to a century earlier). Under the so-called Albazero principle, a contract can be deemed to be a contract for the benefit of all persons who have or may acquire an interest in the goods.

The narrow road brings the issue of transferred loss close to the debate regarding privity. In fact, the narrow road challenges the way how privity has been conceived and even surmounts the Third Party Rights act (perceived as the answer to the shortcomings of privity).

So far the issue of transferred loss had primarily been dealt by the Courts through the narrow road within the field of carriage of goods. As such, through the Bills of Lading Act, which provided a statutory answer to the transferred loss issue in the carriage of goods field, the narrow road had lost relevance.

The developments in construction law revived the narrow road. The leading speech in the Saint Martins case, by Lord Browne-Wilkinson, is clear in this matter: "*[I]t seems to me proper, as in the case of the carriage of goods by land, to treat the parties as having entered into the contract on the footing that (...) [one party] would be entitled to enforce contractual rights for the benefit of those who suffered from defective performance*".

IV.3.2 – From an intention based to an objective approach

The narrow road greatly evolved since it was judicially recognized as the Albazero principle. In Albazero a contractual approach was adopted in solving the transferred loss issue. Albazero's "*contract for the benefit of all persons who have or may acquire an interest in the goods*" is based on the parties' intention to acknowledge third party loss.

As we have seen through out the preceding chapters, English courts have had either overtly intention based approaches, either unclear approaches regarding the need to demonstrate the parties intentions. In this context, Panatown was a cornerstone in shifting towards an objective approach.

An intention based approach, requiring courts to determine whether the parties wanted third party damages to be compensated (or whether if they would have wanted so, in case they had considered the possibility of third party damages) relies in judicial interpretation. An objective approach operates through defined legal criteria, irrespectively of the parties will.

The answer is not yet definite, but there is a clear tendency for attaining an objective solution. For a case-by-case intention test approach, courts moved to a wider legal fiction and with Panatown an objective approach was attained.

This objective approach in which legally *loss suffered by the third party but transferred to the promise is then accountable to the third party* may have prevailed in Panatown due to the then existing court composition. This issue remains controversial and the current *stare decisis* may be overturned.

IV.3.3 – From fragmentation to a general principle

The fragmentation of transferred loss (that is to say, the emergence of transferred loss issues in determined fields of law, owing to specific circumstances), hasn't detained the Courts from gradually attempting to bring the several judicial decisions into a coherent system.

In fact, transferred loss was first clearly identified in the law of transportation – receiving a specific statutory answer. Yet, latter, when facing the very same conceptual problem under the different circumstances of a different field of law, English courts retained and enhanced the dogmatic framework which had been developed for transferred loss in the law of transportation, prior to the specific statutory answer.

Undeniably, the judicial and scholarly legal development of transferred loss has been chiefly conducted within the law of construction's field. The role of St Martins, Darlington and Panatown cases can hardly be over emphasized.

Still, the solutions judicially put forward for the transferred loss issue do not offer any conceptual resistance to their applicability in other fields of law. Whether one considers the parties actual or presumed intention to contractually encompass transferred loss, a standing legal fiction or an objective approach, nothing prevents their applicability in other fields.

Moreover, the legal reasoning adopted by English courts in this matter is formulated in general terms, so as to express general rules of law, not limited to the strict scope of a given law field. In light of the XXth century judicial development of the narrow road, the narrow road could arguably be interpreted as instituting a principle of transferred loss, irrespectively of how privity is to be construed.

Once again, taking into account the away how privity has been uphold, the flood-gate arguments, and overall the opposition transferred loss faces, this wide conception of a transferred loss principle risks being overturned.

IV.3.4 – An alternative route: extending the concept of loss

An alternative route exists and should not be promptly dismissed. Transferred loss issues are raised from the transfer of interest from the promisee to a third party, is as much as it is said that the loss for non-performance or defective performance is sustained by the third party. It is true that the financial loss is sustained by the third party. Ultimately, when the interest has been shifted, it is the third party that may be harmed.

Nevertheless, a broader concept of damages could be taken into account. The promisee has given consideration, owed in view of the obligor's performance. If the consideration is provided but there is no performance, then – has not only the obligor enriched[62] - the promise has lost. The performance itself as value. The lack of performance has a specific cost to it: to cost of having another render the expected performance or to repair the consequences of it having not been performed.

In this context, the "broad ground" of recovery is the doctrine according to which, in case of default of contractual obligations, the contracting party suffers a nominal loss in the value of the non-performed obligation – even though no proprietary interest was damaged.

This is the path purported by Lord Griffiths and, to some extent, Lord Goff – which was rejected in *Panatown*. As decided in *Panatown*, "*a breach of contract may cause loss but is not itself a loss in any meaningful sense*". As such, the courts have adopted a rather restrictive interpretation of the principle according to which damages for breach of contract should restore "*so far as money can do it (...) the same situation (...) as if the contract had been performed*".

It should be noted, however, that if such broad road were to be applied, it might not be as far reaching as a transferred loss principle, by not expressly addressing the third party and having as a reference the value of the performance.

[62] Which could ultimately even lead to a discussion on the applicability of an unjust enrichment regime.

V - Conclusion

The first conclusion to be drawn on this matter is the complexity of the transferred issue within the context of third party loss and the complexity of the existing legal framework. No legal study can be entertained regarding this subject without broadly encompassing the various fields of law (from tort to contract, from carriage of goods to construction law). In fact, transferred loss presents itself as a challenge to lawyers, in which legal paradigms and public policy are confronted, leading to an array of – hard to reconcile – answer.

Notwithstanding the importance of the subject and the enriching existing case-law, the topic has often remained under the scholar's radar. Several papers question the role of third party loss (and transferred loss) in each specific field of law, but rather few dwell into a comprehensive analysis. And among those, there is a perceived influence of German legal reasoning.

A second conclusion is related to the doctrine of privity. As it was shown, several qualifications to such doctrine are known and transferred loss cases may predate its clear establishment. Therefore, although it is an important doctrine in the English law of contract, solutions can be sought outside its strict scope and complementary principles may be developed or rediscovered.

Last, but not least, there are currently clear reasons to consider a transferred loss principle is emerging. One might dare – in light of recent judicial developments – to claim that following *Panatown* a general principle of transferred loss has emerged, reshaping English law in general. Yet, caution is advised. The development of law – and in particular the development of English law – is often a dialectic process. The English legal world has moved from a thesis of non-recoverability of third party loss, to an antithesis of *narrow road* transferred loss.

Will the narrow ground be the final synthesis or will the broad ground be favored?

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