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THIRD PARTIES RIGHTS IN A CONTRACT AND THE EFFECT OF THE CONTRACT

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ABSTRACT: *The principle of relative effect of the contract with regards to third parties is presented as a limit and also a guarantee of freedom of contract.The direct effects are only those created by the stipulation in favour of third parties. The indirect effects are, on the one hand, those effects on third parties which result from the legal activity of another. English law reflects the principle of relative effect of contracts in the Doctrine of Privity of Contract. The aim of this paper is to show how this principle finds placein Community law and in national law. European law is centred on the protection of third parties to the contract constituting the company. In the Unidroit Principles, the principle only appears from an a contrario.In some legal systems, the effect ofthe contract with regard to third parties is particularly strongly regulated. In others it is only through the sanctioning of the violation of third party rights that these effects are taken into account.Within the Common law systems, it is generally admitted that the contract only produces effects between the parties, and the situation of third parties is rarely studied. The approach is different once again in those systems that are today essentially still based on Roman law.*

KEYWORDS: Third Parties, Contract Law, Rights, Effects, Obligations.

INTRODUCTION

Exceptionally, the contract may also have legal effects for third parties who are not party to it, foreseen in the law. In these contracts, the third person who earns the right in his favor does not participate as a party neither at the moment of the conclusion of the contract nor later in its implementation.As examples of a third-party contract, as foreseen by Albanian legislation, we can mention the property and life insurance contract. The insurance contract is a very important contractual relationship today in civilian circulation. In recent decades, there has been a major development of the insurance market, a quantitative and qualitative development[1]. To understand the importance of the insurance contract in the life of a national community, it is not enough to describe the essential characteristics of this contract, but it is also necessary to evolve and describe the changes that relate to the social aspect and the subjects of this contractual relationship . The quantitative development has to do with increasing the number of citizens addressing the insurance institute, while the qualitative part relates to the market entry of the insurance broker, which provides the best possible conditions for insurance contracts.

The contractual relationship of insurance in our country has begun to be regulated since the “birth” of the Albanian state, but for the first time the legal arrangement of this relationship was made with the adoption of the Albanian Code of Commerce, 1932. During the post-World War II years, this contract was regulated by the law "On legal transactions and obligations", and then by decree no. 4209 of 1967. Likewise, the Civil Code of 1981, in a number of its dispositions has regulated this relationship. Article 1113 of the Civil Code gives the meaning of the insurance contract, which provides: "*With the insurance contract,*

[1]A. Nuni, E drejta e detyrimeve II, Tiranë 2008, p. 276.

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one party (the insurer), if the event foreseen in the contract is verified, is obliged: a) in the case of insurance of the property to reimburse the other party or a third person for the benefit of which the contract is concluded, the damage suffered within the limits of the amount provided for in the contract; b) in the case of providing the person to pay to the other party or to a third person for the benefit of which the contract is concluded, the amount of the security provided for in the contract. The insured is obliged to pay the premium (insurance price) fixed in the contract. The insurer may be a public or a private person.

There is not a provision in the Principles of European Contract Law that specifies the effect of a contract on third parties, which is explained by the fact that there is no text dealing with the situation of third parties to the contract, with the exception of the stipulation in favour of a third party.

A BRIEF OVERVIEW OF HISTORICAL DEVELOPMENT OF THE CONTRACT FOR THE BENEFIT OF A THIRD PERSON

The Roman law projection

Although the contract in favor of a third person was created and is present in all modern legal systems of civil law, on the other hand, as a general rule, Roman law did not accept this contract. There were examples where the responsibility for mismanagement of the student was born or the one who was forced more to build or donate a fund and that later he made a similar conclusion to the others by offering services as the original promoter.

The prediction under the traditional customary law of "Common Law"

According to the customary traditional law of the Common Law, the contract for the benefit of a third person was not known by linking with the doctrine of the contract, which expresses the rights obligations and facilities obtained from it towards the contracting parties. However, a number of changes and exclusions to the contract for the benefit of a third person are late in the "Common Law" countries, and recent legal changes are underway in this regard.

According to English legislation, the third-party beneficiary is defined as a person who is not party to a contract but has legal rights to enforce the contract or to participate in the proceeds that because of the contract was made for the benefit of the third party.

A contract concluded between the two parties is a contract for the benefit of a third party, when the latter has no detrieve as parties to the classical contractual obligations where the parties have rights and obligations. A contract for the benefit of a third person is a life insurance contract intended to benefit a living person. For real estate, the concept of this contract constantly comes as an attempt by the injured individuals to claim that they are beneficiaries of the contract for the benefit of third parties, as a third party, between property owners, observers, assessors or distributors and this is why the third beneficiary gets the right to file a lawsuit for breach of contract.

Legal Provisions in Different Legislations

The principle according to which the contract only produces effects between the parties is recognised in the majority of national laws. In some legal systems, the effect ofthe contract with regard to third parties is particularly strongly regulated. In others it is only through the

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sanctioning of the violation of third party rights that these effects are taken into account.Within the Common law systems, as with those influenced by German law, it is generally admitted that the contract only produces effects between the parties, and the situation of third parties is rarely studied. Therefore, there is no distinction between binding force and the effect of the contractual situation. The approach is different once again in those systems that are today essentially still based on Roman law. There we generally distinguish between binding force and the invocability of the contract, even where the latter concept is not described in those terms. In the Common law systems, and in particular in English law, the question of the rights and duties of third parties is hardly ever considered. In English law, the only reference of note is to the relative effect of the contract, which results from the rule named the *Privity Rule* or the *Doctrine of Privity of Contract*[2]. As a result, the question of third party rights is only approached from the angle of exceptions to the rule of privity of contract. In the following, the paper gives a brief overview how this principle is treated in different legal systems.

In German law, although the BGB does not contain any general provision on the effectsof the contract with regard to third parties, the principle "*is that a contract of an obligatorytype […] only has effect between the contracting parties, that it does not give rise to anycontractual relationship, any obligation or any claim on the part of a third party; thisprinciple can be inferred from certain specific provisions of the BGB (§ 311, 328, 333). Itappears as the negative side of freedom of contract*". However, *'the principle of relativeeffect is placed to one side when the contract produces beneficial effects for the third party or[…] when the third party is included in the contractual relationship of obligation (§328onwards)"*[3].

Article 1165 of the French Civil Code states that "*agreementsproduce effect only between the contracting parties; they do not harm a third party, and theybenefit only in the caseof the stipulation in favour of third parties*". This provision is considered to be the textual basis of the principle of relative effect. On the other hand, Art. 1119 of the Civil Code entertains the same idea[4]. The parties cannot act in a way that would illegitimately undermine third party rights as their contract will produce effects with regard to everyone. This principle is the foundation of several of French law's tools and techniques for dealing with third parties. Entering into a contract should not be a way of threatening third party rights. Thus, the parties cannot enter into a contract that compromises the performance of a right of a third party.

Following the same logic, Art. 1257 of the Spanish Civil Code poses the principle of the relative effect of the contract, which therefore cannot threaten the rights of third parties. The same provision nevertheless then recognises contracts in favour of a third party and contracts that are the obligation of a third party. Also, in Italian law, Art. 1372, paragraph 3 of the Civil Code provides that the contract "*only produces effects with regard to third parties in the cases provided forby the law"*while paragraph 1 states that "*the contract has the force of law between the parties"*[5]. The principle of relative effect of the contract with regards to third parties is presented as a limit and also a guarantee of freedom of contract.Italian law also acknowledges the effect of the contract with regard to third parties. The direct effects are only

[2]For an examination of this rule see, G. H. Treitel, *An outline of the Law of Contract*, Oxford University Press, 6thedition 2004, pp. 97 to 101. – S. A. Smith, *Atiyah's Introduction to the Law of Contract*, Clarendon Law Series,Oxford University Press, 6th edition, 2005, pp. 335 and 336.

[3]https://www.gesetze-im-internet.de/englisch_bgb/

[4]This article states that "*as a rule, one may, bind oneself and stipulate in his own name, only foroneself".*

[5]http://www.wipo.int/wipolex/en/details.jsp?id=14526

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those created by the stipulation in favour of third parties. The indirect effects are, on the one hand, those effects on third parties which result from the legal activity of another[6]. In addition, Italian law also sanctions, on a specific basis, the case of infringements of the rights of the specific third party who is the creditor of one of the parties.

English law reflects the principle of relative effect of contracts in the unwritten rule of the *Doctrine of Privity of Contract*[7]or *Privity Rule.* According to this rule, only the parties to a contract can request the performance of it or be pursued in order to perform it. According to the doctrine, the *Privity Rule* is used to distinguish between the rights arising from the law of contract and the law of property. In 1995 in the Court of Appeal in Darlington Borough Council v Wiltshier Northern Ltd' Steyn LJ, said the following: "*The case for recognising a contract for the benefit of a third party is simple and straightforward. The autonomy of the will of the parties should be respected. The law of contract should give effect to the reasonable expectations of contracting parties. Principle certainly requires that a burden should not be imposed on a third party without his consent. But there is no doctrinal, logical, or policy reason why the law should deny effectiveness to a contract for the benefit of a third party where that is the expressed intention of the parties. Moreover, often the parties, and particularly third parties, organise their affairs on the faith of the contract. They rely on the contract. It is therefore unjust to deny effectiveness to such a contract. I will not struggle with the point further since nobody seriously asserts the contrary."*[8]

This principle finds place also in Community law. European law is centred on the protection of third parties to the contract constituting the company.Here is to be mentioned the first Directive of 9 March 1968[9]which aims to ensure the protection of the interests of third parties with regard to companies limited by shares in so far as they only offer their authorized capital as guarantee, and in order to do this it imposes, for example, the compulsory disclosure of some of the company's original documents. Lastly, the ECJ has recognised that, within the framework of competition disputes[10], all third parties can assert the nullity of an agreement prohibited by Article 81 EC and can demand compensation for the harm suffered if there is a causal link between it and the prohibited agreement. If the anti-competitive agreement can be called into question by third parties, it is because it unlawfully impinges on their rights.

[6]This is for example the case with a contract for a lease which has effect with regard to the ultimate acquirer of the leased goods.
[7]G. H. Treitel, *An outline of the Law of Contrat*, Oxford University Press, 6th edition 2004,pp. 97 - 101. – S. A. Smith, *Atiyah's Introduction to the Law of Contract*, Clarendon Law Series, OxfordUniversity Press, 6th edition, 2005, pp. 335 and 336.
[8][1995] 1 WLR68.
[9]First Council Directive 68/151/EEC 9 March 1968, on co-ordination of safeguards which, for the protectionof the interests of members and others, are required by Member States of companies within the meaning of thesecond paragraph of Article 58 of the Treaty, with a view to making such safeguards equivalent throughout theCommunity, OJ L 65 14.3.1968, p. 8–12.
[10]ECJ,13 July 2006, Vincenzo Manfredi v Lloyd Adriatico Assicurazioni SpA (C-295/04), Antonio Cannito vFondiaria Sai SpA (C-296/04) and Nicolò Tricarico (C-297/04) and Pasqualina Murgolo (C-298/04) v AssitaliaSpA, Aff. joint C-295/04 to C-298/04, Rec. 2006 page I-06619.

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In the Unidroit Principles, the principle only appears from an *a contrario* reading of Article 1.3 on the binding character of contract, which states that "*a contract validly enteredinto is binding upon the parties. […]*". It cannot benefit or obligateother people. The stipulation in favour of a third party is expressly provided for by Articles5.2.1 onwards.

Third Parties Liabilities

As a general rule, two persons cannot, by any contract into which they may enter, thereby impose contractual liabilities upon a third party. This principle may be illustrated by reference to building contracts, where a person (the employer) engages a contractor to carry out certain building work. The contractor frequently sub-contracts parts of the work to sub-contractors. A sub-contractor has no cause of action against the employer for work done or materials supplied under the sub-contract, since the employer is not a party to that contract. Even if the employer has nominated the sub-contractor and taken the benefit of the sub-contractor's work, the employer will not be liable to the subcontractor for the price, as there is no privity of contract between them. Conversely, the employer has no claim in contract against the subcontractor, since the sub-contractor is not a party to the main contract between the employer and the contractor.

There are certain situations where contractual liabilities may affect third parties.

1. Firstly a contract concerning property may impose liabilities on third parties who subsequently acquire the property with notice of the contract.

The property may be tangible, as where a contract is made concerning land or goods, or it may be intangible, as where the contract concerns intellectual property such as a patent or copyright. A similar principle may apply where information subject to a contractual obligation of confidentiality comes to the knowledge of a third party with notice of the contract, although confidential information does not have all the attributes of a property interest, and it is not generally treated as such.

2. Secondly, person who knowingly interferes with contractual rights without justification will be liable in tort and may be restrained from doing so by an injunction.

Under the English Law the general rule is that contractual liabilities cannot be imposed upon a stranger to the contract. Normally parties to a contract cannot transfer contractual burdens to a stranger to the contract. However, there are certain cases, e.g., contract relating to land, contract relating to chattels (i.e. restriction upon resale price, patents, ships under charter-party, other chattels, hire-purchase) where contractual liabilities can be transferred to a stranger to the contract.In the U.K legislation, there has been a radical development in the doctrine initiated by Tulk v. Moxhay[11], 1848, and it has been established since the later years of the nineteenth century that something more than mere notice by the third party of the existence of the covenant is necessary to render him liable. In particular it is essential that the covenanted, i.e. the original vendor, should have retained other land in the neighborhood for the benefit and protection of which the restrictive covenant was taken. If an owner sells only a portion of his property, the selling value of what he retains will often depreciate unless restrictions are placed upon the enjoyment of the part sold and it is only

[11]Tulk v Moxhay [1848] EWHC J34 (Ch).

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where the covenantee has retained land of being benefited in this way that equity will enforce a restrictive covenant against a third party[12].

United States

There is vast literature on third party rights in the United States. The New York Court of appeal in Lawrence v. Fox 20 NY 268 (1859) it has become generally accepted that the third party is liable to enforce a contractual obligation made for his benefit.

New Zealand

The New Zealand Contracts (Privity) Act 1982, The New Zealand Contracts (Privity) Act 1982, does not limit enforceability by a beneficiary to express promises only. It reverses the onus of proof by requiring that the parties to the contract have to establish that their promise was not intended to have the effect of creating a legally enforceable obligation in favour of the third party. It requires that the third party must be sufficiently designated in the contract. Parties to the contract cannot vary or alter the promise benefiting the third person after he has materially altered his position in reliance on the promise, or has obtained judgement or award on the promise.

CONCLUSIONS

The contract has legal effects for third parties who are not party to it. This happens only in the cases foreseen in the law. As mentioned, the third person who earns the right in his favor does not participate as a party neither at the moment of the conclusion of the contract nor later in its implementation.

The Albanian civil code provides for this contract only a definition in Article 694, from the content of which the main features of this contract arise, whereas in concrete cases of daily life are provided in the provisions of special contracts of the Civil Code.

A contract for the benefit of a third person is valid when the person who links has interest in it. A person who has accepted the promise in favor of the third person or the latter has the right to request the performance of the contract, unless there is another agreement. The contract cannot be broken or changed after the moment the third person has declared that he or she agrees to benefit from its affiliation, unless the proposer has reserved this right. In the event of a revocation of the contract award or refusal of the third person to benefit from it, the obligation remains in the benefit of the proposer, unless it is otherwise contrary to the will of the parties or the nature of the contract.

From the understanding of the contract to the benefit of a third person it appears that the third person or the third party benefiting is the purpose of the contract concluded between the two parties that realize it, who decide that through the contract between them to profit intentionally the third party .

The third party beneficiary in the contract law is a person who may have the right to sue in a contract despite being not an initial party to that contract. This right arises when the third party is the intended beneficiary for the purpose of the contract, as opposed to a random

[12]See Formby v. Barker [1903] 2 Ch. 539, and LCC v. Atten [1914] 3 KB 642.

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beneficiary. Depending on the circumstances in which the third party participates in the contractual relationship, it is entitled to sue the person charged with rights or even the person charged with obligations under the contract.

The contract forms for the benefit of a third person date back to Roman law, continuing with the English system of law and beyond.The treatment of the rights and duties of third parties is different within the differentnational legal systems studied.

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