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CONTRACTS FOR THE BENEFIT OF A THIRD PARTY: THE PROBLEM OF CLASSIFICATION

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**CONTRACTS FOR THE BENEFIT OF A THIRD PARTY:
THE PROBLEM OF CLASSIFICATION²**

On the basis of analyzing disputes connected with the classification of contracts for the benefit of third parties, history, and development of this construct in Russian law and analyzing its use in foreign legal systems, this work shows that the formal approach, applied in Russia with regard to contracts for the benefit of third parties, considerably belittles the sphere of application of the construct. Another approach, based on conferring material benefit upon a third party, is developed. It is also shown that the former approach allows us to resolve a number of problems that arise when applying of the analysed contractual construct.

JEL Classification: K12.

Keywords: contract law, contract for the benefit of a third party, privity of contract, classifying characteristics of contract.

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Introduction

The right to demand performance of a contract by a third party that did not take part in concluding the contract, has for a long time been used in Russian civil law as evidence that a particular contract is a contract for the benefit of a third party. However, as I show below, this qualification often fails.

In modern civil practice there are many contracts that should evidently be qualified as contracts for the benefit of third parties, even though the existence of the corresponding right of the third party is not obvious. The discussion of whether a third party has a right to demand performance of a contract is often in the core of the problem. Therefore, in my opinion, it is necessary to find other characteristics that would help to qualify a contract as a contract for the benefit of a third party. The existence or non-existence of a third party's right should follow from that qualification.

In this work I identify such classifying characteristics. To achieve the sought result, Section 1 discusses contracts for the benefit of third parties in modern Russian legal practice and analyses the difficulties that occur upon their classification. A variety of cases are discussed. The cases show that the modern Russian classification of contracts for the benefit of third parties, based on the presence or absence of a right of the third party to demand performance for its benefit, gives rise to many disputes, the reason for which is the use of a formal rather than a substantial basis. The presence or absence of such a right for the third party is difficult for courts to establish. The history of development for this legal concept is also discussed. The history shows how such a classification of contracts for the benefit of third parties was developed in the Russian legal practice and what alternative points of view existed.

Section 2 discusses the approach of foreign legal practice to the same construction; both common law and continental legal systems are taken into account. This section shows also that the main problems with classification arise when formal and non-substantial characteristics are applied for classification.

Section 3 analyses the classification of contracts for the benefit of third parties based on the purpose of such contracts to confer benefit to the third party. In this situation a legal order that protects the reasonable expectations of people should apply the presumption of existence of a third party's rights in a contract whose is to confer benefit upon the third party. This presumption may be rebutted, but conferring a benefit out of a contract should lead to the existence of a right, unless proven otherwise.

1. Contracts for the Benefit of Third Parties in Modern Russian Legal Practice

1.1. Contracts for the Benefit of a Third Party in Civil Practice

I will start the study by discussing of how contracts for the benefit of third parties are used in practice.

Development of the theory of contracts for the benefit of third parties was connected with the growth in life insurance contracts in the second half of the XIX century.³ The goal of such a contract is to immediately provide relatives of the deceased with money or repay a debt that would otherwise burden the estate.

Contracts for trust management of property can also be concluded for the benefit of third-party beneficiaries. The same applies to bank deposit contracts.

If the delivery of goods is organized in such a way that the seller is obliged to deliver goods to the buyer, the seller, who is also the consignor, includes in the transportation contract the right of the buyer to claim the cargo from the carrier.

Contracts for the provision of services for the benefit of third parties are also common. For example, one can give a gift certificate for a beauty salon to another person. Such contracts are called contracts for the benefit of unnamed third parties.

Let us consider the structure of a contract between an insurer and a car service that repairs cars insured with the insurer.⁴ It is a contract of independent work where the insurer is a customer and the car owners are beneficiaries. The owner of the car acts as if he or she ordered the car repair. However, it is the insurer who negotiates the terms and conditions of that contract since for a car-owner the contract price would be much higher.

Here is another example, in this case a man who wants to have flowers delivered to his girlfriend. It is unlikely that the sale and purchase contract between the man and the florist would be classified as a contract for the benefit of a third party. It is more likely that it would be considered a contract that is performed to a third party under which the third party accepts the performance but has no right to demand performance.

The right to demand performance for their benefit is a characteristic of contracts for the benefit of third parties that distinguishes them from contracts performed to third parties. A lot of

3 Serebrovskiy V.I. Life insurance contract for the benefit of third party (Cause of a beneficiary's right) VIJuN Proceedings, 1947, Issue 9 Moscow, P.356 (Серебровский В.И. Договор страхования жизни в пользу третьего лица. (Основания возникновения права выгодоприобретателя) // Ученые труды ВИЮН. - М.: Юрид. изд-во МЮ СССР, 1947, Вып. 9, С.356)

4 Complicated problems which arise here are considered in Nenashev M.M. Casco Payments in the Form of Repairs: Legal Issues of Theory and Practice // Yurist, 2012, No. 4 p. 15-20 (Ненашев М.М. Выплаты по КАСКО в виде ремонта: правовые вопросы теории и практики // Юрист. 2012. N 4. С. 15 – 20).

disputes occur in connection with this issue. Let us discuss several examples where disputes are connected with the qualifying contracts as being for the benefit of third parties.

A Housing Complex Administrator had a building belonging to the city in its operational control. The building was sold upon consent of the owner. The sale and purchase contract provided that the buyer pay part of the purchase price to the Housing Complex Administrator, and the remaining part to the city budget. The city budget part was not paid. The court refused the claim of the city administration on the grounds that the administration was not a party to the contract and had no right to demand performance since no such right was given to it in the contract.⁵ In another case, agreement for the lease of land under which lease payments were supposed to be paid to the city property management committee was classified as concluded for the benefit of the committee.⁶

Yet another example is as follows. A company was granted a license for the use of subsoil. After that, a contract for the use of the subsoil was concluded that obliged the subsoil's user to transfer 3% of revenues to the local budget. The local budget payments were not paid and the local administration, considering itself a beneficiary, brought a claim to recover the due sums. The court of appeals clarified that the absence of a direct mentioning in the contract of the municipal body's right to demand performance of the contract does not mean that the contract is not a contract for the benefit of a third party. Therefore, the court recognized the city administration's right of action.⁷

In the next case, cargo was lost in the course of transportation due to a fault by the company that provided security. The contract with the security company was concluded by the cargo sender. The property title for the cargo passed to the cargo recipient at the moment when the cargo was loaded onto the lorry. The cargo recipient filed a claim for the compensation of damages caused by a breach of contract by the security company. Some courts satisfied such claims,⁸ while others refused to satisfy them.⁹ In 2009 the Presidium of the Supreme Commercial Court clarified that the discussed contracts were not contracts for the benefit of third parties and the cargo recipient had no right to bring a damage claim based on a contract against the security company.¹⁰

5 Resolution of Federal Commercial Court of Ural District of 28.02.2007, case №09-982/07-C6.

6 Resolution of Federal Commercial Court of Central District of 16.05.2011, case №A62-5216/2010.

7 Resolution of Federal Commercial Court of Far Eastern District of 11.08.2009 №Ф03-3105/2009, similar position can be found in other resolutions of this court, see, for instance, Resolution of Federal Commercial Court of Far Eastern District of 13.05.2010 №Ф03-2942/2010.

8 Resolution of Federal Commercial Court of North Caucasus District of 22.11.2007 №Ф08-7742/07, Ruling of Supreme Commercial Court of 13.05.2009 №BAC-5665/09.

9 Resolution of Federal Commercial Court of Volgo-Vyatskiy District of 19.09.2007, case №A82-9414/2006-11.

10 Resolution of Presidium of Supreme Commercial Court of 01.12..2009 №11320/09.

1.2. Qualification of Contracts for the Benefit of Third Parties in Modern Russian Legal Practice

1.2.1. Qualification based on Article 430 of the Civil Code. A rule for qualifying contracts for the benefit of third parties, based on Article 430 of the Civil Code, was developed in modern Russian legal practice. It rule is clearly explained by V.V. Vitryanskiy: Two characteristics are inherent to contracts for the benefit of third parties. First, such contracts should provide that the debtor perform the obligation not to the creditor but to a third party. Secondly, the third party, for whose benefit the performance should be made, is provided with an independent right to make a demand from the debtor under the contractual obligation.¹¹

How can one define the existence of these two characteristics in particular relations? Situations when a contract directly stipulates these characteristics are more reliable.¹² No disputes arise when it follows from a law that a third party has a right to demand performance for his or her benefit or when a law sets forth that a certain kind of contract is for the benefit of third parties.

Thus, there is a range of contracts on which there is a consistent opinion that they should be qualified as contracts for the benefit of third parties.

In all cases when there is no consistent quality practice, we can see two types of situations. In the first type of situation there is doubt as to whether the performance is provided to the third party, while in the second type the performance is provided to a third party but neither law nor the contract stipulates that the third party has a right to demand performance.

In all such cases “...discovering the will of the parties aimed at providing the third party with a right to demand from the debtor and, thus, classifying the transaction as a contract for the benefit of a third party are impossible without interpretation.”¹³

Consequently, the rule for qualifying a contract by the two abovementioned characteristics cannot be considered useful for dispute resolution because one of the main problems when analyzing the structure of rights and duties based on a particular contract is the problem of the existence of the right of a third party to demand performance for his or her own

11 Vitryanskiy V.V. Certain Aspects of Study of Civil Contracts during the Reform of Civil Legislation / In: Problems of the Development of Private Law: a Collection of Articles devoted to anniversary of Yem V.S. (ed. by Sukhanov Y.A., Kozlova N.V.). Moscow, Statut, 2011. P.33 (Витрянский В.В. Некоторые аспекты учения о гражданско-правовом договоре в условиях реформирования гражданского законодательства / В кн.: Проблемы развития частного права: Сборник статей к юбилею Владимира Саурсевича Ема (отв. ред. Е.А. Суханов, Н.В. Козлова), М.:Статут, 2011, С.33).

12 In one of the cases, the court included in the decision the following: “The right of a third party to demand performance of an obligation for its benefit, which is stipulated in a contract, is a necessary characteristic of a contract for the benefit of a third party.” See Resolution of Federal Commercial Court of East Siberian District of 31.08.2005, case №А33-27269/04-С2-Ф02-4200/05-С2.

13 Burobina Y., Burobin V. Legal Assistance to an Appointed Person // EZH-Yurist. 2010. No. 21. P. 8-9 (Буробина Е., Буробин В. Юридическая помощь назначенному лицу // ЭЖ-Юрист. 2010. N 21. С. 8 – 9).

benefit. Furthermore, Article 430 of the Civil Code fully excludes a waiver of debt, contracts that have a protective effect for third parties, and the similar spheres of regulation.

1.2.2. Criticism of Article 430 of the Civil Code. The question of whether the wording of Article 430 of the Civil Code is compatible with modern life is currently of interest. This position is very clearly expressed by E.V. Tyichinskaya, who analyses the construction of a contract for performing the functions of an executive body of an open joint-stock company and considers this contract to be a particular type of contract for the benefit of third parties which does not fall under Article 430 of the Civil Code because this Article does not describe all types of such contracts.¹⁴

The same applies to qualifying a contract between a company and its registrar, which some authors consider to be for the benefit of third parties.¹⁵ Their opinion is based on the position of O.N. Sadikov,¹⁶ who thinks that Article 430 of the Civil Code does not regulate all contracts for the benefit of third parties.¹⁷ The Presidium of the Supreme Commercial Court refused to qualify this as a contract for the benefit of a third party.¹⁸

A similar situation occurs with a contract for the provision of medical services to insured persons between a medical insurance company and a medical institution. In one such case the insurer, having paid for the services provided by a hospital, discharged the contract with the hospital. The insured individuals, however, continued to use medical services provided by the hospital. The hospital brought a claim against the insurer, demanding payment for the services. The hospital referred to Part 2 of Article 430 which prevents discharge of a contract when a third party expresses its will to use the rights out of the contract for his or her benefit. The court stated

14 Tyichinskaya Y.V. Contract for the Performance of the Functions of Single Executive Body of a Company / ed. by Mikheyeva L.Y. Moscow, Statut. 2012. P. 102, 103 (Тычинская Е.В. Договор о реализации функций единоличного исполнительного органа хозяйственного общества / под ред. Л.Ю. Михеевой. М.: Статут, 2012. С.102, 103).

15 Rozhkova M.A. On Liability of an Issuer of Securities and a Specialized Registrar for a Breach of the Procedure for Maintenance of a Registry of Securities // Security measures and liability measures: a collection of articles / supervised and ed. by Rozhkova M.A. Moscow, Statut. 2010. P. 386-388 (Рожкова М.А. Об ответственности эмитента и специализированного регистратора за нарушения порядка ведения реестра // Меры обеспечения и меры ответственности в гражданском праве: сборник статей / рук. авт. кол. и отв. ред. М.А. Рожкова. М.: Статут, 2010. С. 386 – 388).

16 Sadikov O. N. Liability of the parties upon maintenance of a registry of nominal shares // A commentary of court and arbitration practice. Issue 13 / ed. by Yakovlev V.A. Moscow: Yuridicheskaya Literatura. 2006. P. 36-46 (Садиков О.Н. Ответственность сторон при ведении реестра владельцев именных ценных бумаг // Комментарий судебно-арбитражной практики. Выпуск 13 / под ред. В.Ф. Яковлева. М.: Юридическая литература, 2006. С. 36 – 46).

17 Commentary to the Civil Code of the Russian Federation, Part I (by articles) / 3d edition, reviewed and supplemented / ed. Sadikov O.N. Moscow, CONTRACT, INFRA-M. 2005. P.968-969 (Комментарий к Гражданскому кодексу Российской Федерации, части первой (постатейный) / 3-е издание, исправленное, переработанное и дополненное / под ред. О.Н. Садикова – М.: КОНТРАКТ, ИНФРА-М, 2005, С.968-969).

18 Novoselova L.A. Case of Ozimov L.A. v. Kubantekhgas and Registrar R.O.S.T. (Resolution of Presidium of Supreme Commercial Court of 1 February 2005 No. 12158/04) / In: Legal Positiona of the Supreme Commercial Court of the Russian Federation: Selected Resolutions of 2005 with commentaries (ed. Ivanov A.A.). Moscow, Statut. P. 15 (Новоселова Л.А. Дело «Озимова А.В. против обществ «Кубаньтехгаз» и «Регистратор Р.О.С.Т.» (Постановление Президиума ВАС РФ от 1 февраля 2005 г. N 12158/04) / В кн: Правовые позиции Президиума Высшего Арбитражного Суда Российской Федерации: Избранные постановления за 2005 год с комментариями (под ред. А.А. Иванова) М.: Статут, 2010, С.15).

that it was not obvious that the contract was concluded for the benefit of third parties. The court also mentioned that “...Part 1 of Article 782 of the Civil Code does not provide for the right of a client to terminate an agreement dependent on the expression of the will by third parties”.¹⁹ In my opinion, it is apparent that this contract is a contract for the benefit of third parties – the insured individuals – but not all norms of Article 430 of the Civil Code apply to it.

Modern turnover also encountered a problem with burdening third party, which is not a party to the contract, with certain duties. Cargo recipient bears certain obligations under cargo transportation contract and for that reason a number of authors do not consider such contract as contracts for the benefit of third parties.²⁰ The logic is the following: it is impossible to impose contractual obligations on anyone who is not a party to the contract, thus, we are dealing not with a third party beneficiary but a party to the contract, i.e. we have a multiparty contract.

O.N. Sadikov does not consider it unusual that certain obligations are imposed on third parties, not only under contracts but also by law. He writes, “...Both the beneficiary of an insurance contract (Article 939 of the Civil Code) and the cargo recipient in a cargo transportation contract (Article 35 of Article of Rail Transport, Article 160 of the Code of Marine Trade) bear obligations along with rights. Burdening third parties, to the benefit of which the contract is concluded, with certain obligations should be possible upon agreement between the contracting parties.”²¹

1.2.3. The Problem of Qualification. The dominant factor in modern Russian contract theory and practice is the qualification of contracts for the benefit of third parties, which, as described above, causes a number of problems. The first problem is that sometimes it is hard to establish that the right of a third party to demand performance under a contract exists. Another problem is that even an obvious existence of certain rights of third parties does not always allow for the application of Article 430 of the Civil Code to these relations simply due to the nature of the relations.

In my opinion, it is necessary to start with whether a contract is concluded for the benefit of third parties or not, and then make conclusions regarding the right of third parties to demand performance. Then the existence or non-existence of the right to demand performance would be a consequence of its qualification and not the other way round. The existence of the right would be based not only on the judicial interpretation of the text of a contract but also on some factual basis.

19 Resolution of Federal Commercial Court of Far Eastern District of 01.06.2009 №Ф03-2229/2009.

20 See for example Vygodyanskij A.V. Legal status of consignee in the contract of air shipment of cargo // Jurist, 2010, N 5 (Выгодянский А.В. Правовое положение грузополучателя по договору воздушной перевозки груза // Юрист, 2010, №5)

21 See footnote 16.

From the above mentioned court decision about the subsoil user who was obliged to pay 3% of revenues to the local budget,²² we see that the court first qualified the contract as concluded for the benefit of a third party and then, based on that qualification, applied Article 430 of the Civil Code. Only then from that qualification did it make a conclusion on the existence of the right of a third party to demand performance.

Let us look at one more case. A company bought premises from the city property management committee. The contract provided for the right of utility providers to have access to engineering networks located at the premises. When such access was needed, the company failed to respect the provision of the contract. The committee brought a claim against the company but the claim was refused because the contract "... stipulated an obligation of the buyer to give access to the premises to utility providers, thus the obligation is stipulated in the interest of such providers. In accordance with Article 430, the right to demand performance for one's benefit belongs to the party to which the debtor provides performance. Thus, the committee did not prove that it has the right of action."²³

Practice knows many cases when performance is provided not to a party to the contract, but to a third party. Above we discussed contracts that are performed – or should be performed – in the interest of third parties. Such contracts do not always provide that third parties acquire any rights from such contracts or mention that contracts are concluded for the benefit of third parties. Nor does the law.²⁴ We can see from the discussed examples that third parties often try to defend their assumed rights in court, but fail due to the absence of contract-based rights. Today this problem is resolved simply: If a court cannot deduce the existence of a third party's right in a contract, then there is no subject-matter to defend.

When people conclude contracts, they primarily intend to obtain certain benefits for themselves. Civil law should provide people with rights such that contracts could be performed with the least amount of difficulties.

I read the following phrase in an American textbook of contract law: "...If the parties to a contract had the time and the vision to negotiate and articulate every element that could conceivably bear upon their relationship, weighing every contingency and imagining all possible future states of the world, there would be little need for contract rules as such."²⁵ For some

22 Resolution of Federal Commercial Court of Far Eastern District of 11.08.2009 №Ф03-3105/2009.

23 Resolution of Federal Commercial Court of North Western District of 01.10.2012, case №A56-53137/2011

24 A suggestion to qualify as contracts for the benefit of third parties only those contracts that directly state that a contract is concluded for the benefit of a third party can be found in Tarasenko Y.A. Contract for the benefit of third parties: special characteristics of the legal construct // In: Transactions: problems of Theory and Practice: a collection of articles. Moscow, Statut. 2008. P. 308 (Тарасенко Ю.А. Договор в пользу третьих лиц: особенности правовой конструкции // Сделки: проблемы теории и практики. Сборник статей. - М.: Статут, 2008. - С.308).

25 Marvin A. Chirelstein Concepts and Case Analysis in the Law of Contracts. Fourth Edition – Foundation Press, New York,

reason this idea is not taken into account in modern Russia legal practice when dealing with contracts for the benefit of third parties. Very often courts behave as if the wording of norms has primary significance and the essence of actual relations is only secondary.

Despite everything stated above, I do not necessarily want to return to a well-known dispute about the legal significance of will and expression of will. I do not support the idea that it is always necessary to find out the actual will of the parties. However, in the examples discussed above the problem is not connected with doubts regarding the expression of the will of the parties. In all cases when a third party was refused judiciary protection, the expression of the will of the parties regarding facts was clear. But the parties did not take into account the necessity to also express their will regarding the rights of third parties.

There is a question as to whether civil law can confidently assert that a contract performed to a third party or in the interest of a third party should in any case deprive the third party of a right to demand performance when a clear term regarding the right of a third party to demand performance is missing.

This work intends to find characteristics of actual relations that, considering the facts of the case, would let us define whether a third party should have a right to demand performance for his or her benefit.

1.3. Qualification of Contracts for the Benefit of Third Parties in Russian Legal Order in the Pre-Soviet and Soviet Periods

1.3.1. Late 19th – Early 20th Century. Little pre-Revolutionary literature discusses contracts for the benefit of third parties. It does mention such possibility and gives reference to the same characteristic – the existence of a right of a third party to demand performance for his or her benefit.

There was no regulation of such contracts and practice did not have to deal with a large variety of contracts of this type. In 1903 the first Draft Civil Code was published, Articles 1589-1592 of which provided for the regulation of such contracts. Most analytic work, however, were written before the publication of the Draft.

Below is a brief summary of opinions from civil law scholars of that time.

From a paragraph on contracts for the benefit of third parties in a textbook by G.F. Shershenevitch, it can be concluded that the author connects the existence or non-existence of the right of a third party to demand performance for its benefit with the presence of a relevant contract clause, even though it is not directly mentioned.²⁶

2001, P.9.

26 Shershenevitch G.F. A Textbook of Civil Law. Tula, Avtograf. 2001. P. 408 (Шершеневич Г.Ф. Курс гражданского права – Тула, Автограф, 2001, С.408).

In connection with the right of a third party to demand performance under a contract concluded by other parties, K.P. Pobedonostsev wrote, “The question of the right of a third party to bring an independent claim based on a contract, to which it was not a party, but which stipulates an obligation for its benefit, is resolved, though indirectly, in the Decision of the Court of Appeals of 1873 No. 1623. It reads that the third party, if its rights are directly stipulated in a contract (between two other persons), can demand performance of the contract in everything that is connected with its interests with an independent claim.”²⁷

From the Commentary to Part 1 of Book 4 of the Code of Laws, compiled by V.L. Isachenko and V.V. Isachenko, it can be seen that the authors treat the incurrance of benefit on a third party as the main qualifying characteristic of contracts for the benefit of third parties, and the right to demand that benefit can follow or not follow from a contract. For the purpose of our research, this framing of the problem is important.²⁸

Now let us discuss two works fully devoted to contracts for the benefit of third parties. First is a work by Y. Dubovitskiy. This author demonstrates that different legal systems came to the possibility of vesting a third party with a right under a contract to which it was not a party due to practical necessity. The intention to confer benefit on a third party is, according to the author, a qualifying characteristic of contracts for the benefit of third parties. The right follows the benefit.²⁹ The same position as Dubovitskiy’s will be the focus of my further attention.

A book by baron A.M. Nolken is the most extensive book on contracts for the benefit of third parties of that period. A.M. Nolken, just as G.F. Shershenevitch and K.P. Pobedonostsev, thought that in order to give third parties legal protection, the will of the parties to a contract should be directed at the stipulation of the right of third parties to demand performance of a contract for their own benefit. The author shows a close connection between the will of the parties to stipulate the right of a third party to demand performance of a contract for its own benefit and the will of the parties to confer material benefit on a third party.³⁰ A points of interest

27 Pobedonostsev K. P. Textbook of Civil Law: in three volumes. V.3 / ed. Tomsinov V.A. – Moscow, Zertsalo Publishing, 2003, P.247 (Победоносцев К.П. Курс гражданского права: В трех томах. Том 3 / под редакцией В.А. Томсинова – М.: Издательство «Зерцало», 2003, С.247). It is also worth mentioning that here one of the cases discussed by Y. Dubovitskiy (see below) is described (Imberkh v Skobeltsin).

28 Obligations out of contracts: General Part. Practical Commentary to Russian Civil Laws: Commentary to book 4, part 1, vol. 10 of Collection of Legislation. Vol. 1 / Compiled by Isachenko V.L., Isachenko V.V. St. Petersburg. Typ. of M. Merkushev. 1914. P. 99 (Обязательства по договорам: Общая часть. Опыт практического комментария русских гражданских законов: Комментарий на 4 книгу 1 ч. 10 т. Св. зак.. Т. 1 / Сост.: Исаченко В.Л., Исаченко В.В. - СПб.: Тип. М. Меркушева, 1914, С.99).

29 Dubovitskiy Y. Contracts for the benefit of a Third Parties// Juridichesky vestnik, June – July. Printed by Moscow Society of Jurists – Moscow, Typ. of A.I. Mamontov & Co, 1885, N 6-7, P.242 (Дубовицкий Ю. Договоры в пользу третьих лиц // Юридический вестник: Июнь - июль. Издание Московского Юридического Общества. - М.: Тип. А.И. Мамонтова и Ко, 1885, № 6-7, С.242).

30 Nolken A.M. Contracts for the benefit of a Third Parties. Attempt of theoretical study in Civil Law. – St. Petersburg, Typ. of Imperial Academy of Science, 1885, P34 (Нолькен А.М. Договоры в пользу третьих лиц. Опыт теоретического

is that the purpose of a contract is to stipulate a right or to confer material benefit. According to A.M. Nolken, these are closely connected. The will of the parties in such a contract to stipulate a right is always directed at simultaneously conferring material benefit.

1.3.2. Contracts for the benefit of third parties in Soviet law. The Soviet Civil Codes of 1922 and 1964 did not regulate contracts for the benefit of third parties and did not contain a definition of such contracts. Since there was no legal definition, legal scholars of that time developed definitions and described defining characteristics of such contracts in legal literature.

What follows is a definition of a contract for the benefit of a third party given by N.S. Kovalevskaya in her dissertation: “A contract for the benefit of a third party is an agreement to confer a direct and independent right on a third party that took part in concluding the contract neither directly (as a counterpart) or indirectly (via a representative).”³¹

A book by I.B. Novitskiy and L.A. Lunts names the stipulation of a right based on a contract to a third party as a qualifying characteristic of such a contract.³² B.G. Haskelberg also qualifies contracts for the benefit of third parties by the existence of rights of third parties to demand performance of the contract.³³ V.I. Serebrovskiy and M.K. Suleimenov shared this point of view.³⁴

Contracts having a protective effect for third parties or contracts that waive a debt were not considered to be contracts for the benefit of third parties in Soviet times.

It is clear from this brief overview that Russian legal doctrine of both the pre-Soviet and Soviet periods considered stipulating the right of a third party to demand performance of a contract concluded for its benefit to be the qualifying characteristic of such contracts. Though some authors mention a benefit, rather than a right, such are in the minority. In Soviet literature, benefit is mentioned only once in a textbook of civil law from 1950.³⁵

2. Contracts for the Benefit of Third Parties in Foreign Legal Systems

исследования по гражданскому праву – СПб, Типография Императорской Академии наук, 1885, С.34)

31 Kovalevskaya N.S. Contract for the benefit of a third party. Phd dissertation. Leningrad. 1988. P. 25. (Ковалевская Н.С. Договор в пользу третьих лиц-граждан. Дис. ... канд. юрид. наук. - Л., 1988, С.25).

32 Novitskiy I.B., Luntz L.A. General study of obligations. Moscow, Gosyurizdat. 1950. P. 139 (Новицкий И.Б. Лунц Л.А. Общее учение об обязательстве - М.: Госюриздат, 1950, С.139).

33 Khaskelberg B.L. To the question of classification of a contract for the benefit of a third party // In: Presentations of the final scientific conference of law faculties (December 1971). Tomsk. Publishing House of Tomsk University. 1973. P. 34 (Хаскельберг Б.Л. К вопросу о сущности договора в пользу третьего лица // В кн.: Доклады итоговой научной конференции юридических факультетов (декабрь 1971 г.). - Томск: Изд-во Том. ун-та, 1973, С.34).

34 Suleymenov M.K. Third parties in civil law // Soviet state and law. 1978. No. 3. P. 127. (Сулейменов М.К. Третьи лица в гражданском праве // Советское государство и право, 1978, №3, С.127).

35 Bratus S.N., Genkin D.M., Luntz L.A. and Novitskiy I.B. Soviet civil law. Textbook. Vol. 1 / ed. Genkin D.M. Moscow. Gosyurizdat. 1950. P. 382-384. (Братусь С.Н. Генкин Д.М. Лунц Л.А. Новицкий И.Б. Советское гражданское право. Учебник. Т.1 /Под ред. Генкин Д.М. – М.: Госюриздат, 1950, С.382-384).

That it was initially considered impossible to stipulate a valid independent right of a third party in a contract it did not help to construct, is common for all most modern legal systems, except for Germany. But later, under pressure from the needs of businesses, this possibility gradually became acceptable.

2.1. Common Law Countries

2.1.1. England. The doctrine of privity is one of the cornerstone ideas of English contract law. It has two aspects. Firstly, a third party cannot be burdened by a contract to which it is not a party, and, secondly, a third party cannot bring a claim under a contract to which it is not a party to receive performance stipulated for its benefit, even if the contract was concluded with the purpose to confer benefit to the third party.

The doctrine of privity has not always been a part of English law. Until 1861 in a number of cases it was confirmed that a third party could demand performance of a contract concluded for its benefit.³⁶ However, in 1861, in *Tweedle v. Atkinson* the court held that a third person does not have rights under a contract to which it is not a party.³⁷ The House of Lords confirmed this conclusion 50 years later in *Dunlop Pneumatic Tyre Company Ltd. v. Selfridge*.³⁸

The doctrine of privity was an obstacle for the normal development of business practices and for that reason a number of exceptions were developed by court practice and established by legal acts. For example, the Married Women's Property Act provided that wives who outlived their husbands had a right to bring claims against insurers under life insurance policies.³⁹

The doctrine of privity was widely criticized by judges, legal scholars, and practitioners. The common position on that issue was expressed by the Law Commission in a report, the main conclusion of which is that reforming the doctrine of privacy is necessary and should happen at the legislative level.⁴⁰ A draft law offered by the Law Commission was adopted by Parliament with certain amendments, which received royal assent and came into force on 11 November 1999.⁴¹

In accordance with Article 1(1) of the Contract (Rights of Third Parties), Act a person who is not a party to a contract (a "third party") may in his own right enforce a term of the contract if either of the following is met:

(a) the contract expressly provides that he may, or

36 E.g. *Dutton v. Poole* (1677) 2 Lev 211; quoted from M. A. Millner. *Ius Quaesitum Tertio: Comparison and Synthesis*. The International and Comparative Law Quarterly, Vol. 16, No. 2 (Apr., 1967), P.447.

37 Privity of Contract: Contracts for the Benefit of Third Parties. Report by the Law Commission of England and Wales. P.6, text available at http://lawcommission.justice.gov.uk/docs/lc242_privacy_of_contract_for_the_benefit_of_third_parties.pdf

38 Ibid P.8.

39 Ibid P.9-44

40 Ibid P. 164-173 u Appendix 1 (Draft Act).

41 Contracts (Rights of Third Parties) Act 1999. Text available at <http://www.legislation.gov.uk/ukpga/1999/31/contents>

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

Section 1(2) stipulates that the third party does not acquire a right 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. This norm provides for the presumption of the existence of a third party's right under a contract from which it gains some benefit. The presumption means that a third party is obliged to prove that a contractual term provides for the provision of some benefit. If a third party successfully proves that the burden of proof shifts to the debtor who should prove that the parties did not have an intention to make the contractual term enforceable by the third party.

A third party has a right to enforce a contract term only together with all other terms of the contract that are connected with the claim; a third party cannot "cherry-pick" advantageous contract terms and refer only to them.⁴²

2.1.2. USA. It was traditionally considered in the USA that contracts for the benefit of a third party do not create a right for the third party due to the effect of the doctrine of privity for a contract. However, American courts gradually washed out the doctrine.⁴³

In *Lawrence v. Fox* the court held that "a third party may only sue for breach of contract, however, if the contract was entered into for the party's direct benefit; if the third party's benefit is merely incidental, then it has no right to recovery on the contract.... Whether a third party is a direct beneficiary depends on the intention of the parties, which must be 'gleaned from a consideration of all of the contract and the circumstances surrounding the parties at the time of its execution.'"⁴⁴

The (First) Restatement of Contracts⁴⁵ tried to create the theoretical grounds for granting rights under a contract to third parties and distinguished two categories of third parties: Donee beneficiaries and creditor beneficiaries. Courts in different states define donee beneficiaries and creditor beneficiaries differently. One of the simplest definitions can be found in Tennessee: The beneficiary is classified as a donee when "a purpose to make a gift" is present, and as a creditor when performance "will satisfy an actual or asserted duty".⁴⁶

The authors of the (Second) Restatement of Contract faced a large number of cases where third party beneficiaries could not be classified as donees or creditors, as defined by the First Restatement. They had two options available, either to introduce new categories or to develop an

42 Michael Bridge. The Contracts (Rights of Third Parties) Act 1999. 5 *Edinburgh Law Review* P.93.

43 *Gifford v. Corrigan*, 117 N.Y. 257, 22 N.E. 756 (1889); *Lawrence v. Fox*, 20 N.Y. 268 (1859). Cases quoted from David M. Summers. *Third Party Beneficiaries and the Restatement (Second) of Contracts*. *Cornell Law Review*, Vol. 67, Issue 4, P.885

44 *Ibid.* P.886

45 Restatements are collections of rules and principles regulating different spheres. They are common opinions of leading experts on the state of law. See e.g. Charles E. Clarke. *The Restatement of the Law of Contracts*, 42 *Yale Law Journal* 643 (1933)

46 Harry G. Prince, *Perfecting the Third Party Beneficiary Standing Rule Under Section 302 of the Restatement (Second) of Contracts*, 25 *B.C.L. Rev.* 919 (1984).

analytical instrument that would allow defining when a third party should have rights under a contract.

The authors decided to combine both approaches. They developed a test to determine intent to benefit and at the same time used classification. In accordance with Section 302 of (Second) Restatement of Contracts:

(1) Unless otherwise agreed between the promisor and promisee, a beneficiary of a promisee is an intended beneficiary if recognizing the right to performance in the beneficiary is appropriate to effectuate the intention of the parties, and either

(a) the performance of the promise will satisfy an obligation of the promisee to pay money to the beneficiary, or

(b) the circumstances indicate that the promisee intends to give the beneficiary the benefit of the promised performance.

(2) An incidental beneficiary is a beneficiary who is not an intended beneficiary

In accordance with this approach, the courts should discover the intentions of the parties in order to make a decision regarding a third party's rights.

The benefit intention test stipulated by the (Second) Restatement of Contracts resolves a lot of problems that appeared when the (First) Restatement was applied.

A question closely connected with the intention to benefit a third party regards the evidence that is essential to prove the intention to benefit a third party. As is mentioned in the literature,⁴⁷ presumption against a third party's standing is one of the most commonly accepted aspects of proving the intention to benefit a third party.

In tipping the balance towards denying third party rights, the courts are making a judgment that exposing the promisor to a potential liability to a third party when the promisor has not explicitly contracted to assume that obligation is more undesirable than allowing a party to completely escape the consequences of breaching contract when the promisee is disabled from being interested in enforcing the promise.

2.1.3. Canada. In Canada, as in other common law countries, the doctrine of privity is in force.⁴⁸ It is actively criticized by the Supreme Court of Canada, which also created a number of exceptions. However, it insists that the reform should be legislative. In some provinces of Canada, such legislation was adopted and will be discussed below.

In the 1992 case *London Drugs Ltd.*, the Supreme Court of Canada carved out a "principled exception" to the traditional doctrine of contract privity and allowed a negligent third

47 See e.g. Harry G. Prince, Perfecting the Third Party Beneficiary Standing Rule Under Section 302 of the Restatement (Second) of Contracts, 25 B.C.L. Rev. 919 (1v984)

48 Except for Quebec and New Brunswick, which apply continental law. Quebec law will be discussed below.

party beneficiary to rely to a provision in their employer's contract, limiting liability for damaged goods to \$40.⁴⁹

The exception was further developed in the *Fraser River* case, where a third party beneficiary sought to rely on a contractual provision in defense against an action brought by one of the contractual parties – specifically the insurer. The Court held that the third party beneficiary was entitled to rely on waiving a subrogation clause, whereby the insurer expressly waived any right of subrogation against the third party beneficiary. In reaching its decision, the Court declared that the *London Drugs* decision was not limited to employer/employee situations and that a non-contracting third party could enforce the waiver or limitation if:

- 1) the parties to the contract intended to benefit the third party; and,
- 2) the third party was performing the very activities contemplated by the contractual provision.⁵⁰

Relying on these statements from the Supreme Court, some subsequent lower court decisions have interpreted the “principled exception” narrowly such that it could not be used by a third party as a sword, but only as a shield. That is, the exception would not allow a third party to sue on a contract, rather it would only apply where a third party seeks to rely on a provision in a contract to which it is not a party in its defense. Others have interpreted the exception more broadly.⁵¹

2.1.4. Other common law countries. In Australia the doctrine of privity was also not reformed at the legislative level. In Malaysia the situation is the same and no principled exception was developed. A number of exceptions were introduced by legal acts; furthermore there are court mechanisms that allow overriding the effects of the doctrine of privity, such as a broad judiciary interpretation of who can be considered a party to the contract. This mechanism was used by the Supreme Court in *Parimala a/p Muthusamy v. Projek Lebuhraya Utara-Selatan*.⁵²

New Zealand reformed the doctrine of privity by statute in 1982 when the Parliament of New Zealand adopted the Contracts (Privity) Act.⁵³ In accordance with Section 4 of the Act, where a promise contained in a deed or contract confers, or purports to confer, a benefit on a

49 The decision is available at <http://ca.vlex.com/vid/london-drugs-kuehne-nagel-international-37667470>

50 The decision is available at <http://ca.vlex.com/vid/fraser-river-pile-dredge-can-dive-services-37669614>

51 See e.g. Ontario Court of Appeal in *Tony & Jim's Holdings Ltd. v. Silva* (The decision is available at <http://www.canlii.org/en/on/onca/doc/1999/1999canlii969/1999canlii969.html>), British Columbia Court of Appeal in *R.D.A. Film Distribution Inc. v. British Columbia Trade Development Corp.* (Information is taken from the report of Law Commission of Canada on Privity of Contract and Third Party Beneficiaries 2007 available at <http://www.ulcc.ca/en/2007-charlottetown-pe/216-civil-section-documents/574-privity-of-contract-and-third-party-beneficiaries-2007?showall=&limitstart=>)

52 See Tan Pei Meng, Circumventing the Privity rule in Malaysia. *Journal of International Commercial Law and Technology* Vol. 4, Issue 4 (2009).

53 Text available at <http://www.legislation.govt.nz/act/public/1982/0132/latest/DLM63971.html>

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

The term “benefit” used in this section is given a wide meaning by Section 2 of the Act. It is defined as including (a) any advantage; (b) any immunity; and (c) any limitation or other qualification of an obligation or a right to which a person other than a party to the contract is or may be subject.

Section 4 creates a presumption that where a promise contained in a contract confers, or at least purports to confer, a benefit on a designated third party, the promisor will be under an obligation, enforceable upon a suit of that third party, to perform the obligation.

2.2. Continental law countries

2.2.1. Germany and other Germanic legal systems. In accordance with part 1 of §328 of the German Civil Code, performance to a third party may be agreed by contract with the effect that the third party acquires the right to demand the performance directly. In the absence of a specific provision, it is to be inferred from the circumstances, in particular from the purpose of the contract, whether the third party is to acquire the right, whether the right of the third party is to come into existence immediately or only under certain conditions, and whether the power is to be reserved for the parties to the contract to terminate or alter the right of the third party without his approval (part 2 §328 GCC).

The German Civil Code stipulates rules that allow defining whether the third party has a right to demand or not. In certain cases the Code sets forth a presumption of absence of third party rights. For instance, §329 provides that “where one party to a contract agrees to satisfy an obligee of the other party without assuming the obligation, then in case of doubt it may not be assumed that the obligee is to acquire the right to demand satisfaction from him directly.” This rule is a result of application of the doctrine of “main” and “secondary” purpose of contracts for the benefit of third parties.⁵⁴

Courts are obliged to find out the intentions of the parties. The general tendency in contemporary court practice is to let the third party enforce a contract when the intentions of the parties are not clear.⁵⁵

54. It was mentioned when the position of A.M. Nolken was discussed. See also next paragraph.

55 Zweigert K., Kötz H. Introduction to Comparative Law in the Sphere of Private Law. Vol. 2. Moscow. Mezhdunarodniye Otnosheniya. 2000. P. 184). (Цвайгерт К. Кёцц Х. Введение в сравнительное правоведение в сфере частного права: В 2-х

German courts also allow third parties to enforce contracts having protective effect for third parties.⁵⁶

A similar approach is used in Switzerland. In accordance with part 2 of article 112 of Part Five of the Swiss Civil Code, a third party or his legal successors have the right to compel performance where that was the intention of the contracting parties or is the customary practice.⁵⁷

The approach of Germany was also perceived by some countries that do not have historic connections with German law, such as Israel.⁵⁸

2.2.2. France and other countries which implemented French law. Article 1119 of the French Civil Code provides that contracts only have effect between the parties. However, Article 1121 makes an exception from the general rule and allows the parties to make “stipulation pour autrui”. Such a contract for the benefit of a third party is valid if it is the condition of a contract made for the stipulator/promisee or of a gift made to another.⁵⁹

The growth in popularity of life insurance at the end of the 19th century made French courts broaden the definition of contracts for the benefit of third parties. It is mentioned in the literature that, by way of broad and constitutive interpretation, French courts and scholars have overcome the limits set by the Civil Code and made almost any contracts for the benefit of third parties enforceable.⁶⁰ The most important authority is a decision of the Court of Appeals of 1886 on life insurance contract where the court held that the right of a third party is “droit proper”, or, in other words, a right based on contractual obligation (stipulation).⁶¹

Other legal systems based on French law developed in a similar manner. For example, the Quebec Civil Code of 1866 used the approach of the Napoleonic Code. However, with time Quebec legal practice developed an understanding of contracts for the benefit of third parties that is nowadays applied.

The Legal regime of contracts for the benefit of third parties is stipulated in Articles 1444-1450 of the Civil Code of Quebec.⁶² The code provides that the stipulator need only have a moral interest in bestowing a benefit on the third person. Other than the requirement of a clearly

тг. – Том 2 – Пер. с нем. – М.: Междунар. отношения, 2000, С.184).

56 Ibid. P.186, 187

57 English translation of Swiss Civil Code is available at <http://www.admin.ch/ch/e/rs/220/a112.html>

58 English text of Contracts (General Part) Law, 1973) available at <http://www.israelinsurancelaw.com/contract-laws/contracts-general-part-law-1973.html>

59 M. Boodman. Third-Party Beneficiaries in Quebec Civil Law. Canadian Business Law Journal. Vol. 35 (2001). P.218.

60 Zweigert K., Kötz H. Ibid. P.187

61 Ibid. P.188

62 The Quebec Civil Code in English is available at <http://www.canlii.org/en/qc/laws/stat/lrq-c-c-1991/>

expressed or implied intention on the part of the stipulator to benefit a third person, the stipulation for another is subject to the normal rules for forming a contract.

In accordance with Article 1411 of the Italian Civil Code, contracts for the benefit of third parties are valid when the promisee has his own interest. In that case, the third party gains an independent right to enforce a contract for his or her benefit, if otherwise not stated by the contract.⁶³ Here a presumption similar to the one of English law is stipulated.

Not all countries of French tradition came to the broad interpretation of contracts for the benefit of third parties. For example, according to Article 154 of the Civil Code of Egypt,⁶⁴ a promisee has the right to conclude a contract for the benefit of a third party if he has a material or moral reason to do so. After that, the third party has a right to demand from the debtor performance of the contract. It is mentioned in the literature that, for a benefit promised to a third party to be valid, the contract should directly confer benefit to the third party. Third parties do not gain rights when the promisee sets forth an obligation for his benefit, but the third party gains performance. For instance, Egyptian law does not see liability insurance contracts as a contract for the benefit of a third party.

2.2.3. Other continental jurisdictions. The Civil Code of Estonia⁶⁵ distinguishes between contracts for the benefit of third parties and contracts that have a protective effect for third parties.

A contract may prescribe or the nature of an obligation may indicate that the obligation is to be performed for the benefit of a third party in lieu of the obligee (a contract for the benefit of a third party). A third party may require performance of a contract if so prescribed by the contract or determined from law (Paragraphs 1 and 2 of Article 80 of Civil Code of Estonia).

Contracts having protective effect are described as follows:

(1) A contract may prescribe the obligation to take into account the interests or rights of a third party to the same extent as the interests or rights of the obligee. Such obligation shall be presumed if:

1) in the course of performing the contract the interests and rights of the third party are at risk to the same extent as the interests and rights of the obligee; and,

2) the intent of the obligee to protect the interests and rights of the third party can be presumed; and,

63 Il Nuovo Codice civile e le leggi complementari / a cura di Francesco Bartolini, Casa Editrice la Tribuna, Piacenza, 2007

64 Salah-Eldin Abdel-Wahab, John H. Brinsley. The Stipulation for a Third Person in Egyptian Law. The American Journal of Comparative Law. Vol. 10, 1961

65 English translation available at <http://www.legaltext.ee/text/en/X30085K3.htm>

3) the third party and the intent of the obligee to protect the interests and rights of the third party are identifiable by the obligor.

(2) In the case of non-performance of the obligation, specified in subsection (1) of this section, the third party may claim compensation for damage caused thereto.

In accordance with part 1 of Article 6:253 of the Dutch Civil Code,⁶⁶ an agreement creates the right for a third party to claim performance from one of the parties or to appeal otherwise against one of them to the observance of their agreement, if the agreement contains a stipulation to that effect (a third party clause) and the third party has accepted this stipulation. The third party may as well, to the extent that this is in conformity with the underlying purpose of the stipulation (third party clause), derive rights from it over the period prior to the moment on which he had accepted that stipulation. Part 1 of Article 6:254 provides that after the third party has accepted a stipulation made for its benefit, he will be a full party to the agreement.

Contracts having a protective effect for third parties are also accepted in the Netherlands (even though this term is not used there). According to Article 6:257, if, in order to ward off his liability for damages caused by one of his subordinates, a party to an agreement may raise a defense against his counterparty that directly or indirectly results from their agreement, then his subordinate, if he is held liable for these damages by the counterparty, may as well raise that defense as if he himself was a party to that agreement.

Contract law of the Republic of South Africa regulates contracts for the benefit of third parties in a similar way.⁶⁷

2.2.4. International codifications. According to part 1 of article 6.110 of the Principles of European Contract Law,⁶⁸ a third party may require performance of a contractual obligation:

1) when its right to do so has been expressly agreed upon between the promisor and the promisee; or,

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

Article 5.2.1 of the UNIDROIT Contract Law Principles 2010⁶⁹ provide that the parties may confer by express or implied agreement a right on a third party. The existence and content

66 English translation available at <http://www.dutchcivillaw.com/civilcodebook066.htm>

67 L. Getz. Contracts for the Benefit of Third Parties. Acta Juridica. 1962.

68 Available at <http://www.jus.uio.no/lm/eu.contract.principles.1998/doc.html#338>

69 Principles and Comments available at

<http://www.unidroit.org/english/principles/contracts/principles2010/integralversionprinciples2010-e.pdf>

of the beneficiary's right against the promisor are determined by the agreement of the parties and are subject to any conditions or other limitations under the agreement.⁷⁰

It is mentioned in comments to Article 5.2.1 of the UNIDROIT Principles that the mere fact that a third party will benefit from the performance of the contract does not in and of itself give that third party any rights under the contract.

UNIDROIT also accepts contracts having protective effect for third parties. According to Article 5.2.3 of the Principles, the conferment of rights to the beneficiary includes the right to invoke a clause in the contract that excludes or limits the liability of the beneficiary.

3. The Purpose of Conclusion of Contracts for the Benefit of Third Parties

3.1. Legal Consequences as a Purpose of a Contract

It follows that the most important necessary characteristic of contracts for the benefit of third parties is the purpose of a contract to confer certain benefits on a person who is not a party to that contract. In all legal orders, except for Soviet law, this characteristic was considered to be inherent to all contracts for the benefit of third parties.

But is this characteristic also sufficient? In other words can it be used as a qualifying characteristic?

The general question which arises was formulated above and I will repeat it here: The idea is whether any contract between two persons to confer material benefit on a third person is a contract for the benefit of a third party. Is it right that in order to provide a third person with a right to enforce a contract for its own benefit, the will of the parties to provide material benefit to the third party is not sufficient? And is it essential that the will of the parties provide the third party not just with a material benefit but also a right to demand its provision?

I would also like to raise a more general question: Is it correct that the purpose of the parties concluding a contract is the creation of not only factual, but also legal consequences? When the question is set forth this way, it is easy to answer. It is enough to refer to Part 1 of Article 420 of the Civil Code, where the following definition of a contract is given: "A contract shall be considered to be an agreement of two or several persons concerning the establishment, change, or termination of civil rights and duties." Thus, exactly those agreements that create legal consequences are considered to be contracts in Russian legal practice.

But how can one decide whether an agreement creates rights and duties? The same problem arises regarding how to define whether the purpose of an agreement is to create legal consequences.

In order to find out how this general problem is solved in practice, let us consider agreements that are frequently used where the parties stipulate that such agreements do not create legal consequences. For instance, so-called “organizational agreements” are concluded where the parties define general terms for a big number of standard agreements that they are planning to conclude in the future. Today such contracts do not create any legal consequences until one of the planned contracts is concluded on terms set forth by the organizational contract.

However, Draft Amendments to the Civil Code of the Russian Federation⁷¹ include Article 429.1, a “Framework Contract”, part 2 of which contains the following norm: “The general terms contained in a framework agreement shall apply to relations between the parties that are not regulated by separate contracts, including situations when such contracts were not concluded.”

It is surprising to find out from the literature that no textbooks on Russian Civil Law, commentaries to the Civil Code, or books on contract law answer the question of how to define whether an agreement is a contract based on the text of an agreement – in other words, whether an agreement creates legal rights and duties.

There are disputes connected with this problem regarding the legal consequences of signing a memorandum of understanding. In most cases, such memoranda are treated as a preliminary contract when they contain all material terms of the contract to be concluded and they are not given legal effect when any material terms are missing.⁷²

Thus, there is practically no reference on how to check whether a particular agreement has legal effect when a dispute arises.

In my opinion, when separating contracts from all agreements, Russian civil law follows the principle that an agreement of the parties, which purports to provide certain benefits to its parties, creates rights and duties, meaning that it is a contract unless proven otherwise.

3.2. The Purpose of a Contract for the Benefit of a Third Party and Its Qualification

The main disputes connected with contracts for the benefit of third parties arise in situations when it is clear that the main purpose of a contract is to confer benefit to a third party,

71 Available at the website of the State Duma at

<http://asozd2.duma.gov.ru/main.nsf/%28SpravkaNew%29?OpenAgent&RN=47538-6&02>

72 Relatively detailed research into court practice, including Russian, on that issue is presented in Burkov A.Y. Memorandum of Understanding in international practice: legal force // *Pravo i Ekonomika*. 2010. No. 11. P. 20-23. (Бурков А.Ю. Протокол о намерениях в международной практике: юридическая сила // *Право и экономика*. 2010. N 11. С. 20 – 23).

but when it is unclear whether the parties to the contract also intended to provide the third party with a right to demand this benefit.

In my opinion, in this situation there is no need to deviate from the general rule of the Russian legal order: If a contract provides for conferring a benefit to a person, it is presumed that he or she also obtains the corresponding right. If a benefit is conferred to a third party, we should presume that this person is also given a right to demand the provision of the benefit.

As shown above, this rule is implemented in many jurisdictions, such as in most common law countries, in Italy, Egypt, and so forth. Let me restate here that the rule in force in England is that the third party is obliged to prove that the parties, having concluded a contract, intended to confer a certain benefit upon him or her, and, when it is proven, the parties can only contest their intention to give him or her the right to enforce the contract.

Here I suggest paying attention to one detail that distinguishes the suggested presumption from the English approach of “until proven otherwise”. Specifically, the clause “Until other intentions of the parties are proven.” In practice there are plenty of cases when the intention of the parties to confer a benefit on a third party is obvious, but the existence or non-existence of intentions to give a third party the right to enforce a contract is not clear. The presumption shall be introduced for such cases.

I would also like to draw your attention to the use of the phrase “purports to confer a benefit” in the text of the English Contracts (Rights of Third Parties) Act. If we use the more direct wording “confers benefit”, contracts for the provision of security services for transported cargo, discussed in the previous section, shall not be considered contracts for the benefit of third parties. However, the contract term on securing cargo exactly purports to benefit the cargo recipient.

The word “purports” gives very broad freedom of discretion to law enforcement bodies. Other trends in Russia are directed to this as well. Draft Amendments to the Civil Code introduce the general requirement to act in good faith to the text of the Civil Code (new versions of Articles 1 and 10 of the Civil Code). It is hardly possible to broaden even further the limits of discretion for law enforcers, including courts. This, however, is dictated by the needs of business practices and accepted throughout the whole world.⁷³

I assume that part 1 of Article 430 of the Civil Code should be rephrased similar to the English approach. Such contracts shall be described as contracts for the benefit of third parties, which purport to benefit third parties that are mentioned or not mentioned in the contract. The

73 See e.g. Novitskiy I.B. Principle of good faith in draft on law of obligations // Vestnik Grazhdanskogo Prava. 1916. Petrograd, 1916, No.6. P. 81. (Новицкий И.Б. Принцип доброй совести в проекте обязательственного права. // Вестник гражданского права, Пг, 1916, № 6, с.81).

right to enforce a contract for his or her benefit should belong to a third party in the following cases: (a) If such right is directly stipulated in the contract; and, (b) If it is not proven that the parties did not intent to provide the third party with such right, or that such a right cannot be stipulated due to requirements of law. Such a rule will comply with modern Russian legal practice and will reduce the number of disputes, or at least will make their resolution easier.

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