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An App for Third Party Beneficiaries

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AN "APP" FOR THIRD PARTY BENEFICIARIES

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Abstract: Every year, more than 100 reported court opinions consider the question of whether an outsider can sue for damages under a contract made by others—in part because the law is so ambiguous. While contract enforcement by a third party is controlled largely by the facts of the particular case, it also materially depends upon the relevant legal standards. At present, not just the standards, but also the reasons for these standards, are unclear.

Eighty years ago, Lon Fuller,[1] a professor teaching contracts at a then-Southern law school,[2] and William Perdue, a student at that school, significantly clarified and improved decision-making on damages issues in contract law by proposing a new vocabulary and analytical model.[3] The senior author of this Article is a professor at a Southern law school, but he does not need an academic Lloyd Bentsen[4] to tell him that he is "no Lon Fuller," and

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1. *See generally* Albert M. Sachs, *Lon Luvois Fuller*, 92 HARV. L. REV. 349 (1978) (describing the legacy of Lon Fuller).

2. Professor Fuller was a professor at Duke Law School in Durham, North Carolina—a Southern town if ever there was one. (Remember the movie *Bull Durham*?) While Duke Law School is still located in the Southern town of Durham, its website shows that only 19% of its students are from the South. *Class of 2019 Profile*, DUKE LAW, https://law.duke.edu/admis/classprofile/ [https://perma.cc/L4MT-7YDG]. The website provides no information about how many of that 19% went to Eastern prep schools and Ivy colleges or how many of the faculty come from the South. Duke is, of course, a fine law school. Duke is no longer a Southern law school.

3. *See* L.L. Fuller & William R. Perdue, Jr., *The Reliance Interest in Contract Damages*, 46 YALE L.J. 52, 53–54 (1936).

4. *See* Educational Video Group, *Excerpt from Vice Presidential Debate in 1988 Between Lloyd Bentsen and Dan Quayle*, YOUTUBE (Oct. 1, 2012), https://www.youtube.com/watch?v=9PCsXqbSZxc (last visited Nov. 4, 2016). The late Professor Robert Summers would have happily played the role of Senator Bentsen. In Professor Summers' biography of Lon Fuller, Professor Summer referred to Professor Fuller as "one of the four most important American legal theorists of the 20th century." *See* ROBERT S. SUMMERS, L. LON FULLER 1 (1984). The senior author of this article was not one of the other three.

the younger co-authors hold no "William Perdue illusion," given that Mr. Perdue was the father-in-law of their law school dean. Nonetheless, we believe that the new vocabulary and analytical model we are proposing would clarify and improve decision-making on third party contract rights.

INTRODUCTION

The third party beneficiary doctrine is the red-headed stepchild of contract law as contract law is "practiced" in law schools. In the

standard contracts casebook, two or three third party beneficiary cases are inserted at the back of the book.[5] Most contracts professors do not even cover the third party beneficiary cases.[6]

Moreover, there has been comparatively little attention to third party beneficiary concepts in American law reviews. The two most cited third party beneficiary articles were published in 1985[7] and 1992.[8] The last lead article devoted to the general topic of third party beneficiary law was published in 1993.[9]

Third party beneficiary law gets far more attention from those who practice contract law in law offices and courtrooms.[10] Practitioner texts regularly address third party beneficiary possibilities, recommending that commercial contracts include provisions excluding third party beneficiaries.[11] Such provisions are often enforced.[12]

However, these recommendations that commercial contracts include provisions excluding third party beneficiaries are not universally followed, or when followed, the provisions are ignored by plaintiffs' attorneys anyway.[13] We have found more than 500 judicial opinions

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5. *E.g.*, IAN AYRES & RICHARD E. SPIEDEL, STUDIES IN CONTRACT LAW 1168–91 (7th ed. 2008) (chapter 9 of 9); JACK GRAVES, LEARNING CONTRACTS 694–707 (2014) (chapter 10 of 10).

6. *Cf.* MARK P. GERGEN, TEACHER'S MANUAL TO BASIC CONTRACT LAW NINTH EDITION 149 (2013) ("Chapter 19. Third-Party Beneficiaries (pp.941–987) I do not cover these materials.").

7. Anthony Jon Waters, *The Property in the Promise: A Study of the Third Party Beneficiary Rule*, 98 HARV. L. REV. 1109 (1985).

8. Melvin Aron Eisenberg, *Third Party Beneficiaries*, 92 COLUM. L. REV. 1358 (1992).

9. Jean Fleming Powers, *Expanded Liability and the Intent Requirement in Third Party Beneficiary Contracts*, 1993 UTAH L. REV. 67. There have been subsequent law review articles that discuss third party concepts as a part of some other, more specific topic. *See, e.g.*, George S. Geis, *Broadcast Contracting*, 106 NW. U. L. REV. 1153 (2012); Nicolas Cornell, *The Puzzle of the Beneficiary's Bargain*, 90 TUL. L. REV. 75 (2015); Alan Schwartz & Robert E. Scott, *Third Party Beneficiaries and Contractual Networks*, 7 J. OF LEGAL ANALYSIS 325 (2015).

10. *Cf.* Harry G. Prince, *Perfecting the Third Party Standing Rule Under Section 302 of the Restatement (Second) of Contracts*, 25 B.C. L. REV. 919, 920 (1984) ("A subject that should be of measureable concern to every practicing lawyer whose clients have even a minimal involvement in the American socio-economic environment.").

11. *See, e.g.*, SCOTT T. WITTAKER, ET AL., ABA SECTION OF BUS. LAW, WHO INVITED YOU? THIRD PARTY BENEFICIARY ISSUES IN M&A TRANSACTIONS 4–134 (2005), http://apps.americanbar.org/buslaw/newsletter/0038/materials/pp7.pdf [https://perma.cc/S7ZQ-K3TU].

12. *See, e.g.*, Fornazor Int'l, Inc. v. Huntsman, No. 2:14-CV-291 TS, 2015 WL 6142962, at *8 (D. Utah Oct. 19, 2015) ("Utah courts have dismissed a third party beneficiary claim pursuant to a Rule 12(b)(6) motion where the contract contained a clause declaring that there was no intended third-party beneficiary.").

13. *Id.* ("Fornazor argues that [the] 'no third party beneficiary' disclaimer does not preclude a factual finding of the third party beneficiary status in the face of conflicting evidence. However, that is not the law in Utah."); *see also* Wolf v. Celebrity Cruises, Inc., 101 F. Supp. 3d 1298 (S.D. Fla. 2015) ("The Tour Operator Agreement at issue here contains the following language with respect to third party beneficiaries: 'Other than as expressly set forth herein, this Agreement shall not be

issued in the last five years that have considered the question of when a person, who is not a party to a contract, is able to enforce that contract because the individual is an "intended third party beneficiary."[14]

Most of the cases use not only the term "intended third party beneficiary," but also the terms "promisor" and "promisee." These familiar terms can be confusing because in most contracts each party is making a promise to the other. In third party beneficiary terminology, the person whose promise the third party is seeking to enforce is the promisor and the other contracting party is the promisee.[15]

Consider this hypothetical:[16] Ed Blomquist contracts with Bud Jorgenlen to buy Bud's Butcher Shop in Luverne, Minnesota. Ed breaches the contract. Bud's Butcher Shop closes. Noreen Vanderslice, who worked at the butcher shop, sues Ed for breach of contract. Even though promisor Ed made his promise to promisee Bud, courts in Minnesota and elsewhere will, today, hold that third party Noreen can recover from promisor Ed for breach of contract if Noreen is an "intended third party beneficiary."[17]

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deemed to provide third persons with any remedy, claim, right, or action or other right.' Through its express terms, no reading of that language would allow for a finding of either an express or implied intent by the parties to primarily or directly benefit Mr. Wolf. Not only does the contract expressly disclaim any intent to provide third parties with any rights, but there are no other provisions in the contract from which to infer any intent to directly benefit passengers like Mr. Wolf. Mr. Wolf argues that the requisite intent should be gleaned from contract provisions requiring OCT to acquire insurance before operating, but I disagree." (internal citations omitted)).

14. Our use of the term "intended third party beneficiary" to describe a third party who can enforce a contract is consistent with the usage of most courts and the Restatement. *See* RESTATEMENT (SECOND) OF CONTRACTS § 302 (AM. LAW INST. 1979). There are some courts that use the term "third party beneficiary" to mean a third party who can enforce a contract. *See, e.g., In re* Lehman Brothers Holding, Inc., No. 08-13555, 2014 WL 2766164 (Bankr. S.D.N.Y. June 18, 2014) ("Under New York law, a party claiming *to be a third-party beneficiary* of a contract bears the burden of demonstrating that the parties to the contract intended to confer a benefit on the third party." (emphasis added)).

15. SUZANNE DARROW-KLEINHAUS, ACING CONTRACTS 335–36 (2010) ("[T]he 'promisor' is the contracting party who is to render the performance to the beneficiary and the 'promisee' is the contracting party whose right to performance has been conferred on the beneficiary.").

16. *But cf. Fargo (TV Series)*, WIKIPEDIA, https://en.wikipedia.org/wiki/Fargo [https://perma.cc/7WXH-6LRT] (noting each episode of the TV series Fargo begins with the superimposed text, "This is a true story.").

17. *See* Caldas v. Affordable Granite & Stone, Inc., 820 N.W.2d 826, 832 (Minn. 2012) (defining intended third party beneficiary as "intended beneficiary with legal rights under a contract," relying on the RESTATEMENT (SECOND) OF CONTRACTS § 302 (AM. LAW INST. 1979)). The result would be the same if the subject matter of the contract were the sale of a butcher shop in England such as Flackies of Luttenworth, Leicestershire. *See* FLACKIES OF LUTTENWORTH, http://flackies.net/ [https://perma.cc/KTS6-TBDX]. In November of 1999, the Contracts (Rights of Third Parties) Act 1999 came into effect in England, allowing a third party to enforce a contract term if "the term purports to confer a benefit on him." *See* Contracts (Rights of Third Parties) Act 1999 c. 31, § 1(1)

At present, Noreen's contract law rights turn on intent. Any doctrine based on intent is inherently ambiguous from the start. In third party beneficiary cases, ambiguity is especially problematic because of unanswered questions about: (1) whose intent is relevant; and (2) what the relevant intent is.

Hence the cases are widely divided as to outcome.[18] And, collectively, these cases present an analytic mess in dire need of a cleanup. This paper undertakes that project. It is an attempt to clean up the doctrine as well as to answer its basic questions. That project, we contend, requires a different vocabulary and, more importantly, a different analytical approach—an approach that focuses on practical consequences.

The primary practical consequence of determining that Noreen is an "intended third party beneficiary" is that Noreen becomes an additional possible plaintiff on the contract entered into by Ed and Bud. And determining that Noreen is an additional possible plaintiff can have possible practical consequences to the person she sues for breach of contract. Accordingly, the operative question should be whether Ed and Bud had reason to know at the time of their contract that Noreen could be an additional possible plaintiff ("APP"). Our approach substitutes an "APP" for third party beneficiary.

To be clear, we do not contend that our approach will eliminate litigation over whether a person who was not a party to a contract can nonetheless sue for breach of that contract. Nor do we contend that it will necessarily effect significant changes in the results of such litigation. Rather, our claim is that our approach should simplify the litigation process and should produce litigation results more consistent with generally accepted contract concepts.

This Article proceeds in three parts. Part I explains the development of third party beneficiary law. Part II looks to recent cases to illustrate problems with the present third party beneficiary law. Part III explains our proposed analytical framework.

(Eng.), http://www.legislation.gov.uk/ukpga/1999/31/pdfs/ukpga_19990031_en.pdf [https://perma.cc/4QGE-CN9B]; *see generally* ROBERT MERKIN, PRIVITY OF CONTRACT: THE IMPACT OF THE CONTRACTS (RIGHTS OF THIRD PARTIES) ACT 1999 (2000).

18. The cases are even divided as to whether the term is "third party beneficiary" or "third-party beneficiary." Indeed, sometimes the same judge seems to be "divided," using both terms in the same opinion. *See, e.g.*, J.C. Penney Properties, Inc. v. Hiram LL, LLC, No. 1:13-CV-02984-CC, 2016 WL 302095 (N.D. Ga. Jan. 25, 2016). Most cases and commentaries use the term "third party beneficiary" and so does this article.

I. AN EXPLANATION OF THIRD PARTY BENEFICIARY LAW: HOW WE GOT TO WHERE WE ARE

Generally, a person has no legal right to enforce a contract they[19] did not make. Courts and commentators invoke the contract concept of privity to explain this general rule.

A. Privity

An article by Jesse W. Lilienthal,[20] in the first issue of the *Harvard Law Review*, provides a short and easy-to-understand[21] working explanation of privity:

> PERHAPS the tradition in the elementary law of contracts most thoroughly grounded in the minds of law students is the general proposition that an agreement between A and B cannot be sued upon by C, even though C would be benefited by its performance. It always was, with Harvard law students at all events, an article of faith that rights founded on contract belong to the person who has stipulated for them; and that even the most express agreement of contracting parties would not confer any right of action on the contract upon one not a party thereto.[22]

Lilienthal's statement is followed by three items: (1) a footnote from the law review editors explaining that "[t]his doctrine [privity] is not taught in the School at the present day";[23] (2) an attempt at explaining the case that "exploded"[24] the privity rule, *Lawrence v. Fox*;[25] and (3) repeated efforts to explain later courts' application of *Lawrence v. Fox*.[26]

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19. Jeff Guo, *Sorry, Grammar Nerds. The Singular 'They" Has Been Declared Word of the Year*, WASH. POST (Jan. 8, 2016), https://www.washingtonpost.com/news/wonk/wp/2016/01/08/donald-trump-may-win-this-years-word-of-the-year/ [https://perma.cc/B2Y8-7P77].

20. Despite contributing only one article to third party beneficiary law, Jesse Lilienthal was an uncommonly accomplished and interesting person. *See* LILLIE BERNHEIMER LILIENTHAL, IN MEMORIAM: JESSE WARREN LILIENTHAL (1921), https://archive.org/details/inmemoriamjessew00liliiala [https://perma.cc/CEZ7-WLAA].

21. For a more complete (and complex) explanation of privity, see generally MICHAEL FURMSTON & GREGORY TOLHURST, PRIVITY OF CONTRACTS (2015); VERNON VALENTINE PALMER, THE PATHS TO PRIVITY (1992).

22. Jesse W. Lilienthal, *Privity of Contracts*, 1 HARV. L. REV. 226, 226 (1887).

23. *Id.* at 226 n.1. This footnote inserted by the student editors is consistent with the surprisingly conversational tone of the article—very different from the tone of the articles in volume 129.

24. *Id.* at 226. *But cf.* ARTHUR CORBIN, CORBIN ON CONTRACTS § 778 (1951) [hereinafter CORBIN] ("It is sometimes believed that all that is necessary to bring the third party into 'privity' with the promisor is that the contract shall be expressly made for his benefit.").

25. 20 N.Y. 268 (1859).

26. Lilienthal, *supra* note 22, at 226.

"At present day," privity is no longer taught at most law schools—not just "the School"[27]—except in answering the question of when third parties can enforce warranties of quality in sale of goods contracts made by others. Section 2-318 of the Uniform Commercial Code (UCC) answers this question.[28]

Our paper does not deal with section 2-318 of the UCC. Section 2-318 has been fully explored and explained by other articles.[29] Courts have comparatively few problems applying section 2-318 to determine whether a person who was not a party to a sale of goods contract can still recover for breach of a UCC warranty. Section 2-318's answers[30] to the question of when third parties can enforce warranties arising from sale of goods contracts[31] made by others are based on a public policy of balancing the protection of third parties from defective products, and the protection of sellers from unlimited liability. Section 2-318 does not look to the intention of the parties and is not based on cases like *Lawrence v. Fox*.[32]

Courts continue to have problems applying the common law's answers to the question of when third parties have rights under contracts—answers based on the intention of the parties and cases like *Lawrence v. Fox*. And so, like Jesse Lilienthal in volume 1 of the *Harvard Law Review*, we first try to explain *Lawrence v. Fox*.

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27. There are contracts casebooks that do not even have an index entry for "privity." *See, e.g.*, RANDY BARNETT, CONTRACTS (4th ed. 2008); DAVID G. EPSTEIN, BRUCE A. MARKELL & LAWRENCE PONOROFF, CONTRACTS: MAKING AND DOING DEALS (4th ed. 2014). The absence of "privity" from the index is more of a commentary on the "quality" of the index prepared by one of the co-authors than the book's coverage of third party beneficiary law prepared by a different one of the co-authors.

28. U.C.C. § 2-318 (AM. LAW INST. & UNIF. LAW COMM'N 2002).

29. *See, e.g.*, David G. Epstein, *Strict Liability in Tort: A Modest Proposal*, 70 W. VA. L. REV 1, 7–11 (1967).

30. UCC § 2-318 provides three alternative balances. Happily, an article comparing the various versions of the Uniform Commercial Code's section 2-318 with the various versions of the common law of third party beneficiary has already been written. *See* Gary Monserud, *Blending the Law of Sales with the Common Law of Third Party Beneficiary*, 39 DUQ. L. REV. 111 (2000).

31. We use the qualifying term "arising from sale of goods contracts" because neither UCC § 2-314's implied warranty of merchantability nor UCC § 2-315's implied warranty of fitness depends on the intention of the parties. U.C.C. §§ 2-314–15 (AM. LAW INST. & UNIF. LAW COMM'N 2002).

32. In a review of section 2-318, the Permanent Editorial Board Study Group called the third party beneficiary analysis for extension of warranties "a fiction." PERMANENT EDITORIAL BD. FOR THE UNIF. COMMERCIAL CODE, AM. LAW INST. & NAT'L CONFERENCE OF COMM'RS ON UNIF. STATE LAWS, PEB STUDY GROUP UNIFORM COMMERCIAL CODE ARTICLE 2: PRELIMINARY REPORT, pt. 3, at 110 (1990).

B. Lawrence v. Fox

Most law review commentaries begin the discussion of third party beneficiary law with the facts[33] of *Lawrence v. Fox*,[34] an 1859[35] case. Often referred to as the "landmark" third party beneficiary case,[36] *Lawrence v. Fox* involved a third party who was a creditor of the promisee and was expressly named in the contract. Lawrence had loaned $300 to Holly.[37] The next day, Holly loaned the same amount of money to Fox.[38] In return, Fox agreed to repay the $300 loan from Holly by paying Lawrence, thus extinguishing Holly's $300 debt to Lawrence.[39] When Fox failed to pay the $300 to Lawrence, Lawrence sued Fox for breach of contract.[40] The jury found for the plaintiff Lawrence. A divided Court of Appeals affirmed.[41]

There was no dispute about intent in *Lawrence v. Fox*. The only fact disputed by the defendant Fox was the existence of Holly's debt to the plaintiff Lawrence.[42] The appellate court concluded that there was "clearly competent" evidence of this debt.[43]

The dispute in *Lawrence v. Fox* was over the legal significance of an undisputed fact—that Lawrence was not a party to the contract, i.e., "the

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33. Professor Lawrence Cunningham explains why he begins his discussion of third party beneficiary law: "[e]ach formulation of a legal rule depends on the facts of the case germinating the rule . . . ." Lawrence A. Cunningham, *The Common Law as an Iterative Process*, 81 NOTRE DAME L. REV. 747, 750 (2006).

34. 20 N.Y. 268 (1859).

35. 1859 was thus not only the year for *On the Origin of the Species* but also the origins of third party beneficiary law. CHARLES DARWIN, ON THE ORIGIN OF THE SPECIES (1859).

36. Schaefer v. Aetna Life & Casualty Co., 910 F. Supp. 1095, 1099 n.14 (D. Md. 1986); JOSEPH M. PERILLO, CALAMARI & PERILLO ON CONTRACTS 578 (6th ed. 2009). *But see* CORBIN, *supra* note 24, at § 827. ("*Lawrence v. Fox*, can hardly . . . be said to have created a new rule of law."). Of course, a case can be a "landmark" even though it does not create a new rule of law. Consider, for example, the law review descriptions of *Alaska Packers' Ass'n. v. Domenico*, 117 F. 99 (9th Cir. 1902), an opinion that not only relies on but liberally quotes from two prior cases. Paul F. Kirgis, *Bargaining with Consequences, Leverage and Coercion in Negotiations*, 19 HARV. NEGOT. L. REV. 69, 123 (2014) (describing *Alaska Packers* as the "most famous case of this type"); Rachel Arnow-Richman, *The Role of Contract in the Modern Employment Relationship*, 10 TEX. WESLEYAN L. REV. 1, 7 (2003) ("chestnut case").

37. *Lawrence*, 20 N.Y. at 269.

38. *Id.*

39. *Id.*

40. *Id.*

41. *Id.* For an extended discussion of the facts of *Lawrence v. Fox*, see Anthony Jon Waters, *The Property in the Promise: A Study of the Third Party Beneficiary Rule*, 98 HARV. L. REV. 1109, 1116–48 (1985).

42. *Lawrence*, 20 N.Y. at 269.

43. *Id.* at 270.

want of privity between the plaintiff and defendant."[44] The defendant Fox contended that under New York law, only a contract party could maintain an action on a contract, except in the case of a trust.[45] The majority opinion rejects this contention, stating "a promise made to one for the benefit of another, he for whose benefit it is made may bring an action for its breach"[46] and concludes, "if . . . a more strict and technically accurate application of the rules would lead to a different result . . . the effort should not be made in the face of *manifest justice*."[47]

The opinion does not provide a legal principle based explanation for its less "strict and technically accurate application of the rules" of privity or when courts should be less "strict and technically accurate."[48] What is the "manifest justice" of Lawrence's claim? Is it anything more than that a debt was owed to him, and the contract between Fox and Holly provided for the payment of that debt?

The "manifest justice" in *Lawrence v. Fox* becomes more understandable by slightly changing the facts. Assume that Lawrence National Bank makes a home loan to Holly. Fox later buys the house from Holly and agrees to assume the mortgage, i.e., Fox promises to make the mortgage payments to Lawrence National Bank.

If Fox later breaches this contract with Holly and fails to make the mortgage payments to Lawrence National Bank, Lawrence National Bank has contract-law rights under this contract it did not make. A rule recognizing the contract rights of a third party when that party is a creditor of the promisee and is expressly named in the contract is easy to understand, and easy to apply. This is "manifest justice."

There is nothing in the majority opinion in *Lawrence v. Fox* to suggest that it should be limited to creditor third parties. And there are later New York cases recognizing the contract rights of third parties

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44. *Id.* at 271.

45. *Id.* at 270 (based on a narrow reading of an earlier case, Farley v. Cleveland, 4 Cow. 432 (N.Y. Sup. Ct. 1825), *aff'd*, 9 Cow. 639 (N.Y. 1827)).

46. *Id.* at 274–75. In a concurring opinion, two of the six justices in the majority stated a different basis for the decision. *Id.* at 275. Holly was making the contract as an agent for Lawrence and since Lawrence was a disclosed principal, Lawrence could enforce the contract. *See* RESTATEMENT (SECOND) OF AGENCY § 292 (AM. LAW INST. 1958).

47. *Lawrence*, 20 N.Y. at 275 (emphasis added).

48. Vrooman v. Turner, 69 N.Y. 280, 284 (1887) ("Judges have differed as to the principle upon which *Lawrence v. Fox* and kindred cases rest.").

other than creditors. The most frequently referenced of these cases[49] is *Seaver v. Ransom*.[50]

C. Seaver v. Ransom

In the 1918 New York case *Seaver v. Ransom*, Miss Seaver, the third party, was the niece of the promisee, Mrs. Beman.[51] The promisee's husband, Judge Beman, made "an unqualified promise on a valuable consideration to make provision for the third party by will."[52] Later Judge Beman "came to die"[53] and, notwithstanding the promise to his wife, his will made no provision for her niece.[54] The third party niece sued Ransom, the representative of Judge Beman's estate, alleging breach of contract by Judge Beman.[55]

The Court of Appeals relied on *Lawrence v. Fox* and its progeny in ruling for the third party niece.[56] In an effort to distill a doctrinal test from these cases, the court identified four classes of cases in which the New York courts had recognized third party contract rights and found room in one of the classes for Miss Seaver.

Three[57] of the *Seaver v. Ransom* categories focused on the relationship between the promisee and the third party: (1) cases like *Lawrence v. Fox* in which there was a debtor-creditor relationship between the promisee and the beneficiary; (2) cases in which the promisee had both a donative intent and a close family relationship with the third party; and (3) cases described as "public contracts", i.e.,

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49. *See* CHRISTINA L. KUNZ & CAROL L. CHOMSKY, CONTRACTS: A CONTEMPORARY APPROACH 1107–16 (2010) ("Third-party beneficiary doctrine developed from the two early New York cases below." (*Lawrence v. Fox* and *Seaver v. Ransom*)).

50. 120 N.E. 639 (N.Y. 1918).

51. *Id.* at 642.

52. *Id.*

53. *Id.* at 640.

54. *Id.* at 639–40.

55. *Id.* at 640.

56. *Cf.* Douglass G. Boshkoff, *More Selected Poems on the Law of Contracts: Raintree County Memorial Library Occasional Paper No. 2*, 91 NW. U. L. REV. 295, 301 (1996) (And if there ever has been an appropriate footnote for the use of "*cf.*", this is it.).

Beman, J. failed to honor his word
To his wife for the good of a third.
When the court made him pay,
The old judge had his say.
'But for Fox, this would not have occurred.'

57. *Seaver* describes the fourth category as "cases where, at the request of a party to the contract, the promise runs directly to the beneficiary although he does not furnish the consideration." 120 N.E. at 641.

contracts that a government entity made to "protect its inhabitants by covenants for their benefit."[58] One of the "public contract" cases cited by *Seaver v. Ransom* involved a contract between a village and a private water company to provide water to the residents of the village.[59] The court placed Miss Seaver in the second category and labeled her a "donee beneficiary."[60] This is a term that is still in use and warrants further explanation.

Just as the assumed home mortgage is a clearer paradigm for creditor beneficiaries than *Lawrence v. Fox*, a life insurance contract is a clearer paradigm for donee beneficiaries than *Seaver v. Ransom*. Assume that Mrs. Beman instead uses "valuable consideration" to buy life insurance from the Ransom Life Insurance Co. (RLI). The life insurance policy, a contract between Mrs. Beman and RLI, names Mrs. Beman's niece, Miss Seaver, as the beneficiary. If RLI breaches this contract with Mrs. Beman by failing to make the promised policy benefits payment to Miss Seaver, then Miss Seaver has contract law rights under the life insurance contract she did not make. A rule recognizing the contract rights of a third party who was a donee of the promisee when that party was expressly named in the contract is easy to understand, and easy to apply.

Around this time, courts in states other than New York were writing about contract rights of third parties.[61] And so were the two leading contracts law professors of the era, Samuel Williston and Arthur Corbin.

D. Williston and Corbin

Williston wrote about contract rights of third parties in a 1902 law review article[62] and in his 1920 treatise on contracts.[63] Williston began his 1902 article with the following quote:

> In no department of the law has a more obstinate and persistent battle between practice and theory been waged than in regard to the answer to the question: Whether a right of action accrues to a third person from a contract made by others for his benefit? Nor is the strife ended; for if it be granted that the scale inclines in

58. *Id.* at 640–41.

59. *Id.* at 640; *see* Pond v. New Rochelle Water Co., 76 N.E. 211 (N.Y. 1906).

60. *Id.* at 642.

61. *See, e.g.*, W. H. Page, *Beneficiary Contracts in Wisconsin*, 1 WISC. L. REV. 216 (1922).

62. Samuel Williston, *Contracts for the Benefit of a Third Person*, 15 HARV. L. REV. 767 (1902).

63. *E.g.*, SAMUEL WILLISTON, THE LAW OF CONTRACTS § 381 et seq. (1920) [hereinafter WILLISTON]. There are three later editions of this book. The 1920 edition is the only edition authored solely by Williston. All our references to "Williston" will be to this first edition.

> favor of practice, yet the advocates of this result are continually endeavoring to extend the territory which they have conquered and to apply the doctrines thereby established to cases which should be governed by other principles.[64]

In our opinion, Williston's primary "other principle" was privity. Unlike Lilienthal, Williston did not believe that privity had been "exploded" by *Lawrence v. Fox*.[65] Because of privity, Williston viewed recognition of third party contract rights as a theoretical "anomaly."[66] In both his article and his treatise, Williston grudgingly supported contract rights for donee beneficiaries,[67] some creditor beneficiaries,[68] and some persons who benefit from contract with a municipality.[69]

Corbin expressed a very different view of privity and third party contract rights in six law review articles published from 1916 to 1930.[70] The first of Corbin's articles begins:

> By the great weight of authority in the United States the same facts that operate to create contractual relations between the offeror and the acceptor may also operate to create rights in a third person. . . . To many students and practitioners of the common law privity of contract became a fetish. As such, it operated to deprive many a claimant of a remedy in cases where according to the mores of the time the claim was just.[71]

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64. Williston, *supra* note 62, at 767.

65. WILLISTON, *supra* note 63, § 357 ("The beneficiary is not a party to a contract, and apart from some special principal (sic) governing this class of cases cannot maintain an action.").

66. *Discussion of Tentative Draft, Contracts, Restatement No. 3*, 5 A.L.I. PROC. 373, 385 (1927). In his treatise, Williston characterized the rights of third parties to contracts as equitable, not legal. WILLISTON, *supra* note 63, § 358. ("Common-law procedure contemplates but two sides to a case, and cannot well deal with more. Equity can deal successfully with any number of conflicting interests in one case . . . .").

67. WILLISTON, *supra* note 63, § 357; Williston, *supra* note 62, at 772.

68. WILLISTON, *supra* note 63, §§ 361–63; Williston, *supra* note 62, at 772.

69. WILLISTON, *supra* note 63, § 373; Williston, *supra* note 62, at 772. According to Williston, these contracts between a private party and a municipality should be analyzed differently from contracts between two private parties. *Id.* at 784 ("[T]he object of the promise is to benefit the community as a whole, and the city as the representative of the community is the proper plaintiff.").

70. Arthur Corbin, *Contracts for the Benefit of Third Persons*, 27 YALE L.J. 1008, 1008 (1918) [hereinafter Corbin, *Third Persons*]; Arthur Corbin, *Contracts for the Benefit of Third Persons in Connecticut*, 31 YALE L.J. 489, 490–492 (1922); Arthur Corbin, *The Law of Third Party Beneficiaries in Pennsylvania*, 77 U. PA. L. REV. 1, 3 (1928) [hereinafter Corbin, *Beneficiaries in Pennsylvania*]; Arthur Corbin, *Third Parties as Beneficiaries of Contractors' Surety Bonds*, 38 YALE L.J. 1, 2–3 (1928); Arthur Corbin, *Contracts for the Benefit of Third Persons*, 46 LAW Q. REV. 12, 12 (1930); Arthur Corbin, *Contracts for the Benefit of Third Persons in the Federal Courts*, 39 YALE L.J. 601, 603 (1930).

71. Corbin, *Third Persons*, *supra* note 70, at 1008.

In these law review articles, Corbin advocated: (1) the total abandonment of a privity requirement;[72] (2) the same legal treatment for creditor and donee beneficiaries;[73] and (3) intent of the contracting parties as the test for third party contract rights.[74] Additionally, Corbin proselytized for the judicial acceptance of the Restatement of Contracts position on contract rights of third parties.[75]

E. First Restatement

Williston was the reporter for the Restatement of Contracts.[76] Corbin was given the title of "Special Adviser."[77]

Legal scholars are divided as to whether Chapter 6 of the Restatement—"Contractual Rights of Persons Not Parties to the Contract"—is based on the views of Williston or the views of Corbin.[78] We believe that it can be read as a fusion of Williston and Corbin's views.

On the surface, the Restatement seems simply to mirror Williston's treatise. The Restatement, like Williston's treatise, employed categories to identify third parties with contract rights—seemingly, the same categories as Williston's: donee beneficiaries and creditor beneficiaries under private contracts covered in Restatement section 133,[79] and beneficiaries under service contracts made with villages or other governmental entities covered in Restatement section 145.[80]

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72. Corbin, *Beneficiaries in Pennsylvania*, *supra* note 70, at 3 ("[I]t is time to abandon the repetition of the misleading doctrine.").

73. *Id.* at 21 ("[T]he question is where to draw the line between beneficiaries with rights and third parties as to whom performance might be beneficial but who have no rights.").

74. Corbin, *Third Persons*, *supra* note 70, at 1009 ("The reasons for recognizing the rights in the contract beneficiary are *substantially* the same as those recognizing the rights of a *cestui que trust.* By so doing, the intention of the parties is carried out and the beneficiary's just expectations are fulfilled." (first emphasis added)).

75. Corbin, *Beneficiaries in Pennsylvania*, *supra* note 70, at 2–3.

76. *Discussion of Tentative Draft*, *supra* note 66, at 373.

77. *See Bibliography of the Published Writings of Arthur Linton Corbin*, 74 YALE L.J. 311, 320 (1964).

78. *Compare* Eisenberg, *supra* note 8, at 1376 ("followed the view of Williston"), *with* FREDERICH KESSLER, GRANT GILMORE & ANTHONY T. KRONMAN, CONTRACTS CASES AND MATERIALS 1362 (3d ed. 1986) ("almost certainly the handiwork of Arthur Corbin"). *But cf.* Waters, *supra* note 41, at 1166–67 ("Corbin claims . . . that his views prevailed over Williston in the formulation of the chapters on third party beneficiaries in the First Restatement.").

79. RESTATEMENT (FIRST) OF CONTRACTS § 133 (AM. LAW INST. 1932).

80. The last category, government, is dealt with separately from the other two. *See id.* § 145. RESTATEMENT § 145, like *Seaver v. Ransom*, uses the example of a private company's contracting with a municipality to provide sufficient water to maintain needed pressure in fire hydrants. *Id.*

Neither the text of Restatement section 145, nor the "Comment" or "Illustrations" following it, use the terms "creditor beneficiary" or "donee beneficiary." The comment to section 145 describes it as a "special application of the principles stated in section 133."[81] Both the illustrations to section 145 and later cases suggest that, at best, section 145 governing third party rights under "government contracts"[82] is a "[*very, very*] *special* application of the principles stated in Restatement section 133"[83] that govern third party rights under private contracts.

One of section 145's illustrations is similar to a case included in many contracts casebooks, *H.R. Moch Co. v. Rensselaer Water Co.*[84] There, the City of Rensselaer contracted with the defendant water company to provide enough water to have sufficient water pressure at the hydrant.[85] The plaintiff's warehouse burned down because the defendant failed to maintain adequate pressure. The plaintiff sued, alleging, inter alia, "[a] cause of action for breach of contract within *Lawrence v. Fox*."[86] The court, in an opinion by Judge Cardozo, rejected the third party beneficiary claim.[87]

Although Cardozo's *H.R. Moch* opinion mentions *Lawrence v. Fox*,[88] all of the cases it discussed and relied on involved government contracts. The same statement can be made about *Astra USA Inc. v. Santa Clara County*,[89] a 2011 United States Supreme Court decision denying the right to bring a breach of contract action as third party beneficiaries of a contract between federal government and drug manufacturers.

Courts treat third parties' suits to enforce government contracts differently from third parties' suits to enforce contracts between private parties.[90] This Article focuses on what courts do and should do when a third party sues to enforce a contract between private parties.

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81. *Id.* § 145 cmt. a.

82. The government contracts that raise third party issues are different from the typical government contract, which is simply a procurement contract—e.g., government entity contracts to buy widgets. Third party issues arise in the atypical contract in which a government entity contracts with a private entity to provide services to the public. *See id.* § 145 cmt. a, illus. 1–5.

83. *Id.* § 145 cmt. a (emphasis added).

84. 159 N.E. 896 (N.Y. 1928).

85. *Id.* at 896.

86. *Id.* at 897.

87. *Id.*

88. *Id.* at 898.

89. 563 U.S. 110 (2011).

90. GECCMC 2005-C1 Plummer St. Office Ltd. P'ship. v. JPMorgan Chase Bank, Nat'l Ass'n, 671 F.3d 1027, 1034 (9th Cir. 2012) ("[H]eightened standard required of third-party beneficiaries to government contracts."); *see also* Geis, *supra* note 9, at 1157 n.20 (Government contracts "present

Under the First Restatement, a third party has contract rights under a contract made by other private parties if they were a "creditor beneficiary" or a "donee beneficiary."[91] If the third party does not come within the Restatement's "creditor beneficiary" or "donee beneficiary" categories, then she is in the "incidental beneficiary" category and has no contract law rights.[92]

On a closer reading of the Restatement's description of "donee beneficiary," in section 133(1)(a), we see Corbin's influence. Even though "donee beneficiary" is a term used in Williston's treatise and in cases such as *Seaver v. Ransom*, the Restatement uses the term "donee beneficiary" differently.[93]

Under Restatement section 133(1)(a), a third party has contract rights if "it appears from the terms of the promise in view of the accompanying circumstances that the purpose of the promisee . . . is to make a gift to the beneficiary or to confer upon him a right against the promisor."[94] Thus, a third party who was not a donee would still have contract rights if a reasonable person would believe that was "the purpose of the promisee."[95]

While section 133 does not use the term "reasonable person," it does use the word "appears."[96] The First Restatement is making an objective test for intent—an outsider's view of the promisee's purpose.

This focus on the intent of a contracting party, rather than the status of the third party, is consistent with what Corbin advocated in his six law review articles that preceded the first Restatement. The Restatement

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different legal issues from private contracting and involve considerations more closely related to the determination of private rights of action in statutory interpretation."). *But cf.* Eisenberg, *supra* note 8, at 1406–07 (acknowledging that courts treat suits by third parties under government contracts as "special" and raise "particularly difficult third-party beneficiary problems" but concluding "[t]here is no more reason to apply a categorical rule to government contracts than to any other contracts.").

91. *See generally* RESTATEMENT (FIRST) OF CONTRACTS § 133–35 (AM. LAW INST. 1932).

92. *Id.* §§ 133(1)(c), 147.

93. The Restatement also uses the term "creditor beneficiary" differently from Williston and prior cases. In *Lawrence v. Fox*, the defendant promisor Fox moved for nonsuit on the ground "[t]hat there was no proof tending to show that Holly was indebted to the plaintiff." 20 N.Y 268, 269 (1859). The court found that there was competent evidence of the debtor-creditor relationship. *Id.* at 270. No such finding was required by the Restatement. RESTATEMENT (FIRST) OF CONTRACTS § 133 (AM. LAW INST. 1932). A person can be a "creditor beneficiary" as that term is used in the Restatement even if she is not actually a creditor of the promise: a "supposed or asserted duty" sufficed. *Id.* If Holly tells Fox that Holly owes Lawrence money and contracts with Fox to pay Lawrence, then Lawrence can enforce the contract regardless of whether Lawrence was actually Holly's creditor.

94. RESTATEMENT (FIRST) OF CONTRACTS § 133 (AM. LAW INST. 1932).

95. *Id.*

96. *Id.*

provisions are not, however, consistent with the case law in most states before the release of the First Restatement. In his multivolume treatise published in 1951, Corbin described the provisions as "working rules based upon the judicial 'trend'"[97] and acknowledged that "it cannot be said that the rules represent the old 'common law' or that they are in exact harmony with the law of any jurisdiction."[98]

Nor are the provisions of the First Restatement consistent with the case law in most states after the release of the First Restatement. Because of the Restatement's "creditor beneficiary" and "donee beneficiary" nomenclature, some courts recognized contract rights only in third parties who were indeed creditors or actual donees.[99] Still other courts found the Restatement provisions unhelpful in identifying which third parties, other than creditors and actual donees, had contract rights.[100]

F. Second Restatement

In his 1951 treatise, Corbin suggested that the terms "creditor beneficiary" and "donee beneficiary" be replaced with the single term "intended beneficiary."[101] The Restatement Second of Contracts (hereinafter "Restatement Second") followed this suggestion.[102]

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97. CORBIN, *supra* note 24, at 4.

98. *Id.*; *see also* Ira P. Hildebrand, *Contracts for the Benefit of Third Parties in Texas*, 9 TEXAS L. REV. 125 (1931).

99. *See, e.g.*, Insbrandtsen Co. v. Local 1291 of Int'l Longshoremen's Ass'n, 204 F.2d 495, 498 (3d Cir. 1953) (holding that third party was not a donee beneficiary because "this fact situation . . . completely negatives a gift transaction under any possible interpretation of that term."); United States v. Minnesota, 123 F. Supp. 488, 497 (D. Minn. 1953); *see also* JOHN EDWARD MURRAY, JR., MURRAY ON CONTRACTS 853 (5th ed. 2011) ("Because of the 'donee' characterization, however, the . . . beneficiary under this category who was not a true 'donee' could be easily ignored by courts who would limit this compartment to third parties who could demonstrate a promisee's donative intent.").

100. *See, e.g.*, Moore Constr. Co. v. Clarksville Dept. of Elec., 707 S.W.2d 1, 8 (Tenn. Ct. App. 1985) (noting that the Tennessee Supreme Court had adopted the Restatement position on third party beneficiaries, and stating, "[t]his process, however, has not been uniformly acceptable, and there have been a number of cases where this rationale has been ignored in order to enable the court to permit a person to maintain an action as a third party beneficiary."); Gary Monserud, *supra* note 30, at 122("[W]hatever its deficiencies, section 133 of the Restatement First and its related sections performed an enormous service for contract law. The widespread hesitancy about allowing third party suits on contracts . . . disappeared. . . . The recurring question was: In what type of case is allowing a third party beneficiary suit appropriate?").

101. CORBIN, *supra* note 24, at 8 ("It might be supposed that the one essential classification of beneficiaries should be 'intended' beneficiaries and 'unintended' ones.").

102. For an account of Corbin's role in and impact on the American Law Institute's work on third party beneficiary law, see Waters, *supra* note 7, at 1148–73. Unfortunately, Corbin's account of his

The introductory note to the Restatement Second's chapter 14, "Contract Beneficiaries," states that the terms "creditor beneficiary" and "donee beneficiary" "carry overtones of obsolete doctrinal difficulties" and so the terms "are avoided in the statement of rules."[103] Instead, the operative terms are "intended beneficiary" and "incidental beneficiary."[104]

If a third party comes within the definition of "intended beneficiary," she has contract rights.[105] Section 302 provides the following definition of "intended beneficiary":

> (1) Unless otherwise agreed between promisor and promisee, a beneficiary of a promise is an intended beneficiary if recognition of a right to performance in the beneficiary is appropriate to effectuate the *intention of the parties* and either
>
> (a) the performance of the promise will satisfy an obligation of the promisee to pay money to the beneficiary; or
>
> (b) the circumstances indicate that the *promisee intends* to give the beneficiary the benefit of the promised performance.[106]

There is also language in comment d[107] to Restatement 302 that seems to suggest that a third party's reasonable reliance is a basis for

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role in and impact on the American Law Institute's work on third party beneficiary law has been lost. *See generally* Scott D. Gerber, *An Ivy League Mystery: The Lost Papers of Arthur Linton Corbin*, 53 S.C. L. REV. 605 (2002).

103. RESTATEMENT (SECOND) OF CONTRACTS ch. 14, intro. note (AM. LAW INST. 1981). In looking at third party beneficiary law at about the same time as the American Law Institute, Professors Grant Gilmore and Frederick Kessler saw the social evolution, not doctrine or rules:

> In our own century we have witnessed what it does not seem too fanciful to describe as a socialization of our theory of contract. The progressive expansion of the range of non-parties allowed to sue as contract beneficiaries . . . is one of the entries to make in this ledger.

FREDERICK KESSLER & GRANT GILMORE, CONTRACTS: CASES AND MATERIALS 1118 (2d ed. 1970).

104. RESTATEMENT (SECOND) OF CONTRACTS ch. 14, intro. note (AM. LAW INST. 1981).

105. *Id.* § 304.

106. *Id.* § 302 (emphasis added).

107. *Id.* § 302 cmt. d ("*Other intended beneficiaries.* Either a promise to pay the promisee's debt to a beneficiary or a gift promise involves a manifestation of intention by the promisee and promisor sufficient, in a contractual setting, to make reliance by the beneficiary both reasonable and probable. Other cases may be quite similar in this respect. Examples are a promise to perform a supposed or asserted duty of the promisee, a promise to discharge a lien on the promisee's property, or a promise to satisfy the duty of a third person. In such cases, *if the beneficiary would be reasonable in relying on the promise as manifesting an intention to confer a right on him, he is an intended beneficiary. Where there is doubt whether such reliance would be reasonable*, considerations of procedural convenience and other factors not strictly dependent on the manifested intention of the parties may affect the question whether under Subsection (1) recognition of a right in the beneficiary is appropriate. In some cases an overriding policy, which may be embodied in a statute, requires recognition of such a right without regard to the intention of the parties.") (second emphasis added).

concluding that the third party is an "intended beneficiary." We believe that this language in comment d is relatively insignificant for the following reasons:

The word "reliance" does not appear in the text of section 302.

The comments appended to a Restatement section, like the comments to a statute such as the Uniform Commercial Code, have a limited purpose—explanation of what is in the black letter of the section.[108]

The words of comment d do not support the proposition that a third party's reliance on one of the contracting parties' promise is a separate basis for the third party's contract rights. Instead they seem to say that such reliance is a basis for concluding that the contracting parties intended to benefit the third party: "[I]f the beneficiary would be reasonable in relying on the promise as manifesting an intention to confer a right on him, he is an intended beneficiary."[109]

We use the *weasel word* "seem" because we are somewhat uncertain in our understanding of the quoted words and are even less certain as to how the reliance of C to the words of A and B provides an independent basis for ascertaining A and B's intent.

The Restatement Second separates contract rights based on the bargain of two parties from contract rights based on the reliance of one person.[110]

Restatement Second section 90, discussing promissory estoppel, provides an independent basis for granting third parties contract rights because of their reliance. Section 90 begins: "A promise which the promisor should reasonably expect to induce action or forbearance on the part of the promisee or a *third party* . . . is binding if *injustice* can be avoided only by enforcement of the promise."[111]

Thus, if the promisee or a third party relies on Restatement Second section 90, they can recover only if they can prove not only reasonable reliance but also "injustice."[112] Comment d to Restatement Second

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108. AM. LAW INST., CAPTURING THE VOICE OF THE AMERICAN LAW INSTITUTE: A HANDBOOK FOR ALI REPORTERS AND THOSE WHO REVIEW THEIR WORK 42 (rev. ed. 2015).

109. *Id.*

110. In essence, Restatement (Second) of Contracts section 17 sets out two different bases for contract: bargain and reliance. Compare section 17(1) with section 17(2): "(1) Except as stated in Subsection (2), the formation of a contract requires a bargain in which there is a manifestation of mutual assent to the exchange and a consideration. (2) Whether or not there is a bargain a contract may be formed under special rules applicable to formal contracts or under the rules stated in §§ 82–94." RESTATEMENT (SECOND) OF CONTRACTS § 17 (AM. LAW INST. 1981).

111. *Id.* § 90 (emphasis added).

112. *Id.*

section 302 makes no mention of "injustice."[113] It should not be easier for a third party to recover because of reliance under Restatement Second section 302 than for either a third party or a promisee to recover because of reliance under Restatement Second section 90.

For the above seven reasons, this Article deals only with third party contract rights based on the bargain between two other parties.[114]

Returning then to our focus on the language of section 302 set out above, we think it is instructive to compare the two underscored phrases: intention of the parties and promisee's intent. The difference in the two phrases creates the question of whose intention is relevant: "the parties" or "the promisee."

Professor E. Allan Farnsworth, one of the reporters for the Restatement Second, acknowledged, "[i]n view of the Restatement Second's requirement that a right in the beneficiary be 'appropriate to effectuate the intention of the *parties*,' its additional requirement that the *promisee* have an intention to benefit the third person seems curious at first."[115] He then suggests that the phrase "promisee intends" be "*paraphrased* to require an indication 'that the promisee would have been willing to pay the fair value for the promisor's undertaking a duty to the beneficiary.'"[116]

We are not sure that Professor Farnsworth was using the term "paraphrase" in the same way we do. We are sure that no reported case has used Professor Farnsworth's "paraphrase."

Some paraphrasing may in fact be necessary to bring Restatement Second section 302 in line with the objective theory of contract formation and interpretation.[117] Compare both of the subjective underscored phrases in Restatement Second section 302, "intention of the parties" and "promisee intends,"[118] with the objective Restatement First section 133 phrase "appears from the terms of the promise in view of the accompanying circumstances that the purpose of the promisee."[119]

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113. *Id.* at cmt. d.

114. For an article on third party contract rights based on promissory estoppel, see Michael B. Metzger & Michael J. Phillips, *Promissory Estoppel and Third Parties*, 42 SW. L.J. 931 (1988).

115. 3 E. ALLAN FARNSWORTH, FARNSWORTH ON CONTRACTS 23 (2d ed. 1998).

116. *Id.* at 24 (emphasis added).

117. For the most part, contract law looks to the objective intent, rather than subjective intent. *See, e.g.*, Indus. Am., Inc. v. Fulton Indus., Inc., 285 A.2d 412, 415 (Del. 1971) ("[O]vert manifestation of assent—not subjective intent—controls the formation of a contract."); *see generally* GRANT GILMORE, THE DEATH OF CONTRACT 42–43 (2d ed. 1995).

118. RESTATEMENT (SECOND) OF CONTRACTS § 302 (AM. LAW INST. 1981).

119. RESTATEMENT (FIRST) OF CONTRACTS § 133 (AM. LAW INST. 1932).

The words "appears," "terms," and "circumstances" in the Restatement First are consistent with an objective test of the promisee's intent: what would a reasonable person understand the promisee to intend? The words "the intention" in Restatement Second section 302 are more consistent with a subjective inquiry into the actual intent of the parties (or promisee).

Some courts have stated that omission of the terms "creditor beneficiary" and "donee beneficiary" is the only difference between Restatement Second section 302 and Restatement First section 133.[120] Even more courts have continued to use the Restatement First terms "creditor beneficiary" and "donee beneficiary."[121] There are of course cases that use Restatement Second's "intended beneficiary" and "incidental beneficiary" language.

Regardless of what language courts use, it is difficult to reconcile courts' resolution of cases in which the understanding of both parties to the contract is less obvious than in *Lawrence v. Fox* and *Seaver v. Ransom*. There is little consistency in those cases because of the inherent vagueness in the questions of (1) whose intent is relevant and (2) how that intent should be defined and proved.

II. REVIEW OF CURRENT CASES: CONFUSION AS TO WHERE WE ARE

Where we are analytically with respect to third party contract rights depends very much on where the litigants are geographically. We

120. *See, e.g.*, Lake Almanor Assocs. L.P. v. Huffman-Broadway Grp., Inc., 101 Cal. Rptr. 3d 71, 75 n.2 (Cal. Ct. App. 2009) ("Section 302 of the Restatement Second of Contracts omits the terms 'donee beneficiary' and 'creditor beneficiary,' instead employing the term 'intended beneficiary' for a beneficiary with enforceable rights and 'incidental beneficiary' for a beneficiary lacking such rights. However, the basic framework regarding which third parties can enforce contracts is unchanged.") (citation omitted); Lovell Land, Inc. v. State Highway Admin., 969 A.2d 284, 297 (Md. 2009) (The change made in the Second Restatement "was not one of substance, but only of terminology."); *see also* Prince, *supra* note 10, at 990 ("[M]any courts have not perceived any change.").

121. *See, e.g.*, MCI Telecoms. Corp. v. Tex. Utils. Elec. Co., 995 S.W.2d 647, 651 (Tex. 1999) (plaintiff must show that he is either a donee or a creditor beneficiary); Cory H. Howard, *Towards a Broader Understanding of Privity Exceptions in Contract Law: Bestowing Limited Rights on Incidental Third Party Beneficiaries in Construction Litigation to Fulfill Public Policy Objectives*, 51 GONZ. L. REV. 187, 205 (2015–16) ("Most, if not all, common law recognizes two discrete categories of intended third-party beneficiaries who can enforce a contract to which they are not privity: (1) a donee beneficiary and (2) a creditor beneficiary."); *see also* 13 SAMUEL WILLISTON & RICHARD A. LORD, A TREATISE ON THE LAW OF CONTRACTS §§ 32–33 (4th ed. 2000) ("[T]he vast majority of courts continue to speak of third party creditor and third party donee beneficiaries when considering protected beneficiaries."); STEVEN J. BURTON, PRINCIPLES OF CONTRACT LAW 616 (4th ed. 2012) ("[R]emains embedded in the law of many jurisdictions . . . .").

conducted a fifty state and federal court survey of cases from 2010 to January 1, 2016 that considered whether third parties had contract rights. We focused on the questions: (1) whose intent was relevant and (2) what intent was relevant. We also looked for differences between the damages earned by a third party beneficiary and the damages that would have been awarded to the promisee of the contract. We found no discernible majority rules.

A. Whose Intent Is Relevant?

We divided the recent cases into three categories: (1) cases that focus on the promisee's intent; (2) cases that focus on the promisor's intent; and (3) cases that look to the intent of both the promisor and the promisee. The following cases are representative of these three answers to the question: whose intent is relevant?

1. Promisee's Intent

In *Logan-Baldwin v. L.S.M. General Contractors, Inc.*,[122] New York homeowners hired L.S.M. General Contractors, Inc. (LSM) to perform restorative work on their house.[123] LSM, in turn, hired Henry Isaacs, a subcontractor, to help with roofing.[124] Henry Isaacs then hired Hal Brewster to assist him with the project.[125] Unfortunately, Hal Brewster "botched" the job and caused extensive damage to the house.[126] LSM and Isaacs attempted to fix the damage, but ultimately abandoned the project, leaving the homeowners to address it themselves.[127]

The homeowners sued their general contractor LSM and subcontractor Isaacs for breach of contract.[128] While the homeowners received judgment against LSM, the court granted Isaacs's motion for summary judgment.[129] The appeal involved only Isaacs' summary judgment and the appellate court reversed and remanded.[130]

Isaacs contended that the homeowners did not have standing to enforce its subcontract with LSM because: (1) there was no privity of

122. 94 A.D.3d 1466, 1466 (N.Y. App. Div. 2012).

123. *Id.* at 1466–67.

124. *Id.*

125. *Id.* at 1467.

126. *Id.*

127. *Id.*

128. *Id.*

129. *Id.*

130. *Id.*

contract and (2) the homeowners were not intended third party beneficiaries of the subcontract between LSM and Isaacs.[131] The court held that the homeowners were intended third party beneficiaries to the contract, and therefore had standing against the promisee Isaacs.[132]

The opinion states that generally:

> An obligation rooted in contract may [nevertheless] engender a duty owed to those not in privity when the contracting party knows that the subject matter of a contract is intended for the benefit of others . . . . An intention to benefit a third party must be gleaned from the contract as a whole.[133]

Thus, privity is not always required.

The opinion goes on to say that homeowners who are

> asserting third-party beneficiary rights under a contract must establish '(1) the existence of a valid and binding contract between other parties, (2) that the contract was intended for [the third party's] benefit and (3) that the benefit to [the third party] is sufficiently immediate, rather than incidental, to indicate the assumption by the contracting parties of a duty to compensate [the third party] if the benefit is lost.'[134]

The opinion states that the focus is solely on the intent of the promisee, LSM.[135] The explanation for focusing solely on the intent of the promisee was that "the promisee procured the promise by furnishing the consideration therefor."[136]

The opinion provides no explanation as to why the "promisee [LSM] furnishing the consideration therefor"[137] should affect the liability of the promisor, Isaacs. Instead, the court provides citations to prior opinions, which are no more fully reasoned, stating that the focus is on the intent of the promisees.[138]

The remainder of the opinion in this case is more enlightening. The court stated: "Here . . . it is 'almost inconceivable' that the Isaacs defendants did not know that plaintiffs, the owners of the home, would

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131. *Id.*

132. *See id.* at 1470.

133. *Id.* at 1468 (quoting Van Vleet v. Rhulen Agency, 180 A.D.2d 846, 848–49 (N.Y. App. Div. 1992)) (brackets in original).

134. *Id.* (quoting Burns Jackson Miller Summit & Spitzer v. Lindner, 451 N.E.2d 459, 469 (N.Y 1983)).

135. *Id.* at 1468.

136. *Id.* (quoting Drake v. Drake, 45 N.Y.S.2d 420, 422 (N.Y. App. Div. 1982)).

137. *Id.* at 1468.

138. *Id.*

be the ultimate beneficiaries of the services being provided by the Isaacs defendants pursuant to their contract with LSM."[139] After stating that LSM's intent was determinative, the court focused on what the promisor Isaacs had reason to know at the time of the contract.

2. Promisor's Intent

Several cases and a Michigan statute expressly focus on what the promisor had reason to know. *Muhammad v. Pub. Storage Co.*[140] is an example of a recent case stating that the promisor's intention is the one that is relevant to a third party beneficiary's status.[141] *Muhammad* concerned plaintiffs Wallace and Edna Muhammad who wanted to rent a storage unit.[142] They entered into an agreement with the defendant, Public Storage. Wallace Muhammad signed the contract with Public Storage as the "occupant."[143] Edna Muhammad signed the contract as "occupant's authorized access person."[144]

Eventually, the Muhammads fell behind on payments, and by the end of January were nearly two months delinquent, owing $161 to Public Storage.[145] Public Storage then sold all of the items in the Muhammads' storage unit.[146] When the Muhammads attempted to get reimbursement for the near $200,000 worth of items sold, Public Storage refused, and the Muhammads sued.[147] Public Storage filed a motion to dismiss.[148]

The suit alleged several causes of action.[149] Count II, a breach of contract claim, is our only concern.[150]

Defendant Public Storage filed a motion to dismiss Edna Muhammad's breach of contract claim, contending that Edna Muhammad could not assert a claim for breach of contract because of lack of privity—she was not a party to the agreement with Public Storage.[151] In response, the Muhammads argued that Edna Muhammad

139. *Id.* at 1469 (citations omitted).

140. No. 14-0246-CV-W-ODS, 2014 WL 3687328 (W.D. Mo. July 24, 2014).

141. *Id.* at *1.

142. *Id.*

143. *Id.*

144. *Id.*

145. *Id.*

146. *Id.*

147. *Id.* at *1–2.

148. *Id.* at *2.

149. *Id.*

150. *Id.* at *4.

151. *Id.* at *3.

could assert a claim for breach of contract as an intended third party beneficiary.[152]

The court rejected the Muhammads' argument and granted the Public Storage motion to dismiss Edna Muhammad's contract cause of action.[153] More important than the court's result is the court's reasoning, or lack thereof. The opinion states in pertinent part: "Third party beneficiary status depends not so much on a desire or purpose to confer a benefit on the third person, but rather on an intent that the *promisor* assume a *direct obligation* to him."[154] The court does not explain why the promisor's intent should be the determinative test. Instead, the court simply cites an earlier case, which is no more fully reasoned.[155]

In some cases, it is not the case law that directs whose intent is relevant, but a state statute. For example, Michigan's third party beneficiary statute provides:

> Any person for whose benefit a promise is made by way of contract, as hereinafter defined, has the same right to enforce said promise that he would have had if the said promise had been made directly to him as the promisee.
>
> A promise shall be construed to have been made for the benefit of a person whenever the *promisor* of said promise had undertaken to give or to do or refrain from doing something directly to or for said person.[156]

Recent cases applying this Michigan statute, such as *Shathaia v. Travelers Causality Insurance Company of America*,[157] are not helpful in understanding the policy basis for the statute. *Shathaia* involved a property insurance policy issued to a business entity.[158] The building at issue was insured but later destroyed in a fire.[159] The building belonged to the owner of the business entity, Shathaia, not the business entity that was a party to the insurance contract.[160] When Shathaia sued the

152. *Id.* at *4.

153. *Id.*

154. *Id.* (quoting McKenzie v. Columbian Nat'l Title Ins. Co., 931 S.W.2d 843, 845 (Mo. Ct. App. 1996)) (first emphasis added).

155. *Id.* at 4 (referring to *McKenzie*, 931 S.W.2d 843).

156. MICH. COMP. LAWS § 600.1405 (2012).

157. 984 F. Supp. 2d 714 (E.D. Mich. 2013).

158. *Id.* at 714.

159. *Id.*

160. *Id.*

insurance company, it asserted rights under the insurance contract, and the insurance company successfully moved for summary judgment.[161]

In concluding that Shathaia was not an intended third party beneficiary, the court looked to the "plain language" of the Michigan statute. Nothing in the opinion or the cases cited in the opinion, however, clarifies the reason for the Michigan statutory rule.[162]

3. *Both Parties' Intent*

Lilley v. JP Morgan Chase[163] involved a contract between a mortgage lender and an appraiser. The Lilleys signed a mortgage contract with JP Morgan Chase Bank, NA ("Lender") in 2005.[164] Prior to approving the Lilleys' loan, Lender contracted with Ingram, a real estate appraiser, to appraise the home.[165] The Lilleys defaulted on their loan and sued Ingram, alleging that Ingram breached his contract with Lender by preparing an inflated appraisal of the home.[166]

Only Lender and Ingram were parties to the appraisal contract.[167] The Lilleys had to establish that they were intended third party beneficiaries of that contract in order to sue for the breach of contract between Lender and Ingram.[168]

The Court explained that the existence of third party beneficiary status is determined by examining the written contract. "The written contract must show that the *contracting parties clearly intended* to confer a separate and distinct benefit upon the third party."[169] The Court did not explain why it was the "contracting parties'" intent that was relevant and not merely the intent of the promisee or the intent of the promisor. Again, the opinion simply provided precedent, not policy.

B. *What Intent Is Relevant?*

Once an attorney representing a third party to a contract knows whose intent[170] will be relevant in determining whether their client can enforce

161. *Id.*

162. *Id* at 722.

163. 317 P.3d 470 (Utah Ct. App. 2013).

164. *Id.* at 472.

165. *Id.*

166. *Id.*

167. *Id.*

168. *Id.*

169. *Id.* at 472 (emphasis added).

170. Promisee, promisor, or both promisee and promisor.

that contract, they then confront the question of what intent is relevant. Most of the cases in our survey simply refer to an intent to benefit a third party. Other opinions seem to require an intent that the promisor assume a direct obligation to the third party. Still fewer courts refer to an intent that the third party have legal rights in the contract.

1. Intent to Benefit the Third Party

For example, in *Tarr v. Narconon Fresh Start*,[171] plaintiff Michael Tarr sued Narconon for breaching a drug rehabilitation contract.[172] Michael alleged that: (1) Narconon promised a secular program based on medical science and counseling; and that (2) during his time in the Narconon program, he was required to study Scientology and participate in Scientology rituals, receiving counseling only on Scientology.[173]

Narconon filed a motion to dismiss based in part on the fact that Michael was not a contracting party, i.e., he lacked privity. Narconon had contracted with Mrs. Tarr, Michael's mother, who was seeking treatment for her twenty-four-year-old, heroin-addicted son.[174]

The court denied Narconon's motion to dismiss.[175] The court explained that "[u]nder Nevada law, a third party has standing to sue for breach of contract (1) if the agreement was formed with *the intent to benefit* a third party and (2) if the third party's reliance on the agreement was foreseeable."[176] The court found that Ms. Tarr's *sole purpose* had been to benefit her son.[177] And, since the drug rehabilitation program required Michael to travel to the Narconon facility, Michael's reliance on the contract was foreseeable.[178]

What the court did not explain was the reason for its rule. The opinion does, however, provide the requisite nexus between either the promisee Mrs. Tarr's intent and Narconon's liability to Michael, or Michael's reliance and Narconon's liability on a third party beneficiary theory.[179]

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171. 72 F. Supp. 3d 1138 (D. Nev. 2014).

172. *Id.* at 1140.

173. *Id.* at 1139.

174. *Id.* at 1142.

175. *Id.* at 1139.

176. *Id.* at 1142 (emphasis added).

177. *Id.*

178. *Id.*

179. *Id.*

2. *Intent to Assume a Direct Obligation*

Known Litigation Holdings, LLC v. Navigators Insurance,[180] a case involving a potential loss payee of an insurance policy, used a different intent test to reach the same result.[181] There, the plaintiff, an assignee of Domestic Bank, sued the defendant insurance company on an insurance contract between the insurance company and the bank's couriers.[182] Domestic had contracted with NECD and IMS to courier cash from the bank to the bank's ATMs.[183]

The contract between Domestic and NECD and IMS provided that NECD and IMS would be liable for any loss resulting from employee malfeasance.[184] The contract required that NECD and IMS get insurance to cover any such liability.[185] NECD and IMS contracted with Navigators Insurance.[186] That contract included coverage of loss caused by employee wrongdoing, and designated Domestic as the sole potential loss payee.[187]

After four years of service, a government investigation alerted Domestic of discrepancies in the ATMs.[188] Domestic conducted its own audit and found that employees of NECD and IMS had conspired to defraud Domestic out of over $5 million over the course of those four years.[189] Domestic demanded compensation from NECD and IMS.[190] When those companies did not respond, Domestic demanded compensation directly from Navigators.[191]

Navigators claimed that Domestic could not sue for breach of the insurance policy, because Domestic was not a named insured and therefore was not a party to that contract.[192] The court found that third party Domestic had a right to sue as a third party beneficiary if the parties intended that "'the promisor should assume a direct obligation to

180. 934 F. Supp. 2d 409 (D. Conn. 2013).
181. *Id.* at 418.
182. *Id.* at 412.
183. *Id.* at 413.
184. *Id.*
185. *Id.*
186. *Id.*
187. *Id.*
188. *Id.* at 414.
189. *Id.*
190. *Id.*
191. *Id.*
192. *Id.*

the third party beneficiary.'"[193] Under the terms of the insurance contract, Domestic had a right to receive direct payment from Navigators.[194] The court found that this granted Domestic rights as a third party beneficiary, despite language in the contract explicitly disclaiming rights for the insured's designee.[195]

The opinion lists several other cases that employed the same test.[196] The test states that the third party has a right to sue as a third party beneficiary if the parties intended that "the promisor should assume a direct obligation to the third party beneficiary."[197] Neither this opinion, nor prior opinions, provide an explanation for this rule.

3. *Intent to Grant the Third Party Legal Rights in the Contract*

In *Armbruster v. WageWorks, Inc.*,[198] Paul Armbruster sued WageWorks because WageWorks fired Armbruster's ex-wife, Lauren Coppock, causing her to forfeit her stock options.[199] As part of Armbruster and Coppock's divorce agreement, Armbruster was entitled to exercise half of Coppock's stock options if Armbruster so directed.[200] Armbruster was to provide any necessary funds ninety days before the exercise date, and Coppock was to deliver to Armbruster title to the resulting shares.[201]

Armbruster never directed Coppock to exercise his half of the options.[202] When WageWorks terminated Coppock, neither she nor Armbruster had the funds to exercise a majority of the stock options.[203] Thus, as the Stock Options Plan stipulated, the stock options were forfeited three months after Coppock's termination.[204]

WageWorks moved to dismiss the contract claim, citing a lack of privity.[205] The Stock Options Plan was a contract with Coppock alone.[206]

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193. *Id.* (citing Grigerik v. Sharpe, 721 A.2d 526, 536 (Conn. 1998)).

194. *Id.*

195. *Id.*

196. *Id.*

197. *Id.*

198. 953 F. Supp. 2d 1072 (D. Ariz. 2013).

199. *Id.* at 1074.

200. *Id.*

201. *Id.*

202. *Id.*

203. *Id.*

204. *Id.*

205. Defendants' Motion to Dismiss Complaint at 11, Armbruster v. WageWorks, Inc., 953 F. Supp. 2d 1072 (D. Ariz. 2013) (No. CV-12-2058-PHX-ROS), 2012 WL 6569035.

Armbruster alleged that he was an intended third party beneficiary of the Stock Options Plan.[207] The court held that Armbruster was not an intended third party beneficiary.[208] The court explained that in order for a third party beneficiary to have standing in Arizona, the contracting parties must:

> i. Intend to directly benefit the third party;
>
> ii. [i]ndicate that intent in the contract itself; and
>
> iii. [i]ntend to recognize the third party as the primary party in interest and as privy to the promise.[209]

Even if the contract shows an intent to benefit the third party, the parties must also intend to recognize the third party as privy to the promise, and thus legally able to sue for breach of contract, or the third party does not have standing.[210]

The Arizona court found no such intent in the contract between WageWorks and Coppock, and dismissed Armbruster's breach of contract claim.[211] And, again, we found no explanation by the Arizona court as to why the test for third party contract rights should be "intent to recognize [the third party] as the primary party in interest."[212]

C. *Summary of Cases*

We have used these representative cases to point out the division on intent issues. These cases can be used to make three additional points. First, the facts of present day cases contesting third party contract rights are more challenging than the simple loan repayment involved in *Lawrence v. Fox* or the causa mortis gift of *Seaver v. Ransom*. Second, the cases are conclusory rather than reasoned. Third, the conclusions are rooted in history rather than policy and practical consequences.

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206. *Armbruster*, 953 F. Supp. 2d at 1074.

207. *Id.* at 1076.

208. *Id.*

209. Note that the court does not define "privy to the promise." *See id.* (citing Sherman v. First Am. Title Ins., 38 P.3d 1229, 1232 (Ariz. Ct. App. 2002)).

210. *Id.*

211. *Id.*

212. *Id.*

III. WHERE WE SHOULD BE

Nineteenth century cases and early twentieth century law review articles on third party contract rights focused on privity and whether privity barred a third party from recovering on a contract made by others. In answering this question, cases like *Lawrence v. Fox*[213] and *Seaver v. Ransom*[214] and Professor Corbin and Williston's law review articles[215] borrowed from trust law cases, concepts, and terminology.[216]

The early cases and scholarly commentary influenced the 1932 Restatement of Contracts chapter "Contractual Rights of Persons Not Parties to the Contract"[217] and, in turn, the comparable 1981 Restatement Second provisions. Even the recent cases on deciding when third parties have rights under contracts look to these early tests.

The test for deciding when third parties have legal rights under contracts made by others should reflect the practical consequences of that decision. The practical consequences of an affirmative decision on the third party deemed an "intended beneficiary" are obvious—obviously "beneficial" to the third party.

Let us consider the less obvious practical consequences of third party contract rights on the promisee and the promisor. Everyone likes a benefit. It is the imposition of a detriment that can be problematic. Therefore, the focus of the courts should be on the detriment that results from legal recognition of third party contract rights.

A. Consequences of Third Party Contract Rights on the Promisee

Under current third party beneficiary law, an intended third party beneficiary is in every sense a "third party," not a new "second party." In other words, an intended third party beneficiary is not a replacement for the promisee, but rather a true third party, i.e., an additional party. As a result, deciding that a third party has contract rights against the promisor because the third party is an intended third party beneficiary does not affect the promisee's contract rights. An intended third party beneficiary transaction does not effect a transfer of contract rights.[218]

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213. 20 N.Y. 268 (1859); *see also supra* section I.B.

214. 120 N.E. 639 (N.Y. 1918); *see also supra* section I.C.

215. *See supra* section I.D.

216. E. ALLAN FARNSWORTH ET AL., CONTRACTS 927 (8th ed. 2013) (using the phrase "centered on the law of trusts" while describing history of third party beneficiary law).

217. RESTATEMENT (FIRST) OF CONTRACTS ch. 6 (AM. LAW INST. 1932).

218. *See, e.g.*, Campbell v. Parkway Surgery Ctr., LLC, 354 P.3d 1172, 1181 (Idaho 2015) ("[A] promise in a third-party beneficiary contract creates a duty in the promisor to the promisee to

That is one of the major legal differences between third party beneficiary law and the law governing assignments. When A contracts with B and then later A assigns her contract right to C, the assignor A no longer has any contract rights.[219] C, the assignee, replaces A, the assignor.[220] The consequence of an assignment is that the assignee replaces the assignor—the assignor no longer has contract law rights against the obligor.

In third party beneficiary law, both the terminology and consequences are different from assignment law. The promisee of a third party beneficiary contract has the same rights as the promisee of any other contract.[221]

Reconsider the facts of our "first" third party beneficiary case, *Lawrence v. Fox*.[222] Remember that Lawrence had loaned $300 to Holly.[223] Holly then entered into a contract with Fox in which Holly loaned $300 to Fox.[224] Fox then promised to pay $300 dollars to Lawrence.[225] After the promisor Fox breached, the third party Lawrence recovered $300 breach-of-contract damages from the promisor Fox, extinguishing Holly's debt to Lawrence in the process.[226]

In response to Fox's nonperformance, Lawrence could have instead sued Holly to recover the $300, extinguishing the original debt. Holly could have then sued Fox for breach of contract and recovered the $300 of general expectation damages. In sum, like most promisees in third party beneficiary contracts, Holly would not be adversely affected by recognition of third party contract rights.

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perform the promise even though he also has a similar duty to the third-party beneficiary." (citing RESTATEMENT (SECOND) OF CONTRACTS § 305(1) (AM. LAW INST. 1981))).

219. PERILLO, *supra* note 36, at 605 ("[A]ssignment extinguishes the right in the assignor and transfers it to the assignee.").

220. *Id.*

221. *See, e.g.*, *Campbell*, 354 P.3d at 1180 ("Parkway's argument completely ignores the well-established rule in contract law that even though a third-party beneficiary contract creates a duty to the beneficiary, the promisee still has a right to performance."); RESTATEMENT (SECOND) OF CONTRACTS § 305 cmt. a (AM. LAW INST. 1981) ("[P]romisee of a promise for the benefit of a beneficiary has the same right to performance as any other promisee.").

222. 20 N.Y. 268 (1859).

223. *Id.* at 269.

224. *Id.*

225. *Id.*

226. *Id.*

B. Consequences of Third Party Contract Rights on the Promisor

1. No Double Recovery

What could not have happened in *Lawrence v. Fox* was both the third party Lawrence and the promisee Holly's recovering $300 in general expectation damages from Fox for breach of contract. The promisor is protected from double liability for a single breach.

That protection can take various forms. If Lawrence, the third party beneficiary, sues the promisor Fox first and recovers, then the promisee Holly's debt has been extinguished and Holly has no cause of action—no expectation damages. Lawrence's recovery from Fox would satisfy Holly's debt to Lawrence, leaving the promisee Holly in the same position as if the contract had been performed. If, on the other hand, the promisee Holly is the first to sue Fox, then Fox could protect itself from the possibility of double liability by interpleader.[227]

Double recovery from the promisor for the same loss is not a consequence of third party contract rights. The third party and the promisee cannot both recover from the promisor for the same loss.[228]

2. More Damages

In *Lawrence v. Fox*, the promisor Fox's breach had the same effect on both the third party Lawrence and the promisee Holly. Both Lawrence and Holly would sustain the same $300 loss from the breach. The general expectation damages that a court would award for Fox's breach would be the same amount, $300, regardless of whether the plaintiff was Holly the promisee or Lawrence the third party.

In *Lawrence v. Fox*, as in other cases involving a "creditor beneficiary," permitting a third party to be a plaintiff did not change the plaintiff's loss, and therefore did not change the damages that the plaintiff could recover from the breaching promisor.

As our second third party beneficiary case, *Seaver v. Ransom*, illustrates, intended third party beneficiaries are not always creditor beneficiaries. And, as *Seaver v. Ransom* and the other cases set out below illustrate, a promisor's breach will not always have the same effect on both the third party and the promisee. Permitting a third party

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227. PERILLO, *supra* note 36, at 600 (describing how to avoid double liability by "utilizing interpleader procedure or other procedural techniques").

228. *See* RESTATEMENT (SECOND) OF CONTRACTS § 305(2) (AM. LAW INST. 1981) ("[S]atisfaction of the promisor's duty to the beneficiary satisfies to that extent the promisor's duty to the promisee.").

to be a plaintiff can change the damages that can be recovered from the breaching promisor.

Recall that the contract in *Seaver v. Ransom*[229] included a promise by Judge Beman to his wife that he would leave $6000 to her niece, Marion Seaver.[230] Mrs. Beman predeceased the Judge who then breached the contract to leave $6000 to Marion Seaver in his will.[231] Because the court held that Marion Seaver was an intended third party beneficiary, she was entitled to recover expectation damages from the promisor, Judge Beman's estate.[232] And her expectation damages were $6000, which put her in the same financial position as if there had been no breach.[233]

The promisee would be Mrs. Beman or her estate. And, if Mrs. Beman's estate had sued Judge Beman's estate for breach of contract, any expectation damages awarded to Mrs. Beman's estate (the promisee) would have been $0 because the promisor Judge Beman's breach had no financial impact on the promisee Mrs. Beman's estate. Under the contract, Judge Beman promised to pay $6,000 to Marion Seaver; thus, permitting Mrs. Beman's estate to recover the $6,000 would have put the estate in a better position that it would have been had Judge Beman performed.

On the *Seaver v. Ransom* facts, permitting a third party to be the plaintiff can change the damages that can be recovered from the breaching promisor. And the possibility that the third party can recover more from the promisor than the promisee is not limited to the facts of *Seaver v. Ransom*.

Much more recently, the Supreme Court of South Carolina recognized intended third party beneficiary rights in *Fabian v. Lindsay*.[234] In this case, Dr. Denis Fabian ("Denis") contracted with the law firm of Lindsay & Lindsay ("Lindsay") to prepare a trust under which Erika Fabian ("Erika") would receive half of his estate, subject to Denis's wife's life estate.[235] The court recognized intended third party beneficiary rights in Erika.[236] This imposed liability on the promisor (Lindsay), that would not have been imposed in a lawsuit by the

229. 120 N.E. 639 (N.Y. 1918).

230. *Id.* at 639–40.

231. *Id.*

232. *Id.*

233. *Id.*

234. 765 S.E.2d 132 (S.C. 2014).

235. *Id.*

236. *Id.* at 134.

promisee (Denis).[237] All parties involved acknowledged that Denis had intended to include Erika in his trust.[238] After Denis's death, Erika discovered that, due to Lindsay's drafting error, she had been effectively disinherited.[239]

Erika sued Lindsay, alleging, inter alia, that Lindsay had breached its contract with Denis and that she was an intended third party beneficiary of that contract.[240] In ruling for Erika, the Court noted that, because Denis was dead and his estate lacked both a cause of action and damages, the only person entitled to damages for Lindsay's breach of contract was the third party beneficiary, Erika.[241]

Since Denis's estate was worth approximately $13 million, the liability exposure of the promisor Lindsay to the third party Erika was substantial.[242] Even if Denis's estate could sue Lindsay for its breach of contract, the estate's recovery would be minimal or too uncertain to award. Lindsay's breach did not cause any financial loss to the estate. At best, Denis's estate could argue that Lindsay's breach would have distressed Denis if Denis were still alive. How can a court measure expectation damages for distress of a deceased person? Answer: the court cannot and so there is no recovery by the promisee.[243]

Both Seaver and Fabian involved donee-beneficiaries who recovered more than the promisee was entitled under the contract. However, this outcome extends to other classes of third party beneficiaries, as well. For example, in *Cianciotto v. Hospice Care Network*,[244] a New York District Court permitted a third party beneficiary to recover consequential damages despite the fact that such damages were not available to the promisee.[245] The litigation arose after Cianciotto's father contracted with Hospice Care Network ("HCN") to provide him with palliative care for a period of up to six months or until his death, depending on which occurred first.[246] HCN allegedly breached the contract by refusing to

237. *Id.*

238. *Id.*

239. *Id.*

240. *Id.* at 134.

241. *Id.* at 137.

242. *Id.* at 134.

243. *Cf.* RESTATEMENT (SECOND) OF CONTRACTS § 353 cmt. a (AM. LAW INST. 1981) ("Damages for emotional disturbance are not ordinarily allowed. Even if they are foreseeable, they are often particularly difficult to establish and to measure.").

244. 927 N.Y.S.2d 779 (Dist. Ct. Nassau Cty. 2011).

245. *Id.*

246. *Id.* at 781–82.

provide care after "only a few weeks," which forced Cianciotto to resume caring for her father.[247] Upon her father's death, Cianciotto filed a suit claiming damages of $15,000 based on economic loss and emotional distress stemming from missed employment opportunities and being forced to watch her father deteriorate.[248]

The Court held that because the contract expressly contemplated a benefit to Cianciotto by relieving her of some caregiving duties, her claim should survive the motion to dismiss.[249] In so ruling, the court noted that Cianciotto's father and his estate did not suffer the damages Cianciotto sought.[250]

Obviously, in a lawsuit brought by the promisee, Cianciotto's father, or his estate, no expectation damages would be awarded for the third party Cianciotto's lost economic opportunities or pain and suffering. Such damages are "special" to the third party beneficiary Cianciotto, i.e., the third party beneficiary's consequential damages.[251]

Third party beneficiaries can recover their consequential damages[252] unless the contract between the promisor and the promisee limits remedies to exclude consequential damages.[253] And, the amount of those consequential damages can be many times greater than the gross contract price.[254]

As a result, contracting parties should be, and are, concerned about consequential damages. That is why so many commercial contracts contain provisions eliminating liability for consequential damages.

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247. *Id.* at 782.

248. *Id.* at 782, 785–86. Although emotional damages are not usually recoverable under breach of contract claims, there is a special exception for contracts dealing with end of life care and the handling of dead bodies, especially when the harm is a "direct" result of the breach as opposed to being "consequential."

249. *Id.* at 784.

250. *Id.* at 785–86.

251. *See* MURRAY, *supra* note 99, at 767 ("'Special damages' are often called 'consequential damages.'").

252. *See, e.g.*, Delgado v. Kornegay, 395 N.Y.S.2d 126, 127 (Dist. Ct. Suffolk Cty. 1977) (ruling home purchaser was entitled to recover consequential damages resulting from breach of termite inspection contract between home seller and inspector).

253. *See, e.g.*, Harris Moran Seed Co. v. Phillips, 949 So. 2d 916, 930–31 (Ala. Civ. App. 2006) ("As a third-party beneficiary of the contract between HMSC and Clifton Seed Company, the farmers step into Clifton Seed Company's shoes for purposes of the consequential-damages exclusion.").

254. *Cf.* Metro. Life Ins. v. Noble Lowndes Int'l, Inc., 643 N.E.2d 504, 508 (N.Y. 1994) (noting that the seller "would be under inordinate economic pressure to complete performance, being at risk of incurring liability for consequential damages in sums . . . many times greater than the gross contract price" without a clause limiting liability).

Indeed, concern about the impact of third party consequential damages led to the Restatement excluding a third party's recovery of consequential damages under government contracts.[255] The test for determining when a third party has contract rights under contracts between private parties should at least reflect concern about the impact of third party consequential damages on the promisor.

In sum, recognition of third party contract rights exposes the promisor to the possibility of a different liability. The promisor's breach might have a different effect on the third party than on the promisee, leading to different and possibly greater damages.

3. *More Litigation*

Obviously, a determination that if a person breaches a contract then not only the other contracting party but also a third party can be a plaintiff, increases the possibility of litigation. Two tigers behind one of the doors is more problematic than only one tiger behind one of the doors.[256] While we cannot predict that enabling twice as many people to be plaintiffs will result in twice as much litigation, it is reasonable to argue—even without supporting empirical data—that determining that a third party has contract rights means more litigation.

And, it is reasonable to argue that a third party might initiate litigation in situations in which the other contracting party would not. Moreover, this argument is supported by empirical data.

For example, as Professor Chapin Cimino recently wrote, "most legal scholars accept the core insight of what is called *relational contract theory*: most commercial contracts involve repeat players who seek to maximize wealth while still maintaining cooperative relationships."[257] These relationships are generally maintained by relying on non-legal sanctions. These repeat players are reluctant to file a lawsuit because litigating "threatens to disrupt the norms necessary to continuing relations."[258] Third parties have no such concern about disrupting continuing relations because they have no cooperative relationship with

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255. *See* RESTATEMENT (SECOND) OF CONTRACTS § 313(2) (AM. LAW INST. 1981) ("[A] promisor who contracts with a government or governmental agency to do an act for or render a service to the public is not subject to contractual liability to a member of the public for consequential damages.").

256. *Cf.* Frank R. Stockton, *The Lady, or the Tiger?*, CENTURY, Nov. 1882, at 83.

257. Chapin F. Cimino, *The Relational Economics of Commercial Contract*, 3 TEX. A&M L. REV. 91, 91 (2015) (emphasis in original). *See generally* Stewart Macaulay, *Non-Contractual Relations in Business: A Preliminary Study*, 28 AM. SOC. REV. 55 (1963).

258. Jean Braucher, *The Afterlife of Contract*, 90 NW. U. L. REV. 49, 79 (1995).

the promisor to continue. Therefore, third parties are more likely to sue for breach of contract than a contracting party.

In sum, recognition of third party contract rights increases the possibility that the promisor will be sued if it breaches and, at least in some cases, increases the amount of damages that the plaintiff can recover for such a breach.[259]

C. *An Analytical Approach that Reflects Practical Consequences*

The primary practical consequence of determining that a third party can enforce a contract that an individual did not make is remedial:[260] more specifically, the creation of an additional possible plaintiff. Remember, the third party is not merely a "beneficiary"; they are a "plaintiff."

The use of the term "beneficiary" to describe the third party only makes sense in a historical context. Early cases such as *Lawrence v. Fox*[261] and *Seaver v. Ransom*[262] relied on trust cases for precedent,[263] and the term "beneficiary" is of course an important part of trust law. Under what Professor Lawrence Cunningham describes as common law's "iterative process," subsequent cases continued to use the term "beneficiary."[264]

In light of the practical consequences of determining that a third party can enforce a contract, "additional possible plaintiff" is a more descriptive contract law term than "third party beneficiary." "Intent" that someone can "benefit" from your performance of a contract is very

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259. *Cf.* Eisenberg, *supra* note 8, at 1429 ("[A]llowing a third party to enforce a contract may unduly enlarge a promisor's liability.").

260. *Id.* at 1430 (labeling third party beneficiary law a "remedial device"); *see also* HENRY M. HART, JR. & ALBERT M. SACKS, THE LEGAL PROCESS: BASIC PROBLEMS IN THE MAKING AND APPLICATION OF LAW 136 (William N. Eskridge, Jr. & Philip P. Frickey eds., 1994) ("If A promises B that he will pay B's debt to C and the promise is valid and binding, it is obvious that C has a primary 'right' at least in the sense of a claim to the benefit of the performance of A's promise. But as every first-year law student knows it has not been obvious to many courts that C has a right of action against A if A fails to pay the debt. Only B, these courts have held, enjoys the remedial capacity to hail A into court and enforce a sanction against him for breach of his promise. A system of analysis which permits confusion between a primary claim to a performance and a remedial capacity to invoke a sanction for nonperformance is dangerous at best.").

261. Lawrence v. Fox, 20 N.Y. 268 (1859); *see also supra* section I.B.

262. Seaver v. Ransom, 120 N.E. 639 (N.Y. 1918); *see also supra* section I.C.

263. *See* Cunningham, *supra* note 33, at 751 ("The court's [Lawrence v. Fox] input rule was from the law of trusts and produced an output rule of contract law that permitted a stranger to a contract to enforce it."); Waters, supra note 7, at 1122, 1138.

264. Cunningham, *supra* note 33, at 750–57 (using *Lawrence v. Fox* and the third party beneficiary cases following *Lawrence v. Fox* to illustrate common law as an "iterative process").

different from understanding that someone can sue you for not performing a contract.

The use of the term "intended," like the use of the term "beneficiary," creates unnecessary ambiguities because "intent" is more in the nature of a conclusion than a test. "Intent" is a recurring concern in contract law, and contract cases are divided as to what factors should lead to a conclusion of intent.[265]

Ascertaining contractual intent is difficult enough in the typical breach of contract action in which both the plaintiff and the defendant were parties to the contract. Questions of intent become much more complicated when a third party is the plaintiff because the jury will be hearing the plaintiff's arguments about contractual intention in a deal that the plaintiff did not personally negotiate or document.

Consider the recently revised Florida jury instruction on third party beneficiaries:

> 416.2 THIRD-PARTY BENEFICIARY
>
> (Claimant) is not a party to the contract. However, (claimant) may be entitled to damages for breach of the contract if [he][she][it] proves that (insert names of the contracting parties) intended that (claimant) benefit from their contract.[266]

An article in the Florida Bar Journal describes this as "a concise instruction to give the jury to determine easily if someone is a third-party beneficiary."[267] With all due respect[268] to the author who is the "former elected-Chair of the 1700-member Florida Appellate Practice Section,"[269] we disagree. Perhaps we have read too many Carl Hiaasen

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265. *Compare* Dietrich v. Stephens, No. 05-CV-72113, 2010 WL 1286204, at *4 (E.D. Mich. Mar. 30, 2010) ("[I]ntent exists only at the time the contract was made."), *with* Stender v. Twin City Foods, Inc., 82 Wash. 2d 250, 510 P.2d 221, 224 (Wash. 1973) ("Determination of the intent of the contracting parties is to be accomplished by viewing the contract as a whole, the subject matter and objective of the contract, all the circumstances surrounding the making of the contract, the *subsequent acts and conduct of the parties to the contract*, and the reasonableness of respective interpretations advocated by the parties." (emphasis added)). *See also* Uribe v. Merch. Bank of N.Y., 693 N.E.2d 740, 743 (N.Y. 1998) ("'[R]easonable expectation and purpose of the ordinary business[person] when making an ordinary business contract' serve as the guideposts to determine intent." (brackets in original)).

266. *In re* Standard Jury Instructions—Contract and Bus. Cases, 116 So. 3d 284, 304 (Fla. 2013).

267. Dorothy F. Easley, *Florida's New Jury Instructions in Contracts and Business Law Cases: A Primer*, 88 FLA. B.J. 40, 40 (Apr. 2014).

268. *See With All Due Respect - Ricky Bobby.flv*, YOUTUBE (Apr. 19, 2012), https://www.youtube.com/watch?v=xVTpCViyUwM (last visited Nov. 4, 2016).

269. *Lawyers*, EASLEY APPELLATE PRACTICE, http://www.easleyappellate.com/Appeal_Attorney.html [https://perma.cc/3VGT-J8E8].

novels,[270] but we believe that a Florida jury will neither "determine easily if someone is a third party beneficiary" nor fully understand the consequences of such a determination.

Professors Alan Schwartz and Robert Scott recently wrote about the "uncertainty that attends the intent test."[271] More specifically, they question, "Does it mean acting with a motive to achieve a result or knowing the result is likely to follow? Does it refer to the 'ends' the actor seeks to achieve or the 'means' to those ends?"[272] Professors Scott and Schwartz then suggest that "[a] law and economics analysis would support an objective, functional test."[273] While we do not warrant that we understand all the law and economics formulae in the Schwartz and Scott article, we also suggest an objective, functional test.

The function of third party beneficiary law is to identify when a contracting party has the risk of additional possible plaintiffs.[274] Each party to a contract is entitled to know the risks and liabilities involved in entering a contract and that "necessarily includes the range of potential third persons who may enforce the terms of the contract."[275] Such knowledge is essential to an informed decision on entering the contract and pricing its terms. That is why the Florida instruction on special damages is as follows:

> 504.2 BREACH OF CONTRACT DAMAGES
>
> * * * . . .
>
> b. *Special damages*:
>
> . . . To recover special damages, (claimant) must prove that when the parties made the contract, (defendant) knew or reasonably should have known of the special circumstances leading to such damages.[276]

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270. *Cf.* Erin Z. Bass, *Carl Hiaasen's Most Memorable Characters*, DEEP S. MAGAZINE (June 11, 2013), http://deepsouthmag.com/2013/06/carl-hiaasens-most-memorable-characters/ [https://perma.cc/XQ4A-JALB].

271. Schwartz & Scott, *supra* note 9.

272. *Id.*

273. *Id.*

274. *See* FARNSWORTH, *supra* note 115, at 6 (describing third party beneficiary law as "one aspect of the extent of risk undertaken by a contracting party"); Eisenberg, *supra* note 8, at 1430 (labeling third party beneficiary law a "remedial device").

275. Gazo v. City of Stamford, 765 A.2d 505, 514 (Conn. 2001). *See* Powers, *supra* note 9, at 78 (suggesting "overriding policy" in third party beneficiary law should be "how is a contracting party to evaluate the risks and liabilities involved in entering a contract.").

276. *In re* Standard Jury Instructions—Contract and Bus. Cases, 116 So. 3d 284, 333 (Fla. 2013) (emphasis in original).

And that knowledge of possible obligations necessarily should include the range of third persons who can enforce the contract—the additional possible plaintiffs. Accordingly, the jury instruction in Florida and other states for whether a third party can be a plaintiff in an action to enforce a contract that she did not make should ask: "did the defendant have reason to know at the time of the contract that the third party was an additional possible plaintiff who could ultimately recover damages?"

Under the law governing contract damages, Ed's liability exposure to Bud for breach of the butcher shop sale contract would be limited to the losses he had "reason to foresee as a probable result of the breach when the contract was made."[277] Under the law governing third parties' contract rights, Ed's possible liability exposure to Noreen or other third parties should be similarly limited. Simply put, the question should be whether Ed would have made the contract with Bud on the same terms if he had reason to know at the time of the contract that Noreen was an additional possible plaintiff in the event of his later breach.[278]

CONCLUSION

As Albert Camus (and perhaps Noreen[279]) would tell us, "One recognizes one's course by discovering the paths that stray from it."[280] The present law of third party beneficiaries "strays." It reflects its nineteenth century analytical origins, not its twenty-first century application. In determining whether a third party has the legal right to enforce a contract she did not make, courts ask whether the contracting

277. *See* RESTATEMENT (SECOND) OF CONTRACTS § 351(1) (AM. LAW INST. 1981). The language of the Restatement is not identical to the language of the Uniform Commercial Code or the Florida jury instruction. The Restatement uses the phrase "reason to foresee," *id.*, while Uniform Commercial Code section 2-715 and the Florida jury instruction use "reason to know" and "reasonably should have known." U.C.C. § 2-715(2)(a) (AM. LAW INST. & UNIF. LAW COMM'N 2002). A comprehensive review of the consequential damages case law suggests "courts freely interchange these expressions." Thomas A. Diamond & Howard Foss, *Consequential Damages for Commercial Loss: An Alternative to* Hadley v. Baxendale, 63 FORDHAM L. REV. 665, 669 (1994).

278. *Cf.* Immanuel Kant, *An Answer to the Question: What Is Enlightenment?*, *in* PRACTICAL PHILOSOPHY 20 (Mary J. Gregor ed. and trans., 1996) ("The touchstone of everything that can be concluded as a law for a people lies in the question whether the people could have imposed such a law on itself.").

279. *Cf.* Terri Schwartz, *Fargo: The Gift of the Magi*, IGN (Nov. 10, 2015), http://in.ign.com/m/the-gift-of-the-magi/82994/review/fargo-the-gift-of-the-magi-review [https://perma.cc/5R25-PFYB] ("Noreen, the butcher shop cashier, was reading 'The Myth of Sisyphus' in scenes.").

280. *See* ALBERT CAMUS, *Absurd Creation: Ephemeral Creation*, *in* THE MYTH OF SISYPHUS AND OTHER ESSAYS 93, 113 (Justin O'Brien trans., 1955).

parties intended to confer a benefit on the plaintiff. In short, the test is "intent to benefit."[281]

We have argued here that this is the wrong test and the wrong question. And, of course, asking juries the wrong question is more likely to lead to the wrong result than asking the right question.

The "course" should be appropriate liability exposure for contracting parties. The result of recognizing third party contract rights is enlarging a contracting party's liability exposure.

Enlarging a contract party's liability exposure and finding a contract party's intention to benefit someone are not the same thing. The function of the test for whether a third party has contract rights should be to assure that a person can enter into a contract with the confidence that she will not later find herself bound to unanticipated obligations.

Accordingly, courts should take a different, more functional "path" to third party contract rights. Instead of determining whether buyer Ed Blomquist and/or seller Bud Jorgenlen intended for the contract for the sale of Bud's Butcher Shop to benefit Noreen Vanderslice as courts now do, a court should determine whether Ed had reason to know, at the time he contracted with Bud, that Noreen or some other third person similar to Noreen was an additional possible plaintiff in the event he breached, i.e. an "APP."

281. *See, e.g.*, Hickman v. Safeco Ins. Co. of Am., 695 N.W.2d 365, 367 (Minn. 2005) ("The issue in this case is whether appellant . . . is a third-party beneficiary . . . under the 'intent to benefit' test.").