PRIVITY OF CONTRACT

- **Privity of Contract:** As a general rule, only the parties to a contract -- the promisor(s) and the promisee(s) -- owe any duties and enjoy any rights arising from the contract. Common law recognizes three exceptions:

- **Assignment (of Rights):** A transaction whereby a party to the contract (the *assignor*) transfers his or her rights to some third party (the *assignee*). As a consequence, the assignee may demand performance of the contract by the *obligor*, and the *assignor’s contract rights are extinguished*.

- **Delegation (of Duties):** A transaction whereby a party to the contract (the *delegator*) frees himself or herself from his or her duties by having some third party (the *delegatee*) perform those duties. Unlike the assignor, whose contract rights are extinguished by the assignment, the *delegator remains liable* for his or her contract duties if the delegatee fails to perform.

- **Third-Party Beneficiary:** A third party, X, who is intended, by the terms of the contract between Y and Z, to benefit from Y’s and Z’s performance of the contract.
SCAPE OF ASSIGNMENT

As a general rule, all contract rights may be assigned, except where:

(1) the assignment is prohibited by statute;

(2) the contract to be assigned is for personal services, unless all that remains under the contract is a money payment for services previously rendered;

(3) the assignment would materially increase the risk or alter the duties of the obligor; or

(4) the contract specifically forbids assignment.

There are exceptions to this exception, namely the contract may not prevent the assignment of:

(a) the right to receive money;

(b) rights in, or the alienation of, real property;

(c) negotiable instruments; or

(d) the right to recover damages for breach of contract or for payment of an account under the U.C.C.
NOTICE OF ASSIGNMENT

Once a valid assignment of rights has been made to a third party, the third party (the assignee) should notify the obligor of the assignment.

Note: Notice that we say “should,” rather than “must,” because the assignment is effective immediately, whether or not notice is given to the obligor.

However, until the obligor receives notice of the assignment, he or she may satisfy his or her contractual obligations by performance to the assignor -- even if the assignor has already assigned its rights to the assignee.

If the assignor assigns the same rights to two or more parties, the obligor may not know to whom his or her duty to perform is owed. There are two general rules:

The “Majority” Rule: The first assignment made takes priority over subsequent assignment; and

The “English” Rule: The first assignment recorded or otherwise made known to the obligor takes priority -- even over an assignment made before it.
As a general rule, all contract duties may be delegated, except where:

(1) performance depends on the personal skills or talents of the delegator;

(2) the delegator owes the obligee fiduciary duties or other duties arising from a special trust in the delegator;

(3) performance by the delegatee would materially vary the performance expected by the obligee; or

(4) the contract specifically forbids delegation.
THIRD-PARTY BENEFICIARIES - PART I

- The law distinguishes between intended and incidental third-party beneficiaries. Only intended beneficiaries acquire actionable legal rights in a contract.

- **Intended Beneficiary:** A third party for whose benefit a contract is formed.

- **Incidental Beneficiary:** A third party that benefits from the performance of a contract, but whose benefit was not the reason the contract was formed.

In determining whether a third party is an intended or incidental beneficiary, courts generally use an objective, “reasonable person” test: Would a reasonable person have intended to confer on the third party (1) the right to bring suit to enforce the contract, and, thereby, (2) the right to benefit from the contract? Courts consider whether:

- performance was rendered directly to the third party;

- the third party has the right to control details of the performance; and

- the third party is expressly designated in the contract.
THIRD-PARTY BENEFICIARIES - PART II

- **Types of Intended Beneficiaries:** Two of the more widely recognized classes of third-party beneficiaries are:

  - **Creditor Beneficiary:** A third party that benefits from a contract in which the promisor promises to pay a debt owed by the promisee to the third-party beneficiary.

  - **Donee Beneficiary:** A third party for whose benefit a contract was made whereby the promisor promised the promisee to make a gift to the third-party beneficiary.

- An intended third-party beneficiary’s rights *vest* (i.e., become enforceable), subject to any reservation of rights to the contracting parties, when either of the following occurs:

  - The third party demonstrates *manifest assent* to the contract (e.g., sends a letter acknowledging awareness of and consent to the contract for his or her benefit); or

  - The third party *materially alters* his or her position in *detrimental reliance* on the contract (e.g., sells his or her automobile in anticipation of receiving a new automobile pursuant to the contract).
**DISCHARGE, PERFORMANCE, AND TENDER**

- **Discharge:** The termination of a party’s obligations arising under a contract.

  Discharge occurs either when:

  1. Both parties have **fully performed** their contractual obligations; or

  2. Events, conduct of the parties, and/or operation of law **release** the parties from their obligations to perform.

- **Performance:** Fulfilling one’s contractual duties.

  A party’s obligations to perform under a contract may be either **absolute** or **conditioned** on the occurrence or nonoccurrence of one or more event(s).

- **Tender:** An unconditional offer to perform an obligation by a person who is ready, willing, and able to do so.
CONDITIONAL PERFORMANCE

- **Condition**: A contractual qualification, provision, or clause which creates, suspends, or terminates the obligations of one or both parties to the contract, depending on the occurrence or nonoccurrence of some event(s).

- **Condition Precedent**: A condition that must be satisfied before a party’s contractual obligation to perform becomes absolute (e.g., Bob promises to hire Terry as a driver as soon as Terry gets his license).

- **Condition Subsequent**: A condition of which the occurrence or nonoccurrence will terminate a party’s absolute obligation to perform (e.g., Mary agrees to let Sue stay in Mary’s spare room for as long as Sue remains unmarried).

- **Concurrent Conditions**: Mutually dependent conditions that must occur or be performed at the same time in order to give rise to any absolute obligation to perform (e.g., Nikki offers to pay Tina $100 in exchange for Tina’s class ring).
CONTRACTUAL PERFORMANCE

- **Discharge by Performance:** A contract terminates when both parties fulfill their respective duties by performing the acts they have promised.

- **Complete vs. Substantial Performance:** When a party fails to completely perform his or her contractual duties, the question arises whether the performance was nonetheless sufficiently substantial to discharge the contractual obligation. If so, then the party is said to have substantially performed.

- In order to qualify as substantial performance, the party’s performance must not vary greatly from that promised in the contract, and it must create substantially the same benefits as those promised in the contract.

- If one party substantially performs, the other party’s duty to perform remains absolute -- although the other party may be entitled to recover damages, if any, for the substantially performing party’s failure to fully perform.

- If a party fails to either substantially or fully perform, the other party’s remaining obligations, if any, under the contract are discharged.
BREACH AND REPUDIATION

- **Material Breach of Contract:** A party’s failure, without legal excuse, to *substantially* perform the obligations he or she has promised to perform.

  - If a party’s breach is non-material, the non-breaching party’s duty to perform may be *suspended* until the breach is remedied, or “cured.” However, a non-material breach will not *excuse* performance by the non-breaching party. Only a *material* breach will excuse the non-breaching party from its contractual obligations.

- **Anticipatory Repudiation:** An action by a party to a contract that indicates that he or she will not perform a contractual obligation due to be performed in the future.

  - Such a repudiation will *excuse* the non-repudiating party from performing under the contract.

  - However, until the non-repudiating party treats the repudiation as a material breach, the repudiating party can *retract* his or her repudiation and *restore* the parties’ contractual rights and obligations.
DISCHARGE BY AGREEMENT

- **Rescission:** The process by which the parties cancel a contract and return one another to their pre-contract status.

- **Novation:** Substituting, by agreement, a new contract for an old one, and thereby terminating the parties’ rights and duties under the old contract.

  Novation differs from *assignment* or *delegation* because novation requires a new agreement.

- **Novation** requires:

  1. a **valid, prior agreement**, for which
  2. all parties agree to **substitute** a new **third party** in place of one of the original parties to the contract;
  3. **discharge** of the prior obligation of the original party who is now being released from the contract; and
  4. a **valid, new agreement**.

- **Accord and Satisfaction:** An agreement between the parties to accept different performance than that promised in the contract.
DISCHARAGE BY OPERATION OF LAW

- **Contract Alteration:** The innocent party may elect to be discharged under a contract when the other party has unknowingly materially altered a written contract.

- **Statute of Limitations:** A statute which limits the time period for initiating a lawsuit to recover damages for a breach of contract.

- **Bankruptcy:** A contractual debt or obligation that is discharged in a bankruptcy proceeding is barred from future enforcement.
IMPOSSIBILITY OF PERFORMANCE

- **Impossibility of Performance:** A doctrine which permits a party to be relieved of his or her contractual duties when performance becomes either impossible or totally impracticable through no fault of either party to the contract.

- **Objective vs. Subjective Impossibility:** Only *objective* impossibility excuses performance. The following will generally excuse performance as objectively impossible:

  1. **Death or incapacitation** prior to performance of a personal services contract;
  2. **Destruction of the subject matter** of the contract prior to performance;
  3. A change in the applicable law which renders performance *illegal*; and
  4. Changing market conditions that make performance *commercially impracticable*.

- **Temporary Impossibility:** A change in circumstances that makes performance temporarily impossible will act to *suspend*, but *not* excuse performance.