Instructor Manual

Miller, Business Law Today – Comprehensive Edition: Text and Cases 13e 2022, 9780357634783; Chapter 18: Third Party Rights

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# Purpose and Perspective of the Chapter

This chapter begins its discussion of third-party contractual rights by considering the extent to which non-contract­ing parties have rights in or to a contract. Because a contract represents an agreement be­tween the parties who made it, only those parties have rights and liabilities under it. A party not in privity of contract has no rights in or to a contract.

There are two exceptions. A third-party benefici­ary contract is made with the intent to benefit a third party, and the third party has rights in the contract and may sue the promisor, which under some circumstances, the promisee has to have it en­forced. Under an as­signment of rights or a delega­tion of duties, one of the parties transferscontractual rights or obligations to a third party, giving the third party the rights or obliga­tions of the transferor.

Cengage Supplements

The following product-level supplements provide additional information that may help you in preparing your course. They are available in the Instructor Resource Center.

* Transition Guide (provides information about what’s new from edition to edition)
* Test Bank (contains assessment questions and problems)
* Solution and Answer Guide (offers textbook solutions and feedback)
* PowerPoint (provides text-based lectures and presentations)
* Guide to Teaching Online (provides technological and pedagogical considerations and resources for teaching online)
* MindTap Educator Guide (describes assets in the MindTap platform with a detailed breakdown of activities by chapter with seat time)

# Chapter Objectives

The following objectives are addressed in this chapter:

1. Define privity.
2. Identify the rights of third-party beneficiaries.
3. Explain circumstances that would require disputing parties to be in privity of contract and bring a breach of contract claim.
4. Describe the legal rights and obligations of each contracting party when a contract is assigned or delegated to a third party.
5. Discuss the permissibility of an assignment or delegation under a personal satisfaction contract.
6. Identify the Restatement’s rule on liability to third parties.
7. Distinguish between intended and incidental beneficiaries.

# Key Terms

**Alienation:** the transfer of title to real property (which “alienates” the real property from the former owner).

**Assignee:** a party to whom another party’s rights under a contract are transferred, or assigned.

**Assignment:** the transfer to another of all or part of one’s rights arising under a contract.

**Assignor:** a party who transfers (i.e., assigns) rights under a contract to another party (i.e., the assignee).

**Delegatee:** a party to whom contractual obligations are transferred, or delegated.

**Delegation of duties:** the transfer to another of a contractual duty.

**Delegator:** a party who transfers (i.e., delegates) obligations under a contract to another party (i.e., the delegatee).

**Incidental beneficiary:** a third party who benefits from a contract even though the contract was not formed for that purpose; an incidental beneficiary has no rights in the contract and cannot sue to have it enforced.

**Intended beneficiary:** a third party for whose benefit a contract is formed; an intended beneficiary can sue the promisor if the contract is breached.

**Obligee:** one to whom an obligation is owed.

**Obligor:** one who owes an obligation to another.

**Third-party beneficiary:** one who is not a party to the contract, but who stands to benefit from the contract’s performance.

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# What's New in This Chapter

The following elements are improvements in this chapter from the previous edition:

* **1 New Numbered Case Example:**
  + on creditor beneficiaries (2019)

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# Chapter Outline

*In the outline below, each element includes references (in parentheses) to related content. “PPT Slide #” refers to the slide number in the PowerPoint deck for this chapter (provided in the PowerPoints section of the Instructor Resource Center). Introduce the chapter and review objectives for Chapter 18 (PPT Slide 3).*

1. **18-1 Assignments** (PPT Slides 5-11)
   1. **Effect of an Assignment**
      1. In a bilateral contract, the two parties have corresponding rights and duties. One party has a right to require the other to perform some task, and the other has a duty to perform it.
         1. The transfer of contract rights to a third person is known as an **assignment**.
         2. **Example 18.1**
      2. In an assignment, the party assigning the rights to a third party is known as the **assignor**, and the party receiving the rights is the **assignee**.
         1. Other terms traditionally used to describe the parties in assignment relationships are **obligee** (i.e., the person to whom a duty, or obligation, is owed) and **obligor** (i.e., the person who is obligated to perform the duty).
      3. **Extinguishes the Rights of the Assignor –** When rights under a contract are assigned unconditionally, the rights of the assignor are extinguished. The assignee has a right to demand performance from the other original party to the contract, the obligor.
         1. **Example 18.2**
         2. ***See* Exhibit 18-1 – Assignment Relationships**
      4. **Assignee Takes Rights Subject to Defenses –** The assignee obtains only those rights that the assignor originally had. In addition, the assignee’s rights are subject to the defenses that the obligor has against the assignor.
         1. **Example 18.3**
         2. ***See* Case 18.1: *JP Morgan Chase Bank N.A. v. McNeill***
   2. **Rights That Cannot Be Assigned**
      1. **When a Statute Expressly Prohibits Assignment –** If a statute expressly prohibits assignment, the right in question cannot be assigned.
         1. For instance, in many states, workers’ compensation statutes prohibit an employee who is receiving benefits from assigning them to another.
      2. **When a Contract is Personal in Nature –** When a contract is for personal services, the rights under the contract normally cannot be assigned unless all that remains is a monetary payment.
         1. **Example 18.4**
      3. **When an Assignment Significantly Changes the Risk or Duties of the Obligor –** A right cannot be assigned if assignment will significantly alter the risks or the duties of the obligor.
         1. **Example 18.5**
      4. **When the Contract Prohibits Assignment –** If a contract stipulates that the right cannot be assigned, then ordinarily it cannot be assigned. This restraint operates only against the parties themselves. It does not prohibit an assignment by operation of law, such as an assignment pursuant to bankruptcy or death.
         1. Whether an anti-assignment clause is effective depends, in part, on how it is phrased. A contract that states that any assignment is void effectively prohibits any assignment.
         2. **Example 18.6**
   3. ***Knowledge Check Activity (1) PPT Slide: 1 minute(s) total (5 minutes with discussion and review of answer).*** *Tests students’ knowledge of when rights cannot be assigned. After answer is provided, review with students the concept of when rights cannot be assigned in a contract.*
   4. **Notice of Assignment**
      1. Giving notice is not legally necessary to establish the validity of the assignment because an assignment is effective immediately, whether or not notice is given.
         1. However, two major problems arise when notice of the assignment is not given to the obligor.
      2. **Priority Issues –** If the assignor assigns the same right to two different persons, the question arises as to which one has priority—that is, which one has the right to the performance by the obligor.
         1. **Example 18.7**
      3. **Potential for Discharge by Performance to the Wrong Party –** Until the obligor has notice of an assignment, the obligor can discharge any obligations by performance to the assignor, and this performance constitutes a discharge to the assignee.
         1. Once the obligor receives proper notice, only performance to the assignee can discharge the obligor’s obligations.
         2. **Example 18.8**
2. **18-2 Delegations** (PPT Slides 12-15)
   1. **Duties That Cannot Be Delegated** 
      1. Normally, a **delegation of duties** does not relieve the party making the delegation (i.e., the **delegator**) of the obligation to perform, in the event that the party to whom the duty has been delegated (i.e., the **delegatee**) fails to perform.
         1. ***See* Exhibit 18-2 – Delegation Relationships**
         2. As a general rule, any duty can be delegated. This rule has some exceptions, however. Delegation is prohibited in the following circumstances:
            * When performance depends on the personal skill or talents of the obligor.
            * When special trust has been placed in the obligor.
            * When performance by a third party will vary materially from that expected by the obligee.
            * When the contract expressly prohibits delegation.
      2. **When the Duties Are Personal in Nature –** When special trust has been placed in the obligor or when performance depends on the obligor’s personal skill or talents, contractual duties cannot be delegated.
         1. **Example 18.9**
      3. **When Performance by a Third Party Will Vary Materially from That Expected by the Obligee –** When performance by a third party will vary materially from that expected by the obligee under the contract, contractual duties cannot be delegated.
         1. **Example 18.10**
      4. **When the Contract Prohibits Delegation –** When the contract expressly prohibits delegation by including an anti-delegation clause, the duties cannot be delegated.
         1. **Example 18.11**
   2. **Effect of Delegation**
      1. If a delegation of duties is enforceable, the obligee (i.e., the one to whom performance is owed) must accept performance from the delegatee (i.e., the one to whom the duties are delegated)
         1. **Example 18.12**
      2. A valid delegation of duties does not relieve the delegator of obligations under the contract. Although there are exceptions, generally the obligee can sue both the delegatee and the delegator for failure to perform.
         1. **Example 18.13**
         2. ***See* Case 18.2: *Mirandette v. Nelnet, Inc.***
   3. **“Assignment of All Rights”**
      1. Sometimes, a contract provides for an “assignment of all rights.” This wording may create both an assignment of rights and a delegation of duties.
         1. Typically, this situation occurs when general words are used, such as “I assign the contract” or “I assign all my rights under the contract.”
      2. A court normally will construe such words as implying both an assignment of rights and a delegation of any duties of performance.
         1. The assignor remains liable if the assignee fails to perform the contractual obligations.
3. **18-3 Third-Party Beneficiaries** (PPT Slides 16-22)

Another exception to the doctrine of privity of contract arises when the contract is intended to benefit a third party. The original parties to a contract can agree that the contract performance should be rendered to or directly benefit a third person. When this happens, the third person becomes an *intended* **third-party beneficiary** of the contract. As the **intended beneficiary** of the contract, the third party has legal rights and can sue the promisor directly for breach of the contract.

* 1. **Who is the Promisor?**
     1. Allowing a third party to sue the promisor directly circumvents the “middle person” (i.e., the promisee) and thus reduces the burden on the courts. Otherwise, the third party would sue the promisee, who would then sue the promisor.
        1. ***See* Classic Case Example 18.14: *Lawrence v. Fox***
        2. ***See* Case 18.2: *Bozzio v. EMI Group, Ltd.***
  2. **Types of Intended Beneficiaries**
     1. **Creditor Beneficiary –** A *creditor beneficiary* benefits from a contract in which one party promises another party to perform a duty that the promisee owes to a third party (i.e., the creditor beneficiary).
        1. As an intended beneficiary, the creditor beneficiary can sue the promisor directly to enforce the contract.
           + ***See* Case Example 18.15: *Goonewardene v. ADP, LLC***
     2. **Donee Beneficiary –** When a contract is made for the express purpose of giving a *gift* to a third party, the third party is a *donee beneficiary*.
        1. **Example 18.16**
  3. **When the Rights of an Intended Beneficiary Vest –** An intended third party beneficiary cannot enforce a contract against the original parties until the third party’s rights have vested, meaning that the rights have taken effect and cannot be taken away.
     1. Until these rights have vested, the original parties to the contract—the promisor and the promisee—can modify or rescind the contract without the consent of the third party.
  4. **Incidental Beneficiaries** 
     1. Sometimes, a third person receives a benefit from a contract even though that person’s benefit is not the reason the contract was made (i.e., an **incidental beneficiary**).
        1. Because the benefit is unintentional, an incidentalbeneficiary cannot sue to enforce the contract. Only intended beneficiaries acquire legal rights in a contract.
           + ***See* Classic Case Example 18.17: *Bowers v. Federation Internationale de L’Automobile***
  5. **Identifying Intended vs. Incidental Beneficiaries** 
     1. In determining whether a party is an intended or an incidental beneficiary, the courts focus on the parties’ intent, as expressed in the contract language and implied by the surrounding circumstances. Any beneficiary who is not deemed an intended beneficiary is considered incidental.
        1. ***See* Exhibit 18-3 – Third-Party Beneficiaries**
     2. Although no single test can embrace all possible situations, courts often apply the *reasonable person* test:
        1. Would a reasonable person in the position of the beneficiary believe that the promisee intended to confer on the beneficiary the right to enforce the contract?
     3. In addition, the presence of one or more of the specific factors strongly indicates that the third party is an intended beneficiary of the contract.
        1. **Case Example 18.18: *Dormitory Authority of the State of New York v. Samson Construction Co.***
  6. ***Knowledge Check Activity (2) PPT Slide: 1 minute(s) total (5 minutes with discussion and review of answer).*** *Tests students’ knowledge of beneficiaries. After answer is provided, review with students the different types of beneficiaries to a contract.*
  7. ***Knowledge Check Video Activity (3) PPT Slide: 2 ½ minute(s) total (5 minutes with discussion and review of answer).*** *Tests students’ knowledge of third-party rights. After answer is provided, review with students the concept of third party rights and what third-party beneficiaries are allowed to do.*

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# Discussion Questions

You can assign these questions several ways: in a discussion forum in your LMS; as whole-class discussions in person; or as a partner or group activity in class.

1. **Discussion – Effect of an Assignment and Rights That Cannot Be Assigned ([18-1 Assignments], PPT Slides 5-11). Duration 15 minutes.**
   1. **How do assignments function?** 
      1. Assignments are involved in many business financing devices. Assignments may involve accounts receivable, proceeds from executory contracts, or general intangibles. Assignments act as assurances of payment for millions of dollars of loans every day.
      2. The most commonly assigned contractual right is the right to the payment of money.
   2. **What rights cannot be assigned?** 
      1. Generally, all rights can be assigned, unless:
         1. An applicable statute expressly prohibits assignment (i.e., assignments of future rights to workers’ compensation are statutorily prohibited);
         2. The contract expressly prohibits assignment;
         3. The right is uniquely personal (i.e., attorney services); or
         4. Assignment would materially alter the risk of the obligor.
2. **Discussion – Effect of Delegation and the Delegatee’s Obligation to Perform ([18-2** **Delegations], PPT Slides 12-15). Duration 5 minutes.**
   1. **What happens if the delegatee fails to perform?** 
      1. Ordinarily, the delegator is still liable to the obligee. The obligee can also hold the delegatee liable if the delegatee has promised performance that will directly benefit the obligee (e.g., a contractor who delegates the construction of a house is liable if the delegatee fails to build the house—the obligee can sue either the contractor or the delegatee). However, after a novation, a delegator has no further liability.
3. **Discussion – Intended vs Incidental Beneficiaries and Vestment of a Third-Party Beneficiary’s Rights ([18-3** **Third-Party Beneficiaries], PPT Slides 16-22). Duration 10 minutes.**
   1. **What are the factors indicating that a third-party beneficiary is an intended beneficiary?** 
      1. The presence of one or more of the following indicates a third party is an intended beneficiary:
         1. Performance is rendered directly to the third party;
         2. The third party has rights to control the details of performance; or
         3. There is an express designation in the contract.
   2. **When do the rights of a third-party beneficiary vest?** 
      1. When the rights of a third party vest, that party can enforce the contract. The rights vest when the original parties cannot rescind or change the contract without the third party’s consent.
      2. When the rights of a third-party beneficiary vest, that party can enforce the contract. Their rights have vested when the beneficiary:
         1. Learns of the contract and manifests assent to it at the request of the promisor and promisee;
         2. Sues on the contract; or
         3. Materially alters his or her position in detrimental reliance on the contract.
      3. If a contract expressly reserves to the contracting parties the right to cancel, rescind, or modify the contract, the rights of the beneficiary are subject to those changes.

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# Additional Activities and Assignments

1. **MindTap** – Why Do Third-Party Rights Matter to Me?
   1. Online auto-graded activities connect the upcoming chapter to a real-world scenario designed to pick engagement and emphasize relevance. Consists of 1 multiple choice question in each.
2. **Mind Tap** – Learn It:
   1. Get familiar with one of the key concepts from the chapter.
3. **MindTap** – Check Your Understanding: Delegation
   1. Online auto-graded activity that assesses students’ foundational knowledge of the concepts presented in this chapter. Consists of 10 multiple choice questions.
4. **MindTap** – Case Problem Analysis: Third-Party Beneficiaries
   1. Online auto-graded activity that first walks students through a fact pattern, and then asks them to answer similar questions with slight variations in the fact pattern. Consists of approximately 5 fill-in-the-blank questions.
5. **MindTap** – Brief Hypotheticals: Third-Party Beneficiaries
   1. Online auto-graded activity that presents 5 fact patterns in which students are asked to apply the concepts of the chapter, and to come up with a legal conclusion. Consists of 5 multiple choice questions.

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# Additional Resources

## Cengage Video Resources

* MindTap Quick Lesson Videos
  + Contract Performance. Duration 2:10 minutes.
  + Third-Party Rights. Duration 3:02 minutes.

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