

Retention of title provisions are appropriate wherever goods are supplied without being paid for in advance of delivery.

A well drafted retention of title clause is designed to enable the seller to recover the goods unpaid for in the event of a buyer's insolvency in accordance with the principles established in the *Romalpa* case (*Aluminium Industrie Vaassen BV v Romalpa Aluminium Ltd* [1976] 2 All E.R. 552).

If the seller has not retained title to the goods supplied, on the buyer's insolvency it will rank as an ordinary creditor behind preferential creditors and the holders of fixed and floating charges, and will probably be unable to recover the purchase price of the goods in full, if at all. However, if the contract of sale contains an effective retention of title clause, this will allow the seller to reclaim the goods supplied even though the buyer is in receivership or liquidation (but see the comments in paragraph (10) below concerning administration).

Receivers and liquidators frequently try to challenge the validity of a retention of title clause, since recovery of the goods by the seller will reduce the assets available to creditors, and so it is vital that any such clause is carefully drafted and reviewed regularly.

The law on this topic is complex and has undergone frequent development since *Romalpa*, but the following general points may be made:

- (1) The retention of title clause **must** be incorporated into the contract i.e. at or before the time the seller accepts the buyers offer to buy the goods or the buyer accepts the sellers offer to sell the goods. All too often they are printed on the reverse of invoices or delivery notes which is simply too late and will render such clauses ineffective (unless of course a dealing argument can be made out, but that is highly uncertain and should not be relied upon).
- (2) The seller must reserve legal title to the goods. If legal title passes to the buyer and only beneficial ownership remains with the seller, this will amount to the grant of a charge over the goods by the buyer which will be void for want of registration under the Companies Act or, where the buyer is not a company, for non-conformity with the statutory form for a bill of sale under the Bills of Sale Acts (see *Clough Mill Ltd v Martin* [1984] 3 All E.R. 982).
- (3) The seller should reserve the right to enter the buyer's premises in order to recover the goods, or else the seller will be guilty of trespass if it does so. If the goods are stored on a third party's premises, the seller must obtain the owner's

- (4) permission to enter the premises before it can recover the goods. The goods must be identifiable as being those supplied to the buyer by the seller, and the clause should therefore provide for the buyer to store the goods separately. A retention of title clause will frequently provide that the seller remains the owner of the goods until the buyer pays not only the purchase price for the goods supplied under the contract in question but also all other amounts owed to the seller. If the clause merely reserves title until payment of the purchase price for the goods supplied, the seller will have to show that the goods it is seeking to recover were supplied by it under unpaid invoices. For this purpose the goods will have to be readily identified.
- (5) Unless the contract otherwise provides, risk in the goods will remain in the seller while it remains the owner. A retention of title clause should in any event require the buyer to insure the goods while the seller remains the owner.
- (6) The seller can only exercise the right to recover the goods where the purchase price (or, if ownership is reserved pending payment of all amounts due, some other amount) is due and payable. However, the buyer will usually have a specified period by which to pay the price. The seller's terms of sale should therefore provide for the purchase price of the goods supplied to become payable immediately on the appointment of a receiver or liquidator or any other event of insolvency.
- (7) If the buyer uses the goods to create another product and the goods cannot be separated from the new product without serious damage, or because the old product no longer exists, the new product will belong to the buyer. If the retention of title clause provides that the seller's rights are extended to the new product, this will create a registrable charge (*Re Peachdart* [1984] Ch. 131). Accordingly, most retention of title clauses do not include such a further provision to avoid the situation outlined in paragraph (2) above arising.
- (8) A retention of title clause must for commercial reasons permit the buyer to use or resell the goods in the ordinary course of its business. At common law the seller is in theory entitled to trace the price of the goods into their proceeds of sale. However, a contractual provision giving the seller such a right was held in *Compaq Computer Ltd v Abercorn Group Ltd & Ors* [1991] B.C.C. 484 to create a registrable charge and again such provisions should be avoided.

- (9) In *Armour v Thyssen Edelstahlwerke AG* [1991] 2 A.C. 339, HL (a Scottish case but probably persuasive) it was held that a provision reserving title to the seller until payment of all debts due to him by the buyer does not amount to the creation of a right of security (what would be a charge in an English law context). Such a provision is therefore commonly included in a well drafted retention of title clause.
- (10) If the buyer is a company and enters administration under Schedule B1 to the Insolvency Act 1986 (as inserted by the Enterprise Act 2002), then for so long as the company is in administration no steps may be taken to repossess goods in the company's possession under any retention of title agreement, except with the consent of the administrator or the permission of the court (Insolvency Act 1986, Schedule B1, paragraph 43(3)).

At KBL we have considerable experience of drafting retention of title clauses and (without wishing to tempt fate) know that clauses drafted by us have stood up to challenge by administrators and liquidators on many occasions.

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