INTRODUCTION
In an economic downturn all parties to construction and supply contracts must adopt strategies to minimise exposure to the risk of insolvency of their contract counterparties. This involves considering contractual safeguards, adopting contract administration procedures designed to minimise exposure to risk and the early identification of risk minimisation measures for both principals and subcontractors.

Important for a supplier will be the use of a retention of title clause (also known as a Romalpa clause) within its supply contract. However using these clauses effectively can be difficult as the law surrounding their use has often been described as either a ‘maze or a minefield’. Below is a snapshot of the critical issues to be considered and how to best address these when using the various types of retention of title clauses available.

WHAT IS A RETENTION OF TITLE CLAUSE?
A retention of title clause is a clause in a contract for the sale of goods providing that ownership of the goods is retained by the seller until full payment is made. This is based on the concept of the separation of ownership of the goods and the actual possession of the goods.

The term ‘Romalpa’ clause is derived from the case in which retention of title clauses first received international attention, Aluminium Industry Vaasen BV v Romalpa Aluminium Ltd [1976] 1 WLR 676.

Retention of title clauses are an acceptable legal device for suppliers to ensure that, if the buyer becomes insolvent, the supplier will have priority for the goods over other secured and unsecured creditors.

WHY ARE THEY USED?
A retention of title clause stops ownership of the goods from passing with possession and will generally prevent goods becoming available for distribution among creditors when the buyer is in liquidation. It can also prevent the sale or use of goods by an administrator except in the ordinary course of business (as outlined later in this article in the section on the Corporations Act 2001 (Cth) (Corporations Act).

The meaning of ‘ordinary course of business’ was discussed by the Court in Osbourne Computer Corporations v Riddell (1995) 13 ACLC 1210. The Court held that goods supplied subject to a retention of title clause could be resold until such time as a demand for their return is made by the supplier. If a sale was made contrary to the terms of trade for the supply of the goods, the sale would not be in the ordinary course of business. Where a buyer is insolvent and a valid retention of title claim exists, the liquidator must return the goods if in their possession or risk a damages claim for conversion by the unpaid supplier.

How does a supplier retake possession of the goods?
As the goods still belong to the supplier, they are entitled to take them back. A good retention of title clause would also give the supplier a right to enter the buyer’s property and recover the goods if payment is not made.

TYPES OF RETENTION OF TITLE CLAUSES
There are three common types:
• Title of Goods clauses.
• All Monies clauses.
• Tracing & Fiduciary or Trust Relationship clauses.
Title of Goods clauses
The most basic type of retention of title clauses state that ownership does not pass until the buyer pays the full purchase price of the goods. Title of Goods clauses allow the supplier access to collect the goods supplied under an unpaid invoice. However, they do not permit suppliers to collect goods supplied under invoices that have been paid, nor do they allow suppliers to collect money that may have been received by the buyer after the on-sale of the goods.

All Monies clauses
An All Monies retention of title clause has the same effect as a Title of Goods clause but also retains title in all goods supplied, even if some invoices have been paid (see Chattis Nominees Pty Ltd v Norman Ross Homeworks Pty Ltd (1992) 28 NSWLR 338). An All Monies clause may be desirable where there is a regular trading relationship between the parties and it is difficult to associate particular invoices with particular goods. However, they can be difficult to enforce particularly where a buyer reduces his or her indebtedness to nil at anytime. This means title to all goods supplied will pass to the buyer. If the supplier attempts to collect goods supplied in the future under an unpaid invoice, he or she will need to be able to identify those particular goods. The supplier cannot collect the goods supplied earlier.

Tracing & Fiduciary or Trust Relationship clauses
These clauses have the same effect as the previous two clauses but also contain a ‘tracing clause’. This normally requires the buyer to keep the proceeds from the on-sale of the goods in a separate bank account on trust for the supplier. If the monies are not kept separately, a properly drafted clause will allow a supplier to trace the proceeds of on-sale of the goods into the bank account of the buyer.

WHAT ARE THE ISSUES?
Numerous issues need to be considered when using any of the above. This includes:
• The retention of title clause must be communicated to and accepted by the buyer for it to be enforceable.
• The goods collected usually have to be the ones that were sold under invoices that remain unpaid.
• The supplier must be able to identify the actual goods supplied under the invoice containing the retention of title clause.
• The goods must be in a collectable condition, i.e. not incorporated into other goods etc.

Incorporating retention of title clauses into contracts
Retention of title clauses can be included in documents such as the terms and conditions of supply or trade, any credit application or supply or distribution agreement. They may also be printed on the invoices and statements issued after the supply of goods. The clauses are given statutory authorisation in sale of goods legislation applicable in the State or Territory in which the sale takes place.

However, regardless of where the retention of title clause is displayed, the supplier must be able to show the clause has been incorporated into the contract. This can be done by ensuring the retention of title clause is in the written contract for the sale of the goods, signed by both parties before the goods are supplied.

Where a retention of title clause is not written in the signed contract, the seller may be able to argue that it was incorporated into the contract by implication.

A retention of title clause is a clause in a contract for the sale of goods providing that ownership of the goods is retained by the seller until full payment is made. ... [it] stops ownership of the goods from passing with possession and will generally prevent goods becoming available for distribution among creditors when the buyer is in liquidation.
 Recent amendments to the 
Corporations Act, effected 
by the Corporations 
Amendment (Insolvency) 
Act 2007 (Cth), give the 
administrator of a company 
the right to dispose of 
property that is the subject 
of a retention of title clause.

This requires an examination of 
the general course of conduct 
between the parties, including 
the use of order forms and 
invoices to identify if a retention 
of title clause included on such 
documentation forms part of the 
contract.

Identifying goods
Under a simple Title of Goods 
clause, the supplier must be able 
to identify the goods supplied as 
those under an unpaid invoice. 
The supplier of goods has the 
onus to prove that the goods on 
hand are the goods in which title 
has not passed.

This can be difficult when the 
goods are mixed with other 
similar goods, unless the goods 
contain a unique barcode or 
other method of identification. 
Generally, title will be lost if 
the supplier cannot identify the 
goods.

Goods in collectable 
condition
The supplier’s ownership of 
goods under a valid retention of 
title clause may be extinguished 
where:

• Goods are mixed or 
incorporated with other goods 
so as to lose their identity (as 
mentioned above). This will 
depend on the circumstances 
of each case and depend 
on the degree and extent of 
incorporation with other goods. 
The knowledge of the supplier 
at the time of supply is also 
important. If the supplier knew 
the goods were to be mixed with 
other goods, title will more likely 
have passed.

• Goods have been irretrievably 
fixed to the buyer’s own or 
other suppliers’ goods. The 
question then is can the goods 
be separated without destroying 
or seriously damaging the whole 
item.

• The goods are ‘fixtures’ and 
have become by law ‘land’ by 
being fixed to the land. This also 
applies to instances where a good 
is fixed to a building on the land, 
provided the degree of fixation is 
sufficient.

Sale of goods to third party
Many retention of title clauses 
allow the buyer to on–sell the 
goods before payment has been 
made. Where a retention of title 
clause is silent on this issue, the 
courts will generally imply the 
buyer is entitled to on–sell the 
goods in the ordinary course of 
business.

The ability to on–sell goods can 
cause difficulty for the supplier 
of the goods where payment has 
not been made to the supplier. 
Section 27(2) of the Sale of 
Goods Act 1896 (Qld) and similar 
legislation in other States and 
Territories, provides that where 
a third party purchases goods 
from the buyer in good faith and 
without any notice of any lien or 
right to title of the supplier, the 
third party will gain a clear title to 
the goods.

Proceeds of sale
In such cases, a Tracing & 
Fiduciary or Trust Relationship 
retention of title clause would 
be of assistance to the seller. An 
example of such a clause is:

Any proceeds of re–sale of the 
goods shall be held in trust for 
the supplier in a separate account 
until the supplier has been paid 
in full.

To maintain the effectiveness 
of this type of retention of title 
clause, the seller should ensure 
the buyer does actually keep the 
proceeds of on–sale in a separate 
account. Otherwise, it is difficult 
to trace the proceeds of on–sale.

The ability of the seller to trace 
proceeds of on–sale can be 
further improved if the retention 
of title clause establishes a
fiduciary relationship between the seller and the buyer. This relationship is more likely to be found when the contract and retention of title clause requires the buyer to keep the goods separate and keep the proceeds of on-sale of the goods in a separate account.

A recent example is the High Court of Australia’s decision in Associated Alloys Pty Ltd v ACN 001 452 106 Pty Ltd [2000] HCA 25. In this matter, a retention of title clause provided:

In the event that [the buyer] uses the goods in some manufacturing or construction process of its own or some third party, then [the buyer] shall hold such part of the proceeds of such manufacturing or construction process as relates to the goods in trust for [the seller]. Such part shall be deemed to equal in dollar terms the amount owing by [the buyer] to [the seller] at the time of receipt of such proceeds.

The High Court held that this retention of title clause was valid against the liquidator. The retention of title clause created a trust relationship between the parties whereby the proceeds from the manufactured goods are held on trust for the seller. In turn, the seller was entitled to trace the proceeds of the sale if the buyer has not paid and recover the proceeds of on-sale in priority over the rights of other creditors including secured creditors.

AMENDMENTS TO THE CORPORATIONS ACT
Recent amendments to the Corporations Act, effected by the Corporations Amendment (Insolvency) Act 2007 (Cth), give the administrator of a company the right to dispose of property that is the subject of a retention of title clause.

Normally, an administrator is prohibited from selling goods except in the ordinary course of the business, with the written consent of the owner, or with the leave of the Court (see section 442C(2) of the Corporations Act).

With the changes to the Corporations Act, an administrator can dispose of goods, even after a demand has been made by the supplier for their return, provided the administrator acts reasonably (section 442CB(2)). Such disposal could still be considered in the ordinary course of the company’s business (section 442C(8)).

Accordingly, when an administrator disposes of goods in a reasonable manner and in accordance with the exceptions in the Corporations Act, the supplier will lose its title to the goods even if the retention of title clause is enforceable.

BEST PRACTICE IN USING RETENTION OF TITLE CLAUSES
Retention of title clauses are a useful mechanism to protect suppliers of goods against buyers who do not pay the full purchase price. When including these clauses in a contract, a supplier should:

• Ensure that the retention of title clause forms part of the contract.
• Determine the type of retention of title clause required i.e. whether it is required to protect the supply of goods under a single supply arrangement or under a standing periodic supply contract.
• Include a provision in the retention of title clause that the buyer keep the goods and proceeds of sale separate so that they remain identifiable and traceable where the goods are likely to be mixed with other goods and/or on-sold.
• Consider obtaining and registering a charge over the goods and the sale proceeds as security for payment where the goods are to be incorporated into an end product where the supplier does not retain legal ownership.

• Be aware of the recent amendments to the Corporations Act, which have seemingly eroded some of the advantages of a retention of title clause.

Andrew Kelly and Richard Atkin’s article was previously published in DLA Phillips Fox’s Construction Update—April 2009. Reprinted with permission.