



Retention of Title Clauses

Drafting, Incorporation and Identification

In the last regular issue of this Newsletter we reviewed how retention of title clauses are treated by Australian courts. In the second part of our analysis of retention of title clauses we discuss the appropriate means of incorporating retention of title clauses into contracts and the practical hurdles that need to be overcome in enforcing them.

Generally speaking, for a retention of title clause to be effective, three steps must be taken, namely:

1. the clause must be properly drafted;
2. the clause must be incorporated into the contract between the parties; and
3. the goods which are to be subject to the retention of title clause must be able to be identified by the seller.

These requirements are discussed in greater detail below.

Types of Retention of Title Clauses

There are three broad categories of retention of title clauses:

1. Payment for Goods in Full

The most basic retention of title clause simply states that ownership or title in the goods sold does not pass to the buyer until the buyer has paid the purchase price for the goods in full. Such clauses are effective where single large items are sold and the goods, because of their nature, are not likely to be resold or exhausted or incorporated into another product. This would apply to large machinery or equipment, custom-made vehicles and the like;

2. All Monies Clause

If there is a regular trading relationship between the parties or multiple goods are supplied, but again the goods are not likely to be resold or exhausted or incorporated into another product then an "all monies clause" may be appropriate. Such a clause allows the seller to retain title over all goods sold until all invoices are paid. However, a difficulty arises if the buyer reduces its indebtedness to the seller to nil at any given time in the trading relationship. The seller would then only be able to rely on the retention of title clause to claim back goods sold after that point in time (and also be able to identify which goods they in fact are) and not goods sold before then; and

3. Trust or Tracing Clause

If the goods are likely to be used, on-sold to third parties or incorporated into another product then a "trust clause" or a "tracing clause" is usually more effective. These clauses require the buyer to keep the proceeds of the sale of the on-sale of the goods or the end-products in trust for the seller. Such clauses offer the best protection to a seller in the circumstances. However, there are a number of circumstances that could render such clauses ineffective.

Incorporation into Contracts

Written Contracts and Exchange of Correspondence

In order for a retention of title clause to be enforceable, the seller must be able to demonstrate that the clause has been incorporated into the contract between it and the buyer. The most obvious case is where the parties have entered into a written supply or distribution contract signed by both parties that includes the clause in its terms. However, this is not the most common situation where the commercial sale of goods is concerned. Usually commercial dealings are conducted and sales are concluded by an exchange of communications such as emails, phone calls, faxes, order forms, order confirmations, invoices, etc.

Buyers' and Sellers' Standard Terms

These days it is very common for both sellers and buyers to have standard terms and conditions of trade and for a retention of title clause to be included in both parties' standard terms. From the seller's perspective, it is important to make sure that the seller's, and not the buyer's terms form the basis of the contract between the parties. In order to do so, the seller must not only make sure that the buyer has notice of the seller's terms and conditions and that such terms and conditions form part of the contract, but also make sure that these terms and conditions are included in the last document or communication that is the "final act" or "last shot" forming the contract.

Final Act or Last Shot

This may not be as simple as it sounds. As an example, consider the following (not unusual) scenario: the buyer telephones the seller requesting a quote, the seller faxes through the quote stating that its terms and conditions apply, the buyer then emails through a "purchase order" with its own terms and conditions, the purchase order is followed by the seller's "order confirmation" which again restates its own terms and conditions and the goods are finally supplied with a "tax invoice" that also states that the seller's terms and conditions apply. In this case, the Court would need to determine which communication was in fact the "final act" or "last shot" when the parties reached mutual agreement on the terms of their contractual dealing.

Incorporation by Reference to Website etc

Another issue arising from the formation of contracts by the exchange of various documents is that sometimes the documents themselves do not include the "fine print" of the standard terms and conditions of either party but, instead, refer to them as being available on request or on a website. Care must be taken in such circumstances for the seller to make sure that the buyer is fully aware of the existence of the seller's terms and conditions, that such terms and conditions do not contain "unusual" or "onerous" terms and that the terms and conditions are in fact readily accessible. It is often preferable to include the standard terms and conditions in the written communications rather than merely to refer to them as being available elsewhere.

Identifying the Goods

Identifying Markings and Packaging

As a general rule, in order to be able to rely on a retention of title clause, the seller must be able to specifically identify the goods supplied as those that are subject to the unpaid invoice or, with an "all monies" or "trust" clause, demonstrate that the goods in the possession of the buyer were indeed supplied by the seller and not by someone else. This will be difficult if the goods do not carry serial numbers or barcodes or have distinctive packaging or if they are mixed in with other similar goods from other suppliers.

Goods Incorporated into other Items

If the goods supplied by the seller are mixed with or incorporated into other goods so as to lose their individual identity or if they have become irretrievably "fixed" to other goods or the land of the buyer then any retention of title clause may be defeated. This is particularly the case if the seller knew at the time of the supply that the goods would be used or handled in this way. The most common situation is where the goods have been sold to a third party before they are fully paid for by the buyer. In this case, the sale of goods legislation in Australia protects a third party purchaser who bought the goods from the buyer in good faith for valuable consideration and who had no notice of the retention of title by the seller. In such circumstances, the seller will not be entitled to recover the goods.

Tracing Funds Received

However, if the seller has used a trust or tracing clause, the seller would be entitled to obtain the monies received by the buyer for the goods but only if the seller can “trace” the monies received. In addition, the seller must be able to trace those funds from the hands of the third party purchaser through to the funds of the buyer or be in a legal position to assert that the monies received by the buyer were held by the buyer on trust for the seller. This is not an easy task without an appropriately drafted retention of title clause that can be demonstrated to apply in the circumstances.

Concluding Lessons

As sellers, it is important to:

- have the retention of title clause properly drafted or reviewed for the type of sale being made;
- ensure that the clause is incorporated into the contract between the parties; and
- be proactive about asserting title to the goods if the buyer is in default of payment.



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