

## RETENTION OF TITLE, LIQUIDATORS AND SECTION 234 INSOLVENCY ACT 1986

1. The credit crunch has led to an increase in the number of insolvencies. Liquidators are anxious to sell as much of the stock of the company as they consider appropriate. This can, at times, lead to disagreements over a retention of title clause. Thereafter there may be a dispute as to what, if any, defence s.234 provides to an alleged wrongful sale. A recent unreported dispute provides an opportunity to examine some of the problems which may arise.

2. A manufacturer agreed to manufacture goods for a retailer as a result of an agreement negotiated by an agent. The agent gave a confirmation of the order to the retailer on a form which made no mention of conditions nor did it make any mention of a retention of title. The manufacturer had been dealing with the retailer for a number of years and had, over the previous few years, introduced not only a statement of the retention clause on the invoice but also on the acknowledgment of order. The retailer, having taken delivery of the goods but not having sold them, went into liquidation. The liquidator took the point that the contract was made by the agent on behalf of the company and, no retention of title clause having been mentioned, the claimed retention did not apply.

3. The managing director of the retail company which had gone into liquidation had in fact signed the delivery note which itself had, in accordance with longstanding practice, contained the retention of title clause.

4. The clause read "Title to the goods on any sale shall only pass from (the manufacturer) to the buyer when the buyer has paid for the goods in full". On occasions when an acknowledgment of order was sent the same wording was used. Having rejected the validity of the retention of title clause the liquidator then sold the goods in a liquidation sale and retained the proceeds of sale.

5. The question of remedies open to the manufacturer therefore arises. It is necessary to examine three areas;

- 5.1 The Sale of Goods Act 1979
- 5.2 Retention of title
- 5.3 S. 234 Insolvency Act 1986

### Sale of Goods Act 1979

6. By s.16 of the Act "Subject to section 20A below, where there is a contract for the sale of unascertained goods no property in the goods is transferred to the buyer unless and until the goods are ascertained".

7. It has to be remembered that property and risk are not the same thing. Property is defined in s.61(1) as "...the general property in goods, and not merely a special property".

8. A contract for the sale of unascertained goods is, by s.2(5) of the Act, not a sale but an agreement to sell since the transfer of property will take place in the future. The section provides “where under a contract of sale the transfer of the property and the goods is to take place at a future time or subject to some condition later to be fulfilled the contract is called an agreement to sell”. Whilst the Act does not define “unascertained goods”, it is clear that they must include future goods which are defined by s.61(1) the Act as “goods to be manufactured or acquired by the seller after the making of the contract of sale”.

9. In the absence of a different intention, the passing of property in future goods is governed by s.18, rule 5 of the Act. The Rule provides “where there is a contract for the sale of unascertained or future goods by description, and goods of that description and in a deliverable state are unconditionally appropriated to the contract, either by the seller with the assent of the buyer or by the buyer with the assent of the seller, the property in the goods then passes to the buyer; and the assent may be express or implied, and may be given either before or after the appropriation is made.” Thus in the case postulated, of manufacture by the seller, property will, in the absence of any indication to the contrary, pass to the buyer when the goods have been manufactured and appropriated to the contract by the seller with the assent of the buyer.

10. Whilst questions may arise as to whether there has been an assent from a buyer in such circumstances there can be no difficulty with regard to s.18, rule 5(2), which provides “where in pursuance of the contract the seller delivers the goods to the buyer or to a carrier or other bailee or custodian (whether named by the buyer or not) for the purpose of transmission to a buyer and does not reserve the right of disposal he is to be taken to have unconditionally appropriated the goods to the contract”.

11. Thus, the property in ascertained goods will, in the absence of a contrary intention, pass by delivery to the buyer or his agent. In those circumstances the carrier is deemed to be the buyer’s agent for the purpose of taking delivery.

12. As is frequently emphasised under the Act property will not pass if there is a different intention.

13. In the postulated case the parties had been in a continuous relationship and that will affect the question of the passing of title. This is dealt with below under retention of title.

14. Assuming, for the moment, that this had been the first negotiation between the parties and that an agreement to sell was constituted by the agent’s action in accepting the order on behalf of the manufacturer, the point taken by the liquidator would still fail.

15. In an interesting article by J. R. Bradgate entitled “The Post-Contractual Reservation of Title” (1988) JBL 477 at 480 he makes the point that “.....where the contract is for the sale of unascertained goods, as will generally be the case in commercial sale contracts, s.19 will allow the seller to reserve title by the terms of the appropriation. Thus, even if the seller fails to incorporate his retention of title into the contract, either because it is made by telephone or because he loses the battle of forms so that the contract is governed by the buyer’s terms, he may impose a reservation by the terms of the appropriation. It should be noted that s.19 does not require that the reservation shall be brought to the attention of the buyer. The exact moment of appropriation will depend on the terms of the contract, but it seems that in most cases the seller will appropriate goods to the contract where he despatches them either by post or by carrier. Thus if the seller consigns the goods together with a delivery *“or despatch note including a reservation of title, then that reservation should be effective to prevent title passing to the buyer.”*

16. The author goes on to point out that it may be that there is a breach of contract if there were terms in the main contract which prevented the manufacturer from imposing an effective reservation of title. However, this would not stop the reservation of title being effective, it would simply be a breach of contract, see Ellershaw v Magniac (1843) 6 Exch 570n. There is a suggestion at p.484 of the article that a receiver or liquidator of the buyer would be entitled to bring a claim against the seller for damages. Whether that is so would depend upon the precise wording of the contract and the appropriate interpretation of s.12(2) of the Act. It is unlikely that most contracts would be so specific as to prevent retention at the moment of appropriation.

### Reservation of Title

17. It is well established that a reservation of title validly imposed does not create a charge upon the goods in question, see Clough Mill v Martin [1985] 1 WLR 111.

18. S.19(1) of the Act makes express provision for a decision on retention of title to be made at appropriation. It provides "Where there is a contract for the sale of specific goods or where goods are subsequently appropriated to the contract, the seller may, by the terms of the contract or appropriation reserve the right of disposal of the goods until certain conditions are fulfilled".

19. In the United States of America the terms "C.O.D." have been held to have sufficient effect for that purpose, see US v Lutz [1944] 142 M.2d 985. The validity of the point about the reservation on appropriation being valid even if there is a breach of contract seems to be accepted by the editors of Benjamin on Sale of Goods 7<sup>th</sup> edition page 274 at 5-132.

20. Where parties have been in a contractual relationship for a number of years and have used a retention of title clause on correspondence the omission of such a clause in one contractual negotiation is hardly likely to make any difference. The court will have regard to the history of the transactions between the parties.

21. The court is perfectly entitled to imply a retention of title until payment and in modern circumstances the courts seem ready to assume that a party would wish to retain title until payment had been made. Thus in the case of Michael Gerson (Leasing) Limited v Wilkinson [2001] QB 514 at 529E-531H the court was very ready to infer that as a matter of commonsense the party involved would not have intended property to pass prior to payment. See also 539C and 540D.

22. The question still arises as to what happens where the liquidator sells goods which the court ultimately finds were not the property of the company in liquidation and had been sold contrary to the wish of the manufacturer who had validly retained title.

23. It is quite clear, as a matter of general principle, that a liquidator selling goods which are not his own or those of the company in liquidation commits the tort of conversion and is prima facie liable in damages. Perhaps because it is clear that such a claim arises there appears to be no reported judgment on the matter. But one potentially relevant decision by the Court of Appeal is Stewart v Engel [2000] LI Rep. P.N. 234 where, although the actual claim brought in contract was dismissed, it was made clear that a claim could be brought in conversion. However, that case does not deal with the main purpose of this article, namely the impact of s.234 of the Insolvency Act 1986.

**s.234 Insolvency Act 1986**

234.(1) This section applies in the case of a company where -

- (a) the company enters administration,
- (b) an administrative receiver is appointed, or
- (c) the company goes into liquidation, or
- (d) a provisional liquidator is appointed;

and “the office-holder” means the administrator, the administrative receiver, the liquidator or the provisional liquidator, as the case may be.

(2) Where any person has in his possession or control any property, books, papers or records to which the company appears to be entitled, the court may require that person forthwith (or within such period as the court may direct) to pay, deliver, convey, surrender or transfer the property, books, papers or records to the office-holder.

(3) Where the office-holder -

- (a) seizes or disposes of any property which is not property of the company, and
- (b) at the time of seizure or disposal believes, and has reasonable grounds for believing, that he is entitled (whether in pursuance of an order of the court or otherwise) to seize or dispose of that property,

the next subsection has effect.

(4) In that case the office-holder -

- (a) is not liable to any person in respect of any loss or damage resulting from the seizure or disposal except in so far as that loss or damage is caused by the office-holder’s own negligence, and
- (b) has a lien on the property, or the proceeds of its sale, for such expenses as were incurred in connection with the seizure or disposal.

24. The section replaces s.551 of the Companies Act 1985 which applied only to a winding up by the court. The protection of s.234 is therefore now provided to every kind of winding up and all other insolvency procedures except a voluntary arrangement.

25. The special protection and s.234(3) and (4) only applies to tangible property and not to choses in action, see Welsh Development Agency v Export Finance Co Limited [1992] BCC 270 at 287.

26. It is suggested that a court will be slow to accept a defence under s.234(3) where the reasonable ground for belief is that the clause did not apply. In order to qualify as a liquidator a candidate is examined on a syllabus which provides that:

“candidates should be able to evaluate and resolve claims in special categories including:

- Retention of title
- Lien....”

27. Plainly there can be difficult problems on occasion but rejection of the retention of title claim in the postulated case cannot be a reasonable decision.

28. Even a paper published by “Business Credit Management UK” deals quite properly with the point and there is no excuse for a liquidator. The BCM paper on Retention of Title makes the point quite clearly at paragraph 5 in that it says:

“If the parties are involved in a ‘one-off’ order, and the terms are conveyed only on the back of the invoice, they will apparently not have been communicated in time as the invoice is usually rendered after the bargain is struck - the bargain having been made earlier when the buyer placed the order and the supplier agreed to supply. However, if the buyer receives a number of such invoices in respect of a succession of separate orders, it could be argued that, as regards the later deliveries, the terms had already been communicated before the bargains were made. Even if the buyer remained silent about the terms, it might be contended that, by continuing to place orders with the supplier, he had accepted his terms.”

29. A more interesting question is what happens if the court finds that there are reasonable grounds for belief and then has to consider the liability of the office holder under s.234(4)(a) which expressly provides that he “is not liable to any person in respect of any loss or damage resulting from the seizure or disposal except insofar as that loss or damage is caused by the office holder’s own negligence.....”

30. At that stage, if he has reasonable grounds for believing that the clause is not valid, then it is likely that he would also be held not to have been negligent for the purposes of s.234(4)(a).

31. There is no authority on what that exemption means. Some books simply recite the section and leave the reader to make up his own mind. In Clerk & Lindsell on Torts, 19<sup>th</sup> edition at paragraph 17-76, having referred to the section, the editor refers to it as making the liquidator/receiver “not liable in damages”. This is not what the section actually says but he adds a footnote (37) stating “A significant limitation. If the liquidator etc sells the property, presumably his liability to account for the sale proceeds – whether by way of an action for money had and received or a tracing action – remains. Such a liability is not a liability in damages.”

32. However the notes in the “Annotated Guide to the Insolvency Legislation”, (10th Edition) edited by Professor Sealy, at p. 255 re s. 234(3),(4) make it quite clear that in his view the immunity “.....does not appear to extend to liability for the wrongful interference per se, and so the owner would not be prevented from suing to establish his right to the return of the property itself or the proceeds of its sale”.

33. Where the manufacturer of goods is supplying them to a retailer for onward sale at a profit, sometimes with a margin of 100%, that would involve the whole of the price received by the liquidator being prima facie due rather than the contractual sum. No doubt most manufacturers would settle for the contractual sum in order to avoid litigation. There can in my view be no total defence to a claim on the part of the true owner. To do so would be a statutory deprivation of property without a remedy. Even if there were any doubt about that construction, that doubt should disappear after the passing of the Human Rights Act 1998.

### **Human Rights Act 1998**

34. By s.6 of the Act it is unlawful for a public authority to act in a way which is incompatible with a Convention right. Therefore, when interpreting a statute the court must strive to interpret it in a way which is consistent with the rights given under the Convention. Only if it is impossible to do so, by reason of the fact that primary legislation is clearly

incompatible with the Convention, can the court ignore a right given by the Convention, see s.6(2)(a). The Act has as already been used by a judge at first instance to depart from a previous decision of the Court of Appeal concerning the construction of a defamation statute, see Culnane v Morris and Naidu [2006] 1 WLR 2880

35. By Article 1 of the First Protocol of the Convention:

“Every natural or legal person is entitled to the peaceful enjoyment of his possessions. No one shall be deprived of his possessions except in the public interest and subject to the conditions provided for by law and by the general principles of international law.

The preceding provisions shall not, however, in any way impair the right of a State to enforce such laws as it deems necessary to control the use of property in accordance with the general interest or to secure the payment of taxes or other contributions or penalties.”

36. Whilst the law on squatters’ title was upheld by the European Court of Human Rights, see Pye (Oxford Limited) v United Kingdom [2008] 46 EHRR 45, such an approach would not be applicable here. The national interest in the clarity of ownership of land led a split Grand Chamber to decide that it was within the government’s power to determine the basis on which title to land could be lost after years of squatting. For a lucid discussion of the right to property see Human Rights Law and Practice by Lord Lester QC, Lord David Pannick QC and Javan Herberg Third Edition 2009 pp 643 – 667.

37. In the postulated case there is no comparable national interest. The court would have to look at the section with a view to avoiding the extinguishment of the manufacturer’s title without leaving him any remedy.

38. Although there are many statutory provisions dealing with the loss of title to a bona fide purchaser for value e.g. s 27 Hire Purchase Act 1964 and ss.24 and 25 of the Sale of Goods Act 1979 they do not leave the original owner without a remedy against someone who can be shown to have converted the goods. These provisions are to be distinguished from the statutory provisions which prevent enforcement of a regulated agreement which has failed to state a prescribed term; see Wilson v First County Trust [2004] 1AC 816.

39. If the interpretation favoured by Professor Sealy at paragraph 31 above permits an action for interference with goods and is to be regarded as the correct construction, the “loss or damage” within s. 234 are in effect interpreted as if they were preceded by the word “consequential”. This would leave the manufacturer with both a restitutionary claim and a claim for conversion of the goods against even a liquidator who can bring himself within s.234. In the postulated example title would have passed by reason of the sale being by the purchaser in possession. (s 25(1))

40. On the tentative view of the editor of Clerk and Lindsell set out at paragraph 30 above the remedy against a non negligent liquidator would be limited to a restitutionary remedy in relation to the proceeds of sale.

41. In my view an action for conversion where the title has passed is an action for damages. No claim can be made for the return of the goods. It would be different if the action were for the return of the goods under s3(2) of The Torts (Interference with Goods) Act 1977 in a case where no title had passed. Therefore despite his eminence as Professor Emeritus of Corporate Law at the University of Cambridge I regard his interpretation of s.

234 as somewhat generous to those seeking to sue. It seems to me that if the court is able to award a manufacturer in the postulated case such sum as the liquidator received it would not strive to reach such a broad construction of the section against a non negligent liquidator.

## REMEDIES

42. If the remedy is in conversion the prima facie claim is for the value of the goods. However, the value of the goods should not be taken as the invoice price from the manufacturer. The value is the open market value at the date of the conversion. The tortfeasor, i.e. the liquidator in this instance, should not profit from the fact that he ignored the request of the owner for the goods to be returned. The usual liquidation sale offers a discount on the recommended retail price. Therefore it is unlikely that the liquidator would be ordered to pay more than the price obtained if reasonable efforts were made to obtain as good a price as the circumstances permitted.

43. The question then arises as to what, if any, deductions a liquidator could seek to make in respect of the costs of the sale. The liquidator who is not negligent, if liable to an action in conversion on Professor Sealy's view, has the protection of s. 234(4) which gives him "...a lien...on the proceeds of sale, for such expenses as were incurred in connection with the seizure or disposal."

44. If the circumstances give rise to a claim in tort the tortfeasor cannot normally expect a sympathetic approach from the court cf Banco de Portugal v Waterlow [1932] AC 452. In some cases losses beyond the market value may be recoverable, subject always to principles of remoteness, see Kuwait Airways Corp v Iraq Airways [2002] 2 AC 883. However, there is some old authority allowing the expense of sale, see Clark v Nicholson (1835) 6 C & P 712 along with the many cases when the cost of mining the converted coal was allowable. These authorities do not seem to be affected by the limitations of s.6 of the 1977 Act re the cost of improvements.

45. On a restitutionary claim the non negligent liquidator may be able to claim that the sale was a bona fide mistake as to title and a change of position on his part. Thus the expenses incurred by him should be deducted from the proceeds of sale. The value of the restitutionary claim would be limited to the net benefit to the liquidator arising from the sale. This would accord with the reasoning in Lipkin Gorman v Karpnale Ltd [1991] 2 AC 548 which recognised the defence of change of position, a recognition which was "long overdue" per Lord Goff ibid at 580B.

46. It should be noted that "The defence of change of position is akin to the defence of bona fide purchase; but we cannot simply say that bona fide purchase is a species of change of position" per Lord Goff ibid at 580H.

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