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Secured Transactions in Moveable Assets Act, Company Charges and Funding Micro, Small and Medium Enterprises under Nigerian Law

Gregory Esangbedo*
XML Ltd
esangbedog1969@gmail.com

Abstract

The clamour for the reform of Nigeria's secured transactions' law has culminated in the recent enactment of the Secured Transactions in Movable Assets Act to stimulate responsible lending to micro, small and medium enterprises (MSMEs), among other objectives. This article evaluates the impact of the act, in particular how it addresses the problems associated with the common law system that made it difficult for small business entities to access loans and other credit facilities. The article further examines the implications of the autonomy the act gives to companies to continue to grant charges pursuant to the old system. The author contends that, despite the act's obvious similarity to reformed systems of personal property security laws (reform now being championed by the UN Commission on International Trade Law), expectations of it meeting its key objective of stimulating credit to MSMEs may be misconceived.

Keywords
Nigeria, reform, secured transactions, charges, MSMEs, funding

INTRODUCTION

Despite some dissent, credit and secured lending remain pivotal business tools by which business organizations realize their objectives globally.[1] Like several other economies, the Nigerian economy relies greatly on credit in meeting both its public sector commitments[2] and private sector needs, particularly those of its micro, small and medium business enterprises (MSMEs), the

* MPhil (University of Oxford). Commercial manager, XML Ltd, London.

1 For a discussion of the importance of credit, secured lending and leading dissents to secured lending, see G McCormack *Secured Credit Under English and American Law* (2004, Cambridge University Press), chap 1.

2 For example, as at 30 June 2019, Nigeria's total external debt stock exceeded US$27 billion. See Debt Management Office "Nigeria's external debt stock", available at: <https://www.dmo.gov.ng/debt-profile/external-debts/external-debt-stock/2944-nigeria-s-external-debt-stock-as-at-june-30-2019/file> (last assessed 10 December 2019).

dominant forms of business entities whose sustenance greatly depends on their access to credit.[3]

However, the importance of credit and secured lending appears matched by the realization that the common law system of secured transactions, adopted by Nigeria[4] and several other countries, may have become inadequate, especially in leveraging MSMEs' access to credit facilities, prompting calls for reform to make credit more readily available to business entities.[5] Some of the common law shortcomings that directly impact MSMEs' access to funding include creditors' dissatisfaction with the common law priorities' scheme, which offers no synchronized or predictive basis for determining priorities between competing interests. This appears exacerbated by the fact that competing security interests also often arise in unco-ordinated ways, potentially rendering each creditor's position unpredictable in comparison to others.[6] Further, priority was often not determined by the order of the publication of security interests, as superior interests that preserve absolute ownership, such as those founded on Romalpa clauses, are not subject to special registration requirements.[7] With reference to specific types of security interests, floating charges (which are particularly beneficial to MSMEs because of the chargor's continued right to deal in the assets during the subsistence of the secured transaction)[8] are subordinated in terms of priority to fixed charges, save where the floating charge contains a negative pledge permitting the

3 The difficulty faced by MSMEs, especially those in developing countries, is well documented. See for example L Gullifer and I Tirado "Financing micro-businesses and the UNCITRAL Model Law on Secured Transactions" (2017) *Oxford Legal Studies Research Papers* 1.

4 Nigeria adopted English law following the end of British colonial rule in Nigeria in 1960. By virtue of the Interpretation Act cap 89, 1958, sec 45, the English common law and doctrines of equity, together with statutes that were in force in England as at 1 January 1900 were adopted in Nigeria, subject to local legislation. This remains the case, with English statutes enacted before the limiting date considered federal Nigerian statutes. English cases are of persuasive authority in Nigerian courts, especially on novel issues. For a detailed discussion of the relationship between both systems, see AEW Park *Sources of Nigerian Law* (1st ed, 1963, Sweet and Maxwell), chap 1.

5 Some examples of recent reformative enactments are Australia's Personal Property Securities Act 2009 and New Zealand's Personal Property Securities Act 1999 No 126. These follow several provincial Canadian statutes enacted in the 1980s and 1990s (such as Saskatchewan's Personal Property Security Act chap P-6.2, Statutes of Saskatchewan 1993). However, the pioneering enactment is art 9 (secured transactions) of the Uniform Commercial Code (UCC) first enacted in the 1950s. See Revised UCC (2010).

6 Under the common law, many such interests were viewed as quasi-security interests because, as they were initially not designed as secured transactions, their form was often seen to override their functionality. By reference to the overall common law security interests, some authors have described the Australian replica of the common law as "a patchwork system of statutory initiatives supplemented by common law and equitable principles". See A Duggan and D Brown *Australian Personal Property Securities Law* (2nd ed, 2016, LexisNexis Butterworths) at 18.

7 See McCormack *Secured Credit*, above at note 1 at 60.

8 This further obviates the need to set aside any specific assets as security for loans.

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creation of a security interest superior to the charge.[9] While this subordinated priority status could discourage creditors from accepting floating charges as security, the use of protective negative pledges impairs the debtor's ability to raise further loans, an ideal fallback for many MSMEs intent on optimizing their continued right to deal.

While these difficulties encourage concerned creditors to seek ingenious protective measures,[10] the situation nevertheless exposes MSMEs to the painful reality of navigating through such measures in order to access credit. Added to this problem is the fact that the informal nature of MSMEs often triggers harsh contractual terms from creditors;[11] their sparse resources limit their collateral options to their tools of trade, trade inventory or receivables from business activities, items that offer doubtful efficacy as security for loans.[12]

In apparent conformity with the objective of the UN Commission on International Trade Law (UNCITRAL)[13] of assisting states to develop modern secured transactions laws to engender credit to smaller businesses, the Nigerian legislature enacted the Secured Transactions in Movable Assets Act of 2017 (STMA),[14] which apparently adopts the unitary security system. With proof that reform can impact secured transactions law,[15] the enactment of the STMA is prima facie commendable as it could be the catalyst through which MSMEs' access to funding is improved.

9 See Companies and Allied Matters Act, cap C20, Laws of the Federation of Nigeria (LFN) 2004, sec 179.

10 It is worth emphasizing that negative pledges and even Romalpa clauses are some of the ingenious measures developed by creditors to protect their interests in secured transactions and that have now become aspects of the common law. Other measures include the insistence on the provision of realty as security for loans, which has become the rule of thumb among Nigerian commercial banks, and charging exorbitant interest rates, some payable upfront in order to reduce future exposure.

11 See below for a detailed discussion of the peculiarities and challenges of these entities.

12 See for example R Kohn and D Morse "UNCITRAL: The UNCITRAL Model Law on Secured Transactions" (2016) 72/9 *The Secured Lender* 48.

13 UNCITRAL's involvement in driving the reform of personal property security laws has been immense, as evidenced by its twin reform guides for states, which now constitute the Magna Carta of global reform activities. See *UNCITRAL Legislative Guide on Secured Transactions* (2010, UN) and UNCITRAL Model Law on Secured Transactions (2016, UN) (UNCITRAL Model Law).

14 The STMA, which became effective on 31 May 2017, was preceded by the Central Bank of Nigeria (CBN) Registration of Security Interests in Movable Property by Banks and Other Financial Institutions in Nigeria Regulation 1 of 2015, issued and gazetted in February 2015 but notified to banks on 29 June 2016. This regulation has similar provisions to the STMA, save for the critical difference that, while the regulation completely excludes company charges, the act gives parties the prerogative to use charges.

15 See for example V Vig "Access to collateral and corporate debt structure: Evidence from a natural experiment" (2013) 68 *Journal of Finance* 881, which found that reform to secured transactions law in India, which facilitated enforcement by creditors, reduced the volume of secured lending.

However, critical analysis reveals that the STMA may not fully realise the objectives for which it was enacted. Section 1 of the act defines its objectives to include "the stimulation of responsible lending to micro, small and medium enterprises".[16] Although section 2(1) defines the scope to include security interests in movable assets created by an agreement that secures payment or the performance of an obligation,[17] section 2(3) provides that "nothing in this Act shall prevent the creation of a security interest in the form of charges by companies registered under the Companies and Allied Matters Act". While there may be no statutory definition or judicial interpretation of the phrase "nothing in this Act shall prevent", it is hardly arguable that it achieves the opposite effect to the phrase "notwithstanding any provision of", which has been judicially interpreted to exclude any impinging or impeding effect of any other provision of a statute or other legislation to enable a section to have full effect.[18] Accordingly, the phrase "nothing in this Act shall prevent" would exclude the application of an enactment to stop the provisions of an alternative enactment having full effect. Against this backdrop, it is contended that companies can create charges in conformity with and subject to the Companies and Allied Matters Act (CAMA),[19] without the STMA impinging or impeding them. Consequently, company charges remain legitimate forms of security devices available to companies pursuant to CAMA without being impinged by the STMA.

This development is worrisome, because the continued legitimization of this form of security device outside the STMA taints the objective of harmonization, an omnipresent feature of similar reforms.[20] It is nonetheless suggested that, despite section 2(3), the STMA's acceptance as a reformative enactment would depend on whether it achieves its key objectives of stimulating funding to MSMEs and following UNCITRAL's recommendations, enabling them to use the value inherent in their receivables as security for loans.

In view of the latter objective, floating charges (which coincidentally developed under similar circumstances, to assist budding business enterprises raise funds during the industrial revolution)[21] could ideally fill this void for the reasons highlighted above. Further, with their validity independent of the

16 The STMA's other objectives include the enhancement of financial inclusion in Nigeria, the facilitation of access to credit secured with movable assets and the establishment of a collateral registry. See sec 1 for a comprehensive list of the STMA's objectives.

17 The breadth of transactions constituting security interests is further emphasized by the STMA, sec 63(1), which defines a security interest as "a property right in collateral that is created by agreement and secures the payment or other performance of an obligation, regardless of whether the parties have denominated it as a security interest".

18 See for example *Saraki v FRN* [2016] 3 NWLR (pt 1500) 531.

19 Cap C 20 LFN 2004.

20 For a discussion of the key elements of a typical personal property security act reform, see H Beale "An outline of a typical PPSA scheme" in L Gullifer and O Akseli (eds) *Secured Transactions Law Reform: Principles, Policies and Practice* (2016, Hart Publishing) 7.

21 See R Pennington "The genesis of the floating charge" (1960) 23 *Modern Law Review* 630.

transfer of ownership or possession of the asset, they raise borrowers' confidence in the preservation of their ownership against losses occasioned by, for example, sale of the asset as a result of repayment default.[22] The potential exclusion of such charges from the scope of the STMA by section 2(3) therefore appears disturbing. This article therefore examines the impact of the STMA, particularly its section 2(3), on the Nigerian law of secured transactions, bearing in mind the act's cardinal objective of stimulating credit to MSMEs.

THE LEGAL FRAMEWORK FOR CREDIT TRANSACTIONS IN NIGERIA

It is suggested that a pinpoint evaluation of the impact on MSMEs of the laws affecting secured transactions should be preceded by an assessment of their peculiarities and challenges in their quest for funding under Nigerian law. In evaluating the legal framework for credit, this article highlights those elements that discourage MSMEs from seeking credit, and creditors from extending the same, bearing in mind that an aversion to credit transactions by both parties is hardly the stimulant required for developing a healthy credit system and engendering economic growth.

The peculiarities and challenges of MSMEs in Nigeria

The National Policy of the Small and Medium Scale Enterprises Development Agency of Nigeria (SMEDAN)[23] on MSMEs[24] is used as the basis for evaluating the peculiarities and challenges of MSMEs in Nigeria. The policy, which came into effect in 2015 for a period of ten years, defines neither MSMEs nor micro entities, but categorizes entities based on two factors: the number of employees and the total assets owned (excluding land and buildings).[25]

Based on these factors, the policy classifies entities employing between one and nine persons and with less than NGN five million[26] in assets as micro enterprises; those with ten to 49 employees, with assets of between NGN five

22 For a detailed discussion of floating charges, see L Gullifer (ed) *Goode and Gullifer on Legal Problems of Credit and Security* (6th ed, 2017, Sweet & Maxwell), chap 4.

23 SMEDAN is a statutory agency established by the SMEDAN (Establishment) Act 2003 to initiate and articulate ideas for small and medium scale industries policy thrusts and to oversee, co-ordinate and monitor their development. See SMEDAN (Establishment) Act, sec 8 for its detailed responsibilities in respect of MSMEs.

24 SMEDAN "Federal Republic of Nigeria: National policy on micro, small and medium enterprises" (2015), available at: <https://smedan.gov.ng/images/PDF/MSME-National-Policy.pdf> (last accessed 10 December 2019).

25 The policy states however that, where conflicts arise between the employment and assets criteria (for example, where an enterprise has assets worth NGN 12 million but employs only seven people), the employment criterion takes precedence and the enterprise will be classified as a micro enterprise. See id, para 1.3.

26 NGN 10 million amounts to approximately GBP 21,000 at the prevailing exchange rate as at December 2019. See currency converter, available at: <https://www1.oanda.com/currency/converter/> (last assessed 3 December 2019).

and NGN 50 million are small enterprises, and those with 50 to 199 employees and an asset base of between NGN 50 and NGN 500 million are categorized as medium enterprises.[27] The policy estimates that 37 million micro enterprises exist in Nigeria, providing employment for approximately 58 million people (about a third of the entire Nigerian population), providing services across virtually every spectrum of retail trade, artisanship, sale of household goods, manufacturing, agriculture, hospitality, and transport and storage businesses.[28]

In terms of modus operandi, the policy provides that the typical micro enterprise is operated by a semi-literate or illiterate sole proprietor assisted mainly by unpaid family members and the occasional paid employee or apprentice with low output value and an even lower dependence on technology.[29] With their poor structures, their funding is typically derived from personal savings and friendly loans from family members and traditional mutual funds, with bank loans rarely sought and even less rarely obtained.[30]

There are just under 70,000 small enterprises, which cover about the same spectrum of activities as micro enterprises, employing fewer than two million people.[31] While most small enterprises are also sole proprietorships, an increasing number are incorporated enterprises. On the other hand, there are about 5,000 medium enterprises employing fewer than one million people. Most medium enterprises are incorporated companies, well structured and with good access to bank loans.[32] Based on SMEDAN's assessments, small and medium enterprises employ approximately three million people, a grossly insignificant percentage of a population exceeding 170 million people.

SMEDAN classifies the challenges facing MSMEs into two broad groups: internal and external.[33] While internal challenges are usually within their control and include concerns around aversion to joint ownership, financial mismanagement, family ties, lack of basic business capacity, poor record keeping and lack of recruitment of qualified personnel, external challenges are often outside their control and include primarily financial and infrastructural challenges.[34]

Since finance is widely acknowledged as the main challenge facing these entities and also constitutes the focus of the STMA, it is important to highlight the depth of this problem from a practical perspective. Considering the low value of micro businesses (approximately GBP 20,000 excluding real estate assets that they often don't own), it is improbable that these entities can

27 SMEDAN "Federal Republic of Nigeria", above at note 24, para 1.3.
28 Id, para 1.4.1.
29 Ibid.
30 Ibid.
31 Ibid.
32 Ibid.
33 Id, para 1.5.
34 Ibid.

provide often-pricey realty as security for loans. There are also serious limits to how many movable assets such a business can afford, bearing in mind the high cost of equipment in sectors with significant numbers of MSMEs, such as agriculture.[35] Bearing in mind other operational expenses, taxes and the huge infrastructural outlay involved in running businesses in Nigeria,[36] the probability of MSMEs providing acceptable collateral for loans is remote.[37]

While this clearly justifies classifying finance as an external challenge, the importance of SMEDAN, the body charged with supervising MSMEs, making this classification lies in the fact that the strategies it would adopt to combat the identified problems will probably be influenced by how it perceives the problem. Thus, an incorrect definition of the challenge will probably result in poorly defined objectives, which in turn can only result in poor strategies. Thus, while finance is consistently seen as a militating factor to MSME growth, a greater problem is often that MSMEs are unable to meet the conditions set by financial institutions to access loans, not that funds are unavailable. It is thus inappropriate to define the problem as a lack of finance, as that could result in the proliferation of schemes that are ultimately unsuccessful.[38] While conceding that the government's role in enhancing this sector is indubitable, it is suggested that MSMEs have an equally significant impetus to "kick-start" their eligibility for loans and ensure that past loans are fully repaid.[39] This issue falls outside the scope of this article and accordingly is not discussed further.

In summary, most MSMEs in Nigeria are unstructured micro enterprises and are therefore small and impecunious, with their survival tied to their access to loans. However, their desperation to secure loans often places

35 For example, the cost of purchasing a single piece of agricultural equipment, such as a tractor, usually exceeds GBP 20,000 and, even when instalment payments are permitted, the instalments may exceed what these impecunious entities can comfortably afford from their meagre earnings.

36 For a discussion of Nigeria's infrastructural challenges, see V Foster and N Pushak "Nigeria's infrastructure: A continental perspective" (an Africa infrastructure country diagnostic report by the International Bank for Reconstruction and Development, February 2011), available at: <https://ppiaf.org/documents/3154/download> (last assessed 3 December 2019).

37 The provision of security is just one of the conditions set by institutional creditors for obtaining loans. See for example the First Bank of Nigeria's conditions for term loans and advances to SMEs, available at: <https://www.firstbanknigeria.com/business-banking/loans/sme-product-financing/import-finance/> (last assessed 3 December 2019).

38 For a list of more than 15 government schemes since the 1960s, see SMEDAN "Federal Republic of Nigeria", above at note 24 at 20.

39 A recent review of repayment by SMEs on loans disbursed under the supervised credit scheme of the Nigeria Agricultural Cooperative and Rural Development Bank in Kaduna State found that only about a quarter of a total sum of NGN 88.7 million disbursed was repaid by borrowers. See generally AO Sambo et al "A critical evaluation of the legal framework for SMEs' loan redemption in Nigeria" (2014) 22 *International Islamic University of Malaysia Law Journal* 56.

them in a weak negotiating position in credit transactions, forcing them to accept the oppressive terms that are sometimes imposed by creditors. It is however noteworthy that the depth of their impecuniousness and lack of structure may not even be remediable by a perfect law of secured transactions.

Business platforms

Since the seminal decision of the English House of Lords in *Salomon v Salomon*,[40] which established the separate legal personality of a registered company as opposed to other business entities, the incorporated company has for many reasons provided the greatest leverage to business financing.[41] First, incorporation confers perpetual succession on the entity, which assures investors and creditors that the demise of an alter ego does not necessarily result in the cessation of the business. Further, through the concept of capitalization, an investor's share, benefits and liabilities in the business relative to other investors are easily ascertainable.[42] The complex procedure for winding up a company further enhances a company's access to loans, as the durability of the debtor's existence potentially influences credit decisions, since creditors are generally less comfortable extending credit to ephemeral entities.[43]

Section 37 of CAMA recognizes the concept of limited liability and separate personality. The effect is that companies, in contrast to other forms of business entities, are empowered to carry out several activities in their corporate persona as opposed to the personae of individual members.[44]

Nevertheless, despite the obvious benefits of incorporation, sole proprietorships and registered business names continue to outnumber companies in Nigeria,[45] perhaps because of the misconception that sole proprietorships are informal, unregulated entities while registered business names are easier and cheaper to set up than companies.[46]

40 [1897] AC 22.

41 For a detailed discussion of the elements of the incorporated company and the value they hold in engendering the economic exigencies for the modern business enterprise, see R Kraakman at al *The Anatomy of Corporate Law* (3rd ed, 2017, Oxford University Press), chap 1.

42 Capitalization also plays a critical role in engendering venture capital in the first place because, without it, the investment cannot easily be ascertained. See for example the Banks and Other Financial Institutions Act, cap B3, LFN 2004, sec 21.

43 See for example CAMA, sec 578 and the entire part XV, consisting of 130 sections dedicated to the winding-up of companies.

44 See id, secs 38–39, which spell out a company' specific powers and the limits on the exercise of such powers. See also *FCDA v Unique Future Leaders International Ltd* [2014] 17 NWLR (pt 1436) 217.

45 See for example "CAC registered 91,609 business names in one year" (6 September 2017) *The Guardian Newspaper*, showing the number of entities registered between July 2016 and June 2017, available at: <https://guardian.ng/business-services/cac-registered-91609-business-names-in-one-year/> (last assessed 3 December 2019).

46 It is however necessary to correct the inaccurate general perception that companies are more complex to create. For example, the current charges for registering a business

Although Nigerian law does not generally oblige promoters to utilize any specific platform for carrying on business,[47] where a promoter decides against incorporating a company, there arises an obligation to register the name of the entity in accordance with section 573(1) of CAMA. This section requires every individual, firm or corporation carrying on business under a business name to be registered if the name consists of more than the true forenames or surnames in the case of individuals and firms, and the name of the incorporated company when it subsequently becomes part of a business name registration, such as through a joint venture. Accordingly, the sole eligibility criterion for registration as a business name is the name selected by the promoters, irrespective of the business's size or activities.[48]

With the prevalent notion in Nigeria, also expressed by SMEDAN,[49] that MSMEs are mainly informal business entities, a gap exists between the prevalent notion and reality. This raises the likelihood that the legal liability of micro and small entities to formalize their business through any of the two platforms is indeed higher than perceived, making it imperative to consider the relative benefits of utilizing either of the two formal platforms as a basis for evaluating their financing needs.

Following the above and the categorizations discussed earlier, since most MSMEs are informal micro entities, they are unable to secure loans by virtue of having a corporate persona. This has various disadvantages. In a non-corporate capacity, they cannot grant floating charges as security for loans, because only companies can create such charges under Nigerian law.[50] Consequently, in addition to losing the benefits of such devices, only assets belonging to promoters of these entities can readily be available as security for loans, a situation bound to discourage risk-averse promoters of these entities from seeking credit facilities. Further, as the risk of lending to individuals far outweighs that of lending to companies, MSMEs typically face onerous terms, such as higher interest rates, which creditors impose as a buffer against the risks of lending to individuals.

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name are the same as those paid for incorporating small companies. See summary of Corporate Affairs Commission fees, available at: <http://new.cac.gov.ng/home/summary-of-fees-and-forms/> (last assessed 3 December 2019). Furthermore, the documentation requirement and incorporation process are considerably less onerous for smaller companies.

47 Under CAMA, sec 18, any two or more persons may incorporate a company. This is however subject to a few exceptions, including the obligation in CAMA, sec 19 that obliges any group exceeding 19 members to be incorporated as a company.

48 Failure to register attracts punitive measures under CAMA. See CAMA, sec 584. There is however no means of tracking compliance with sec 573 and, considering the government's desire to boost the growth of small companies, sanctions against them are invariably never pursued.

49 This can be gleaned from SMEDAN "Federal Republic of Nigeria", above at note 24, para 3.2.1.

50 See CAMA, secs 166 and 178.

Secured financing options

Since the STMA only applies to movable property[51] and following the assertion made above that most MSMEs in Nigeria are unable to provide realty as security, this evaluation is limited to secured transactions in moveable assets.[52] Consequently, the consensual securities examined here are the pledge, the mortgage of personal property (also known as a bill of sale), charges and vendor credit.[53]

A pledge is a common law security interest created by delivery of the possession of tangible property to the pledgee as security for the payment of a debt or performance of another obligation.[54] A pledge confers on a pledgee a number of rights, including the rights to possession,[55] to sell the property on default[56] and to sub-pledge without destroying the pledge.[57] However they do not transfer title or ownership of the pledged property to the pledgee during the subsistence of the pledge.[58] In view of the challenges involved in pledging physical assets, especially when large commercial loans are involved, pledges are currently more often used in two main ways in the commercial context: where documents of title are pledged in trade finance to give security over goods to which they relate and where negotiable instruments are pledged as security for deposits.[59]

It must however be highlighted that, in view of the very limited scale of transactions carried out by micro enterprises, they rarely use such documents as security. Nigerian creditors still however often resort to constructive possession of the pledgor's moveable assets, such as where access to farm produce and farming equipment in barns is controlled by the pledgee, thus ensuring that pledges remain a veritable type of financing device for small business entities.

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51 STMA, sec 2(1)(a).

52 It must be highlighted that MSMEs may also seek alternative forms of financing, such as venture capital and unsecured loans. However, for many reasons, these options present even greater difficulties than secured financing; for example venture capital as a means of finance is unsuitable for entities without capitalization and the desire of venture capitalists to participate in the business usually discourages small business promoters. On the other hand, the highly regulated nature of the Nigerian financial sector makes it difficult for these entities to meet the onerous conditions set by financial institutions for unsecured loans.

53 Although resembling security devices, liens are merely passive legal rights to retain another's property until certain demands have been satisfied. See W Clarke (ed) *Fisher and Lightwood's Law of Mortgages* (2014, LexisNexis) at 6.

54 See *Ihunwo v Ihunwo and Others* [2013] 8 NWLR (pt 1357) 550.

55 H Beale et al *The Law of Security and Title-Based Financing* (2nd ed, 2012, Oxford University Press) at 563.

56 Ibid.

57 See *Donald v Suckling* (1866) LR 1 QB 585.

58 E McKendrick *Goode on Commercial Law* (5th ed, 2016, Penguin Books) at 687.

59 J Naughton "Commentary on commercial pledges" in M Gillooly *Securities over Personalty* (1994, The Federation Press) 154.

It is noteworthy that the requirement for the transfer of possession of the asset by the pledgor to the pledgee immobilizes the physical use to which the pledgor can put such assets while the secured transaction subsists. With limited resources, such curtailment constitutes a significant disadvantage, as it robs the pledgor of the optimal use of the asset. The disadvantage of immobilization is however ameliorated by the pledgor's retention of ownership of the curtailed asset, which on the other hand constitutes a disincentive to the pledgee, who as a result is unable to realise the value of the asset without the pledgor's consent.[60]

A mortgage of personal property created in writing is usually subject to the provisions of the Bills of Sales Act.[61] A bill of sale is an instrument in writing by which one person transfers to another the property in goods or chattels, or a document given with respect to the transfer of goods or chattels in cases where possession is not intended to be given.[62] The delivery of possession of the goods or chattels is therefore not essential, and is in fact prohibited.[63]

With respect to the use of bills of sale as security for loans, the English 1882 act applies, as it specifically deals with security bills of sale.[64] Section 9 of that act provides that a security bill of sale is void against everyone, including the grantor, unless made in accordance with the form specified in the schedule to the act.[65] Further, section 4 of the same act provides that every bill of sale must contain an inventory of the chattels comprised in it for it to be effective; otherwise it will be void. The implication of sections 4 and 9 is therefore that failure to comply with the statutory form by including an inventory renders the bill void against third parties, with the grantee losing priority against competing parties.

Further, the requirement for a description of the chattels in the inventory implies that bills of sale cannot be given in respect of after-acquired property.[66] These elements of bills of sales discourage both parties to the secured transactions and render them cumbersome forms of security devices. Finally, as bills of sale are forms of mortgages, they require the transfer of title, with the unwanted consequence that the grantee is unfettered in the ability to sell the chattel upon default in the repayment obligation, a situation that micro business promoters find uncomfortable.

The term "charge" is often used interchangeably with "mortgage"; with regard to companies, such usage may be justified in view of section 197(11)

60 *Ahmed El-Hag v GKJ Amachree* (1962) LLR 10.

61 Bills of Sales Act 1878, sec 4. Bills of sale are governed by the provisions of the English Bills of Sales Acts of 1878 and 1882, as amended by the Bills of Sales Acts of 1890 and 1891, all of which are statutes of general application in Nigeria. See above at note 4.

62 JO Orojo *Nigerian Commercial Law and Practice* (vol 1, 1983, London Sweet & Maxwell), para 11.42.

63 *Mills v Charlesworth* (1890) 25 QBD 421.

64 Bills of Sales Act 1882, part III, secs 7–11.

65 *Thomas v Kelly* (1888) 13 App Cas 506.

66 *ACB Ltd v Oladapo* (1951) 12 WACA 285.

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of CAMA which, with reference to the registration of charges, provides that a charge includes a mortgage. However, several differences exist between a charge and a mortgage. At the very least however, whereas mortgages can convey both the legal and equitable interests in the secured asset from the mortgagor to the mortgagee,[67] a charge is an appropriation of the chargee's interest in the asset.[68] As it does not convey the asset, a charge only creates equitable interests in favour of chargees.[69] In Nigeria, charges are either fixed or floating,[70] with the former closely resembling pledges because they limit the chargor's right to deal in the assets during the subsistence of the charge. However, this article is more concerned with floating charges because of their potential benefits to MSMEs.[71] However, as it is only companies that can grant all forms of charges in Nigeria, most MSMEs remain ineligible to grant them. Further, by potentially excluding charges from the STMA, the opportunity has been lost to elevate these devices from mere equitable interests to legal interests.[72]

Vendor credit arises under any situation in which a seller of goods agrees to part with possession of those goods to the buyer before the complete liquidation of the sale price. In most instances, until the sale price has been fully paid, the seller continues to have some interest, functionally equivalent to a security interest in the goods sold.[73] Secured vendor credit generally arises in one of three main ways: conditional sales, hire purchase and finance lease transactions.

In conditional sales, although the seller parts with possession, he retains ownership of the goods, for example by inserting a title retention clause in the agreement until the complete liquidation of the purchase price.[74] A critical reason for ascertaining the passing of property is the fact that it determines whether the buyer can pass title in the goods received to a third party. In the context of MSMEs and their desire to utilize assets sold subject to vendor credit as inventory before liquidating the purchase price, sales are preferable in view of the principle of *nemo dat quod non habet* [one cannot give what one does not have]. On the other hand, sellers would prefer agreements to sell, as they preclude buyers from selling for precisely the same

67 See IO Smith *Nigerian Law of Secured Credit* (2001, Ecowatch Publications Ltd) at 35.

68 See *Ogundaini v Araba* (1978) 1 LRN at 280.

69 Ibid. See also CAMA, sec 178.

70 CAMA, sec 178.

71 See id, para. 2.2.

72 The harmonization of security interests should ideally remove compartments associated with the common law system, such as the demarcation between legal and equitable interests. See for example the definition of security interests in STMA, sec 63(1).

73 A Hicks *Nigerian Law of Hire Purchase* (1977, ABU Press) at 1. In cases where the seller agrees to part with both possession and ownership, his interest is limited to a personal action against the buyer with no attendant or consequential interest in the goods. Such cases amount to unsecured credit sales and are not discussed further in this article. See *Ajagbe v Idowu* [2012] 1 BFLR 102.

74 See *MIA & Sons Ltd v Afrotech Technical Services Ltd and Another* [1991] 5 NWLR (pt 194) 724.

reason, although such goods could become lost to the seller if disposed of by the buyer to a third party by virtue of the provisions of section 25(2) of the Sales of Goods Act of 1893 notwithstanding the retention of title.

However, a contract of hire purchase is a bailment of the goods coupled with an option to purchase them, which may or may not be exercised. Only when the option is exercised is there a contract of sale.[75] Hire purchase transactions are not designed for inventory, because the hirer's express or implied permission is always required in order to resell the goods. These transactions therefore hold limited value as a means of business financing for small business entities. Although both forms of credit may be used in acquiring equipment (save where the equipment directly results in income, such as through sub-hiring), MSMEs would find it difficult to sustain the instalment payments from their meagre earnings. Finance leases, like hiring agreements, are also forms of bailment with no transfer of title in the asset from the lessor to the lessee. However, the critical difference between a hire purchase transaction and a finance lease is that, unlike hire purchase where the parties' intention is ultimately to pass title when the instalments are fully paid and the option to purchase is exercised, the parties under a finance lease never intend title to pass; the hirer of the goods hires them for their entire useful life.[76] By their very nature therefore, finance leases do not enable small entities to use the assets subject to them as inventory.[77]

COMPANY CHARGES AND THE IMPACT OF THE STMA

This section examines the impact of the reforms introduced by the STMA, by first evaluating the extent to which the STMA reform objectives align with global reform objectives. It then assesses the impact of the STMA on the problems associated with the laws applicable to credit transactions as they affect MSMEs' access to loans examined earlier and, finally, it discusses the implication of section 2(3) of the STMA, which empowers companies to grant charges as security devices under CAMA. In evaluating the STMA's alignment with global requirements, UNCITRAL's *Legislative Guide*[78] and Model Law[79] are used as primary sources for comparison. The Australian Personal Property Security Act 2009 (APPSA) is also referenced.

The Nigerian reform objectives

Although the STMA's apparent adoption of a unitary system of security interest presupposes a legislative intent to adopt the model recommended by

75 See *Yakassai v Incar Motors (Nigeria) Ltd* (1975) 5 SC 107.

76 Beale et al *The Law of Security*, above at note 55 at 261.

77 Most finance leases contain an express undertaking by the lessee to retain possession and not dispose of or otherwise encumber the goods with any interest adverse to the lessor financier's title.

78 Above at note 13.

79 Ibid.

UNCITRAL, as will be seen in this section, there are divergences between the STMA and UNCITRAL objectives.

While UNCITRAL's recommendation is guided by the overarching objective of simplifying secured transactions for the benefit of all potential borrowers, the STMA appears focused on achieving a similar objective, albeit with specific reference to MSMEs.[80] Suffice to state that advancing implementation solely for MSMEs should be downplayed, since MSMEs are an integral part of the overall credit system yearning for reform. Further, beyond any specific objective lies the overarching need to liberalize the credit system under which MSMEs, being the dominant characters, would inevitably benefit.

UNCITRAL's broad reform objectives are that the laws governing secured transactions be simplified to harmonize the complex and cumbersome laws in various states that tend to discourage parties from secured transactions. UNCITRAL further recommends the replacement of such cumbersome laws with simplified and, possibly, unitary systems of security interests that make secured transactions more attractive, facilitating credit to potential borrowers.[81] In contrast, the STMA's objectives, contained in its section 1, are to: enhance financial inclusion in Nigeria; stimulate responsible lending to micro, small and medium enterprises; facilitate access to credit secured with movable assets; facilitate perfection of security interests in movable assets; facilitate realization of security in movable assets; and establish a collateral registry and provide for its operations.

It must be highlighted that, while the STMA's primary focus may be to stimulate funding to MSMEs, the act also seeks to ensure that lending is done responsibly, a subtle warning to stakeholders in the financial services sector to ensure that reckless lending should be avoided. Thus, while it can be safely asserted that the imperatives for the enactment of the STMA substantially align with UNCITRAL's objectives, the reference to "responsible" lending in section 1(b) surreptitiously extends its objectives beyond the liberalization of the credit system to the need for shrewd regulation. This contention is buttressed by section 10 of the STMA, which imposes the responsibility of supervising the collateral registry established under the act on the CBN, a financial regulatory agency. While section 10(1) provides for the establishment of a collateral registry "in the CBN", section 10(2) empowers the CBN governor to appoint the registrar and staff of the registry as considered necessary for attaining the objectives of the act.[82] The use of the phrase "in the CBN" suggests that the STMA's objective is to make the registry an organ or department of the CBN. Considering the significance of the collateral registry in implementing

80 However, this objective is not backed by special MSME-centric provisions; in fact, the STMA fails to refer to MSMEs beyond sec 1.

81 *UNCITRAL Legislative Guide*, above at note 13 at 1.

82 The registrar has responsibility for supervising and administering the registry's operations. See STMA, sec 10(3).

this reform,[83] its supervision should have been assigned to the Corporate Affairs Commission (CAC), which already performs a similar role in respect of company charges.[84]

While obviously questionable, the CBN's suitability to perform the responsibilities imposed under section 10 of the STMA may be further evaluated by examining its principal functions (under its enabling enactment) to ascertain whether they align with its section 10 responsibilities. These responsibilities are contained in the Banks and Other Financial Institutions Act (BOFIA)[85] and the Central Bank of Nigeria Act 2007 (CBNA). While section 1 of BOFIA confers extensive regulatory powers on the CBN over financial institutions,[86] the CBNA confers its core functions. These functions are to: ensure monetary and price stability; issue legal tender in Nigeria; maintain the country's external reserves to safeguard the international value of the Nigerian legal tender; promote a sound financial system in Nigeria; and act as banker and provide economic and financial advice to the federal government.[87]

The critical consideration here is whether the CBN's section 10 responsibilities align with its responsibility to promote a sound financial system, being the broadest of its principal responsibilities under section 2 of the CBNA. According to the International Monetary Fund, maintaining a sound financial system involves the control of financial systems to avert disruption in financial intermediation that undermines the effectiveness of monetary policy, exacerbates economic downturns, triggers capital flight and exchange rate pressures, and creates high fiscal costs related to rescuing troubled financial institutions.[88] These necessarily involve setting rigorous regulatory and prudential parameters for financial institutions. It is suggested that there can be no basis on which such a function would enhance the flexibility required to manage a regime that promotes liberal lending.[89] Consequently, it is contended that the CBN's extensive responsibilities in the implementation of the STMA cannot be justified by reference to its statutory functions.

83 See for example the STMA, part V on priorities of security interests.

84 See CAMA, sec 7(1). Although SMEDAN possesses vast statutory powers over MSMEs, the obvious argument against SMEDAN managing this responsibility is, however, that the STMA is not an enactment governing MSMEs, as it applies to all security interests in movable assets. See SMEDAN (Establishment) Act, secs 2, 8, 9 and 27 for SMEDAN's extensive responsibilities.

85 Cap B3 LFN 2004.

86 These include the powers to grant, vary and revoke banking licences, and approve the operation of foreign banks. See generally BOFIA, secs 3, 5 and 8, although other specific powers regarding financial institutions are interspersed in the act.

87 CBNA, sec 2.

88 International Monetary Fund "Financial system soundness" (factsheet, March 2019), available at: <http://www.imf.org/en/About/Factsheets/Financial-System-Soundness> (last assessed 3 December 2019).

89 There is no gainsaying the fact that reform aimed at liberalizing access to credit should not be unduly regulated.

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Since it derives its legitimacy from statute, the validity of the CBN's responsibilities under the STMA cannot however be merely discountenanced by virtue of its inconsistency with its other principal functions, because it is trite law that, once powers have been statutorily prescribed, even the courts are precluded from interfering with them.[90] Thus, despite the apparent misalignment of the CBN's STMA responsibilities with those of its enabling statute, the STMA responsibilities remain intra vires, being responsibilities that have been statutorily imposed.

However, on the propriety of challenging intra vires acts, the following view appears instructive: "into the bed of Procrustes, accordingly must be fitted not only the more obvious cases of inconsistency with statute, such as failure to follow expressly prescribed procedure, irregular delegation, and breach of jurisdictional condition: but also the more sophisticated types of malpractice, such as unreasonableness, irrelevant consideration, improper motives, breach of natural justice and more recently, mere error of law".[91]

On the strength of this authority, it would therefore appear that, despite statutory backing, intra vires acts can otherwise be challenged on the grounds of reasonableness. It is therefore contended that the provisions of section 10 of the STMA on the CBN's powers should be challenged on such grounds.

The STMA and the challenges in the current credit framework

The adoption of the functional approach, which encapsulates all transactions functionally equivalent to security interests, dispenses with the need to transfer possession of, and / or title to, the secured asset from the debtor to the creditor.[92] In practical terms, this should ease the creation of security interests in movable assets irrespective of the nature of the transaction, since all forms of transaction are encapsulated in the unitary security interest.[93]

However, upon closer examination, one cannot but doubt the efficacy of the STMA in achieving this objective. By virtue of section 2(1)(b), the STMA applies to persons who are creditors, borrowers or grantors under the act. While a creditor is defined as the person granting a facility on the back of a security interest created under the act, a borrower is defined as a person to whom credit is extended with a financial obligation to repay under a security agreement.[94] While there is clearly no imposition of any eligibility requirement under either definition, the definition of the term "grantor" raises a significant concern. "Grantor" is defined as "a person that has rights in the collateral, and includes a grantor of any type of security interest in the form of a charge,

90 See *Sani Dododo v EFCC* [2013] 1 NWLR (pt 1336) 468.

91 See H Wade and C Forsythe *Administrative Law* (11th ed, 2014, Oxford University Press) at 27.

92 This is buttressed by the definition of "security interest" in sec 63(1) of the STMA and by the fact that sec 2(1)(a) applies to all security interest in movable assets.

93 See the definition of security interest in id, sec 63(1).

94 Ibid.

chattel mortgage, pledge or lien in movable property".[95] It is suggested that the listing of various types of security interests, specifically "charges", unwittingly invokes the technical meaning of charges under CAMA, the platform through which charges are validly created because of the recognition of a parallel system in section 2(3) of the STMA.[96] By such invocation comes the retention of the undesirable requirement that only companies can grant such devices.[97] Consequently, unincorporated MSMEs such as micro enterprises remain ineligible to grant such devices.

The STMA's impact on pledges as security devices raises further concerns. While the STMA recognizes a creditor's right to take possession of the pledged asset, it curiously provides that such possession does not perfect the security interest.[98] Since repossession of assets to enforce a security is covered elsewhere in the act,[99] it is contended that the right of possession under section 8(2) should be viewed as a right other than for the realization of the security interest; the obvious "other" objective would be to provide the creditor with a means of overreaching a debtor's continued right to deal in apparent protection of the secured asset.

The implications of this conclusion are far reaching. First, not recognizing possession as a means of perfection implies that security interests can only be perfected and made effective against third parties by registering a financing statement pursuant to section 8(1) of the STMA, a position at variance with the structure of previous reforms.[100] Secondly, the non-recognition of possession as a means of perfection conflicts with the freedom to contract and renders rather confusing the effect of section 3(1) of the act, which provides that a security interest is created by a security agreement between a grantor and creditor. Since the validity of pledges has traditionally and inviolately been based on the transfer of possession from the pledgor to the pledgee,[101] it is suggested that section 8(2) renders reliance on a pledge an aberration under the STMA. It is submitted that this effectively "kills" the pledge as a form of security device, rendering it a non-possessory form of device under Nigerian law.[102]

95 Ibid.

96 See discussion of the implications of sec 2(3) in "Introduction", above.

97 See CAMA, secs 166 and 178(1).

98 STMA, sec 8(2).

99 See id, sec 40.

100 See for example UNCITRAL Model Law, art 18(2), which provides for possession as a means of perfection. The APPSA, sec 21(2)(b) also recognizes possession as a means of perfecting and publicizing a security interest over assets.

101 See *Ihunwo*, above at note 54.

102 A benefit of sec 8(2) may be that it could simplify lenders' due diligence by restricting it to searches at the collateral registry. However, it is contended that such simplification comes at a higher cost because it replaces the cheap benefit of taking possession with an obligation to file a financing statement, which could have been totally obviated by possession.

However, several other possibilities exist. First and more positively, with the envisaged hesitance of creditors to take possession, section 8(2) appears to have removed the disadvantage of immobilization of the pledged assets that debtors usually faced, thereby facilitating their continued right to deal in the secured asset(s). Further, while taking possession might in the strict sense not count as enforcement, it could effectively bring to an end the debtor's ability to deal with the collateral and consequently be functionally a close substitute to enforcement. Thirdly, the subsequent non-possessory security interest is capable of being offered by micro business entities as security, considering their ineligibility to create charges. How these possibilities play out in practice remains to be seen.

With respect to the impact of the STMA on bills of sales, it must be pointed out that the cumbersome process for their creation, including the mandatory listing of all secured assets during registration, thereby excluding after-acquired property, and the requirement for the transfer of title from the debtor to the creditor as a basis for their validity have, delightfully, been eliminated by the functional approach.

Unlike pledges and bills of sale, the validity of charges traditionally never depended on the transfer of possession of, or title to, the assets from the debtor to the creditor, charges only being viewed as encumbrances on the assets in favour of chargees.[103] It is thus difficult to ignore the similarity between charges and the STMA's unitary security interest. However, while most MSMEs remain ineligible to grant charges,[104] the security device introduced by the STMA appears available to MSMEs, since the STMA contains no fresh eligibility requirements. Consequently, the value of this interest would depend on how analogous it is to a floating charge, a consideration discussed in the next section.

Regarding vendor credit, the functionality of the unitary security also renders unnecessary the classification of transactions under vendor credit before the enactment of the STMA. Consequently, irrespective of the form of vendor credit granted by the creditor to the debtor, such a grant creates a security interest in favour of the creditor. However, the elevated status of acquisition financiers or holders of purchase money security interests (PMSIs), which is a key feature of global reform initiatives, deserves some elaboration. Acquisition financing embraces the full gamut of transactions that may be deployed to enable buyers to acquire tangible assets on credit.[105] UNCITRAL recommends that state legislation should classify such rights as acquisition security rights and make them subject to a common set of rules devoid of ownership considerations.[106]

103 See *National Provincial and Union Bank of England v Charnley* [1924] 1 KB 431.

104 See "The STMA and the challenges in the current credit framework", above.

105 *UNCITRAL Legislative Guide*, above at note 13 at 320. Unlike the STMA however, UNCITRAL provides two other options for the treatment of acquisition financing by states. See UNCITRAL Model Law, above at note 13, art 38.

106 Ibid, UNCITRAL Model Law, art 38.

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The STMA adopts this approach and defines a PMSI as: a right in collateral taken or retained by the seller to secure all or part of its purchase price; a right taken by a person who provides credit to enable the grantor to acquire the collateral if such credit is in fact so used; or the right of a financial lessor.[107] By virtue of section 27 of the STMA, a PMSI has priority over a non-PMSI in the same collateral created by the same grantor, provided the PMSI was perfected when the grantor obtained possession of the collateral. More significantly, PMSIs render the use of title retention clauses unnecessary, while nevertheless conferring priority on holders as an exception to the first in time rule.[108]

It is submitted that these changes will undoubtedly encourage both micro entities and vendor creditors to participate in vendor credit. While the small entities will be assured about their continued use of the assets, acquisition financiers or vendor creditors should be encouraged to part with the possession of assets bearing in mind their elevated status.

Company charges and the STMA

Section 39(5) of the STMA provides that the remedies under the act are in addition to those available under CAMA, including the right to appoint a receiver. This provision removes any doubt about the implication that section 2(3) creates a parallel system of secured transactions, as it apparently recognizes the existence of an alternative system of secured transactions (ie under CAMA), under which there are remedies that parties transacting under the STMA may adopt.

The existence of a dual regime results in the following possibilities in terms of the choices available to parties under the reformed system: companies can continue to create charges and mortgages in conformity with CAMA without the STMA impinging or impeding such transactions; companies can create charges and mortgages but choose to comply with the STMA by registering a financing statement after registering the charge or mortgage as required by CAMA; companies may create other forms of security interests (not being charges) in accordance with the STMA; and non-companies may create security interests[109] in conformity with the STMA.

While it is obviously the super compliant option for companies as it results in total compliance with the registration requirements of both regimes (ie CAMA and the STMA), the second option nevertheless amounts to dual registration or perfection for the creation of a single security interest. This obviously contradicts the objectives of simplicity advanced by UNCITRAL as a necessary attribute of these reforms.

107 STMA, sec 63(1).

108 See *UNCITRAL Legislative Guide*, above at note 13 at 332.

109 Parties must avoid designating such security interests as charges in order to avoid being entrapped by the definition of charges inadvertently retained by sec 2(3). See "The STMA and the challenges in the current credit framework", above.

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Following the eligibility requirements for the creation of charges discussed above and the fact that most MSMEs remain ineligible to grant charges as security devices, the sole option left to them is therefore the fourth option. This raises the need to compare the STMA's security device with the floating charge, in respect of the benefits they confer on MSMEs. This, and the implication of secured transactions filtering across both systems (ie CAMA and the STMA) are discussed below.

The STMA security interest as a replica of a floating charge

Under the STMA, the description of the collateral is adequate if it is accompanied by certain specifications, such as the item, kind, type or year of manufacture, or a statement that a security interest is taken in all the present and future assets of the grantor.[110] The reference to an interest in future assets is reminiscent of the floating charge as a security device for capturing after-acquired property in favour of the chargee.[111]

Relying on Romer LJ's steers in *Re Yorkshire Woolcombers Association Ltd*,[112] which remain the archetypal means of identifying what security devices may be classified as floating charges, the only apparent feature of such charges missing from the STMA is the company's right to deal in the assets until crystallization. This omission has led to the similar APPSA security interest being described as "a fixed security interest over circulating assets",[113] with the unwholesome implication that the limitations placed on the right to deal in fixed charges are extended to these security interests.[114] However, when this scenario is interpreted in conjunction with section 8(2) of the STMA, which empowers the creditor to take possession of the secured asset, one can only conclude that the debtor's right to deal under the STMA is, unlike a chargor's interest prior to crystallization, defeasible.[115] Thus, while grantors obviously have a right to deal in the assets under the STMA, the effect of section 8(2) is that it empowers creditors to overreach such rights, preventing the STMA security interest from being wholly analogous to the floating charge.

The implication of assets filtering across regimes

Chargees are not currently obliged to conduct searches at any other registry to ascertain the existence of encumbrances on charged assets, a position strengthened by the recognition of a dual regime by section 2(3) of the

110 STMA, sec 6(1)(c).

111 See *Re Yorkshire Woolcombers Association Ltd* [1904] AC 355.

112 Ibid.

113 Duggan and Brown *Australian Personal Property*, above at note 6 at 128.

114 However, arguments also exist to buttress the existence of the debtor's right to deal. For example, the very existence of a creditor's right to take possession implies that the secured asset is ordinarily in the debtor's possession. The right to deal also aligns with UNCITRAL's expectations of the unitary security system. See *UNCITRAL Legislative Guide*, above at note 13 at 83.

115 See *Re Spectrum Plus* [2005] 2 AC 680.

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STMA.[116] While there is a possibility, and perhaps an actual intention, that assets created under one regime should be identifiable by parties transacting under another regime when and if all registries of movable assets are interfaced as intended,[117] there is no assurance that such interface will ever be done or done effectively.[118]

Consequently, there is a possibility where the grantor is an incorporated company that assets emanating from a transaction under the STMA will filter into a subsequent transaction under CAMA.[119] The following example illustrates the possibility of assets filtering across regimes. SP1 acquires a security interest over G's present and future undertakings and registers a financing statement but does not take possession of the secured assets. While this transaction subsists, G grants a fixed charge to SP2 pursuant to section 178 of CAMA; SP2 registers his charge at the companies' registry in conformity with section 197 of CAMA. Before advancing funds to G, SP2 conducts a search at the companies' registry that does not reveal any encumbrance on the assets. SP1 subsequently decides to enforce his undertakings over the assets but is challenged by SP2.[120]

Dual regimes and the limited impact of notice

One implication of sustaining parallel systems of secured transactions is that, legally, parties transacting under CAMA are not bound by the STMA's registration requirements, although the reverse is not the case.[121] Consequently, SP2 is not obliged to conduct a search at the collateral registry to ascertain the existence of the first interest.[122] Suffice to state that imposing such an obligation implies that parties must conform to the dual registration requirement described as the second option above, which clearly contradicts the objective of simplicity that reform ought to advance.

116 However, the converse is not the same with secured parties under the STMA who are, ironically, obliged to conduct searches at the companies' registry if the potential grantor is an incorporated company. It is suggested that this constitutes an additional burden on such secured parties.

117 STMA, sec 2(1)(c).

118 It is noteworthy that the companies' registry, established in the early 1990s following the enactment of CAMA, has never interfaced with any other similar registry, notably the bills of sales registry. Issues of assets filtering between transactions under CAMA and the bills of registry are however rare, because bills of sales are hardly ever used. However, depending on how well STMA is received, its enactment may reverse this trend with this issue attaining greater significance in the Nigerian legal system.

119 This would happen because only incorporated companies remain eligible to create charges pursuant to CAMA.

120 In this example, G is an incorporated company.

121 Potential creditors wishing to lend to companies are expected to conduct searches at the companies' registry to ascertain the state of the company's assets, although this extends beyond the scope of any obligation imposed by the STMA.

122 See for example the definition of registration under sec 63(1) of the STMA as "the processing of a financing statement to bring it in compliance with the requirements of this Act", a process unrecognized under CAMA.

Despite recognizing the dual secured transactions regimes, the STMA ironically fails to provide clear rules for resolving conflicts across both systems. Consequently, such conflicts cannot be resolved solely by considering the notice provided under the STMA, because that notice is not binding on interests created under CAMA.

Resort to general legal principles to resolve priorities

While each system has clear rules for determining priorities for transactions emanating from within them,[123] it is suggested that, in the absence of clear provisions under the STMA for resolving conflicts in respect of transactions across regimes, resort would have to be had to general principles of law to resolve such conflicts. This again negates the intent and objectives of simplification and harmonization that global reforms have portended and that the STMA should have emulated.

Priority under the general law is determined based on a graduated scale of considerations, the first being whether the creator has a legal right to grant the security interest, expressed in the Latin maxim, *nemo dat quod non habet*.[124] Upon overcoming this requirement, further considerations include whether the interest meets the general requirements (such as registration requirements) for the creation of the interest. The order of creation of the respective interests and the exceptional priority rule are then considered.

Regarding the interests of SP1 and SP2, both comply with the requirement of the *nemo dat* principle, as the creation of a security interest in favour of SP1 does not prevent G from creating a further interest in favour of SP2, since the first security agreement did not prohibit the creation of that subsequent interest. Both transactions also apparently fulfil the registration requirements under their respective enabling enactments. While the first registration should ideally constitute notice to potential subsequent creditors whose interest should therefore be subordinated, that scenario is only possible when all transactions emanate from, and are subject to, the same regime.

The origin of the "first in time" rule can be traced to the equitable maxims "where there is equal equity, the law shall prevail" and "where the equities are equal, the first in time shall prevail".[125] Regarding the application of these maxims to the interests of SPI and SP2, SP1's interest would supersede SP2's interest not only because of its earlier time of creation but also because, as an interest created pursuant to and in fulfilment of a statute, it amounts to

123 For example, see the STMA, part V for priority rules for transactions under the STMA; and CAMA, sec 179 for priority rules under CAMA.

124 For a discussion of priorities under the common law, see generally S Worthington *Equity* (2nd ed, 2006, Clarendon Law Series), chap 4.

125 For a detailed discussion of both maxims, see J McGhee (ed) *Snell's Equity* (31st ed, 2005, Sweet & Maxwell), chap 4.

a legal interest.[126] Although SP2's interest was also created pursuant to a statute (ie CAMA), it is nevertheless defined by CAMA as an equitable interest.[127] Consequently, in most cases of conflict between transactions occurring under both regimes, those occurring pursuant to the STMA will for this latter consideration always take precedence, an unfortunate state of affairs that disregards the first in time rule.

This outcome also applies when the exceptional priority rule is applied. Under it, a bona fide purchaser for value of the legal estate without notice of a prior equitable interest takes free of the earlier created interests.[128] The principle relies more on the nature of interest held rather than the time of creation of the interest, ensuring that the presence or absence of notice remains an extenuating factor in determining priority.

Problems of adopting the remedies scheme under CAMA

The adoption of the remedies scheme under section 39(5) of CAMA raises two significant issues: whether such remedies are available to all secured parties or only to chargees who also comply with the requirements of the STMA; and whether, and to what extent, the rights of other secured creditors under transactions consummated pursuant to the STMA are affected by receiverships.

Regarding the first issue, it is contended that, since the STMA does not expressly limit the exercise of the remedies scheme under CAMA to company charges and mortgages, there is no basis to limit the use of such remedies to these security devices. Consequently, the implication of section 39(5) is the wholesale adoption of the remedies' scheme under CAMA for use by all secured parties under the STMA.

On the second issue, receiverships would undoubtedly affect, and perhaps complicate, the rights of other secured parties. Section 209(3) of CAMA for example provides that a receiver appointed by debenture holders has extensive powers, including the power to take possession and sell assets subject to the security. Subject to the security agreement, such a receiver may also: collect debts owed to the company; compromise, settle and enter into arrangements in respect of claims by or against the company; and negotiate terms for the sale of the company's business. Such far reaching powers will clearly affect the ability of other creditors to realise their security interest under the STMA, because they prevent them, even if momentarily, from enforcing their respective interests.[129]

126 The phrase "legal" is used in a different sense to denote an interest created in full conformity with the legal process for its creation, in contrast to the position with equitable interests. See generally id, para 1-002.

127 CAMA, sec 178.

128 Worthington *Equity*, above at note 124 at 96.

129 This difficulty is aggravated by the fact that receivers generally have limited duties to other creditors and often no general duty of care to them. See *Downsview Nominees Ltd v First City Corp Ltd* [1993] AC 295.

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A receiver's right to take possession of the assets and exercise the rights pursuant to his appointment is however subject to the rights of prior encumbrances.[130] In *Union Bank of Nigeria Plc v Tropic Foods Ltd*,[131] the court interpreted this section to mean that a receiver's right to deal with the assets was subject to all "specific charges" validly created in priority to the floating charge.[132] This raises the question of whether SP1's interest created pursuant to the STMA would constitute a prior specific charge for the purpose of encumbering the right of a receiver appointed by SP2 pursuant to the fixed charge. Yet again, the existence of parallel regimes makes this a difficult issue to resolve. If what constitutes a prior encumbrance should be determined by reference to the creation of the security interest rather than its enforcement, as this author contends it should, then only prior transactions consummated under CAMA would be capable of overriding SP2's interest since, to all intents and purposes, transactions consummated under the STMA are outside CAMA's radar.

In other jurisdictions where receiverships outlived reforms, these difficulties were avoided because the functionality introduced by reform was complemented by total harmonization, which therefore avoided dual security systems. Two main methods were adopted to avoid similar difficulties. Under the first method, creditors are defined under the reformed laws to include "receivers".[133] This method is justified by the fact that, as agents of their appointing creditors,[134] receivers functionally step into their principals' shoes to enforce their interests and, as such, are precluded from exercising powers that could prejudice the interest of other creditors. Under the second method, the reformed laws provide for the use of receiverships as an alternative means of enforcing the security interest. However, this method, adopted under the APPSA,[135] has been criticized because it "makes the law governing enforcement of security interests subject to arbitrary variables",[136] an unjustifiable outcome under a system that should be harmonized and predictive.

Unfortunately, the STMA adopted none of these methods. The STMA's definition of a creditor as "the person granting a facility on the back of a security interest created under the Act"[137] obviously omits the receiver, since a receiver does not grant a facility but only steps in subsequently as an enforcement mechanism. Further, despite the STMA, the creation of company charges

130 See CAMA, sec 393(1).

131 [1992] 3 NWLR (pt 228) 231.

132 The statutory rationale can be found in CAMA, sec 179. See also *Intercontractors Nigeria Ltd v UAC of Nigeria Ltd* [1988] NWLR (pt 76) 303.

133 See for example the Personal Property Security Act 1993 (Saskatchewan), sec 56(1).

134 See *Owen & Co v Cronk* [1895] 1 QB 265.

135 See APPSA, sec 116, which provides that chap 4 of the act (which deals with the enforcement of security interests) does not apply if there is a receiver or receiver and manager in control of the collateral, except if the grantor is an individual.

136 See Duggan and Brown *Australian Personal Property*, above at note 6 at 370.

137 STMA, sec 63(1).

remains within CAMA's, not the STMA's, domain. With section 39(5) of the STMA providing that the adopted remedies scheme under CAMA is "in addition", there is no basis to sustain the "alternative enforcement theory".

CONCLUSION

The enactment of the STMA is a significant restatement of the Nigerian government's commitment to liberalizing the credit sector: a commitment dating as far back as the early 1960s. As this article has however shown, the STMA leaves much to be desired in either achieving its objective or the objective of ongoing global reform, primarily for its failure to achieve the total harmonization of security interests by empowering parties to use charges outside the ambit of the act.

Consequently, it is recommended that, in order to achieve total harmonization, section 2(3) of the STMA should immediately be expunged, thereby subjecting company charges to the same rules of perfection and priorities as other forms of security interests.[138] However, to avoid imposing dual perfection schemes on companies and pledgees,[139] section 8(1) of the STMA should be amended to include provisions recognizing registration under CAMA and possession of the secured assets as alternative means of perfecting security interests. The current curtailment of possession as a means of perfection in section 8(2) of the STMA should also be expunged.

Following these recommendations, retaining the CBN as the key implementer of the STMA, especially in respect of its role of managing the collateral registry as provided by section 10 of the STMA, becomes unnecessary. Since companies would be subject to the same rules as non-companies following harmonization, extending CAC's responsibility in respect of companies to non-companies becomes a no-brainer. Consequently, the collateral registry created under the STMA should become a department of CAC, established solely to manage movable assets granted by individuals (as opposed to companies) as security for loans.[140]

CONFLICTS OF INTEREST

None

138 This ensures total harmonization and its attendant benefits, including obviating the need to resort to the general principles of law in resolving priority issues.

139 This follows from the fact that the redundancy of possession arising from sec 8(2) of the STMA renders pledge transactions subject to dual perfection, ie the registration of a financing statement irrespective of possession.

140 This should be easily handled by CAC, since loan transactions by individuals are usually less complex than those by companies that CAC already manages.