International Law Research; Vol. 5, No. 1; 2016
ISSN 1927-5234 E-ISSN 1927-5242
Published by Canadian Center of Science and Education

Statutory Decrystallisation of the Floating Charge: Implications for Business Sustainability

Dr Friday Okafor Onamson[1]

[1] The Purehearts Law Consulting, Kaduna, Nigeria

Correspondence: Dr Friday Okafor Onamson, The Purehearts Law Consulting, Plot 22/24 Aliyu Makama Road, Kaduna, Nigeria. Tel: 234-80-8883-3350. E-mail: onamson@pureheartslaw.com

Received: July 30, 2016 Accepted: September 26, 2016 Online Published: October 30, 2016
doi:10.5539/ilr.v5n1p237 URL: http://dx.doi.org/10.5539/ilr.v5n1p237

Abstract

This paper analyzes the provisions of the Nigerian Companies and Allied Matters Act 2004 which, against the grain of general law rules on decrystallisation of floating charge, provides that a crystallised floating charge can decrystallise or refloat where the creditor withdraws from possession after the debtor has commenced payment or if the receiver, with consent of the creditor, is withdrawn. The analysis is relevant because the provision has dire implications for business sustainability since parties engage in debt transaction to sustain the going concern basis of their businesses. Bearing in mind that uncertainty pervades the boundaries between fixed and floating charge, the paper asks what is the priority status of a decrystallised floating charge as against a floating charge created prior to refloatation; and what is the relationship between the decrystallised floating charge and a fixed charge that predated the decrystallisation on the one hand and a fixed charge created post refloatation on the other hand. Using the case law and existing literature the paper showed that the statutory provision for decrystallisation of floating charge not only failed to clarify the general law rules on decrystallisation of floating charge, but it has cast a veil of uncertainty over the rights of parties to a debt transaction secured by floating charge. Since the provision can impact on the health of businesses, it behoves on the parties to be proactive in crafting debts contracts creating an interest secured by floating charge.

Keywords: business, charge, creditor, decrystallisation, security, sustainability

1. Introduction

When a company borrows money and creates an interest to secure the repayment, it grants or appropriates a right (legal or equitable) over its property, assets, or undertakings to the creditor. Under the Nigerian Companies and Allied Matters Act (CAMA), the commonest interest which a company may create to secure a loan is the charge.[1] Depending on the type of interest created by the company, its right or interest in respect of the property securing the repayment of the loan or debenture may or may not be curtailed. For instance, if the security (McCormack, 2004; Onamson, 2016)[2] is by way of fixed charge, the assets subject to the charge are caught by asset constraint[3] and the company cannot deal with the assets, except with the express consent of the chargee. On the other hand, if the security is by way of floating charge[4], the right of the company to deal with the assets and even remove them from the ambit of the security in the ordinary course of business is not taken away at all. That is, the debtor is free to use the assets subject to the floating charge in the ordinary course of its business. On the occurrence of any specified event[5], the floating interest of the creditor fixes and catches all assets within its

[1] Sections 173(3), 178 and 197(2) CAMA

[2] Like the English jurisdiction, CAMA adopts formalistic approach in its treatment of security as against the functionalism obtainable in the US under Article 9 of the Uniform Commercial Code, Canada under Personal Property Security Act and New Zealand under Personal Security Securities Act. Generally see McCormack, G., Secured Credit under English and American Law

[3] Asset constraint is a basic feature of a proprietary or security interest, especially if it is a fixed charge or mortgage. It is so called because the right of the company/debtor that created or granted the interest to deal with the assets subject to the security is taken away. The company can only deal with the assets on the express consent of the creditor, the chargee or mortgagee as the case may be.

[4] This is known as floating lien under Article 9 of the United States Uniform Commercial Code.

[5] Section 173(3) and 178(1) CAMA

grasp, allowing the creditor to apply such assets towards settlement of the debt. This is known as crystallisation.[6] However, in Nigeria the situation does not end there. Rather the law ambitiously provided that subject to one of two conditions being met, the now crystallised charge, tautologically defined under the law as "fixed equitable charge", can decrystallise (or refloat) to become once again a floating charge.[7] That is the focus of this paper.

Accordingly, the paper sets out to consider the questions which the provision for decrystallisation of floating charge under Nigerian Companies legislation has thrown up. They are that the law failed to (a) protect adequately the interest of the chargor (debtor) who has commenced repayment prior to the withdrawal of the chargee from possession; (b) state what will be the priority status of the decrystallised floating charge (identified as deemed floating charge) as against a floating charge created before the charge crystallised; and (c) determine the relationship between the fixed equitable charge (identified as contingent specific charge**)** and as-created fixed charge that predated the decrystallisation and one which was created post refloatation. Thus the objective of this paper is to show that the statutory provision has failed in its attempt to provide for decrystallisation or transmutation or refloatation of a crystallised floating charge. This paper is structured in five parts: part one looked at charges generally; part two treated the types of charges capable of being created under CAMA; part three looks at crystallisation of floating charges; part four considered the statutory decrystallisation of floating charge and part five concluding the paper considers the implications of statutory decrystallisation for business sustainability.

2. The Equitable Charge

The charge is an equitable principle, but it has been given statutory flavour with its incorporation into and enactment in CAMA.[8] Without a statute there is no such thing as a legal charge. That is, legal charge is a statutory creation, in practice created by deed and registrable under the relevant registration of titles or property laws of the states.[9] For instance, a charge can be created by way of a legal mortgage.[10] However it is important to note that the recognition and incorporation of equitable charge into CAMA does not thereby create legal charge. The charge under CAMA still retains its equitable character. A discussion of the charge under CAMA is thus a discussion of the equitable charge.[11] Atkin LJ posing the question, 'what is meant by a charge' in *National Provincial and Union Bank of England v Charnley (1924)*, said:

> ... where in a transaction for value both parties evince an intention that property, existing or future, shall be made available as security for the payment of a debt, and that the creditor shall have a present right to have it made available, there is a charge, even though the present legal right which is contemplated can only be enforced at some future date, and though the creditor gets no legal right of property, either absolute or special, or any legal right to possession, but only gets a right to have the security made available by an order of the Court. If those conditions exist I think there is a charge.[12]

Hence, a charge is a mere appropriation of property for repayment of a debt. That is no interest is transferred but only an agreement to make the property available on default. If the debtor fails to repay the debt or perform the obligation or any danger threatens the assets subject to the charge, the creditor or obligee has a right of realisation by entering into possession, or by appointment of a receiver or by judicial process.[13] For the same reason, a charge is neither a mortgage as it does not involve a conveyance of a proprietary interest (Gullifer (Ed), 2012) just as the right of foreclosure is not available to the chargee; nor is a charge the pledge since the charge is not coupled with possession.[14] However an exception relates to land where a mortgage by way of legal charge

---

[6] Once a floating charge crystallises, the creditor takes steps immediate steps to take possession of the assets subject to the charge or to appoint a receiver of the assets subject to the charge for the sole purpose of realising the security and repaying the debt thereby secured.

[7] Section 178(2) CAMA

[8] See section 178 CAMA, which creates fixed and floating charges.

[9] For instance see section 109 Property & Conveyancing Law 1959; section 18 Registration of Titles Law, CAP 166 Laws of Lagos State 1994; sections 85-87 English Law of Property Act 1925

[10] See section 110 Kaduna State Law of Property Law 1990

[11] Since the charge under CAMA is equitable in character, it means that any relevant equitable principles not expressly incorporated into CAMA will still be applicable with equal force. It is with this understanding that the charge under CAMA has been examined in this paper.

[12] National Provincial and Union Bank of England v Charnley (1924) 1 KB 451; also see Re Cosslett (Contractors) Ltd (1998) Ch 495; Swiss Bank Corporation v Lloyds Bank Ltd (1982) AC 584

[13] See sections 180(2), 208 and 209 CAMA.

[14] See Re Bond Worth Ltd (1980) Ch 228

can be created under the statute.[15] In some contexts, the terms "mortgage" and "charge" can be used interchangeably so that the former is used to create a legal mortgage over land while the latter is used to create equitable security interests over personal property, like choses in action. (Beale, Bridge, Gullifer & Lomnicka, 2012)[16] For example, an assignment of a debt can be interchangeably referred to as a mortgage or a charge. (Sealy & Hooley, 2009)

Generally, the significant feature of a charge is that a certain property is made available as security for repayment of a debt. Once the property is appropriated, "the charge is said to 'fix'. Where the property is appropriated immediately to the chargee upon the chargor's acquiring an interest therein, the charge is known as a fixed charge" (Haque, 2006); but where it attaches to a shifting *'fund of assets'*, with the chargor having the benefit of using them in the ordinary course of business until crystallisation, the charge is called a floating charge. (Gullifer (ed), 2012; Pennington, 1960; Pennington, 2001; Worthington, 1996)[17] Since "by definition the existence of one excludes the other" (Gough, 1978), it simply comes to the point that "a creditor can take fixed and floating charge over the same asset to secure different liabilities, but not the same liability".(McKendrick (Ed), 2010) That is, because the asset constraint feature of a fixed charge is inconsistent with the freedom to deal in the ordinary course of business trait of the floating charge, "charges may either be 'fixed' or 'floating' with respect to particular assets but not at the same time". Notwithstanding, an instrument of charge can still provide "that it is specific as to some assets and floating as to others". (Haque, 2006) Known as a composite charge, such an instrument of charge is expressed to be a fixed charge on specified fixed assets and a floating charge on the company's whole undertakings and property other than the items covered by the fixed charge. (Mayson, French & Ryan, 1987) Apart from the composite charge, there are other types of charges under CAMA.

3. Types of Charges

Generally, in equity only two types of charges are capable of being created, namely fixed charge and floating charge. However, on a cursory look at the provisions of CAMA relating to the equitable charge, it becomes clear that four types of charges are capable of being created under CAMA. These are (a) as-created fixed charge; (b) fixed equitable charge (identified in this paper as contingent specific charge); (c) as created floating charge; and (d) deemed floating charge.

3.1 As-created Fixed Charge and Contingent Specific Charge

(a) As-created fixed charge. As-created fixed charge is actually equitable charge "that without more fastens on ascertained and definite property or property capable of being ascertained or defined".[18] As-created fixed charge is a fixed charge qua fixed charge that attaches immediately on creation because the assets are permanently appropriated to the payment of the debt thereby secured. This makes as-created fixed charge similar to a mortgage to the extent that the chargee obtains rights enabling it to restrain the chargor from meddling with the property subject to the charge. Any third party who acquires the charged assets holds subject to the fixed charge, except he took it bona fide for value and without notice. Thus, as-created fixed charge may be created over land, plant and machinery, shares in other companies, credit balances in the company's own accounts, book debts and future property. (Thorne & Prentice (Eds), 2002) When as-created fixed charge is taken over future property, the property must be identified and described, so that when subsequently acquired it must match the description.[19]

With respect to credit balances in the company's own account, it has been asked whether the customer can create charge over its own deposit account with the bank. To this question, Mullett J in *Re Charge Card Services Ltd (1987)* advanced the view that it is 'conceptually impossible' for a bank to take a proprietary interest in a deposit by a customer which is owed by the bank to the customer.[20] The conceptual impossibility is borne out of the view that the customer/debtor cannot become his own creditor and sue himself. To overcome this problem, the bank can impose "restrictions on the company's right to withdraw sums on deposit with the bank. Deposits made subject to such restrictions have come to be known as flawed assets". (McKendrick (Ed), 2010) The concept of the flawed assets works to the following effect:

---

[15] This obtains in states subject to Property and Conveyancing Law, section 109 thereof; and in Lagos, see section 18 Registration of Titles Law CAP 166 Laws of Lagos 1994.

[16] Also see, London County and Westminster Bank Ltd v Tompkins (1918) 1 KB 515; Re Bond worth (supra)

[17] There are so many theories concerning the nature of interest created by the floating charge. Among the existing theories, there is the theory that the floating charge creates a fixed charge with a licence given by the creditor to the debtor and another theory that it is a present proprietary interest in a fund of assets. The "interest in a fund of assets" theory is adopted in this paper.

[18] Illingworth v Houldsworth (1904) AC 355

[19] Holroyd v Marshall (infra)

[20] Re Charge Card Services Ltd (1987) Ch 150

> the bank may stipulate that sums deposited by Company A shall not become repayable to A so as money is due to the bank from A's associated company, B. At first this looks like a charge under another name, but there is an important difference. Security over a credit balance is intended, when enforcement becomes necessary, to result in the credit balance being applied in or towards discharge of the indebtedness which it secures (to the end that) the bank takes over the credit balance to the extent necessary to satisfy the secured indebtedness... By contrast, (the flawed assets) merely qualifies the bank's repayment obligation (to A) without giving it rights over the credit balance (and as such) the customer's (Company A) claim against the bank remains at all times intact. (McKendrick (Ed), 2010) (Brackets mine)

The mechanism of flawed assets does not vest any security interest in the bank. It means that the bank does not take over the credit balance just as it is not within its power to withhold repayment to A so as to reduce the liability of B. It only qualifies the bank's duty to repay A. The qualification is not a contractual set off since "the bank's countervailing claim is not against its creditor, A, but against a third party, B, and in any event the credit balance is not reduced by any cross-claim, it is merely frozen until the cross-claim has been discharged". (McKendrick (Ed), 2010) Thus, flawed assets hedge the credit risk of 'subsidiarized' entities in a group.

(b) Contingent specific charge (fixed equitable charge). Contingent specific charge is a strict statutory creation. It is a crystallised floating charge under CAMA following the occurrence of any of crystallisation events under the law.[21] Tautologically called *fixed equitable charge*[22], it has the statutory audacity to decrystallise and thus refloat to become a deemed floating charge. Further discussion of this type of charge is deferred to the topic on decrystallisation below.

3.2 As-created Floating Charge and Deemed Floating Charge

In Nigeria three types of floating charge can be discovered. These are (a) as-created floating charge, (b) general floating charge and (b) deemed floating charge. General floating charge is the same with as-created floating charge but differs in its scope because it is normally taken over the whole undertaking, business and property of the company. Deemed floating charge is a contingent specific charge (fixed equitable charge) that transmogrified by decrystallisation or refloatation to become floating charge. In the eye of the law[23] it never changed its character; albeit it became floating charge by transmutation the law takes the position that it never crystallised in the first place. Hence, the use of the word 'deemed' to qualify it. The deemed floating charge is taken together with the contingent specific (fixed equitable charge) below.

As-created floating charge means an equitable charge over the whole or a specified part of the company's undertakings and assets, including cash and uncalled capital of the company both present and future, but so that the charge shall not preclude the company from dealing with the assets until the occurrence of any or all of the crystallising events.[24] Lord Macnaghten in *Salmon v Salomon (1897)* described the floating charge as being "too convenient a form of security to be lightly abolished"[25] and its convenience can be appreciated in comparisons:

> A specific charge, I think, is one that without more fastens on ascertained and definite property or property capable of being ascertained and defined; a floating charge, on the other hand, is ambulatory and shifting in its nature, hovering over and so to speak floating with the property which it is intended to affect until some even occurs or some act is done which causes it to settle and fasten on the subject of the charge within its reach and grasp.[26]

Construing the above statement, one may wish to ask, is it the subject (that is, the interest created) or the subject matter (that is, the asset constituted in the security) of the floating charge that is ambulatory? If it is the former, then the nature of the asset is inconsequential; if it is the latter, the nature of the asset will be a defining theme. The statement talks of "hovering over and so to speak floating with the property". This means that the nature of the asset may not necessarily be the defining factor when construing a floating charge because what is hovering

[21] Section 178(1)(a)-(c) CAMA

[22] section 178(2) CAMA

[23] For an interesting reading on the metaphor of the "eye of the law", see Michael, S., The Eye of the Law: Two Essays on Legal History, Oxford: Birbeck Law Press, 2009

[24] Section 178(1) CAMA.

[25] Salomon v Salomon (1897) AC 22

[26] Illingworth v Houldsworth (supra)

over and floating with the property is the interest granted by the floating charge, not the asset constituted thereby. Thus, it hovers and floats "over a changing fund of assets, including assets acquired by the debtor after the creation of the charge". (Sealy & Hooley, 2009) However, it is more suited to circulatory assets so that as the assets circulate, the subject of the floating charge vigilantly watches over them by means of hovering.

Characteristically, the floating charge works perfectly with certain asset types, for instance circulating assets. With circulating assets, floating charge operates in its natural habitat and its qualification as "one of the great legal success stories of Victorian times" (Gough, 1987) will be appreciated and the technicalities surrounding the distinction between fixed and floating charges will be largely minimised or altogether avoided. The floating charge towers above asset constraint feature of the fixed charge as the chargor is at liberty to meddle and deal with the assets subject to the charge and indeed take them away from the ambit of the security. While meddling and dealing with the assets, the floating charge interest watches over to ensure that such meddling or dealing is in the ordinary course of business of the chargor only. Consequently, where the chargor purports to set up inconsistent interest, for instance by way of assignment, the floating charge will berth and fix on the subject matter of the charge because such dealing cannot be dealing in the ordinary course of business of the chargor.

Generally, the floating charge may be invalid if created within the twilight period before the commencement of winding up. (Ferran, 2008) This condition was first introduced in 1907[27] to address agency problems (Smith, 2012)[28] which the Salomon's case so starkly revealed. However, it is doubtful if this condition obtains in totality in Nigeria. Accordingly, a charge created within three months of the commencement of winding up is valid *(a) if the chargor was solvent immediately after the creation of the charge; (b) if the company was insolvent at the time of creation, to the amount of any cash paid to the company at the time; or (c) if the chargor was insolvent to the amount of any cash paid subsequently paid pursuant to the charge*.[29]

It is submitted that conditions (b) and (c) of this provision are ill-conceived. Why should the law permit payment at the most vulnerable period in the company's life with sole purpose of giving the party unfair advantage over others? First, it is capable of cutting deep into what otherwise would have been available for unsecured creditors, especially in a system, like ours, that has no simile UK prescribed part regime[30] (Onamson, 2015). Second, the provision could be exploited to secure past unsecured indebtedness.[31] This means that connected transactions concluded not at arm's length and collusive contracts will safely seep through the provision. Third, the condition which allows 'subsequent payment' flies in the face of the anti-deprivation principle. Even if the company was not insolvent at the point of creation, a further advance of credit is what the parties need to validate an otherwise obnoxiously impugnable and unconscionable transaction proscribed by the law, for instance fraudulent preferences.[32]

Anti-deprivation is a common law principle that deals with provisions in contracts entered into before the company became insolvent which have the effect of diminishing the asset pool on insolvency. (Gullifer & Payne, 2011) However, the principle is subject to limitations. Thus, the principle applies only when there is actual diminution in the value of the asset. This means that if the cash paid is equivalent to the security charged, the transaction will survive. Perhaps this might have been within the contemplation of the drafters of the provision in CAMA; but the law, loosely drafted, failed to bring it out. Anti-deprivation principle will not apply to reductions in the asset pool which occurred before winding up commenced. Hence there is no problem with the provision which permits all transactions which took place three months before the onset of winding up.[33] The principle does not apply to assets in which the company has limited interest (e.g., leases).

Specifically, a debenture holder with a floating charge has a right of realisation of the security where the debtor falls in default as to payment of any instalment of interest, or the whole or part of the principal or premium

---

[27] Section 13 Companies Act 1907

[28] Agency problem or cost refers to a conflict of interest immanent in any relationship where one party, the agent, is expected to act in the best interests of another party (the principal). The situation conflict will move the agent to engage in profuse opportunism and thus promote his own personal interests against that of the principal.

[29] Section 498 CAMA

[30] The UK prescribed part regime requires that proportion of the recoveries by floating charge holders to be set aside for the benefit of the general of unsecured creditors. There is no simile system in Nigeria where the unsecured creditor suffers, at the insolvency of the debtor, from the entrenched principle of discrimination by exclusion from the estate of the debtor (Onamson, 2015).

[31] Judicial opinions on this have been inconsistent and contradictory. See Re MC Bacon Ltd (1990) BCLC 324, where it was disapproved; compare Hill v Spread Trustee Co Ltd (2006) EWCA Civ 342, where it was affirmed.

[32] For example, see section 495 CAMA.

[33] Perpetual Trustee Co Ltd v BNY Corporate Trustee Services Ltd (2009) ECWA Civ 1160

owing under the debt.[34] However, where the floating chargee seeks to exercise the remedy which will enable it to realise the security by way of appointing a receiver or getting into possession while the company is a going concern, its ability to make total recovery of principal and interest can be seriously impaired. This is because the law provides that all preferred payments[35] payable in winding up rank in priority to any claim for principal and interest out of the assets coming to the hands of the receiver or other person taking possession.[36] If after reckoning with preferred payments and the balance is insufficient to pay the chargee, the balance represented by the preferential payments shall be recouped as far as may be out of the assets of the company available for payment of general creditors.[37] The creditor's secured status is lost as he becomes unsecured as respects that balance. Thus the creditor can only enforce the payment by ordinary action, or on insolvency of the debtor it may be subject to pari passu payment. This provision of the law is welcome because it serves two functions. One it discourages the creditor from acting opportunistically and thus precipitating premature insolvent liquidation of the debtor. Two, it removes every strand of fear that may be playing in the mind of the debtor and gives him the confidence it needs to deal with the charged assets in the ordinary course of business.

Fundamentally, the floating charge is said to be an irrational "strategy for a lender seeking to gain priority over other creditors in a useful way". (Mokal, 2003) This is because "the creation of subsequent fixed charges and the accumulation of new preferential claims can dilute the floating charge holder's security, as can the debtor's ability to alienate the collateral free of charge". (Mokal, 2003) In other words, any prior fixed chargee or subsequent fixed chargee without notice will always rank in priority. Alternatively, enforcing the floating charge pre-insolvency of the debtor is the best choice but with the likelihood that preferred payments will seriously erode the chargee's intake. Comparatively, in England, the floating chargee struggles with the same challenge as Nigeria, but must additionally contend with the reality that the hived-out Crown's preferential claims has been clawed back and ring-fenced to form the prescribed part[38] for unsecured creditors. This further dilutes the recovery which the floating charge holder will make in England. We need not tow the English line in Nigeria to be able to achieve equity for the general unsecured creditors in the debtor's insolvency. For instance, ex ante the debtor could, by legislation, be restrained from encumbering all its assets by way of proprietary interest.

3.3 Distinguishing between Fixed and Floating Charge

When the provision discouraging the holder of a debenture secured by floating charge from enforcing the security while the chargor is a going concern and the point that floating charge is not an efficient mechanism for a creditor seeking to maintain priority over and above other creditors are considered, the natural question becomes what is the difference between fixed and floating charge? Going by the words "fixed" and "floating", one can easily fall into the pardonable assumption that fixed charges relate to certain types of property while floating charges are amenable to other types of property. So that fixed charge is incapable of being created over circulating assets, for example, inventory, book debts, etc. This view contrasts with an earlier point with respect to floating charge which posits that "the nature of the asset may not necessarily be the defining factor when construing a floating charge because what is hovering over and floating with the property is the 'interest' granted by the floating charge and not the asset constituted thereby."[39] The question of the distinction between fixed and floating charge is a vexed one and constitutes one of the problems which the CAMA jurisdiction did not resolve.

At this juncture, a brief history of this great facility of equity, the floating charge, will give an insight into the issues surrounding the distinction between fixed and floating charge. One of the early cases[40] that equity intervened to remedy the defects of common law involved "the attempted mortgage of the after-acquired machinery operated as a contract to create a proper mortgage which equity would specifically enforce". (Pennington, 1960) After the case, the creation of a floating charge on the assets for the time being of a company became a possibility:

> Thus when a company issued debentures in 1859 charging "the lands, tenements and estate of the company and all their undertaking, it was held in 1864 that the charge *attached only to the fixed assets* of the company at the date the debentures were issued,

---

[34] Section 208(1)(a) CAMA.

[35] For a schedule of preferred payments under the law, see section 494 CAMA

[36] Section 182(1) CAMA; section 754(2) CA 2006

[37] Section 182(3) CAMA; section 40 English IA 1986.

[38] Section 176A English IA 1986; Insolvency Act (Prescribed Part) Order 2003, SI 2003/2097

[39] Illingworth v Houldsworth (supra)

[40] Holroyd v Marshall (1888) 12 App Cas 523. Also see Tailby v Official Receiver (1888) 13 App. Cas. 523; Metcalfe v Archbishop of York (1836) 1 My. & Cr. 547

> and did not extend to calls made on shareholders thereafter nor to the trade debts becoming due to the company thereafter.[41]... In another case[42] where a company issued debentures in 1865 by which it assigned its 'undertaking and real and personal estate' to the debenture holders, it was held in 1868 that they acquired a charge on the *assets owned by the company at the date the debentures were issued*, but not on assets subsequently acquired. (Pennington, 1960) (Italics mine)

This means that the floating charge was not known to English law prior to 1870 with the result that a charge was either on the assets presently owned by the company or a charge on the fixed assets of the company. It was in 1870 that full recognition was accorded to the floating charge in a transaction in which a company had issued debentures in 1866 charging its 'undertaking' with payment of the debenture debt.[43] It was held that "when the company was subsequently wound up, the charge became a *specific charge*[44] on the assets which it then owned, and so the debenture holders ranked for payment before the general creditors." (Pennington, 1960) The court construed the word 'undertaking'[45] as inferring that:

> the company will go on, and that the debenture holder could not interfere until either the interest which was due was unpaid, or until the period had arrived for the payment of his principal and the principal was unpaid. I think the meaning and object of the security was this that the company might go on during that interval, and furthermore, that during the interval the debenture holder would not be entitled to an account of mesne profits, or of any dealing with the property of the company in the ordinary course of carrying on their business.

In line with the above holding, the courts subsequently held[46] that the debentures by which the company bound itself and all its estate, property and effects entitled the debenture holders to a specific charge on the assets of the company which it owned on winding up, but not while it is a going concern. Thus, the proper character of every charge created by a company charging "all its estate, property and effects"[47], or "its real and personal estate"[48] or "its entire undertakings"[49] has always been floating which would ripen into a specific charge on crystallisation or insolvency. At winding up, or upon crystallisation realisation cannot be piecemeal by way of disentangling the assets and systems of the company in order to discharge the secured debt, because the charge security on the property and undertakings of the company as a whole and as a going concern.[50] Then a fixed charge related to a particular piece of property belonging to the company; a floating charge related to all its estate property and effects or its entire undertakings. For fixed charge, realisation can be by sale of the particular property; for floating charge it cannot be piecemeal.

It is submitted that realisation of the security on a going concern basis in respect of floating charge is the basis for the powers of a receiver and manager of the whole or substantially the whole of the property of the company either to carry on the business of the debtor or to dispose the business as a going concern and not in dismembered parts. It is further submitted that this must have been the wisdom behind the new administration procedure under the UK law, which mandates an administrator to pursue one of three hierarchically ordered objectives when the debtor slips into trouble. Thus, the charge as created by the company "could not be a *specific*

---

[41] King v Marshall (1864) 35 Beav 565

[42] Re New Clydach Sheet & Bar Iron Co (1868) L.R. 6 Eq. 514; Re Marine Mansions Co. (1867) L.R. 4 Eq. 601

[43] Re Panama, New Zealand and Australian Royal Mail Co (1870) 5 Ch. App. 318

[44] The argument can be pursued that the word "fixed" meaning something that is secured and not subject to change cannot carry the same meaning with the word "specific" which means something that is precise or particularised. Bearing this in mind, it can be pursued further that the distinction between fixed and floating charge should be based on the nature of the asset. On this basis, fixed charge will relate to assets that are fixed with reference to the business of the debtor; floating charge will relate to assets that naturally revolve or circulate with reference to the business of the debtor. This means what is fixed asset for business A might constitute revolving or circulatory assets for business B. If and when a floating charge crystallises, it becomes a specific (not fixed) charge on such of the assets that fall within its grasp. This view creates a symbiotic relationship between floating charge and specific charge, the latter being a consequence of the former. Without the former there cannot be the latter.

[45] Section 2 of the Companies Clauses Consolidation Act, 1845 defined the word as "the undertaking or works, or whatever nature, which by the company's set of incorporation be authorised to be executed.

[46] Re Florence Land and Public Works Co., ex. p. Moor (1878) 10 ChD 530

[47] Re Florence (supra)

[48] Re Colonial Trust Corporation (1879) 15 ChD 465

[49] Re Panama (supra)

[50] Gardner v London, Chatham and Dover Railway (1867) 2 Ch App 201; Re Florence (supra)

charge on the company's assets while it was a going concern, but must be a charge which becomes enforceable only when the company is wound up or when the debenture holders obtain the appointment of a receiver by the court". (Pennington, 1960)

Following the cases[51] it is submitted that the concept of fixed charge was never intended to be mixed up with the concept of floating charge as to constitute a major concern as far as the distinction between the two is concerned. Thus, a charge over the undertakings of the company created a charge on the company's undertaking as an integrated going concern and incapable of being broken into pieces or all its estate, property and effects[52] could not be a fixed charge. How, then, did we come to the point that the distinction between fixed and floating charges has become an intractable issue? With great respect, the seed of inconsistencies regarding the distinction between fixed and floating charge was sown in the "most celebrated and certainly the most often cited" (Sealy & Hooley, 2009) case of *Woolcombers* where Romer described the features of the floating charge:

> I certainly think that *if a charge has the three characteristics* that I am about to mention it is a floating charge: (1) if it is a charge on a class of asset of a company present and future; (2) if that class is one which, in the ordinary course of the business, would be changing from time to time; and (3) if you find that by the charge it is contemplated that, until some future step is taken by or on behalf of those interested in the charge, the company may carry on its business in the ordinary way as far as concerns the particular class of assets I am dealing with.[53] (Italics mine)

Notwithstanding the point that there should not be much ado "in defining what a floating charge is in contrast to what is called a specific (not fixed) charge"[54], the Romer LJ's characterisation of the floating charge left more problems than it set out to solve. The stage for the problems was set when Romer LJ declared that he certainly did not intend to attempt to give an exact definition of the term 'floating charge' nor was he prepared to say that there would not be a floating charge which did not contain all of the three characteristics. Instead of dissolving the problem his statement fertilized it by bundling up *the nature of the subject matter* that could be subject to a floating charge *with the manner of its taking* to determine if a floating charge exits. Thus, the statement not being authoritatively definitive, the courts and lawyers must engage in the task of unearthing and dissolving the fixed and floating charge albatross by discriminating between the Romer's components: In this light:

> whenever grey areas are encountered (as between two components) lawyers would dissect the two components in order to weigh which matters more to the definition. This is the weakness of the definition (by Romer): no conceptual thought has been given to the exact relationship or weight of the two components relative to the other. (Chiu, 2006) (Brackets mine)

In fact the unsavoury effect of the bundling, and the consequent distortive discrimination between fixed and floating charge, was felt when the court held "for the first time[55] that conceptually at least a company could create a valid fixed charge over future debts" (Addy, 2010). The holding must have emboldened ethically-challenged creditors who now contract to take benefit of two worlds by creating two separate security interests (fixed and floating charge) over an indivisible asset (for instance, book debts and the proceeds of the book debts).[56] Consequently, the Woolcombers case cannot be authority for precisely discovering the difference between fixed and floating charge.

Subsequently the decision of the courts diverged between the nature of assets[57] and the degree of control[58]. Setting the stage for 'negotiated' resolution of the controversy, Lord Millett made a definitive statement on the Romer LJ bundled characterisation and opened a vista for the adoption of control test, rather than the nature of assets test, as the strongest basis and unequivocal criterion for determining the distinction between fixed and floating charge. Per the learned Lord Millet:

---

[51] Illingworth v Houldsworth (supra); Re Panama (supra); Re Florence (supra) and a host of others

[52] Gardner v London, Chatham and Dover Rly (supra); Re Colonial Trust Corporation (supra); Re Florence (supra); Re Panama (supra)

[53] Re Yorkshire Woolcombers Association Ltd (1903) 2 Ch 284

[54] Per Lord Macnaghten in Illingworth v Houldsworth (supra)

[55] This was in Siebe Gorman & Co Ltd v Barclays Bank Ltd (1979) 2 Lloyds Rep 142

[56] Re New Bullas Trading Ltd (1994) 1 BCLC 485 (CA)

[57] On decisions based on the nature of the assets, see Re Cimex Tissues (1995) 1 BCLC 409; Re Atlantic Computer Systems Plc (1992) Ch 505 and Holroyd v Marshall (supra).

[58] The decisions in Re Cosslett Contractors Ltd (supra) and Re Brightlife (1987) Ch 200 are based on this component.

> This (Romer's characterisation) was offered as a description and not a definition. The first two characteristics are typical of a floating charge but they are not distinctive of it, since they are not necessarily inconsistent with a fixed charge. It is the third which is the hallmark of a floating charge and serves to distinguish it from a fixed charge. Since the existence of a fixed charge would make it impossible for the company to carry on business in the ordinary way without the consent of the charge holder, it follows that its ability to do so without such consent is inconsistent with the fixed nature of the security.[59] (Brackets mine)

Determined to dissolve the cloud hovering over the distinction between fixed and floating charge and by extension making a case for control test, Lord Millet continued that:

> what you do require to make a specific security is that the security whenever it has once come into existence, and been identified or appropriated as a security, shall never thereafter at the will of the mortgagor cease to be a security. If at the will of the mortgagor he can dispose of it and prevent its being any longer a security, although something else may be substituted more or less for it that is not a 'specific' security.[60] (Emphasised added)

Based on the control test as the strongest index for determining the distinction between fixed and floating charge Lord Millet then developed the two-stage process. Thus:

> In deciding whether a charge is a fixed or a floating charge, the court is engaged in a two-stage process. At the first stage it must construe the instrument of charge and seek to gather the intentions of the parties from the language they have used. But the object at this stage of the process is not to discover whether the parties intended to create a fixed or floating charge. It is to ascertain the nature of the rights and obligations which the parties intended to grant each other in respect of the charged assets. Once these have been ascertained, the courts can then embark on the second stage of the process, which is one of categorisation. This is a matter of law. It does not depend on the intention of the parties... In construing a debenture to see whether it creates a fixed or a floating charge, the only intention which is relevant is the intention that the company should be free to deal with the changed assets and withdraw them from the security without the consent of the holder of the charge; or, to put the question another way, whether the charged assets were intended to be under the control of the company or of the charge holder.[61]

The first stage recognises the freedom of the parties to go into commercial arrangements according to their promptings. The second stage emphasizes the point that such freedom is bounded by what is legally possible. In other words, the parties are free to characterise their security arrangement (including to assign rights to each other) as they want but the transaction labours under the danger of recharacterisation if it offends "the doctrine of shams" or "the mislabelling principle". (Ferran, 2008) This point was emphasized in Agnew's case:

> (the) label that the parties may attach to the security documentation is not determinative of the nature of a charge: if the rights and obligations that the parties have granted each other in respect of the charged assets are inconsistent with the label attached to the charge by the parties, that description will be disregarded and, as a matter of law, the security will be categorized in accordance with the substantive rights and obligations that it creates.[62]

Thus every security document which purports to be a charge must pass through the two-stage process for the purpose of discovering and attributing "the correct legal label to that package of rights and obligations". (Ferran, 2008) In this connection Lord Walker in *Re Spectrum Plus Ltd (2005)*[63] used the two-stage process to identify clearly the essential difference between fixed and floating charge:

[59] Agnew v Commissioner of Inland Revenue (Re Brumark Investments Ltd) (2001) 2 AC 710

[60] Ibid

[61] Ibid

[62] Ibid

[63] National Westminister Bank plc v Spectrum Plus Ltd (Re Spectrum Plus Ltd) (2005) UKHL 41

> Under a fixed charge the assets charged as security are permanently appropriated to the payment of the sum charged, in such a way as to give the chargee a proprietary interest in the assets. So long as the charge remains unredeemed, the assets can be released from the charge only with the active concurrence of the chargee. Under a floating charge, by contrast, the chargee does not have the same power to control the security for its own benefit. The chargee has a proprietary interest, but its interest in a fund of circulating capital, and unless and until the chargee intervenes (on crystallisation of the charge) it is for the trader, and not the bank, to decide how to run its business. So long as the company trades in the ordinary way... the constituents of the charged fund are in a state of flux (or circulation).[64]

Thus, the controversy over fixed and floating charge distinction appears to have finally been resolved. Accordingly the distinction is one of control. It is does not matter if the nature of the asset is fixed or circulating, present or future. Moss in support of the control paradigm as the definitive basis for distinguishing between fixed and floating charge stated that:

> Lord Millett (in Agnew's case) appears to have identified the difference between fixed and floating charges as being a 'touchstone' question, the 'touchstone' being the ability of the chargor to use the proceeds of the ostensibly fixed charge for his own purposes without the chargee's consent. In the case of book debts, for this purpose, the proceeds of book debts are identified with the debts and are treated as one subject matter, even though it is a matter of strict law, they could be separated. (Moss, 2006)

Following the lines of Moss, and of latest English decisions[65], which established control test prescription, Worthington surmised that:

> The essential difference between a fixed and a floating charge turns upon the ability of the chargor to deal with the charged assets, removing them from the ambit of the security without the consent of the chargee. (...) The charge is fixed if and only if the chargor is required to preserve the charged assets, or their permitted substitutes, for the benefit of the chargee (either absolutely, or as part of the pool of charged assets standing as security for the chargor's obligation). (Worthington, 2006; Worthington, 2010)

On his part, Mokal agreeing that "control is precisely what distinguishes fixed from floating charges" (Mokal, 2003) added a dimension that the distinction between fixed and floating charge is better appreciated when viewed from the point of priority. According to him the grant of security interest is to grant priority to the creditor and the asset subject to security is caught up by asset constraint. Hence, to constrain an asset is:

> to entrench the priority of the chosen claim with respect to the asset and its proceed by giving the claimant a veto over any attempt by the debtor unilaterally to disturb that priority. So understanding that the fixed charge is connected with priority – in a way that the floating charge is not – helps us distinguish between the two types of charge. A charge only encumbers collateral if it entrenches the priority of its holder's claim and an asset can only be encumbered by the charge if the chargee is giving control over the use and disposal of the asset. Not to have control means not to have priority. The floating charge has neither one nor therefore the other. (Mokal, 2003)

Thus, control test helped to open up the weakness of the floating charge as a near worthless form of security. In fact, it is inevitable that the control test would hold sway because (a) most borrowers will dispose of their fixed assets from time to time; (b) a particular type of asset (e.g., a car) may be a circulating asset for one borrower but a fixed asset for another borrower; and (c) the structure of a transaction may affect whether the debtor owns one asset or many circulating assets. (Gullifer & Payne, 2011) Assume the borrower is a leasing company that hires equipment to other entities either on a number of separate consecutive contracts, or under one long-term contract. The asset of the leasing company will generate receivables from the transaction. It could be classified as long-term fixed asset or as circulating assets.

Although it may be argued that a great deal of uncertainty still pervades the boundaries between fixed and floating charges (Gullifer & Payne, 2006), it is submitted that the control test provides a reliable 'touchstone'

[64] This House of Lord's decision is the most current authority on the distinction between fixed and floating charge.

[65] Agnew case (supra) and In Re Spectrum Plus (supra)

that can facilitate the dissolution of all such strands of uncertainties. Notwithstanding and apart from the control test, an alternative basis can be propounded for determining the distinction between fixed and floating charge. Thus, the argument can be pursued that, strictly speaking, the word "fixed" meaning something that is secured and not subject to change cannot carry the same meaning with the word "specific" which means something that is precise or particularised. Bearing this in mind, it can be pursued further that the distinction between fixed and floating charge should be based on the nature of the asset. On this basis, fixed charge will relate to assets that are fixed with reference to the business of the debtor; floating charge will relate to assets that naturally revolve or circulate with reference to the business of the debtor. This means what is fixed asset for business A might constitute revolving or circulatory assets for business B. If and when a floating charge crystallises, it becomes a specific (not fixed) charge on such of the assets that fall within its grasp. This view creates a symbiotic relationship between floating charge and specific charge, the latter being a consequence of the former. Without the former there cannot be the latter. This basis still retains the control test prescription but modifies it to the extent that the assets subject to floating charge will be different as between businesses. Thus, for a equipment leasing company, motor vehicles and power generating plants constitute revolving assets and subject to floating charge, and if the charge crystallises it becomes specific. Conversely, for a manufacturing entity such class of assets is fixed assets and can only be subject to fixed charge.

Does the distinction between fixed and floating charge really matter? It matters because a floating charge is not subject to asset constraint. Subject to conditions, the fixed charge enjoys priority over floating charge[66], so it is imperative that the creditor is seized with the exact nature of the transaction he enters. A floating charge created within a certain period can be vitiated. (Sealy & Hooley, 2009) Equally the distinction makes it less likely that the security agreement between the parties will be recharacterised for failing due to shams or mislabelling. It also matters because the fixed charge is not subject to crystallisation and cannot be a candidate of statutory decrystallisation.

4. Crystallisation of Floating Charge

The great facility of the floating charge lies in its capacity to escape the 'asset constraint' (Westbrook, 2004) feature of security. That is it gives the debtor the latitude to continue, in the ordinary course of its business, to deal with the assets which are subject of the floating charge, remove them from the ambit of the security and even transfer them to third parties unencumbered by the floating security. However, transfer does not mean dealing in a way inconsistent with the rights of the chargee, like charging or assigning the assets to another creditor. It is conceded that the floating charge is a flexible form of security, but there is inherent risk associated with it. By allowing the debtor to remain in control and meddle with the charged assets impliedly means that the debtor may unwittingly, "dispose of the subject matter of the security unprofitably, thereby undermining the value of the security and potentially putting its solvency at risk". (Ferran, 2008)

This means that the creditor must take steps to protect itself against any opportunism of the debtor. First, the creditor will employ the device of negative covenants to impose certain restrictions on dealings which are incompatible with the floating charge and endanger the security. The principal object of negative covenant "is to ensure that the borrower remains able to fulfil its obligations under the loan contract and does not engage in conduct that would prejudice that ability". (Ferran, 2008) The "full set of negative covenants" normally found in debt contracts are "restrictions on debt", "restrictions on prior claims" "restrictions on investments", "restrictions on dividends and other payments to shareholders", "restrictions on mergers and sales of assets", "prepayment alternative", and "early warning covenants". (Bratton, 2006) Second, if the creditor is a debenture holder, secured by floating charge, the statutory provisions on crystallisation applies[67]; if it is a debt secured by a floating charge, the creditor will insert provisions on crystallisation. (Ferran, 2008)

Crystallisation is the process by which floating charge is converted into fixed (specific) security. Events leading to crystallisation can arise under statute (CAMA), by implication of the law or by agreement. Crystallisation by agreement is subdivided into automatic crystallisation events, which arises and makes the charge "to crystallise on the happening of an event provided for in the charge without there being any need for a further act by the charge"[68]; and secondly where "the charge is made to crystallise on the serving of a notice of crystallisation on the company". (Davies, 2003)[69] Generally, the events in which crystallisation can arise by agreement are:

[66] Section 179 CAMA

[67] Section 178(1)(a)-(c) CAMA

[68] Re Brightlife Ltd (supra)

[69] Re Griffin Hotel Co Ltd (1941) Ch 129

> (i) the making of a winding up order, (ii) the appointment of an administrative receiver (Nigerian equivalent is a receiver and manager), (iii) the company's ceasing to carry on business, (iv) the taking of possession by the debenture holder and (v) the happening of an event expressly provided for in the debenture. (Davies, 2003; Mayson, et al, 1987)

Although these events are similarly recognised in Nigeria, it is submitted that those events specifically provided for in the CAMA will fall under the categories of events implied by law. That is, assume those events recognised under CAMA were not so recognised, they would fall under the categories of crystallisation events implied by the law. In other words, crystallisation events implied by the law in, say the English jurisdiction, constitute crystallisation events by statutory provision under the Nigerian legal system.

In this connection, the floating charge will crystallise by express provision of the law in Nigeria (by implication of the law in another jurisdiction)[70] if the security becomes enforceable and pursuant to this a receiver or manager is appointed, whether by the court or out of court; or the debenture holder enters into possession of such assets.[71] The floating charge will also crystallise if the company goes into insolvent liquidation.[72] The floating charge will crystallise if the assets subject to the charge are in jeopardy and the chargee approaches the court for the appointment of a receiver.[73] Where the debenture is secured by general floating charge, crystallisation will occur if the chargor ceases to carry on its business.[74] The scope of the general floating charge makes it imperative that cessation of business should be a crystallisation event.

Conversely, it is not every event that leads to crystallisation. Identifying events the occurrence of which may not bring about crystallisation, Davies (2003) enumerates that:

> Default in the payment of interest or capital are not crystallising events, although... there is no objection in principle to a charge by its terms being made to crystallise on the happening of a stipulated event of default. (Secondly) the crystallisation of an earlier floating charge does not crystallise a subsequent floating charge since the subsequent chargee may pay off the earlier charge or agree to indemnify the company which continues to carry on business despite the crystallisation of the earlier charge with respect to any liability incurred towards the earlier chargee. (Bracket mine)

As to the first condition above, it is respectfully submitted that the position might not be the same in Nigeria. While it is conceded that, in the absence of a specific provision, the chargee, rather than declare crystallisation, has the option, as a holder of an uncrystallised charge of which there is default as to payment of interest or principal, of intervening and obtaining "an injunction to prevent the company from dealing with its assets otherwise than in the ordinary course of its business", (Davies, 2003)[75] the position in Nigeria is dissimilar. When a security becomes enforceable and failure to pay the principal sum or any instalment of interest is one of them[76], the chargee can enforce the charge by appointing a receiver or entering into possession. Where he takes either step, the charge, if floating, crystallises and fixes on the assets subject to the charge.

With respect to the second condition, the Nigerian position is dissimilar if the debt is secured by "a general floating charge". Thus a debenture holder or trustee under a debenture trust deed secured by a general floating is entitled to realise the security where any creditor of the company issues a process of execution against any of its assets or commences proceedings for court-ordered winding up of the company. The provision did not specify whether the creditor is later in time or prior in time to the debenture secured by a general floating charge. This is a red line for prospective creditors. This means that it is in their interest to check the nature of interest which the prospective debtor has granted to any of its existing creditors. However, considering that the priority value of the floating charge is weak, it means that if the creditor, whether first or later in time, is secured by fixed charge or mortgage, the general floating chargee can only hope to recoup from what is left after the interest of the fixed chargee or mortgagee have been reckoned with.

5. Statutory Decrystallisation of Floating Charge

---

[70] Sections 178(1) and 208 CAMA

[71] Section 178(1)(a)-(b) CAMA; Evans v Rival Granite Quarries Ltd (1910) 2 KB 979

[72] Section 178(1)(c) CAMA; Re Crompton & Co (1914) 1 Ch 954; Re Panama (supra).

[73] Section 180(2) CAMA

[74] Section 209(2)(c) CAMA. Re Woodroffes (Musical Instruments) Ltd (1986) Ch 366

[75] Re Woodroffes (Muscial Instruments) Ltd (supra)

[76] Section 208(1)(a) CAMA

Under CAMA a crystallised floating charge can transmute (refloat) to become a deemed floating charge, hence the preferred name '*contingent specific charge*'[77]. A contingent specific charge is a floating charge that, following crystallisation, has become specific on the company's assets as are subject to the as-created floating charge but which can transmute from its crystallised state to floating charge under certain conditions.[78] Except it transmutes or refloats, the contingent specific charge has the same characteristics with as-created fixed charge. The contingent nature of the charge means that, although crystallised, the story may not end there.

Thus if any of the statutorily permitted circumstances supervenes which allows transmutation (refloatation), the contingent specific charge refloats to become a floating charge once again. The first condition[79] is that "*if a receiver or manager is withdrawn with the consent of the chargee, the (crystallised) charge shall thereupon be deemed to cease to be a fixed (contingent specific) charge and again to become a floating charge" (Italics mine)*. The refloatation is conditional on the consent of the chargee that the receiver or manager be withdrawn. That is, the receiver or manager is debriefed. Now, a receiver, who may be appointed out of court or by the court, is someone appointed to realise the security for the benefit of those on whose behalf he has been appointed.[80] The duty of the receiver qua receiver is to stop the business, collect the debts and realise the assets.[81] Technically, the receiver has licence to 'kill' the company. That is why abound are cases where businesses are ruined by receiverships in Nigeria (Nnadozie, 2009), or creditors short changed while pursuing the enforcement tool of receivership, or senior counsels 'apparently' protecting warring parties' interests create unwholesome scenes. (Ezeamalu, 2014) Will the receiver prod the chargee to change its mind as regards his appointment?

The second condition[82] which can give rise to transmutation or refloatation of contingent specific charge into floating charge is that *if the chargee withdraws from possession before the charge has been fully discharged, the (crystallised) charge shall thereupon be deemed to cease to be a fixed (contingent specific) charge and again to become a floating charge" (Italics mine)*. The rationale for this condition is not clear. Where the chargor has commenced discharging the crystallised charge, it means that it has taken steps to begin payment of the debt. It might as well turn out to be penny wise, pound foolish for the debtor. Consider this scenario. The debtor owed N500 million at the time the charge becomes contingently specific, and in consequence of that took steps to commence repayment. Assume that after repaying N350 million the creditor, hitherto in possession, purportedly withdrew. Is it in the interest of the debtor to agree to the withdrawal? If it does agree, it means that the transmuted floating charge carrying a lesser obligation (N150 million) will now float over the entire assets of the debtor previously covered under the original floating charge securing the initial obligation of N500 million but reduced by the repayment of N350 million. In other words, the chargor will be paying more under the transmuted floating charge since the same set of assets that secured a higher obligation under the original floating charge is made to secure a lesser obligation under the transmuted floating charge.

Or will the debtor request for total restructuring of the entire facility by way of the creditor advancing further credit, or reducing the scope of assets that secure the lesser obligation under the transmuted floating charge? If this option is pursued, it means that a new charge will have to come into effect, and will consequentially require registration, being a new registrable charge.[83] But if the debtor/chargor accepts the purported withdrawal from possession by the chargee, the transmuted charge will not require fresh registration since it is statutorily deemed. Albeit it is said to be useful but dangerous because it creates artificiality, the word 'deemed' treats something as if it has qualities that it does not possess. (Garner (Ed), 1999) Thus by deeming it, the decrystallised (or transmuted or refloated) floating charge never transmuted. It is always present and existing in its pre-transmuted form, i.e., as-created floating charge. The debtor may opt for the former since vacation of possession by the creditor gives the debtor reprieve, albeit temporarily, to carry on its business and to channel resources to more critical areas as against payment of debts which will not add to firm value.

Critically, the contingent specific charge can be a source of legal problems. On this two questions are addressed, namely (a) what will be the priority status of the now refloated floating charge (deemed floating charge) as against a floating charge created immediately prior to the transmutation; and (b) what will be the relationship between the contingent specific charge and as-created fixed charge that predated the refloatation and one which

[77] Hereafter the coinage "contingent specific charge" is used to refer to the "fixed equitable charge".

[78] Section 178(2) CAMA

[79] Ibid

[80] Sections 209(1), 388, 389 and 393(1) CAMA; Uwakwe v Odgowe (1989) 5 NWLR (Pt 123) 562

[81] Ponson Enterprises (Nig) Ltd v Njigha (2000) 15 NWLR (Pt. 689) 46; (2000) LPELR-6805 (CA)

[82] Section 178(2) CAMA

[83] Section 197(2) CAMA

was created post refloatation? As to the first question, the issue will turn on what date should be reckoned with as regards the now transmuted floating charge. Is it the original date of its creation or the date in which it transmuted to floating charge from contingent specific charge? Unfortunately, the law did not provide guidance as to what happens to such a charge which becomes floating by way of transmutation. One can only seek guidance from the provision respecting priority of as-created fixed charges over floating charges.[84] Where the date of its original creation is reckoned with the issue will turn on whether the third party with intervening floating charge had notice (i) of the original floating charge, or (ii) of the contingent specific charge, or (iii) of the deemed floating charge.

(1) Third party with intervening floating charge had notice of the original floating charge. Where the third party had notice of the original floating charge and since the transmuted charge is a deemed floating charge, the third party will lose priority. This means that, with notice, the deemed floating charge will take priority over the third party intervening (new) floating charge, even if the third party took for value. This is because the transmuted floating charge is always DEEMED to be floating and not otherwise.

(2) Third party with intervening floating charge had notice of yet-to-refloat contingent specific charge but not of the original floating charge. Where third party had notice of the contingent specific charge, and still accepted the grant of encumbrancing floating charge by the debtor, it is submitted, that the intervening floating charge will still lose priority. This is because in that state it can be equated with as-created fixed charge. And we know that, subject to conditions, as-created fixed charge will never lose priority to floating charge.

(3) Third party with intervening floating charge had notice of the refloated floating charge but not of the contingent specific charge. The third party might have acted innocently when it provided the fund with which repayment of N350 million was made to the original creditor with the contingent specific charge. The relation back effect of the transmuted floating charge, as a deemed floating charge, will significantly improve the position of the deemed floating chargee. This means, it is submitted that the third party will still lose priority.

Generally, the above analyses call for caution on the part of creditors. They have self-interest duty to investigate the status of the assets which the debtor presents as security for the proposed facility. Failure to discharge this duty can erode the sustainability of their businesses. Thus, they can improve their position by extracting counsel's clause from the debtor to the effect that the assets furnished for security are not in any way encumbered by reason of any charge of whatever character or complexion. A later creditor can still safely lend in the presence of floating charge which has not become a contingent specific charge. The creditor who lends in the presence of a floating charge may insist on other forms of security other than fixed or floating charge.[85]

Moreover as to the second question, if the as-created fixed charge was made before the original floating charge (now contingent specific charge), it will have priority. If it was created on the day the original floating charge attached and became a contingent specific charge, it will lose priority because it is coming later in time to another fixed (specific) charge (albeit it is contingent). On the other hand if the as-created fixed charge is created post-transmutation of the contingent specific charge, the position of CAMA will be resorted to. Accordingly, since it is a fixed charge *ab initio*, it will have priority over the deemed floating charge. This is because as soon as one of the two conditions for transmutation is met, the contingent specific charge changes its character and becomes deemed floating charge. Subject to two conditions, the deemed floating charge as against the post refloatation as-created fixed charge can still have priority.

One, there must be a stipulation in the deemed floating charge, and that stipulation must not be an afterthought (that is, it must have been part of the conditions of the original floating charge, now refloated or deemed floating charge) which prohibited the company from granting any later charge having priority over the transmuted floating charge. Two, the post transmutation as-created fixed chargee must have had actual notice of that prohibition at the time when the charge was granted to him.[86] Without such notice, his equities will not be affected in any way and he will sustain a claim to priority. Having met the two conditions, it is submitted that the

---

[84] See section 179 CAMA

[85] The later creditor cannot ask for fixed charge since its position becomes precarious where the floating charge crystallises: where it has notice of the floating charge, its fixed charge will lose priority; if it does not have notice, the position still remains shaky depending on the time the fixed charge was created and the crystallisation of the floating charge. The creditor may not accept second floating charge from the debtor, as it will lose priority at all times during the pendency of the original floating charge. However, the creditor can go into a pre-acquisition agreement and subsequently accept the creation of a purchase money security interest. This effectively overrides the windfall effect of after acquired property clause in the original floating charge.

[86] Hallas v Robinson (1885) 15 QBD 288: A decision involving notice.

principle of relation back which will apply to the deemed floating charge will defeat any claim to priority of the post transmutation as-created fixed chargee.

Generally, it is submitted that contingent specific charge is a botched attempt to legislate decrystallisation or refloatation of floating charge**.** The provision failed to capture all cases that could give rise to decrystallisation. The law is silent on what happens if, after crystallisation, the chargee continued to supply the chargor goods (or to advance further credit) and allowed the debtor to trade and deal with the assets in the ordinary course. For instance, does it amount to waiver by the chargee, so that the charge is still floating? Or does the charge become specific albeit enforcement is waived, so that at insolvency the chargee's interest will be that of a fixed chargee? This enquiry is apt because allowing the chargor to continue trading while the charge is still taken to be fixed is tantamount to allowing the parties to have the best of both worlds.[87]

Secondly, the law failed to provide for what happens in respect of property acquired after a charge expressed to be a charge on present and future assets crystallises into a contingent specific charge.[88] Under the general law the security attaches immediately on acquisition of the property. However, different considerations apply where a later creditor provided the finance for the acquisition of the asset on the security of the asset itself. Known as purchase money security interest (PMSI), the position in our legal system is that the PMSI cannot defeat the after-acquired property clause, except there was a pre-acquisition agreement which effectively ensures that there is no *scintilla tempori*[89] when it could be said that the asset was the unencumbered property of the debtor. In fact the position of the law on after-acquired property clause as against the PMSI remains one of the problems which our legal system, like its English counterpart, has failed to resolve. On the other hand, in the United States, the shortcomings of the PMSI in the face of an after acquired property clause do not obtain. In that jurisdiction the PMSI, accorded super priority ranking status under Article 9 of the Uniform Commercial Code, ranks, subject to conditions, in priority over after acquired property clause (See, McCormack, 2004; Gilmore, 1962-1963).

6. Conclusion

To be sustainable a business must efficiently manage, among other indices, its financial risks, obligations and opportunities. When a company (creditor) extends credit to another company (debtor) and asks for security, it seeks to hedge against the risk of non-payment. On the other hand, when the debtor makes its assets available for repayment of the credit, it cashes in on an opportunity to grow its business. By this simple transaction the parties are engaging in activities with the view to keeping their businesses sustainable. However, in Nigeria if the debt is secured by floating charge, both parties will be caught in the web of an ill-wind. To the debtor whose property and undertaking constitute the subject of the floating charge, especially where it has commenced repayment before the creditor purportedly withdraws from possession, it blows, in all fierceness, adversity and absurdity; and to the creditor, the beneficiary of the interest created by the subject matter of the floating charge it fans the brutal ember of uncertainty as to priority. In other words the statutory provision is mutually impairing and dysfunctional to business sustainability. On the whole, the statutory provision has unsuccessfully failed to make for a commercially efficient case for transmogrification of a crystallised floating charge. Since the basic legal principle remains *lex nil frustra facit***,** the law does not act in vain, this legislative *faux pas* could be remediated by businesses being ingenious in crafting debt contracts involving floating charge with the view to tamp down the harshness of the provision or by legislative excision of the offending provision. Either way, the objective must be to ensure that the sustainable outlook of businesses in Nigeria remains unquestionable when they engage in a debt transaction, the repayment of which is secured by proprietary interest created by floating charge.

References

Addy, C. (2010). Fixed and Floating Charges over Book Debts – the Implications of the House of Lords' Decsiion in Re Spectrum Plus Limited (2005) UKHL 41, Part 1. *International Corporate Rescue (Special Issue)*. Retrieved from http://chasecambria.com/site/journal/article.php%3FiD%3D219

Beale, H., Bridge, M., Gullifer, L., & Lomnicka, E. (2012). *Law of Security and Title-Based Financing* (2nd ed.). Oxford, UK: Oxford University Press.

Bratton, W. W. (2006). Bond Covenants and Creditor Protection: Economics and Law, Theory and Practice, Substance and Process. *European Business Organisation Law Review, 7*, 39. http://dx.doi.org/10.1017/S1566752906000395

[87] Agnew v Inland Revenue Commissioners (supra) and Re Spectrum Plus Ltd (supra)

[88] Re Anglo-Austrian Printing & Publishing Union (Brabourne v the Company (1895) 2 Ch 891; NW Robbie & Co Ltd v Witney Warehouse Co Ltd (1968) 1 WLR 1324

[89] A second in time

Chiu, I. H-Y. (2006). The Fabrication of Security Interests in the United Kingdom. *North Carolina Journal of International Law, 31*, 703.

Davies, P. L. (2003). *Gower & Davies' Principles of Modern Company Law* (7th ed.). London, UK: Sweet and Maxwell

Ezeamalu, B. (2014). Babalakin, Agbakoba in war of words over judge's ruling. *Premium Times.* Retrieved from http:premiumtimesng.com/news/top-news/168864-babalakin-agbakoba-in-war-of-words-over-judges-ruling .html

Ferran, E. (2008). *Principles of Corporate Finance Law*. Oxford, UK: Oxford University Press.

Garner, B. A. (1999). *Black's Law Dictionary* (7th ed.). St Paul, Minn: USA: West Group.

Gilmore, G. (2962-2963). The Purchase Money Priority. *Harvard Law Review, 76*, 1333. http://dx.doi.org/10.2307/1338417

Gough, W. J. (1978). *Company Charges.* London, UK: Butterworths.

Gough, W. J. (1987). The Floating Charge: Traditional Themes and New Directions. In Finn, P. D. (Ed.), *Equity and Commercial Relationships.* In Ferran, E. *Principles of Corporate Finance Law.*

Gullifer, L. (Ed.). (2012). *Goode on Legal Problems of Credit and Security* (4th ed.). London: Sweet and Maxwell.

Gullifer, L., & Payne, J. (2006). The Characterisation of Fixed and Floating Charges. In Getzler, J., & Payne, J. (Eds.), *Company Charges: Spectrum and Beyond*. Oxford, UK: OUP.

Gullifer, L., & Payne, J. (2011). *Corporate Finance Law: Principles and Policy.* Oxford, UK: Hart.

Haque, AKM M. (2006). The Floating Charge as a Security Device. *University of Western Sydney Law Review, 10*(2). Retrieved from http://austlii.edu.au/au/journals/UWSLRev/2006.6.html

Mayson, S.W., French, D., & Ryan, C. (1987). *Mayson, French & Ryan on Company Law* (4th ed.). London, UK: Blackstone.

McCormack, G. (2004). *Secured Credit under English and American Law.* Cambridge: CUP. http://dx.doi.org/10.1017/CBO9780511494789

McKendrick, E. (Ed.). (2010). *Goode on Commercial Law, 4th edition.* London, UK: Penguin

Michael, S. (2009). *The Eye of the Law: Two Essays on Legal History.* Oxford, UK: Birbeck.

Mokal, R.J. (2003). The Floating Charge – An Elegy. In Worthington, S. (Ed.), *Commercial Law and Commercial Practice.* Oxford, UK: Hart. Retrieved from http://ssrn.com/abstract=386040

Moss, G. (2006). Fictions and Floating Charges: Some Restrictions on the House of Lord's Decision in Spectrum. In Getzler, J., & Payne, J. (Eds.), *Company Charges: Spectrum and Beyond.* Oxford, UK: OUP

Nnadozie, E. (2009). Police at war with bank, receiver manager. *The Vanguard Newspaper*. Retrieved from http://vanguardngr.com/2009/11/police-at-war-with-bank-receiver-manager/

Onamson, F. O. (2015). A Case for the Negative Pledge Clause as a Restraint to the Principle of Discrimination by Exclusion of Unsecured Creditors in Nigeria. http://dx.doi.org/10.2139/ssrn.2647214

Onamson, F. O. (2016). *An Appraisal of the Legal Framework for Creditor Protection in Nigeria* (Unpublished PhD Thesis). Ahmadu Bello University Zaria, Nigeria.

Pennington, R. R. (1960). The Genesis of the Floating Charge. *Monthly Law Report* 23. http://dx.doi.org/10.1111/j.1468-2230.1960.tb00630.x

Pennington, R. R. (2001). *Company Law.* London, UK: Butterworths.

Sealy, L. S., & Hooley, R. J. A. (2009). *Commercial Law: Text, Cases and Materials* (4th ed.). Oxford, UK: Oxford University Press.

Smith, A. (2012). *Wealth of Nations.* Hertfordshire, UK: Wordsworth.

Westbrook, L. J. (2004). The Control of Wealth in Bankruptcy. *Texas Law Review, 82*, 795. Retrieved from http://ssrn.com/abstract=518802

Worthington, S. (1996). *Proprietary Interests in Commercial Transactions.* Oxford, UK: Clarendon Press.

Worthington, S. (2006). Floating Charges: Use and Abuse of Doctrinal Analysis. In Getzler, J., & Payne, J. (Eds.), *Company Charges: Spectrum and Beyond.* Oxford, UK: OUP.

Worthington, S. (2010). An 'Unsatisfactory Area of the Law' – Fixed and Floating Charges Yet Again. *International Corporate Rescue (Special Rescue)*. Retrieved from http://chasecambria.com/site/journals/article.php%3FID%3D110

Copyrights

Copyright for this article is retained by the author(s), with first publication rights granted to the journal.

This is an open-access article distributed under the terms and conditions of the Creative Commons Attribution license (http://creativecommons.org/licenses/by/4.0/).