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Enhanced Protection for Secured Creditors in a Winding Up under CAMA 2020¹

Introduction

A liquidator appointed in the winding up of a company has an arduous duty to take into his custody, or under his control, all the assets of the company being wound up. This is with a view to disposing these assets and applying the proceeds therefrom towards settling the liabilities of the company in line with the statutorily defined order of priority. In a winding up by the court, in particular, the language of the law makes the power of the liquidator in this regard so wide that he is empowered to take into his possession “**all the property and choses in action to which the company is or appears to be entitled.**”²

In view of the wide spectrum of the language of the law used above, the asset gathering by a liquidator may sometimes encroach on assets that are subject to security in favour of some creditors, so long as it appears to the liquidator that the assets belong to the company. This has led to the raging war we see in insolvency practice between secured creditors (and by extension the receivers appointed by them to enforce their security) and liquidators. More often than not, it happens that the persons appointed liquidators of companies either (i) do not have sufficient knowledge of the law on the subject, particularly as it relates to the place of secured creditors in a winding up, or (ii) deliberately ignore the provisions of the applicable law. Much of this problem was caused by the passive manner in which the issue—the place of secured creditors in a winding up—was treated under the Companies and Allied Matters Act, Cap C 20, LFN 2004 (the old CAMA). The old CAMA appears not to contain any direct provisions that clearly distinguished and protected secured creditors.

¹ Companies and Allied Matters Act, 2020. And in this article, references to CAMA, *simpliciter*, are references to the Companies and Allied Matters Act, 2020.

² Section 586 of the CAMA

Section 867

of the CAMA defines "secured creditor" as "a creditor who has been granted a security interest in any property, asset or assets for the purpose of securing the performance of a debt or guarantee obligation."

It is (and has always been) understood that secured assets—assets subject to fixed charges—do not come within the insolvency estate and as such do not form part of the pool of assets to be gathered by the liquidator for general distribution to creditors.³ The assets could be dealt with by the creditor in whose favour the security is created by way of enforcing the security save for where the creditor chooses to surrender his security and join the queue of creditors to prove his debt before the liquidator. However, under the old CAMA, there were really no clear provisions to that effect. Worse still, section 403 of the old CAMA was specific that any attachment, distress or sequestration of any asset of a company being wound up would be void. This further placed a hurdle in the way of secured creditors in enforcing their security during winding up.

It was therefore necessary to insert some more definitive provisions in the CAMA to give secured creditors the status and comfort they deserve in an insolvency situation. That is what the Companies and Allied Matters Act, 2020 (the new CAMA or CAMA 2020) has done to some appreciable extent. This article will highlight key provisions of the new CAMA side by side with the provisions of the old CAMA to bring the effects of the new provisions to the fore. The aim is to enlighten secured creditors (particularly financial institutions who are in the business of lending), liquidators and insolvency practitioners on these innovations introduced by the new CAMA to make clear the rights of secured creditors as a means of avoiding or mitigating the conflicts that usually arise between secured creditors and liquidators over secured assets in winding up a company.

The innovations in the new CAMA

The relevant provisions of the new CAMA being highlighted have been juxtaposed with the provisions of the old CAMA in the box below for effective contrast and easy reference. These are the provisions that deal with (a) avoidance of attachment during winding up; (b) application of same rules to the rights of secured and unsecured creditors and (c) order of priority.

a) Avoidance of attachment, sequestration etc., during winding up:

The old CAMA	CAMA 2020
<p>Section 497</p> <p><i>Where a company is being wound up subject to the supervision of the court, any attachment, sequestration or execution put in force against the estate or effects of the company after the commencement of the winding up, shall be void.</i></p>	<p>Section 577</p> <p><i>Where a company is being wound up by the Court, any attachment, sequestration, distress or execution put in force against the estate or effects of the company after the commencement of the winding-up is void:</i></p> <p>Provided the provisions of this section do not apply to a fixed charge or any other validly created and perfected security interest other than a floating charge.</p>

The material difference between the above two provisions is the inclusion of the proviso in the new CAMA. And this is to the effect that the rule against attachment or execution against the assets of a company being wound up does not apply to a fixed

³ See Sykes & Walker: The Law of Securities 5th ed. (1993) Law Book Company Ltd. Page 4

charge or any other valid security interest other than a floating charge. The legal effect of this inclusion is significant and must be of interest to a secured creditor, particularly a holder of a fixed charge. It duly recognizes and adequately preserves the right of a secured creditor—a holder of a fixed charge in this instance—to enforce his security by way of attachment, distress, sequestration or execution, notwithstanding the pendency of a winding up.

It may be said that the right of a mortgagee in a legal mortgage (which is a fixed charge) to enforce his security during a winding up was already implied in the old CAMA. An asset that is subject to a legal mortgage is, in the real legal sense, the property of the creditor (as mortgagee)⁴ subject to the company's (as mortgagor) right of redemption. However, this was only applicable to legal mortgages and not to other fixed charges. And even at that, it was not so clear under the old CAMA and was subject to a lot of legal arguments and debates, more so, when the liquidator is empowered to gather even the assets that the company appears to be entitled to. The proviso was therefore necessary and came handy to lay to rest any such debate and to shed off any fetters on a secured creditor's right to enforce his security by way of attachment, distress, sequestration or execution.

b) Application of same rules to the rights of secured and unsecured creditors:

The old CAMA	CAMA 2020
<p>Section 493</p> <p><i>In the winding up of an insolvent company registered in Nigeria the same rules shall prevail and be observed with regard to the respective rights of secured and unsecured creditors and to debts provable and to the valuation of annuities and future and contingent liabilities as are in force for the time being under the law of bankruptcy in Nigeria with respect to the estates of persons adjudged bankrupt, and all persons who in any such case would be entitled to prove for and receive dividends out of the assets of the company may come in under the winding up and make such claims against the company as they respectively are entitled to by virtue of this section.</i></p>	<p>Section 656</p> <p><i>In the winding-up of an insolvent company registered in Nigeria, the same rules shall prevail and be observed with regard to the respective rights of secured and unsecured creditors and to debts provable and to the valuation of annuities and future contingent liabilities as are in force for the time being under the law of bankruptcy in Nigeria with respect to the estates of persons adjudged bankrupt, and all persons who in any such case would be entitled to prove for and receive dividends out of the assets of the company may come in under the winding-up and make such claims against the company as they</i></p>

⁴ See *Yaro v. Arewa Const. Ltd.* [2007] 17 NWLR (Part 1063) page 333 at 368-369, paras. G-C; *Usenfowokan v. Idowu* (1969) 1 All NLR 125; *Barclays Bank of Nigeria Ltd. v. Ashiru* (1978) 6-7 SC 99

	<p><i>respectively are entitled to by virtue of this section:</i></p> <p>Provided that nothing in this section shall affect the power of any secured creditor to realise or otherwise deal with his security during the winding-up of an insolvent company registered in Nigeria.</p>
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Once again, the *proviso* in the new CAMA is the gamechanger. Under the old CAMA, secured and unsecured creditors were made subject to the same rules with regard to their respective rights and debts provable. A literal interpretation of this provision could create some difficulty for a secured creditor. It could mean that a secured creditor occupies the same pedestal as an unsecured creditor and ought to wait in line with unsecured creditors to prove his debt before the liquidator. The *proviso* introduced by the new CAMA, however, clearly acknowledges and safeguards the right of the secured creditor to realise or otherwise deal with his security during winding up without joining the queue of creditors.

It is noteworthy, however, that the right of a secured creditor under this provision must be read subject to section 577 of the CAMA. Thus, if the security is in the nature of a floating charge, it would not be possible to enforce same by way of attachment, sequestration, distress or execution in the pendency of a winding up.⁵ It is only a holder of a fixed charge, therefore, that can take the full benefit of the *proviso* in section 656 of the CAMA.

c) Order of priority:

The old CAMA	CAMA 2020
<p>Section 494</p> <p>No equivalent provision. Preferential payments ranked above secured creditors.</p>	<p>657</p> <p><i>(6) Notwithstanding the foregoing and any other provisions of this Act and any other law applicable in Nigeria where it relates to settlement of claims in the winding-up of a company, claims of—</i></p> <p><i>(a) secured creditors, as defined under this Act, shall rank in priority to all other</i></p>

⁵ By the provisions of section 203 of the CAMA, a floating charge shall be deemed to crystallise and become a fixed equitable charge on such of the company's assets as are subject to the charge upon commencement of winding up. However, to the extent that a floating has been expressly excluded by section 577 of the CAMA from the nature of charges that can nullify an attachment, sequestration, etc., during a winding up, it necessarily follows that the deemed conversion of a floating charge to a fixed charge still does not give the converted floating charge the same effect as a fixed charge for purposes of section 577 of the CAMA.

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	<p><i>claims, including any preferential payment under this Act or any other debts inclusive of expenses of winding-up; and</i></p> <p><i>(b) the equity holders shall rank last.</i></p>
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This is probably the most significant change made in the new CAMA in favour of secured creditors in insolvency. Before now, preferential payments⁶ ranked higher than all other debts in a winding up, winding up expenses being the *primus inter pares*. The new CAMA has, however, elevated secured creditors ahead of every other debt, including expenses of winding up.

Section 867 of the CAMA defines "secured creditor" as "a creditor who has been granted a security interest in any property, asset or assets for the purpose of securing the performance of a debt or guarantee obligation."

This could be in the form of a fixed charge or a floating charge. The holder of a fixed charge may elect to surrender his security and prove his debt before the liquidator. And where he chooses to enforce his security but the sum realized is not sufficient to satisfy the debt, he may prove the balance of the debt before the liquidator. In any of these cases, he will take the benefit afforded by this section—657(6)(a)—and be paid in priority to other debts, save for other secured creditors.

The new order of priority under CAMA 2020

In any form of winding up, the settlement of creditors is done in accordance with the rules of priority and ranking of claims. Under the new CAMA,⁷ the applicable order of priority and ranking of claims for the distribution of a company's assets is now as follows:

- **secured creditors:**⁸ **these are fixed charge or floating charge holders. They** are paid in priority to all other debts;
- **liquidators' remuneration and other liquidation Costs:** Liquidators' fees and expenses incurred in a company's liquidation have priority over preferential creditors and other debts save for secured creditors;
- **preferential creditors:** these are employees with labour-related claims (such as unpaid wages and contributions to occupational pension schemes) and local rates, charges and tax deductions.⁹ They rank equally among themselves and ought to be paid in full after secured creditors, unless the assets are insufficient to meet them, in which case they shall abate in equal proportions;¹⁰
- **unsecured creditors:** unsecured creditors are creditors who do not have any security interests in the debtor's assets;

⁶ These are the payments outlined in section 657(1) – (5) of the CAMA.

⁷ Section 657 of the CAMA

⁸ Section 657(6), CAMA. A fixed charge holder is a creditor that has a security over a specified asset(s) of the company.

⁹ Section 657(1), CAMA.

¹⁰ Section 657(4), CAMA.

- **shareholders:** any surplus after settling all the above liabilities goes to the shareholders according to the rights attached to their shares.¹¹

Conclusion

In sum, the new provisions of the CAMA highlighted in this article have made significant strides in protecting secured creditors in a winding up in two material respects:

- (i) for secured creditors with fixed charges, the law preserves their rights over the secured assets and duly empowers them to enforce their security even in the face of a winding up;
- (ii) for secured creditors with floating charges or creditors with fixed charges who surrender their security, the law ranks their debt ahead of every other debt, including the cost of winding up. As such, their debts are to be paid in full before every other debt.

Without doubt, these provisions of the new CAMA have greatly enhanced the rights of secured creditors in a winding up, far above what was obtainable under the old CAMA. Indeed, this has brought significant changes in insolvency law and practice in Nigeria generally. It is hoped that secured creditors will get more aware of and take the full benefit of these provisions toward realising their security without glitches in a winding up.

This article and the provisions of the new CAMA highlighted in it should be of interest to commercial banks and other financial institutions who are in the business of lending. To take full benefit of the provisions, the goal should always be to go for secured lending, preferably by way of fixed charges, to hedge against the risk associated with money lending and avoid the legal wrangle involved in securing a repayment in the event of an insolvency.¹²

¹¹ Section 657(6)(b), CAMA.

¹² See I. O. Smith: Nigerian Law of Secured Credit (2001), Ecowatch Publications (Nig) Ltd., Page 3