SECURITIES FOR BANK LENDING:

PERSPECTIVES UNDER NIGERIAN LAW.

BY

ABUBAKAR AHMED. MADUGU

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ABUBAKAR AHMED MADUGU

A Thesis submited to the Post graduate School Ahmadu Bello University Zaria, in partial fulfilment of requirement of

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Department: Commercial Law

Faculty: Law

DECLARATION

I hereby declare that this thesis has been written by me and that it is a record of my own research work. It has not been presented in any previous application for a higher degree.

All quotations are indicated and the sources of information are acknowledged by means of notes and references.

A A Madugu

ABUBAKAR AHMED MADUGU

1998.

DEDICATION

To my Late mother **Hajia Inno Abubakar Madugu** (1931-1991) and the following late friends and classmates. May their souls rest in peace - (Amin), and my father **Alh. Abubakar Madugu,** to whom I made and fulfilled a promise:

1. Altine Na Ruwa
2. Umaru Hamza Bunu (Mulale)
3. Mu'azu Buhari
4. Bello Yusuf
5. Abdullahi Muhti
6. Manu Ummaru Mungadi (Icce)
7. Sama Musa Birnin Magaji
8. Ibrahim Mohammed
9. Abubakar Mohammed (U.K)
10. Inuwa Isah Kaura Namoda
11. Aminu Mahbub Alkali
12. Abbas Mohd. Auwalu (ASCON)
13. Abubakar Ibrahim Dange
14. Hayatu Nakaka
15. Aliyu Wakili Kaura Namoda

for their impact in changing the shape of my life.

CERTIFICATION

THE THESIS TITLED, **SECURITIES FOR BANK LENDING: PERSPECTIVES UNDER NIGERIAN LAW,** by Abubakar Ahmed Madugu, meets the regulations governing the award of the degree of Master of Laws of Ahmadu Bello University, Zaria, and is approved for its contributions to knowledge and literary presentation.

DR. I. J. GOLDFACE IROKALIBE
Chairman Supervisory Committee

Date: 27/3/2007

MR. D. B. APAGU
Member Supervisory Committee

Date: _____

DR. I. J. GOLDFACE IROKALIBE
Head, Department of Commercial Law

Date: 27/3/2007

_____
Dean, Post Graduate School

Date: _____

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ABUBAKAR AHMED MADUGU.

ABSTRACT

Bank lending transactions deal solely with matters that are related with security for advancement. The importance of security in bank lending can not be over-emphasised in business relationship between both banker and customers, in present day Nigeira.

The economy has virtually collapsed or has reached a point of total collapse. Many banks are distressed currently due to the state of the economy, those that have not wound up are struggling to survive and are increasingly finding it difficult to stay on board. Rising inflation cripples both individual banks and financial institutions. These coupled with very poor wages and extreme pressure on the economy, everyone is searching for an alternative source of money. Some to shore up a collapsing business, others expand an existing one or to start a new project. The need to secure these loans has become imperative.

The sole objective of this thesis is to bring the law relating to security for banks lending under Nigeira law, in work for easy reference.

There are five chapters in this thesis. The first is a general introduction, covering the definition and the various type of securities demanded by Nigerian banks, background and meaning of securities and its general outlooks.

Chapter Two deals with land, mortgage, its meaning and use as security. It deals with both legal and equitable mortgage, the form of security that may be created in mortgages.

The third chapter discuss's guarantees, its features, and its termination. It include a discussion on securities generally.

Chapter Four treats issues such as choses in action, shares, life assurance policies, stocks, and implications to the lender in the event of a breach by the borrower.

Chapter Five is the concluding chapter and it deals with problems of the bank, solutions to the problems and the possible reforms which are desirable to sanitise the Industy.

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6. Kenyan Crown Lands Ordinance 1989.

ABBREVIATIONS

A. NIGERIAN

ALL N.L.R.	All Nigerian Law Reports.
NLR	Nigerian Law Reports.
NMLR	Nigerian Monthly Law Reports.
WNLR	Western Nigerian Law Report.
ERNLR	Eastern Region of Nigerian Law Report.
WACA	West African Court of Appeal.
NWLR	Nigerian Weekly Law Report.
NNLR	Northern Nigerian Law Report.
WRNLR	Western Region of Nigerian Law Report.
LRN	Law Report of Nigerian.

B. FOREIGN REPORT

A. C.	Appeal Cases.
ALL E R	All England Report.
Beav	Beavan.
Ch	Law Reports Chancery
Exch.	Exchaquer Reports.
E R	English Reports.
KB	Law Reports - Kings Bench.
LTR	Law Time Reports.
QB	Law Reports - Queens Bench.

Q B D	Law Reports - Queens Bench Division.
RUSS	Russel.
TLR	Times Law Report.
WN	Weekly Notes.
WLR	Weekly Law Reports.

ABSTRACT

Bank lending transactions deal solely with matters that are related with security for advancement. The importance of security in bank lending can not be over-emphasised in business relationship between both banker and customers, in present day Nigeira.

The economy has virtually collapsed or has reached a point of total collapse. Many banks are distressed currently due to the state of the economy, those that have not wound up are struggling to survive and are increasingly finding it difficult to stay on board. Rising inflation cripples both individual banks and financial institutions. These coupled with very poor wages and extreme pressure on the economy, everyone is searching for an alternative source of money. Some to shore up a collapsing business, others expand an existing one or to start a new project. The need to secure these loans has become imperative.

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Q B D	Law Reports - Queens Bench Division.
RUSS	Russel.
TLR	Times Law Report.
WN	Weekly Notes.
WLR	Weekly Law Reports.

CHAPTER ONE

SECURITIES FOR BANK LENDING:

PERSPECTIVES UNDER NIGERIA LAW

INTRODUCTION

1.1 ORIGIN OF THE PROBLEM

Due to many factors among which is lack of sufficient and wider knowledge of banking operations by the majority of banks customers, people, especially the business class, find it difficult to deal with banks in matters of loan's policy, procedures and settlement.

Sometimes strained relationship emerge between banker and customers in matters relating to banking transaction which leads to many avoidable litigations. Some of these court actions at times last for months if not years.

Loans are offered to customers some times without security or where security exists, it is inadequate to cover the amount obtained or in some cases the security given to the bank depreciate in value and the advanced sum ends up being unsecured. This type of development leads to concern on the part of the bank (and some times on the part of the customers too). The fear of loosing both capital and accrued interest then begin to affect the banker's attitude.

Due to poor performance of the national economy people and organisations which largely rely on banks financial assistance to run their businesses are faced with a lot of problems hence their inability to repay loan coupled with interest or to get new loans for their business especially with a grossly under-valued Naira.

The banking sector itself has the problem of indiscriminate growth of financial institutions. This trend has led to competition for deposit among the various institutions and as a result, high interest rates were paid for funds resulting in increased cost for the sector. Additionally regulatory instrument especially from the Central Bank of Nigeria have had stiffling effect on the banking industry.

Another factor is the persistent personalisation and politicisation of banks by their directors and those who own and control large share in them. This has created large portfolios of unsecured loans.

Banks are supposed to be the hub of economic development machine which mobilise funds and allocate them to the vital areas of the economy to ensure growth and stability, however, the reverse seems to now be the case. As a result of massive bank lending in the seventies and early eighties, many States owned banks were either distressed or have been liquidated. An example here is the National Bank of Nigeria and the Cross River State owned Mercantile Bank. The various factors highlighted above, alongside diverse other factors, have greatly affected the working of Nigeria's banking system as far as lending and borrowing are concerned. This forms the necessary background against which the present study is being undertaken, with a view to understanding more appropriately, the mechanism of security in bank lendings in Nigeria.

1.2 OBJECTIVES OF THE RESEARCH

The objective of the present research are manifold. Firstly, is to discover problems relating to inadequacy of security, default in payment and insolvency in relation to Banker/Customer relationship and bank lending. The thrust here will be to dig into the root of the problems of sufficiency of security and safety of lending, in

considering whether or not a bank should grant a loan.

Another objective of the study is to make an assessment of the performance of commercial and mortgage banks in Nigeria in their effort to make loan facility available to the borrowing public, to see how and to what extent success has been recorded in realising these objectives. It is also to assess constraints in terms of funding, personnel, bureaucracy and the public appreciation or otherwise of bank efforts and or services.

Thirdly, the research is to analyse the problems that are encountered by banks and their customers in matters relating to repayment of loans and also to find out whether or not the loans granted serve the particular purpose for which they are given. Finally, this study will also attempt to find out the extent to which the general public, especially the rural dwellers, and or the commerce oriented members of the society appreciate the impact or otherwise of the present security demands of banking institutions, especially with government placing more emphasis on small scale industries due to the need of the general public particularly the rural dwellers.

1.3 PROBLEMS ENCOUNTERED

Modern banking was introduced into Nigeria as far back as 1894, when the Bank of British West Africa was founded. Some banks followed later among which are the Barclays Bank (now called Union Bank). In Nigeria, we now have different banks, both commercial and merchant types.

One of the research problem is that not much information was forthcoming from the banks for some reasons of commercial interest. Where such persons whom outsiders consider to be persons in authority like the branch manager or a director, these were less co-operative in divulging information. The bank staff are not co-operative also for fear of divulging information that is regarded or considered as sensitive.

In some cases, the researcher is directed from one senior officer to another, each trying to avoid responsibility for leaking the bank's secret. Sometimes, the researcher ends up meeting an unco-operative officer and some information given is the type that one can easily find in the pages of newspapers or listen to over radio and television. Public reaction to questions is also another problem; some members of the public are reluctant to respond to enquiries.

At times, banks make a particular disclosure on condition that the material or information given should not be used in reference to that particular bank in-question (that disclosure or revelation should be used with reference to all banks in general.

Information problem apart, there is also the problem of government as banking policy guideline relates to its operations. This is an area where most banks are not ready to co-operate; example, State owned banks. One may find that in some of these banks, the government which is the initiator of the bank hold as little as less than ten percent of the total share holding while the rest of the shares held by individuals are larger in proportion than that of the government which claim to own the bank, in such case, no bank is ready to volunteer information as regard to the powerful interest involved. In such situation, one can only rely on information obtained through private contacts which in most cases of course is anonymous.

1.4 METHODOLOGY OF THE RESEARCH

In the course of Research information on the state of the banking industry in matters relating to loan, the researcher adopted method of extracting genuine information from the relevant sources, like opinion seeking in both academic and non-academic areas.

Other sources which include published texts, bank records, seminar papers, and journal publications will be consulted for additional information.

At the branch office of some of the banks, some who expressed their opinion insisted that they might not want to be quoted either in praise or in criticism.

1.5 LITERATURE REVIEW

The researcher made references to the works of authors in banking law, J. Milnes Holdens Law and practice of banking Vol. 2 (7th edition) Holden deals with Bankers Advances. And like Drover, Paget & Chorley, his work is not universal. This is so because his works are strongly based on British banking system of operation, which tend to exclude other systems and where reference is being made to such system it is in relation to the European common market thus, these works proved immensely of assistance to this research work.

For the purpose of this topic, emphasis is on the Nigerian System of bank lending under Nigerian law. This is because even though Nigeria operates English law in its system, from the time of independence to date, there are some Nigerian laws that have replaced English laws and as such, preference is to be given to Nigerian laws.

As an instance in the book written by Perry, Element of Banking[2]; the author dwelt on the topic "lending against security" based strictly on the British aspect of lending against security with little or no consideration for Nigerian system of lending. Even though Nigeria was a British colony, still some features of British banking system do not apply to the system of bank lending in this country. Farming advances in Britain is not the same with what is obtained in Nigeria because, some items produced by farmers like eggs and milk are sold to a controlling body, like the Milk Marketing Board and so on. In Nigeria, such bodies are not in existence. Also Perry is of the views that things such as seasonal lending as applicable in Britain does not apply in Nigeria. In

Nigeria, there are no bodies as exist in Britain like the Agricultural Development, Advisory Service and the National Agricultural Advisory Service (NAAS).

Femi Adekanye's book "A practical guide to bank borrowing[3]" gives more emphasis on Nigeria Banking System. He has dealt extensively with the types of loans banks advance to individuals and organisations alike. His book was not exhaustive enough as to cover all aspects of securities for banker's advances. Infact, he did not go into details as such, references were also made to the various types of securities and at last made explanatory comments to bank borrowing generally.

While some other authors dwell extensively on the bank borrowing system, another Nigerian author, Omolaja A. Adeniji[6] in his book which deals with bond, guarantees and indemnities discusses different types of guarantees including women guarantors.

Other writers whose work the researcher consulted include J. Milness Holden[7] Sheldon Fidlers - Practice of law and banking[8] and the subsequent editions by the same author[9] all of which proved helpful one way or the other.

1.6 ORGANISATIONAL LAYOUT

In this work, the researcher intends to discuss in full details, about securities for bank lending under Nigerian law. Chapter One consists of general introduction, background to the study of securities and the general outlook of various types of securities. It provides an insight into the objectives of the study, the problems of research, review of literature and an organisational layout.

In Chapter Two, land would be discussed generally, its meaning and land as security. Special features to be discussed include mortgages and its discharge.

Chapter Three discusses guarantee. This will include features of guarantee, joint and several guarantees, liability of guarantors and termination of guarantees will also feature prominently under this chapter.

Chapter Four deals with other forms of securities. These includes assurance policies, stock and shares.

Chapter Five are the recommendations and conclusions.

NOTES AND REFERENCES ON CHAPTER ONE

1. See generally, Perry, P.E. Elements of Banking (Mathvem, London) 4th ed. 1975.
2. See generally, Adekanye F. Practical guide to bank borrowing (July, 1983) (IUP Ibadan) 1983.
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6. J. Milness Holden - the law and practice of Banking, Vol.1, (Bankers and Customers) 4th edition (ELBS) Pitman (1970).

CHAPTER TWO

LAND

2.1 LAND

The most common form of security taken by creditors is land or landed property. This is so because, it is convenient. Land form that type of property known as realty or real property.

For long, property was deemed real if the court restored to the dispossessed owner that thing itself, i.e. the 'res' and not merely give compensation for the loss.

Under English law, with the exception of leases, all interests in land are real property.

This exception was necessary as to leases due to the fact that by their nature, leases were foreign to the feudal system of land holding by tenure under which the economic and social status of societal member was fixed. Leases were for long regarded as personal business arrangements by which a party allows the other the use of his land in return for rent. Thus, they were contracts operating in personam and not creating right in rem. However, as time went by, new recognition was given to leases as interest in land and not merely contractual rights. Land has been defined to include not only the surface of the earth's crust, but include the minerals found in and below the flora and fauna that subsists upon it. The water supplies, it carries and the atmospheric advantage it enjoys.[1]

Another definition of land is that under the Property and Conveyancing Law of Western Nigeria[2] where land was defined as "Land of any tenure, building... or parts of building (whether the dimension is horizontal or vertical or made in any other way) and other corporeal hereditaries, also-ren and other incorporeal hereditaries and on easement, right, privilege or benefit in, over or derived from land. Because of its indestructibility, land is the basic form of wealth and land has been the principal source

of wealth. Land may be transacted for money as in mortgages, pledges or charge.

The nature and concept of mortgage is not easy to delineate. However, a mortgage is the transfer of a legal or an equitable interest in land as other personal property as security for a debt or for the discharge of an obligation. The legal mortgagee has the right to enter into possession of the property where the borrower defaults but has to apply to court for an order of foreclosure. He can also sell the property, appoint a receiver of rents or sue the debtor. But note, he may only resort to these if he is partly secured and desires to obtain judgement so as to issue a bankruptcy notice. Ekwo Sunday[3] submits that: "Security may be created over lease hold interest first, by the assignment of the whole unexpired term with provision for redemption and secondly, by sub-demise i.e. the granting of a term of years to the mortgage less by one day or a few days than the actual term of the lease".

In a pledge, the pledgee may in certain circumstances have the power of sale but the amount in the pledgor is subject to the pledgee's rights. A pledge is a security based on possession. The difference between a mortgage and a pledge is that the security of a mortgage is the ownership of the thing, while the security of a pledge is its possession. The case of **RYALL VS ROLLE**[4] provides for the distinction. This distinction is that the pledgee gets no absolute title at law. He gets what has been called a "Special property" in the property, the subject of the security, while the pledgor retains the general ownership. The rent charge is also a security whereby the payment of an amount is charged on land, so that the sum secured does not rise out of a relationship of landlord and tenant. But note that where sum is merely made payable out of personal estate other than lease hold, it is referred to as an annuity but if charged on land it's a rent charge.

The distinction between a mortgage and a charge is that a charge coveys nothing and merely gives the chargee certain rights over the property as a security for the debt,

while on the other hand, a mortgage is a conveyance of property subject to a right of redemption. Despite these differences, there are certain advantages of a charge. These advantages are to the effect that a legal charge is a convenient way of mortgaging the now non-existent lease hold. This means that one can shorten by stating that all the property in the schedule are charged by way of a legal mortgage.

It may be that, the granting of a legal charge on a lease does not amount to a breach of any covenant in that lease against subletting, for the charge create no actual sublease in favour of the charges, but only gives him the same rights as if he had a sublease. But note that a judicial decision[5] to the effect that, where the covenant in-question also prohibits the tenant from parting with possession of the property, there will be a breach where or if the chargee enforces his right of possession.

2.2 MORTGAGES

2.3 Definition

The statement of Lindley, M.R. In **SANTLEY VS WILDE**[6] approved in **NOAKES VS RICE**[7] that "a mortgage is a conveyance of land or an assignment of chattel as a security for the payment of a debt or the discharge of some other obligations for which it is given".

A mortgage is a form of security created by contract which confers an interest in property defeasible upon performance of the condition of paying a given sum of money with or without interest or of performing some other conditions.[8]

Another academic definition which was proferred is that:-

"... A mortgage in the modern acceptation of the term
in this country (England) is a security created by
contract for the payment of a debt already due or to
become due, or a present or future advance effected
by means of an actual or executory conveyance of real

or personal property charging the mortgaged property with the payments of the money secured, redeemable at Law only according to the strict legal condition of the conveyance but redeemable in equity independently of such condition and enforceable in default of payment by foreclosure or sale in lieu thereof"[9].

It can be deduced from this definition that a mortgage arises only out of contract and it suggests the remedies available to the creditor in case of default by the debtor.

The essential nature of a mortgage is that it is a conveyance of a legal or equitable interest in property with a provision for redemption. This distinguishes mortgage from a gift or a sale. It may be noted, however, a contract between a vendor and purchaser cannot be a mortgage even though there can be contract of sale between a debtor and a creditor. In case of insolvency by the mortgagee, the mortgagee may fall back on the security. But when there is payment, the property goes back to the mortgagor.

Legal mortgage involve execution under seal and the transfer of legal title to the mortgagee. But the transfer of the legal title is not absolute, it is however subject to the mortgagor's right of redemption as the maxim says: once a mortgage, always a mortgage, and any provision to the contrary which extinguish or exclude the right of the mortgagor to redeem the property subsequently after payment of the loan is null and void.

2.4 THE NATURE OF A MORTGAGE

A mortgage, may be either legal or equitable. In an equitable mortgage, the mortgagee takes possession of the title deeds evidencing the transactions while the property continues to remain in the mortgagor's possession. A legal mortgage is created

by a demise for a term of years absolute subject to a provision for a ceaser or redemption or by a "charge" by deed expressed to be by a way of a legal mortgage[10].

It may be noted that at common law, a mortgagor would forfeit his contractual right to redeem his land as soon as he defaults in payment but under equity, a debtor is allowed to redeem after the stated date of redemption once he repays the loan and interest due, including costs. In **OLOWU VS MILLER BROTHERS**,[11] a document which the plaintiff contended was a mortgage of his property to the defendant firm, which had insisted that it was conditional sale, it was proved that the plaintiff within a five year period redeemed his property on repayment of the amount of the loan of £2,400 to the defendant firm and that, the defendant firm should be granted a lease at a rent not exceeding £150 per annum. It further provided that failure to redeem within the period, absolute ownership of the land should be vested in the defendant. The plaintiff in the case failed to redeem within the stipulated time, but soon afterwards offered to repay the total amount and recover his property which he said is nothing more than security for the loan. The court held **(Pennington J)** that the amount of the loan and certain affirmation of the plaintiff led the court to have the impression that a conditional sale and not a mortgage was originally contemplated by the parties and the Judge went on to define mortgage as a security created by contract for the payment of debt, already due or to become due. Also in **SAMUEL VS JARRAH TIMBER CORPORATION**.[12] The doctrine "once a mortgage always a mortgage still applied".

Lord Maghnaghten in **NOAKES VS RICE**.[13] said the right to redeem the property mortgaged is therefore the very nature and essence of a mortgage", which means a collateral stipulation with purposes for a long period of which denise the mortgagor the right to redeem is void. In **NOAKES VS RICE**,[14] there was a lease hold involving a public house. The mortgager covenanted with the mortgagee that he and

his successors and assignees would not during the continuance of the term use or sell in the public any liquors except such as should be purchased from the mortgagee. The court held this covenant to be a clog on the equity of redemption and that the mortgager was; entitled to reconveyance of the property on payment of all that was due upon the security.

The court may not allow an unquestionable advantage in a mortgage, for instance, like an excessive premium which is unfairly imposed. In the case of **CITYLAND & PROPERTY HOLDINGS LTD VS DABRAH,**[15] a house was sold to a tenant by a company, the tenant advanced £2,900 under a mortgage agreement which required a payment of £4,553. The court held that the balance of the premium is an unreasonable and unquestionable collateral advantage, and that by making the charge exceed the value of the house, it makes the equity of redemption valueless. The court went ahead to declare that the mortgagor was entitled to redeem by paying £2,900 with reasonable interest fixed by the court. It may be noted however, that a collateral advantage cannot be objected to simply because, it is unreasonable. It must be unfair and unconsciounable. For instance, where there is element of undue influence or inequality in bargaining, a clog on the equity of redemption, may come in different ways, one of which is, it may arise by way of indefiniteness of the redemption date or even excessive premium as in the case of **CITY LAND AND PROPERTY (HOLDINGS) LTD VS DABRAH**[15(b)] and making it extremely difficult for the mortgager to redeem.

However, there is harm if, (especially in-long-term loans) the equity of redemption is postponed for a long period of time but the most important thing is that a mortgage is always a mortgage and cannot be made irredeemable.

2.4.1 TYPES AND CREATION OF MORTGAGES

There are two types of mortgages, i.e., legal mortgage and equitable mortgage. In law, legal mortgage involves execution under seal and the transfer of legal title from the mortgagor to the mortgagee. But the transfer is not absolute, it is however, subject to the mortgagor's right of redemption.

2.4.2 LEGAL MORTGAGE

A legal mortgage involves execution under seal and the transfer of legal title from the mortgagor to the mortgagee. This means a legal mortgage is a conveyance or assignment of the whole or part of the estate or interest of a debtor in real property of which he is the legal owner or which has the power to transfer. However, this conveyance/assignment must be as provided for within the provision of, for example, the law of property of former Western Region.[16]

Mortgages of right of occupancy are effected to either of the two ways viz:- a charge by deed expressed to be by way of legal mortgage, or a sub-lease for a term of years subject to a provision for cesser of redemption.

However, the essence of the legal mortgage is the vesting of a legal estate in the mortgagee, together with an immediate right of possession.

The legal mortgage must follow the requirement of the law, it must be created by a deed.

2.4.3 EQUITABLE MORTGAGE

Unlike a legal mortgage, an equitable mortgage does not convey a legal estate to the mortgagee. Equitable mortgage is a charge in favour of a person applicable to both freehold and lease hold. The essence of any transaction by way of mortgage is that a debtor confers upon his creditor a proprietory interest in property of the debtor; or undertake in a binding manner to do so by the realisation or appropriation of which the

creditor can procure the discharge or the debtor's liability to him and that the proprietor's interest is redeemable or the obligation to create it is defeasible, in the event of the debtor discharging his liability. An equitable mortgage, is a contract which operates as a security and is enforceable under the equitable jurisdiction of the court.

Banks sometimes take second mortgage as security but they are not generally looked upon with great favour. Nonetheless, banks will certainly take second mortgage, because, as it may turn out that there is a reasonable equity. For instance, a property mortgaged where current value is well in excess of the outstanding mortgage or sometimes as support for a shaky advance even though in some cases, the equity may be dubious. One can say that the distinctive nature of the equitable mortgage, is that it is an agreement to enter into a legal mortgage. Anything that can be interpreted as such an agreement will constitute an equitable mortgage.

Hence, the mere fact that a party deposited a title deed or a mortgage that is executed under hand only, will be an equitable mortgage. This is so, because the deposit of title deeds is implied by law, as a contract to create a mortgage if the mortgagor deposits them as security for a loan, the fact that nothing is said about such a mortgage notwithstanding. In the case of **OLUFINTUYI VS BARCLAYS BANK D.C.O. LTD.**[17] **and BARCLAYS BANK VS ASHIRU,**[18] the court had no difficulty in treating the deposit as an act of part performance of the agreement. It may be noted that equitable mortgage carries the rights of a legal mortgage since equity takes as done that which ought to be done. Specific performance of the agreement can be obtained by an equitable mortgage just like the legal mortgages. In the case of **ASHTON VS. CARRIGAN,**[19] the court effected this by giving the creditor the appropriate remedies or by compelling the debtor to execute a security in accordance with the contract. Also

before the contract to create an equitable mortgage becomes enforceable; the mortgagee must have usually advanced the money, whether the contract is endorsed or not, otherwise it is a mere agreement for a loan which none of the parties can enforce by equitable remedy of specific performance[20] as decided in the case of **RUDGERS VS CHALLIS**.[21]

2.4.4 MECHANISM OF MORTGAGE AND CONSENT PROVISIONS UNDER THE LAND USE ACT 1978

A holder of a right of occupancy is not allowed to sell, lease or alienate his right either by way of assignment or mortgage or transfer of possession whatsoever without the appropriate approval of such by the State Governor or by the Local Government Authority as the case may be.[22] It may be noted that section 22 of the Land Use Act provides that the consent of the Governor shall not be required for the creation of a legal mortgage over a statutory right of occupancy in favour of a person in whose favour an equitable mortgage over the right of occupancy has already been created with the consent of the Governor of a State.[23]

Hence, it is submitted that as Section 51 of the Act defines "mortgage" to include equitable mortgage, as such consent provisions affect both legal and equitable mortgages, except whereas (note Section 22 (a) there was a prior consent granted for the creation of an equitable mortgage which is now intended to be converted in to a legal mortgage). It should be noted that for all types of occupancy, the consent of the relevant authority is a pre-requisite requirement prior to any alienation, but under sections 36 and 34 of the Act, persons that are holders of a deemed grant require no consent for alienation of their rights. But this assertion was deemed to be wrong as decided and as confirmed by the Supreme Court in the case of **SAVANNAH BANK**

VS AJILO[24]. In essence, sections 21 and 22 of the Land Use Act 1990 grant the holders of a right of occupancy a right to alienate but securing the consent of the Governor or Local Government Authority is a condition precedent as the case may be. But such Judicial decisions raised more questions than answers, as for instance at what time or state of the transaction is the consent ought to be sought and when and at what stage can one say an alienation takes place or there is an alienation. Is it when the consent has been obtained or prior to that or what? And finally, what is the effect or implication of an alienation which is done without the consent of the Governor or Local Authority as the case may be. In trying to answer these questions, we have to consider the provisions Section 26 of the Land Use Act which provides that:-

> "Any transaction or any instrument which purposes to confer on or vest in any person any interest or right over land other than in accordance with the provision of this ACT shall be null and void".

Yakubu M.G. notes that "any grant to a right of occupancy or creation of mortgage, lease, transfer of possession and the like which is not done in line with the provision of the ACT is null and void".[25]

But we should note that the transaction is not illegal only that it is unenforceable and either party can repudiate it and absolve himself of any liability arising under it. Whatsoever where it is repudiated, money paid by the mortgager can be recovered as money had and received, but a transferor who repudiate is under an obligation to console for any improvement made by the transferee on the land.

Securing the consent of the Governor or the Local Authority as the case may be, is the most positive part of the provisions of the law but it may be that its essence is to

bring the whole of the land under the government to prevent its abuse by other traditional title holders or Local Speculators, also to ensure that, citizens have a share in the use of the land through grants by the Governor or the Local Authority a the case may be, and in public interest and for good policy, private land rights is subjected to over-riding public interest.

The Land Use Act is aimed at achieving certain objectives.

First, it is to eliminate conflict in respect of land ownership which leads to communal clash, strife and boundary disputes. Second, it is to check land speculation in the country. Third, it checks litigation and simplifies the management and ownership of land. Fourth, it eases the administration of land under the Act itself.

A tendency by the rich to deprive the poor of the land in their possession will lead to accumulation of land in the hands of the few, this will put the poor at a disadvantage. Consent is necessary in the present land system, unlike what prevailed under the common law, in which there is an unrestricted power of alienation.

2.5 WHEN IS CONSENT TO BE SOUGHT?

The provision of section 26 of the Land Use Act states that an alienation without the consent of the relevant authority is "null and void". The question is when does an alienation take place? There are different views both academic and judicial. However, one must agree that a transaction between the mortgagee and mortgagor is void ab-initio where consent has not been obtained.

Another interesting thing is that a transaction is voidable until the consent is granted or with-held. Also the transaction is incomplete until consent is obtained. However, from the judicial point of view, any agreement without the consent of relevant authority has been held to be invalid. For instance, in **BRITISH AND FRENCH**

BANK LTD. VS AKANDE.[26] the court had to interprete section 3 of the Native Lands Acquisition Law of Western Nigeria. The section provides as follows:-

> 'Any agreement and any instrument in writing or under seal by or under which an alien purports to acquire any interest in or right over land.... and which form part of or gives effect to a transaction that has not been duly approved in accordance with the provisions of the Law shall be void and of no effect...'[27]

The court held that the plaintiff was an alien, hence failure to get the approval of the relevant authority makes the transaction void and of no effect. The Supreme Court in **SOLANKE VS ABED**[28] purported to follow the decision of the Judicial Committee of the Privy Council in **DENNING VS EDWARDS**[29] in which a similar provision in the Kenya Crown Lands Ordinance [30(a)] was interpreted. Viscount Simonds in the Privy Council held that the effect of the provision was that such an agreement was only inchoate until the consent was obtained. The agreement was only complete and effective after the consent had been granted. In their lordships view, some sort of agreement was unavoidably necessary before the governor is approached for consent.

Yakubu M.G. holds the view that "it is quite clear that an agreement to alienate any right in land is not complete until the consent of the appropriate authority is obtained.[30(b)] In **ORJIAKO VS ORJIAKO**,[31(a)] the court remarked that the only effect of the section is to make an agreement to alienate conditional upon the necessary consent being obtained.

2.5.1 DISCHARGE OF MORTGAGE

It is a very simple issue to discharge a mortgage especially that of land and particularly if the mortgage is a legal one. What the bank needs to do is to endorse on

the mortgage or receipt for amount secured by the mortgagee. But note that the form of words may be used for free hold and lease holds and it does not mean whether or not the mortgage was created by a legal charge or by a long lease. However, no formalities are necessary when discharging an equitable mortgage under hand unlike a legal mortgage where circumstances warrants that and the mortgagee is obliged to enforce his, certain remedies or options open to him. For example, in cases where he has taken a legal mortgage, he may do any of the following:-

a. **Sell the property**

He has the right to sell the property by public auction or by private contract. However, this power of sale does not arise or become exerciseable unless notice to repay the loan has been served on the mortgagor and default has been made thereafter.

b. **Appoint a Receiver**

The appointment of a receiver of the rents and profits from the mortgaged property takes place only when the power of sale has become exerciseable. But this remedy may often be necessary due to the existence of some interest in the property which is the object of the mortgage and as such, cannot be gotten rid of and such is capable of preventing an advantageous sale from being made.

c **Apply to court for a fore-closure order**

Another option left for an unpaid mortgagor is that he can sue in court to obtain a fore-closure order and when he does this, the property becomes his absolutely but subject to any prior encumbrances. It should, however, be noted that the court has power at the request of an interested person in the mortgage money or in the right of redemption to direct a sale of the property instead. But if the mortgagor thinks that the value of the property exceed the amount of the debt, he will usually ask the court to order a sale and the court will do so.

d **Take possession of the property**

A legal mortgagee could enforce his security by taking possession of the property in a peaceful manner if possible, otherwise, he can do so by means of an action for recovery of the land against the mortgagor. But if the mortgagor is in physical occupation of the property, the mortgagee can take possession by evicting him. But note that if the premises are let out already to tenant, the mortgagee "takes possession" by directing the tenant go pay his rent to him instead of the mortgagee. It is rare for a Bank that enforces a security by taking possession, an alternative course is to appoint a receiver who will collect rent on its behalf.

e. **Sue the Debtor**

This is another option for the mortgagee. An equitable mortgagee who tries to enforce his security will find himself in a much weaker position than a legal mortgagee. For instance, he can sue the mortgagor for the debt, apply for the fore-closure just like a legal mortgagee but there are certain rights exerciseable by a legal mortgagee which an equitable mortgagee can exercise but only as a result of proceedings in court. (These rights include out right sale and appointment of a receiver). Where both mortgages are equitable, the rule of first made, first paid normally applies. But a first mortgagee who fails to ask for the title deed or after obtaining them redelivers them to the mortgagor may be postponed to a second or subsequent mortgagee who has taken all precautions and yet has been deceived.

The practice nowadays is that on the payment by the mortgagor of the mortgage money, the mortgagee must reconvey by deed the legal estate in fee simple to the mortgagor, but Oluyede P.A. [31(b)] is of the view that in cases of lease hold, the mortgage must re-assign and release the property to the mortgagor so long as the original mortgage was by assignment. However, where the mortgagee by sub-lease is the case,

the mortgagee will surrender and release the property to the mortgagor even in cases of a second or later mortgagees. But we should note that in the case of equitable mortgage, a reconveyance is not necessary, a receipt by the mortgages discharges the debt. Also, it is not uncommon for both parties to retain the same solicitor, where they do so, a deed endorsed on the mortgage instrument serves as a reconveyance.

f. <u>Discharge of Mortgage by Endorsed or Annexed Receipt</u>

By section 29 of the conveyancing Act 1881 and also taking into consideration the provision of section 135 of the property and conveyancing Law of 1959, which provides that the receipt endorsed on or written at the foot of or annexed to a mortgage for all money thereby secured, which stated the name of the person who paid the money and paid by the mortgagee, operates (but subject to certain exceptions under the statues) as a discharge of the mortgage property but without prejudy to any term or other interest which is paramount to the mortgage.

However, it should be noted that from the wordings of this section, probably it will appear that the purpose here is to save the parties to a mortgage the trouble of securing a deed of discharge of transfer, when the mortgage debt is paid by giving a receipt the letter of a discharge or transfer depending on who makes the payment. The resultant consequences of this is that, so long as the receipt complies with the statutory provisions, the mortgage is discharged except in cases where the payment is made by someone who is not entitled to the immediate equity of redemption and the effect of the receipt does not negative an intention to transfer the mortgage to the payer or that the payment is out of capital money, or other money in the hands of personal representative or trustee's property applicable for the discharge of the mortgage and that there is no express provision that the receipt is to operate as a transfer, or the

payment is by someone with a limited interest in the immediate equity of redemption and he requires the mortgage to be kept alive.

3.1 LAND CHARGES

3.1.1 Definition

A charge is the appropriation of real or personal property for the discharge of a debt or other obligation, without giving the creditor either a general or specific property in or possession of the subject of the security, e.g. an order upon a third party to apply money in his hands to the discharge of a debt, or a charge of realty for the payment of a specified amount. In such cases, the creditor has the right to realise his security through the court in case of default of payment.

We have the following charges; i.e. legal charge and equitable charge.

3.2 LEGAL CHARGE

This is an option to the creation of legal mortgage by demise or sub-demise, to be "by way of legal mortgage". Section 110 (1) of the Kaduna State Law of Property Edict (1990) provides that, "where a legal mortgage of land is created by a charge of deed expressed to be by way of legal mortgage, the mortgagee shall have the same protection, power and remedies including the right to take proceedings to obtain possession from the occupiers and the person in receipts of rents and profits, or any of them as if:

(a) where the mortgage is a mortgage of a right of occupancy, a mortgage term for three thousand years without impeachment of waste had been thereby created in favour of the mortgagee, and

(b) where the mortgage is a mortgage of a term of years, a sub-term less by one day then the term vested in the mortgagor and had been created in favour of the mortgagee"[31(c)]

According to the provision of this section 110 (1) mentioned above, this means that a creditor with a charge by way of legal mortgage is given all powers and remedies of a full legal mortgagee. Even though he obtains no conveyance of title the thing he has is legal interest in the property under section 3 of the edict which provides that a "legal interest" means an interest, right, or charge in or over land, which by the provision of that edict authorised to subsist to be created as a legal interest. We should note that the only difference between the legal charge and the mortgage is in the formal machinery for creating them but still the difference between them may be drawn.

3.3 EQUITABLE CHARGE

An equitable charge is an agreement whereby specified property is made liable for the discharge of a debt or other obligation without any transfer of title or possession to the creditor. This type of agreement creates in equity a right to have the actual property applied to the satisfaction of the debt, making the chargee a secured creditor for purpose of insolvency or bankruptcy.[32] However, one should not loose sight of the fact that an equitable charge is only enforceable in equity. Also an equitable charge, unlike the statutory chargee cannot fore-close the security because he acquires no title under the charge, but through court process or through an appointment of a receiver, he can realise his security but note that the receiver must be appointed by the court.

3.4 PLEDGE

In a pledge, the pledgee may, in certain circumstances, have the power of sale but the ownership in the pledgee is subject to the pledgor's rights. Lien is different from pledge because lien is a mere right to retain a thing, whereas a pledge gives a special property in the thing pledged.

A pledge (or pawn in the case of Chattels) is the delivery of possession of property by the owner to a lender as security for the loan of money. Although the lender has certain powers of sale, the general ownership in the goods remains in the borrower and the lender has possession [33] unlike property subject to lien, it is not important the thing pledged should be actually owned by the pledger, it is enough if he pledge it with the owner's consent. However, if the pledgee sells the property, he must account to the pledger for any surplus remaining after liquidating the debt and he may sell without resorting to court.

The pledging of land is what is sometimes called the customary or indigenous mortgage.[34] Also under Nigerian and African customary system in general, the pledging of land has been known for long. There are lots of judicial decisions supporting pledge of land under our customary system.[35] Definitions of pledge by both academic and non-academic source has been varied. Professor Nwabueze[39] is of the view that pledge and mortgage are synonymous, albeit he defines mortgage as "security created by contract for the repayment of a debt already due or to become due. [40] Lord Holt defines pledge in the following terms:-

"..... When goods or chattel are delivered to another as a pawn to be security to him for money borrowed of him by the bailor... and this is called "a pawn" or pledge.[41]

It is clear that mortgage of land is not only a common feature in security, but it is convenient. But we have to note that under English law, with the exception of leases, all interest in land are real property. Also mortgage is a conveyance of land as an assignment of chattel as a security for the payment of a debt or the discharge of some other obligation for which it is given.

A mortgage may be either legal or equitable, and that under common law, a mortgagee would forfeit his contractual right to redeem his land as soon as he defaults

in payment, but under equity a debtor is allowed to redeem after the stated period of redemption once he repays the loan and interest due including costs. Also an equitable mortgage, unlike a legal mortgage does not convey a legal interest to the mortgagee. This is because an equitable mortgagee is a charge in favour of a person applicable to both free hold and lease hold.

It should also be noted that a holder of a right of occupancy is not allowed to sell, lease or alienate his right either by way of assignment in mortgage or transfer of possession, whatsoever without the approval of the Governor or the Local Government Authority.

Finally, a mortgage may be discharged in different ways. It can be discharged by out right sell or by appointing a receiver, applying to the court for a fore-closure order or he can even take possession of right or even sue the debtor.

NOTES AND REFERENCES ON CHAPTER TWO

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4. (1882) 22 ch. D. 511 at 516.
5. Twentieth century Banking Corp. Ltd. Vs. Wilkinson (177) ch. 99.
6. (1886) KR, 1 P.C. at 50.
7. (1859) 27 Bear 349.
8. Elvis & Co. Trustee Vs. Dickson Iduson (1924) 2 ch. 451.
9. Re MC Henry (1994) 3 ch. 290, CA. Gurdon Grant & Co. Vs. Bous (1926) AC 781 B.C.
10. Law of Property Act 1925 Section 85 (1) - Cheshires Modern Law of Real Property. 11th edition. (1972) Butterworths & Co. (publishers).
11. (1911) 3, N.I.R. 99, Lazz 3. N.L.R., 110.
12. (1904) A.C. 323.
13. (1902) A.C. 24 at 30.
14. Ibid.

15(a) (1968) Ch. 166.

15(b) Supra.

16. In the Ex-Western & Mid-Western Region States the property and conveyancing law of 1959 still applies.
17. (1956) NMLR 142.
18. (1978) I L N N 266

19. (1871) L. R. 13 Eq. 76.

20. See generally Maithland's Equity, 2nd edition (Butterworth) 1972, page 302.

21. (1859) 27 Bear 175.

22. Section 21 & 22 LAND USE ACT, CAP. 202 Laws of the Federation 1990. See also Land Use Act 1978.

23. Section 22 (1) Land Use Act, CAP. 202 Laws of the Federation 1990.

24. (1989) 17 NWLR Pt. 97, 305.

25. Notes on the Land Use Act (A.B.U. Press) 1986 at pages 35 - 36.

26. (1961) NWLR 272.

27. Cap. 80.

28. (1962) I All NLR 230.

29. (1961) Ac. 245.

30(a) Section 88 (1)

30(b) Yakubu M. G. Land law in Nigeria (Macmillan) (1982) p. 105.

31(a) Suit No. JD/27/1955.

31(b) See Generally, Oluyede P. A., Nigerian Law of Conveyancing 1st edition (1978) I U P.

31(c) Section 108(1) Law of Property Edict (Kaduna State) No. 20 of 1980.

32. Ekwo S. A. Title unpublished (LLM Thesis) submitted to A.B.U. Zaria (1992).

33. Re-Morrtt (1886) 18 Q.B.D. 22.

34. Nwabueze B.O. - Nigerian Land Law (Nwamife Publishers Ltd.) 1982, chapter 10 (CARMEN & CO) 1972, pages 38-46.

35. ADJEI VS. DABANKA (SUPRA), See also IFEANYI VS ADIGHOGU (1957) 2 E. R. N. L. R. 38 and EBIASSAH VS ABABIO.

36. (1957) 2 E.R.N.L.R. 38.

37. (1936) 12 WACA 106.

38. KOFI VS ADDO KOFI. (1933) 1 WACA 284.

39. Nwabueze B. O. (Supra).

40. Peenigton's J. in Olowu Vs. Miller Brothers (of Liverpool) Ltd. (1922) 3 NLR 110.

41. COGGS VS BARNARD (1703) 2 LD Rayner at 913.

CHAPTER THREE

GUARANTEES

3.1 INTRODUCTION

From the dictionary point of view, a guarantee has been defined as a collateral engagement to insure for the debt, default or miscarriage of another person. While a guarantor is like a surety, he is someone who promises to answer for another.

A guarantee is one of the simplest form of security taken by a banker and as such, it is very common. The guarantor has to agree to guarantee the extent of the amount he is guaranteeing. A guarantee is not an absolute state form of security, everything depends on ability in terms of resources and willingness to pay when asked or called upon to do so. However, except in cases where a charge is taken over, a loan secured by a guarantee should be regarded by a banker as unsecured.

Before a banker accepts a guarantee as security for a loan, he must satisfy himself that the guarantor is someone with means to honour his promise in case of insolvency or inability of the borrower to pay. However, one thing has to be considered and that is, that the banker should not regard persons with fixed incomes terminable at death who have no other means as fit persons to guarantee a loan. Also it has to be taken into consideration that a guarantor may at the time of entering into a guarantee agreement has possess the ability to perform all that he agrees to do, but his financial position dwindle through no fault of his own for the worse. In such cases, while the guarantee remains operative the banker may periodically renew his inquiries and in particular, the banker should look out for any evidence that the guarantor has settled (or is about to settle) any substantial

part of his property in trust for his dependents, or that he is otherwise placing his property beyond the reach of his creditors. But we should also bear in mind that the law of guarantee is biased heavily in favour of the guarantor against the banker and as such, the law is always willing to come to his aid, an attitude which inhibit or limit the right of the banker to manouver. this is why a banker normally insists that the guarantor should sign the banker's standard form of guarantee which is normally a lengthy document at least for a banker to be on the 'safe side'. However, Holden[2] defines guarantee in the following manner:

> A guarantee is a promise by one person (called the guarantor or the surety) to answer for the present or future debt of a second person (called the principal debtor) such promise being made to the person to whom the principal debtor is or will become liable. Thus, when a guarantor signs a guarantee in favour of a banker, he is saying in effect you advance money to your customer Mr. X and if he does not repay, I will be responsible, provided that the amount of my liability shall not exceed (say) one thousand pounds.

In dealing with a contract of guarantee, there is a need to differentiate a contract of guarantee from a contract of indemnity as there are certain features which distinguishes them. For instance, a guarantee is unenforceable by action unless evidenced by a memorandum in writing duly signed by the guarantor or someone authorised by him[3]. This is obvious as the legal rules apart, no banker would ever agree to lend money to a borrower against the verbal promise of the

third party to be responsible for its repayment.

Both commercial and mortgage banks that, when a bank is confronted by a would be or potential borrower who has no assets, or has assets but they are encumbered and fearful that it would not grant him an unsecured advance, it will resort to a relative or friend of the would be borrower, who would be prepared to guarantee his account. In other words, a third party (of course of substance) acts as surety. In that he stands behind the debtor and underwrite his indebtedness to the bank.

Reeday[4] is of the view that where a guarantee arrangement is being supported by other security, the bank can take any of the followings, either:- a third party form of mortgage appropriate to the property being offered or a guarantee together with the usual direct form of mortgage. He went further to say that many guarantees are unsupported and in some cases, bank relies solely on the name of the guarantor, normally due to a satisfactory bank reference on him or the bank's own knowledge of his financial standing and general reputation.

As already stated, there must be a written evidence of the guarantee if it is to be enforceable in a court of law. There is no formal shape but it must be made in such a way that it can be shown from the agreement of the parties that a contract of guarantee is entered into. The writing must therefore contain the following:-

(1) Name of the parties

(2) The essential terms of the contract.

The condition necessary to support any simple contract i.e. a contract not under seal must exist but there need not be any written statement. It may be noted that one of the most common methods by which bankers protect themselves

against loss on advances is by taking a guarantee. This is to enable a banker to fall back on them in case of insolvency of the principal debtor. It is up to the banker to judge the financial position (or standing) of the guarantor.

However, sometimes difficulties arise with regard to the form of guarantee, that is the extent to which the guarantors bind themselves and precluding them from, afterwards suggesting that the bank has exceeded the limit of what they undertook to be liable or answerable for next, from the necessity of anticipating conceivable contingencies, unforeseen circumstances, such as death, bankruptcy, change of firm, amalgamation, winding up of a firm, taking collateral security, and reserving to the bank the power to act on an occasion in the manner most appropriate and beneficial to the bank's interest.

Finally, it is safe to say that a guarantee is a promise to answer or to be liable for the debt of another person.

3.2 FEATURES OF GUARANTEES

The features of guarantee consist of the following:-

3.2.1 Consideration

Just like any other contractual relationship, or contract, guarantee (except in cases where such guarantee is under seal), must be supported by consideration. In other words, where the contract is not under seal, it can only be enforceable if sufficient consideration is given. If there is failure of consideration, the guarantor will be precluded from liability under the guarantee.

The usual rule is that consideration "must move from the promisee" and need not be given to the promisee, as such, the consideration for the guarantee must come from the banker but need not be given to the guarantor, it may even consist of some advantages conferred on the principal debtor by the banker at the

guarantor's request, at the express or implied request of the guarantor be agreed to forebear to exercise some legal right he may give a sufficient guarantee. It has been held that the mere fact of forebearance is insufficient for this purpose[6]. There must be either an undertaking to forebear or contractual forebearance at the express or implied request of the guarantor. Also an agreement to forebear for a reasonable period will be sufficient[7] but note that an illegal consideration will not support a guarantee nor will a mere moral or past consideration.[8]

3.2.2 Requirement of writing

In the old law[8(a)] no action may be brought on a guarantee unless and until the guarantee itself is in writing or there is a sufficient "note or memorandum" of the guarantee signed by either the guarantor or where the original written evidence of guarantee is lost, parol evidence is admissible (in other words, an oral evidence that it once existed is admissible in evidence). This is necessary as an oral guarantee is not void on account of the provision of the law [8(b)] but merely un-enforceable by action. Ofcourse the amount paid by the guarantor on the basis of an oral guarantee is valid and is irrecoverable.

For the party to satisfy the provision of the Statute of Fraud 1677, the written note or memorandum' does not necessarily have to be made at the same time as the contract of guarantee. It can be made at a latter date. Furthermore, a guarantee does not have to be under seal unless in exceptional cases where no consideration is given. Note that in guarantee agreement, no special form or words is required and particularly, the instrument does not have to use the word 'guarantee'. All that needs to be done is to name the parties in the agreement and it must contain all the essential terms of the contract.

3.2.3 Parties

A guarantee is an "accessory" contract by which a guarantor undertakes to answer for the debt, default or miscarriage of another person known as the principal debtor.

According to Sheldon and Fidler,[80] a contract of guarantee being an accessory contract, it necessarily involves some other persons whose liability for the debt is primary".

There are certain ways whereby a person may become a guarantor. For instance, a person can become a guarantor either by making an undertaking to be liable for the principal debtor's debt or by giving security for the debt on behalf of the principal debtor. But it may be noted that a person who promises to pay another person's debt, is not necessarily a guarantor in a contract of guarantee. That is why it is very important to differentiate between a contract of guarantee and novation. For example, if A promises B that if B will release A's friend C from a debt, he 'A' will pay the debt instead. This is not a contract of guarantee but a novation of the debt or it can be called a substitution of a new debtor for the original debtor. Another example is that A will agree with B that if B will let C have certain goods, he 'A' will see to it that B is paid for the goods, such a contract is not a contract of guarantee but a contract of indemnity because 'A' has undertaken primary liability to B and not merely secondary liability in case of 'C's insolvency. With regard to the form of guarantee, difficulties mainly arise from the necessity of defining clearly the extent to which the guarantors bind themselves and estopping them from afterward suggesting that the bank had exceeded what they undertook to be answerable for. As one text book writer[9] affirmed, from the necessity of anticipating conceivable contingencies such as

death, bankruptcy, change of firm, amalgamation, taking collateral security, insanity, giving time to the principal debtor receipt of dividends and such others.

The law is solicitous for the most of the securities and one of the main object of the guarantee is to keep a free hand for the bank and a tight one on the guarantor.

3.2.4 JOINT AND SEVERAL GUARANTORS

Where two or more persons agree to join in the giving of guarantee, their liability may be joint, or joint and several in a joint guarantee. Each co-guarantor is liable for the whole of the sum which is guaranteed; and in case of dispute, both of the co-guarantors can be sued together. The implication is that if one of the co-guarantors is sued while leaving others that does not mean that other co-guarantors are free from liability if the banker fails to get satisfaction from the one he decided to sue.

In a joint and several guarantee, each of the co-guarantors, may be sued separately for the whole of the sum which is guaranteed. It should be noted here that an unsatisfied judgement against one does not prevent the banker taking proceedings against each of the other several guarantors. In such cases, the parties may be sued in any way the banker wishes but his right may be limited to the amount (no more) which the guarantee is drawn to cover. To what extent does the death or bankruptcy of any of the several co-guarantors release the estate of a guarantor from liability for advances made before the banker receives notice of these events. Sheldon & Fidlers[10] are of the view that death of a guarantor or bankruptcy does not of itself release his estate from liability.

From the point of view of the banker, it does not matter much whether the guarantee is several or joint and several. Normally it is made joint and several.

However, the agreement should express in unambiguous terms whether or not the liability is joint or joint and several. But note that at any rate, the guarantee should provide a clause entitling the bank to release, or discharge or make any arrangement with anyone of the guarantors, without discharging the rest and this exclude the precedent in the rule that the release of one, or more co-guarantor releases the others.[11]

Also the guarantee should expressly make it clear that it is a continuing guarantee and cannot be determined by notice unless the notice is signed by all the guarantors or their personal representatives. In **EGBERT VS NATIONAL CROWN BANK,**[12] the court held that a reference to notice being given "by the undersigned" meant all of the persons who signed the guarantee.

Where there are co-guarantors, the bank must be sure all the co-guarantors execute the contract and should be careful not to make any advance to the principal debtor till all the co-guarantors have signed.

This is necessary as it was argued and a judicial decision[13] was in favour of a situation, where if some of the guarantors sign while others fail, or refused to sign and those that have already committed themselves and sign can prove that they agreed to enter into the contract on the fact of it being signed by one, or more of those who have refused to sign, they will be discharged from all liabilities.

But the best and easiest way is that where one of the co-guarantors fails or refuses to sign, the banker should get the willing co-guarantors to sign a new guarantee while no alteration or change of any sort be allowed for the amount of the limit, unless all of the parties (i.e. co-guarantors) and of course the bank are aware of the alteration. But if one of the co-guarantors wishes to limit his liability or to reduce the agreed limit, it is better to sign a new guarantee.[14]

3.3 RIGHTS OF THE GUARANTOR

A person whether natural person or a registered company who stands as a guarantor to another has certain rights as a guarantor. From the very moment when the guarantee is entered into, the guarantor has certain implied rights against the bank. These rights are as follows:-

3.3.1 RIGHTS AGAINST THE BANKER

At any time after the principal debt is due, the guarantor has the right to apply to the banker and pay him off and judicial decision[17] has shown that on giving a proper indemnity to the banker for cost, he may sue the principal debtor in the banker's name. However, this right is largely theoretical, it is rarely exercised in practice.

Secondly, the guarantor has the right to ask the banker to call upon the principal debtor to pay the debt at any time after it has become due. But for this right, there seem to be conflicting judicial decisions and the conferment of this right has been questioned, but one thing is clear, that is until and unless the creditor applies to the guarantor for payment, the guarantor reserves the right to ask the creditor to call upon the debtor to pay but that once the creditor calls upon the guarantor, the guarantor then becomes bound to pay.[18]

Thirdly, during the period of the existence of the guarantee, the guarantor has the right to demand from the banker at anytime, for particulars of the extent of his liability and the banker is bound to give necessary information. But the banker should not tell the guarantor the extent of his dealing with the principal debtor as this is covered by duty of secrecy. For instance, he can tell the guarantor how much he is to pay if the guarantee is to be called off immediately.

Fourthly, judicial decision[19] gives the guarantor the right to raise against the banker any defence or right of set-off or counter claim which is open to principal debtor.

Fifthly, the guarantor has the right of subrogation as soon as he pays off the debt to all the rights of the banker against the principal debtor except in cases where he has waived off the right.

Finally, once he settles the debt, the guarantor has a right over any security given to the banker by the principal debtor or by co-guarantor. However, it is usual for the bank guarantee to exclude this right until the whole debt has been recovered by the bank.

3.3.2 Guarantor's Right Against The Principal Debtor

A guarantor has an implied right to be indemnified by the principal debtor if he gives guarantee at the request of the principal debtor, who will give the guarantor an express right of indemnity. However, if the guarantee is given without any request from the principal debtor, the guarantor may not have any request from the principal debtor, the guarantor may not have any implied right to be re-imbursed. Also, if the guarantor's goods are taken in execution of a judgement of the court, or where the guarantor pays a sum to prevent an execution that constitutes payment by the guarantor and need not wait until the banker demands payment from him, he has the option to call the principal debtor to pay the debt in-question, so as to relieve the guarantor from his obligation. But this relief is not normally available till the debt is due and as such, the guarantor cannot ask the debtor to make provision for payment to the banker before the debt is due.

3.3.3 RIGHT OF CO-GUARANTOR AGAINST OTHER CO-GUARANTORS

Under this type of arrangement, the co-guarantor has a "right of contribution" against the other co-guarantors. That means where a co-guarantor paid more than what he is supposed to pay, or is liable for, he is entitled to compel the other to contribute. This right of contribution applies whether the liability is joint, or joint and several, and whether by same or different contract.

The right to contribution arise before or after the guarantor who paid the contribution has paid the banker, and also before asking payment to the banker any, co-guarantor can compel the other co-guarantor to contribute and he has the right to sue in court for declaration of his right to contribution and if a co-guarantor is sued by the banker for payment under the guarantee he can assert his right to contribution by bringing in another co-guarantor as defendant in the action or he can get a court order directing that, if he paid up based on the common liability, the co-guarantor should indemnify him.

But this right of contribution has its conditions and that is a guarantor who has paid, has no right of contribution until he has paid more than his share of the debt which is guaranteed.

3.4 LIABILITY OF GUARANTORS

Unless the guarantee provides otherwise (for instance, if the guarantee is to pay "on demand"), the liability of the guarantor arises when the principal debt becomes due for payment. Here, the liability of the guarantor becomes active from the date the debt becomes due not withstanding that the banker had, or had not informed him or had not demanded payment under the guarantee.

The difficult question is: when and at what stage does the debt become due, especially if the guarantee agreement is silent on that? On the question of

at what stage the debt becomes due, there are contradictory judicial decisions with one view restricting, while the other enlarging the position. For instance, in **PARR'S BANKING CO. VS YATE**[20] the court held that in the case of an overdraft, each advance becomes due as and when it is made by the banker, but in the case of **JOACHIMSON VS SWISS BANKING CORPORATION**[21], it was suggested that an advance made on overdraft does not become due until the banker has actually demanded repayment.

However, with the exception of cases where there is an agreement to that effect, the general rule is that, the banker does not have to request the principal debtor to pay up, or to sue the principal debtor before suing the guarantor, but the banker has no right whatsoever to sue the guarantor before the debt becomes due so that, if the principal debt only become due after any demand by the banker for repayment, the banker must demand the payment of the principal debt before he can sue the guarantor.

3.5 LIMITED, SPECIFIC & CONTINUING GUARANTEES

When a person gives a bank a guarantee today, he usually guarantees all liabilities of the principal debtor to the banker and the liability includes all liabilities in respect of any joint account or partnership account and if the guarantor intends to restrict or limit his guarantee to a particular account, he should see to it that the guarantee is worded accordingly.

However, if it is agreed that the liability of the guarantor should be limited to a specific sum, the guarantee should state that the guarantee is for all the principal debtor's debt with the provision that the guarantor should not pay more than the specified sum.

However, this is based on the fact that as soon as a guarantor makes any payment under the guarantee, he has a right to claim from the principal debtor and also to share pro rata in securities held by the banker on account of the principal debtor. A guarantee may refer to a certain specified transaction only. This type of guarantee is called a "specific guarantee" and it is discharged on repayment of the sum in-question as specified.

Also, a guarantee may be "worded so as to cover the amount of the fluctuation over draft on an account during the continuance of the guarantee, this is called a "continuing guarantee" and this is used by most banks.

However, if a specific guarantee is taken by the banker, the money lent to the debtor should be lent on a separate loan account and if the money is not lent on a separate loan account, the rule in Clayton's[22] case will apply in the absence of express appropriation and any payment made into the account will be used to reduce the amount of the debt, which is covered by the guarantee. But note that the liability of the guarantor to be answerable for the final balance must be clearly stated in the guarantee.

There are cases where the principal debtor is not liable as a guarantee in an accessory contract, and as such it presupposes that other person is primarily liable, that is if for any reason the principal debtor is not liable, or if in fact there is no principal debtor, the guarantor will not be liable under the guarantee. For instance, in the case of **COUTTS & CO. VS BROWNE-LECKY AND OTHERS,**[23] it was held that where two persons had guaranteed the overdraft of a minor, the debt was void under Section 1 of the Infant Relief Act of 1874 and as such, neither the minor nor the guarantor were liable. But if it is construed as an indemnity (not a guarantee) it can be enforceable notwithstanding that the

contract entered into by a minor is void under the provisions of the Infant Belief Act of 1874.

A company is not allowed to give a guarantee unless it is provided in its Article of Association and Memorandum of the Company, and the limit and type of guarantee is specified. If it does so, the Directors had acted ultra-vires and will be personally liable for the amount in-question.

3.6 TERMINATION OF GUARANTEE

Where the principal debtor pays the debt, that automatically discharges or brings to an end the liability or otherwise of the guarantor. But where the guarantor is only revocably discharged, the banker should not return the guarantee to the guarantor and should not write the inscription "Cancelled" across the guarantee. Likewise, a guarantor is also discharged from liability under the guarantee when he pays the principal debt, but however, the discharge will be reasonable until it is clear that the payment will not be off-set by a fraudulent preference.

The various ways in which a guarantee may be put to an end by the parties is as follows:-

3.6.1 By the Guarantor

The guarantor has the right to give whatever notice of determination as enshrined in the guarantee. However, when the guarantee is determined, the account must be broken to prevent the application or the operation of the rule in Clayton's case and any new account opened subsequently, and kept in credit can be closed, or ignored when calculating the liability of the guarantor.

3.6.2 By Change in the Constitution of the Parties

Where there is a change in the constitution or composition of the parties, such change will affect the guarantee to such an extent that it will determine it. The mere change of name will in no circumstances affect the position of the banker as it is still the same legal entity as it is not its constitution, even though one may be tempted to assume that such a change will normally determine a guarantee. In practice the situation is safe-guarded as far as possible by a clause provision for its continuance notwithstanding change in the constitution of the parties.

3.6.3 By the Bank

The Bank as the creditor can at any time demand for an immediate repayment of the principal debt. And unless it is expressly provided to the contrary, such a demand made on the guarantor will determine the guarantee as a continuing security and ofcourse, the account will be broken to prevent the application of the rule in Clayton's[24] case to the disadvantage of the bank. In such a case, the bank need not sue the debtor before resorting to the guarantor.

And as regard limitation of action if the guarantor promises to pay on demand, then no right of action accrue against him until a demand for payment has been made, and till such a demand has been made of him or the expiration of the period of notice of determination given by him, time does not begin to run in favour of the guarantor.[25]

3.6.4 By Death, Insanity, or Bankruptcy

Where a guarantee is given by a person, who subsequently died without discharging his obligation as contained in the guarantee, the liability will be shifted to the administrators of his estate or personal representatives . (But this

depends on the agreement between the parties) but, in most cases, the death of the guarantor (unless otherwise, agrees) determines the guarantee. So also in case of insanity of the guarantor, the liability of the insane guarantor will be to the extent of the balance due.

Where a guarantee is given by a company which was buoyant (then) and was declared bankrupt subsequently, although a company cannot die, it can be made bankrupt, it can be wound up, and as soon as the winding up commences, the guarantee will be determined. The following may be noted:-

3.6.5 <u>Death</u>

Whether or not the death of a guarantor determines the guarantee, depends on whether he has made his personal representative bound by the guarantee. Thus, if he does so then this personal representatives are bound until (such a period of time) when they give some notice of determination to the bank, where there is no express stipulation to such effect, the guarantee is determined, and the account must be broken to prevent the operation of the rule in Clayton's case. To preserve the liability of the personal representatives for the amount credited or lodged after notice of death, will reduce and eventually discharge the secured debt and as such any withdrawals will constitute a fresh and unsecured debt.

As noted earlier, in case of joint and several continuing guarantee, the death of one of the guarantors does not by itself release him from liability. Also note that the death of the principal debtor will determine the guarantee and as such, the debtor's account will be stopped and the extent of the guarantor's liability and his estate is not free from liability even in future under the guarantee.

3.6.6 Insanity

Once the bank reliably learns that the guarantor has become mentally ill, then as a matter of urgency, the principal debtor's account must be stopped because the insane person's estate is to be liable only for the balance due. A Judicial decision [26] held that a clause requiring notice of determination by the personal representatives on the death of the guarantor will not be applicable in the event of his lunacy.

Likewise, the mental disorder of the principal debtor determines the guarantee, for once it comes to the bank's knowledge, the liability of the guarantor will be fixed, and the debtor's account must be stopped.

3.6.7 Bankruptcy

When, the bank receives notice of a receiving order having been made against the guarantor, it must stop the principal debtor's account and demand payment from the principal debtor of the debt.

And on the guarantor being adjudicated bankrupt, the bank can proceed against his estate for his contingent liability under this guarantee as the type of debt is provable in bankruptcy.

3.6.8 By Release or Payment

The discharge of the principal debtor is also a discharge of the surety, because the discharge extinguishes the debt. This principle was backed by a decision of the court in **Commercial Bank of Tasmania Vs Jones**[27] where the court held that the release is absolute and no contract whatsoever between the debtor and the creditor, purporting to reserve remedies against the surety can have any effect.

3.6.9 CONCLUSION

In conclusion, the equitable mortgage is more disadvantageous than the legal mortgage as regards remedies available, except in cases where there is special agreement or assignment. An equitable mortgage can only be enforced by sale by court order. But note that a sale without court order is a nullity and the proper remedy of the equitable mortgage is fore-closure. Also that a holder of a right of occupancy has no right to alienate his right of occupancy by way of assignment, mortgage, transfer of possession, sub-lease or otherwise, howsoever, except with the consent of the governor or the appropriate local government authority as the case may be, so a proper drawn equitable mortgage is very similar in consequence to a legal mortgage because, the remedies which are available to the creditor in both cases are almost on the same footing as legal mortgages.

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CHAPTER FOUR

OTHER SECURITIES

4.1 LIFE ASSURANCE POLICIES

In modern times, policies of life insurance are usually mortgaged to bankers as security but it is obvious and very important to explain the terms of the policy. The amount to which the policy is worth must be stated, so also the event when the policy money will become payable for instance fifty thousand naira when life assured reaches eighty years of age or dies before that age.

When dealing with life assurance policies, as security for a loan, the amount of the annual premium should be noted. One author[1] noted that in these cases usually, a provision is made to the effect that after a certain number of premiums have been paid, the policy will acquire what is called a surrender value i.e. the sum which will be paid by the company to the policy holder if he decides to abandon the policy and to pay no further premiums.

But it is important for one to be satisfied that the policy has been supplied by a buoyant company of a good financial standing as the surrender value increases year by year. In case there is problem in determining the surrender value, the company will divulge this information. But a prospective donor of a life policy as security should note and examine with carefulness any special condition(s) which may likely be incorporated in the policy. This is necessary so as to avoid difficulties in future, because at times, a clause is inserted in the policy that the assured shall not take up certain occupations. Stocks and Shares are often known as quoted securities, so as to differentiate them from securities, which are not quoted on any stock exchange.

The assignment, legal or equitable of a life assurance policy is a form of security for an advance up to the surrender value at the surrender value of the

policy. It is also useful as a supplementary security.

Once the debtor dies, part or whole of the debt is liquidated, once the policy money are paid by the insurance company. In determining the value at a surrender value it should be noted that there is no surrender value on a policy until more than a premium has been paid on it. So also the age of the assured, duration of the policy are all factors to be considered in determining the surrender value.

From the point of view of a banker, the best way of taking a life policy as security is by a deed assigning it to the bank by way of mortgage of course subject to a provision for redemption. For instance, under English Law[4] "a mortgagee has full power to give a valid receipt for any money payable for the sale as the surrender of the policy without the mortgagor's concurrence but it is usual to insert such a provision in the deed".

Also interested parties in deed of assignment must sign the deed and if the life of the children of the assured are included then all those mentioned to benefit in the deed must sign, but note that if any of the children interested is a minor, then in such a case, the policy is not assignable because a minor has no power to assign.

4.2 INSURANCE POLICIES

An insurance policy is a chose in action.[5] Before the enactment of the Policies of Assurance Act 1867, the general law of assignment is what regulated the mortgage of life policies. This means that as legal choses in action, the assignee a life insurance policy had to sue in the name of the assignor. But under the Policies of Assurance Act of 1867, the assignee was enabled to sue in his own name.[6]

Assignment of insurance policies are required to be done in a certain prescribed form. For instance, they must be effected either by an endorsement written upon the policy itself or else by a separate instrument drawn on the lines set out in the schedule to the Act.

However, until and unless the notice of the assignment had been gain to the insurance company, an assignee has no right to sue upon the assignment,[7] priority depends on the date of notice and the company is bound upon a written request to give acknowledgement in writing of the receipt of notice.

From the creditor's point of view, policies can be broadly divided into two types; whole life policies and endowment policies. In the whole life policy, the main object of the assured is the protection of his family against his own death. This means that the amount of the policy is therefore payable on his death. In an endowment policy, the amount involved plus profits is payable either on the assured's death or when he reaches an agreed age. But it has to be noted that the surrendered value of the whole life policy is usually lower than that of the endowment policy for a similar amount. In the end, an endowment policy is therefore a superior security.

Insurance policies are to some extent precarious security.[8] This is because they require to be maintained by periodical payment of premiums. If the mortgagor default in making these payments, then the mortgagee may have to find the money to keep the security in being but where the mortgagee makes such payment, it is essential that the mortgage contains certain provision that such money are added to the mortgage debt. Secondly, the insurance policy is contract of utmost good faith in which the assured owes a duty of absolute honesty and of full disclosure to the company. And where he fails to disclose any materials fact or give any accurate or complete answer to the questions put to him

in the proposal form; the policy is void. Thirdly, the amount of a life policy is not recoverable by the assured's estate if he commits suicide in sound mind. This means suicide by the assured is a bar to recovery from the company.[9] It is not certain that an assignee, too is unable to recover in such a case, but based on a general principle, it is believed that the assignee's position cannot be superior to the estates. A creditor who takes a life policy as security therefore, takes subject to this risk.

Also under section 1 of the Life Assurance Act, a policy is void where the policy holder does not have an insurable interest in his own life and the life of his spouse. Common law also recognises that a person has an insurance interest in the life of another by reason of a valid pecuniary interest.[10] It has also been established that a creditor has an insurable interest in the life of his debtor to the amount of the debt.[11] Hence, the insurance policy may be taken out as security for the mortgage debt, either in the name of the debtor on his own life or in the name of the creditor on the life of the debtor, Judicial decision.[12] The effect of an agreement that the creditor shall effect a policy and the debtor pay the premium is to vest the equitable property in the policy to the debtor, subject to the creditor's security. In other words, there is the presumption that such an agreement is a contract to give the policy as security, which can only be rebutted by plain evidence that the intention was to give an outright bonus to the creditor.

It should also be noted that being a mortgage, there exist right of redemption to mortgagor and any clause or provision in the mortgage, which purports to vest the policy absolutely on the mortgagee on a particular event is void.[13] Also, because the mortgagor failed or refused to pay the premium, that does not give the mortgagee the right to claim the whole benefit of the policy. For instance, it was held that the mortgagee can pay the premium himself to

preserve the security and add them to the mortgage debt, but he cannot acquire the security without fore-closure.[14]

The mortgagee of an insurance policy usually takes possession of the policy and takes subject to equities. If there are several mortgagees, then priority will be regulated by the order in which notice of the assignments was given save that as held in the case of RE-WENIGER'S POLICY.[15] A second mortgage with notice, whether actual, imputed or constructive, of a first mortgage cannot gain priority over the first mortgagee by giving notice before the first mortgagee.

4.3 COMPANY SHARES

Shares are forms of choses in action but are not part of the definition of personal chattels under the Kaduna State Bills of Sale edicts,[16] which means, mortgages of share fall outside the scope of this statute and are subject to their own statutory rules. The Companies and Allied Matters Act 1990,[17] makes the mortgages of shares now assignable. By section 51 of the Companies and Allied Matters Act, a company's share should be transferrable by an instrument of transfer, and except as expressly provided in the company's article of association, the transfer of shares shall be without restrictions.[18] In such situation, a written instrument executed by both the transferor and the transferee is sufficient, unless the position which required that such transfers should be by deed.

It should also be noted that the transfer of company shares shall not be complete until the transferee has been registered in the register of members in respect of the shares as owner, although an assignment not so perfected is still valid in equity although the legal title does not pass without the registration of assignees title. A legal mortgage of a company's share is created by a transfer executed in the manner prescribed by the article of association, the mortgagee been registered as absolute owner. At the same time, a second instrument is

executed which stipulates that the transfer is redeemable. This second instrument sets out the terms of the mortgage transaction. This is not registered, because a company is not concerned to enter equities upon its register.

This type of mortgage is a most satisfactory security to a mortgagee of shares. Here, he receives the dividends and at same time, he has a right to vote in respect of the share. But note that where a full registered transfer is non-desirable, for any reason, then it is usual to create an equitable mortgage by deposit of the share certificates. There are different judicial decision as regard to this. For, in **SOCIETIE GENERALE DE PARIS VS WALKER,**[19] it was held that such a transfer without registration does not pass the legal title to the shares. However in **HARROLD VS PLENTY,**[20] it was held that it is not mere pledge of the document that constitutes an equitable mortgagee of the shares, and equitable mortgagee can compel the mortgagor to execute a registered transfer of the shares and upon subsequent default, the mortgagee is entitle to foreclose or, upon given reasonable notice to the mortgagor to sell.[21] However, in **WISE VS LANDSDELL,**[22] it was held that the mortgagor being the registered holder of the shares, has a right to vote, even though between him and the mortgagee, he being compelled to vote at the mortgagee's direction. A mortgage by deposit of share certificate is accompanied by a written instrument laying down the terms of the mortgage. It is a rule also accompanied by a transfer form executed by the mortgagor with a blank space for the mortgagee's name. The advantage of leaving the mortgagee's name blank is to enable him to unilaterally complete his security by filling in his own name and registering the transfer when the need arise. Secondly, in the event of his realising his security by sale, he can merely fill in the name of the purchaser after due notice to the mortgagor who is in default.[23]

There are certain risks attendant with an equitable mortgage of shares, which the legal mortgage does not contend with. By section 140 of the Act[23(a)] where the shares are not fully paid, the mortgagor could willfully, or negligently incur a forfeiture through his non-payment of the call.[24] Secondly, there may be some unknown earlier equitable assignee who might claim to be registered as owner of the share before the mortgagee is able to do so. Thirdly, the mortgagor may deal fraudulently with the share even after making an assignment of them to the mortgagee. In such case, such an innocent third party who is able to induce the company to register his transfer obtains the legal title and takes priority over the unregistered mortgagee. But this type of situation has already been taken care of by section 154(1) of the Act, [24(a)] which is to the effect that when the holder of any of a company share wishes to transfer them to any person, the instrument of transfer together with the relevant share certificate, shall be delivered to the company for recognition and registration. Before, it was very easy for a dishonest transferor to intimate to the transferee that the share certificates were lost since the company did not compel the production of certificate before registering a transfer. Even then, according to **RAINNFORD VS KEITH**[25] such a provision as section 157(1) of the Act is merely a warning signal to outsiders and does not create a legal obligation binding the company not to register a transfer without production of certificate.

Finally, in view of section 156(1) of the Companies and Allied Matters Act and Section 86 which states that a company is not bound to record notices of equitable interest in shares, is vital that an equitable mortgagee should register his interest upon an assignment of shares to him. If one works on the basis of section 86 of the Act then the rule in **DEARLE VS HALL**[26(a)] has no application to equitable assignment of shares, and that notice to a company is neither sufficient

nor necessary to establish priority of an equitable mortgage of shares. However, in the light of section 156(1) which accord protection of beneficiaries in companies share through the services of notice and affidavits on the company, none of the equitable mortgage of companies share becomes important.

For practical reasons, there is no much difference between company shares and company stock. For instance, fully paid up shares may be converted into stock and vice versa.

Notwithstanding, the minor difference between the two same type of company stocks and shares are safer security for loan than others, however, debenture stock are the safest security for a loan, where a person holds a debenture stock, he has a right to receive interest from the company, hence, the type of security will depend upon what assets are charged by the debenture trust deed.

Another type of safest security is the unsecured loan Stock, the holder of this is regarded as a creditor of the company. Thus, he has a right to receive interest from the company. The next safest security for a loan is a preference share. Unlike the holder of unsecured loan stock, the holder of a preference share is not a creditor of the company and as such, has no right to interest or dividend on his share, the only right he has is that of a dividend on his share before any dividend can be paid to the holder of Ordinary Share. This is necessary because, in case of inability to pay debt, the party concern is a holder of a preference share and is of course, the next in line of priority after all the creditors have been paid.

Also least safe security is an ordinary share as the name implies. Ordinary share represents the company's venture capital and they carry the greatest risk, and if the company prospers the greatest reward, that is why in case of winding up the holder of ordinary shares is last in priority and does not have

a right in a dividend. There is also the deferred shares but these are rarely issued now.

4.4. Creation of a legal mortgage of registered stocks and shares

A legal mortgage is not created unless and until the registered stocks and shares have been registered in the name of the bank or its nominee. A banker takes a legal mortgage of registered stocks and share by obtaining from the registered holder, a properly executed form of transfer together with the stock, or share certificate and then having himself registered as the new registered holder of the registered stocks and shares. But where the registered holder is not the mortgagor himself, but a mortgagor's nominee, the form of transfer must be executed by the mortgagor's nominee not by the mortgagor. But note that deposit of the stock or share certificate will not amount to an equitable mortgage unless it can be shown that the deposit was by way of security. To prove that the deposit of certificate was by way of security, the mortgagee must give the banker a memorandum of deposit, as a blank form of transfer, the intention being that the purchaser or mortgagee shall be at liberty later on to fill the blank and perfect his security by getting himself registered. But note that a person who has an equitable mortgage by taking a blank transfer and the certificate, can sell after reasonable notice.[26(b)] In the alternative, he has the mortgagee's usual right to foreclose.[27] A blank transfer, it should be noted is not a deed. A deed must be signed, sealed and delivered.[28] Also if a person seals and delivered a writing which is left blank in any material part, it is void for uncertainty and is not his deed and it cannot be made his deed merely by filling up the blanks after execution.[29]

4.5 Advantages of a Legal Mortgagee or Registered Stocks and Shares

The main advantages of a legal mortgage of registered stock and share are:-

(a) where a banker obtains a legal mortgage over registered stocks and shares, he is not affected by any prior equitable interest in the same stocks and shares, including any prior equitable mortgage unless he has notice of that interest at the time he or his nominee is registered as the new register holder. But note that where a banker who obtains an equitable mortgage is effected by prior equitable interest whether he had notice of it or not, by virtue of the rule that where the equities are equal the first in time prevails.[30]

In Powell's case,[32(a)] the bank took a deposit of the stock certificate, together with a bank form of transfer, so that an equitable mortgage was created in favour of the bank. The bank did not also obtain from the mortgagor a power of attorney which, as we have seen, would have enabled the bank to convert its equitable mortgage into a legal mortgage, but it subsequently filled in its own name and had itself registered. Later, it emerged that the mortgagor was in fact a trustee and was not entitle under the terms of his trust to mortgage the stock. It was held that the equitable interest of the beneficiaries of the trust had priority over the equitable interest of the bank because, the interest of the beneficiaries were created before the equitable mortgage was created. The beneficiaries were therefore entitled to the stock which had been mortgaged by the trustee, and the bank lost the benefit of its mortgage, if on the other hand, the bank had been authorised by power of attorney to execute the transfer on behalf of the mortgagor, it would have obtained a legal mortgage of the stock, and so would have prevailed over the interests of the beneficiaries, because at the time the legal

mortgage would have been created, the bank would not have had notice of the existence of the trust or of the prior equitable interests of the beneficiaries.

In Coleman's case, [32(b)] Annie Coleman executed a transfer of certain debenture stock to Edward Coleman. The transfer was never registered, so Annie Coleman remained the registered holder of the stock which she held on constructive trust for Edward Coleman, who therefore had an equitable interest in the stock. Sometime later, Annie Coleman regained possession of the stock certificate which she deposited with the bank as security for loan. This meant that the bank also had an equitable interest in the stock, as it had an equitable mortgage. Some years later, the bank learned of the original transfer to Edward Coleman and in order to defeat Edward Coleman's prior equitable interest, it obtained a legal mortgage of the stock. After Edward Coleman died, his personal representatives sued the bank to recover the stock. It was held that the bank legal mortgage did not have priority over Edward Coleman's prior equitable mortgage, because at the time that the legal mortgage was created, the bank had notice of Edward Coleman's interest. If on the other hand, the bank had obtained a legal mortgage of the stock from the outset, the legal mortgage would have had priority over Edward Coleman's interest because, at that time, the bank did not have notice that the prior interest existed. The bank would therefore have been entitled to retain the mortgage stock.

(b) where the banker does not obtain a legal mortgage, the mortgagor remains the registered holder and can therefore dispose of the mortgage stocks and share or exercises the right of a registered share holder to the prejudice of the banker.

(c) If the banker obtains a legal mortgage of registered stocks and share, any document relating to such matters as right, issues, bonus issues, and share

holders meeting will be sent to the banker as registered holder of the mortgaged stocks and share. If the shares are registered in the name of the mortgagor, he cannot prevent the mortgagor from taking up the rights in his own name, or selling them or keeping any bonus shares and can only take steps to recover the shares or the rights or their proceed afterwards.

(d) If the banker obtains a legal mortgage of registered stocks and share, he will be able to transfer the shares as soon as he has power to do so under the terms laid down by the memorandum of deposit. But if on the other hand, the banker only obtains an equitable mortgage, he will not be able to transfer the shares without court order unless he has been given a blank form of transfer by the mortgagor, and where necessary, a power of attorney.

(e) If the banker obtains a legal mortgage of registered stocks and shares, he will have priority over any lien which the company has over the same stocks and shares.

4.6 <u>Disadvantages of Legal Mortgage of Registered Stocks and Shares</u>

Even though the advantages far out-weigh the disadvantages, the banker is entitled to know what the disadvantages are:-

(a) If the registered shares are partly paid, the registered holder is liable for any Calls by the company for further payments on the shares.

(b) A banker who takes a legal mortgage by transfer which is forged or turns out to be forgery, is liable to indemnity by the company for loss resulting, the fact that he acted in good faith notwithstanding. This principle was established in the case of **<u>SHEFFIELD CORPORATION VS BARKLAY</u>**.[33] In that case, Sheffield Corporation stock was mortgaged

to a bank by a transfer from trustees on which the signature of one of the trustees was forged. The bank later sold the stock to a third party who was registered as the holder, and at this stage the forgery was discovered. The innocent trustee successfully brought an action against Sheffield Corporation, which was compelled to buy an equivalent amount of stock and register it in his name. The corporation claimed an indemnity from the bank and succeeded on the ground that the bank, by sending in the forged transfer, for registration had impliedly warranted that it was genuine.

(c) A banker who takes a legal mortgage is entitled as the holder of the shares or stock, to receive any interest or any dividends paid by the company or public body. However, as against the mortgagor, he is not entitled to keep any interest payments or dividends unless and until the mortgagor default until that time, he must pay them over to the mortgagor.

(d) If a director of a company offers director's qualification shares as security for a loan and if it is important to the banker, that the director should remain a director, the banker cannot obtain a legal mortgage of the shares. This is because, the director would no longer be qualified to remain a director if the bank were to be registered as the holder of the director's shares.

Policies, shares and stocks will continue to be credible securities in the bank. However, such must be assessed carefully at the time of transaction

The assignment, legal or equitable of a life assurance policy is a form of security for an advance up to the surrender value of the policy, and once the debtor dies, part or whole of the debt is liquidated.

A contract of life assurance is a contract of utmost good faith). All material facts within the knowledge affecting the life must be disclosed. Insurance policy is a choses in action, and until the notice of the assignment is given to the company, an assignee has no right to sue upon the assignment.

Insurance policies are to some extent precious securities, this is because they require to be maintained by periodical payment of premium. Also the amount cannot be recovered by the assured's estate if he commits suicide. Stocks and shares are often known as 'quoted securities', and this is to differentiate them from securities which are not quoted on any stock exchange.

The Company and Allied Matters Decree 1990 makes the mortgages of share now assignable. We should also note that there is not much difference between company shares and company stocks, but still the two are safer security for loan than others.

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4. Tokington Vs Magee, (1902) 2 KB 247.
5. Section I Policies of Assurance Act 1867.
6. Section 14 (1) of the Nigeria Insurance Act of 1990.
7. Ekwo, A. S. The Law relating to secured credit transactions in real and personal property in Nigeria, Unpublished LL.M Thesis Submitted to A.B.U. Zaria 1992, p.117.
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9. Chitty: Contracts, Vol.2 (Sweet and Maxwell(1972, 25th edition, page 365.
10. Morland Vs Isaac (1885), 20 Beav 389.
11. Salt Vs Marquis of Northampton (1892) AC.
12. Ekwo A. S. (Supra).
13. Drusdale Vs Piggott. (1856), 8 De GM & G. 546.
14. (1910), 2 Ch. 291.
15. No. 10 of 1989, Sec. 3(1).
16. No. 1 of 1990.
17. Ibid sec\. 15(1).
18. (1985), 11 AC 20 at 28.
19. (1901), 2 Ch. 314.

20. Deverges Vs Sandeman (1902) Ch. 579.

21. (1921) 1. Ch. 430.

22. Ekwo A. S. (Supra).

23(a) Companies and Allied Matters Act 1990.

24. Section 152(3) of the Companies and Allied Matters Act 1990 i.e. where the company has a lien on the share.

24(a) Companies and Allied Matters Act 1990.

25. (1905), 1 Ch. 296.

26(a) (1723) 3. Russ 1.

26(b) Stubbs Vs Slater (1910), Ch. 632.

27. Harol Vs Plenty (1910) 2 Ch. 314, at page 316.

28. Powell Vs London and Provincial Bank (1893) 2. Ch. 55, France vs Clark (1884) 26 Ch. D. 257.

29. Markham Vs Ganaston (1598) cro. Eliz. 626.

30. Sheldon's & Fidlers, Practice and Law of Banking (Eleventh Ed.), (MacDonald and Evans Ltd.) 1982, page 421 - 422.

31(a) Ibid.

31(b) Ibid.

32. (1905) A.C. 392.

CHAPTER FIVE

5.1 CONCLUSION AND RECOMMENDATIONS

While trying to understand and analyse the problems of security for bank lending under Nigerian Law, and the implications involved, one should not loose sight as to the other side of the culpability of the banks themselves. Instance of failure to enforce security; or the unenforceability of security would be looked at objectively. At times, banks are the culprit because, they encourage credit to borrowers thereby increasing money (liquidity) in the economy, hence, fuelling inflation in the Country.

One of the many measures the researcher considered to be effective is that Banks should be stopped from granting domestic Loans in the naira based on the Security of Foreign Deposits held abroad and/or in domiciliary accounts with Nigerian Banks. The Central Bank of Nigeria should provide for a stiffer penalty for default of such regulations such as an offending Bank shall be made to deposit with the Central Bank of Nigeria an amount equivalent to the Loan so granted, and the deposit will be non-interest bearing and not eligible for inclusion in the Bank's specified Liquid assets for the purpose of calculating the mandatory statutory Liquidity ratio. Also such amount deposited shall remain with the Central Bank of Nigeria as long as the Loan remains on the Bank's portfolio. Even after the loan has been recalled, the Central Bank shall still not release the penalty amount until after 3 or 4 months, so as to be on the safe side. Also prompt enforcement of this rule or policy should be re-enforced when necessary.

This is necessary as no bank for instance, in the United Kingdom or the United States of America will grant a Loan to a businessman based on a guarantee unlike the case in Nigeria. In reality, this foreigners may have nothing except may be, a Landed Property overseas or some foreign accounts. They simply use

them to borrow millions of naira from Nigerian Banks. We are naive to have allowed it. Since Nigerian banks regarded their guarantees as first class, they are given preferential treatment to the detriment of Nigerian borrowers who do not have such attractive collaterals. Worse of all, these loans they get are not applied to activities which can be considered good for the economy. Most probably, they are used to purchase foreign currencies from the Inter-bank foreign exchange market, (IFEM). Thus, increasing pressure on the few available foreign currencies to the detriment of the Naira. As time goes on, the Foreign Exchange is either re-sold at a higher rate to make profit by simply trading in foreign currencies or to import items that can sell here at any price for quick profits. In addition, items imported are hardly of any real value to Nigeria. This is because, these loan, coupled with others extended by the banks to both the public and private sectors in 1988 resulted in an overheated economy.

Another measure of control is that no bank should be allowed to pay dividends, until the Central Bank of Nigeria approves them, and it should be noted that an approval should also not be given until the bank in-question maintain a ratio of not less than 1:10 between its adjusted Capital Fund and its total Loan advances.

The Central Bank of Nigeria should grant a mandate to Commercial and Merchant Banks of restricting credit expansion in the economy. That is, the Central Bank of Nigeria should reduce the ceiling on Merchant Banks aggregate Loans and advances from a maximum of 47% of eligible assets. By doing so, Merchant Banks will operate at the same credit ceiling as their Commercial counterpart. But it should be noted that, for the aim not to be defeated, these credit ceilings are not to be applied across the board. For instance, it is pertinent to allow small and new Merchant Banks to build up their Credit base to at least

say ₦250 million (Two Hundred and Fifty Million Naira) before the new rules can catch up with them. But banks with ₦500 million and ₦1.0 Billion Naira in loans can expand their lending portfolio. But there is a caveat; lending should not expand by more than 15 (fifteen) percent of their credit base or 20% of their total deposit liabilities at the end of the base period.

However, the negative aspect of this is that, the Central Bank of Nigeria's ability to control bank lending is limited. It does so only through interest rate which the industry now complained is too high. Also the Government, via the Central Bank of Nigeria should impose greater discipline and professionalism in the banking sub-sector. This can be done by bringing in new monetary policies. Despite the fact that the government has given 2 years to Commercial and Merchant Banks to shore up their share capital, or be classified as distressed; thus, raising the minimum paid up capital for banks to ₦500 million. This is necessary because of the rapid erosion of the financial institution's capital base by rising inflation as well as the need to check bubble-banks.

It is discovered that as far back in 1991, the minimal capital bases of ₦50 million and ₦40 million were specified for Commercial and Merchant banks. Inflation rate was put at 15% with the level increasing to 80 percent in 1996. Be that as it is this policy, severely eroded the asset quality and the capital bases of most banks.

The problems within the banking sector is based upon the indiscriminate growth of financial institutions in the country. This trend has led to competition for deposits among the various institutions. Consequently, it led to payment of high interest rates for funds resulting in increased cost for the Sector. Other problems of the Sector include Central Bank of Nigeria's regulatory Instruments which estabilised the bank for instance, the withdrawal of Government Accounts

from Banks in 1989 is a factor that increased Liquidity Problems for banks. So also, the withdrawal of off-shore guarantees on denominated Loans and the use of stabilisation services. The problems of the banking sector has increased with the pegging of interest and exchange rates.

Before lending, it is suggested that banks should ensure that they are in possession of all vital documents and agreements (example title of ground rents ex-cetera) and should ensure that they are kept in safe compartments, fire proof ex-cetera) and statement of accounts should be up-dated during the continuance of the facilities, they should be analysed and used in monitoring the business of the borrower.

Another reason for the instability in the banking sector are as follows:-

(a) Management incompetence;

(b) Favouratism;

(c) Weak internal control;

(d) Board-room politics;

(e) Insider abuses;

(f) Litigation;

(g) Contravention/violation of statutory regulations;

(h) Fraud and forgeries, at which banks may face liquidation if their Internal Control System was not overhauled. The damage these have caused In nation's banking industry are unimaginable and unless the banks avoid these vices, strive to instill discipline and inculcate good management qualities in their operations, no amount of capital pump into them will make them efficient. We should also note that the pegging of lending rates would encourage more corporate customers and entrepreneurs to seek bank assistance. It should be noted that growing incidences of fraud and forgery, poor asset quality, and inadequate capitalisation in banking industry posed a serious threat to

the survival of some Banks.

Banks should re-assess their priorities and use their lending function to encourage enterprenuership in the Country and reduce their in-ordinate quest for profits, because lending money to young entrepreneurs with viable projects proposal is better instead of allowing credits to fraudulent and wealthy Nigerians, engaged in Merchandise business. This is necessary as Banks are supposed to be the heirs of economic development machine which mobilises funds and allocates them to the vital areas of the economy to ensure growth and stability.

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