GENERAL NOTICES

NOTICE 1813 OF 2005

DEPARTMENT OF TRADE AND INDUSTRY

CONSUMER AFFAIRS (UNFAIR BUSINESS PRACTICES) ACT, 1988

I, Mandisi Mpahlwa, Minister of Trade and Industry, do hereby, in terms of section 10(3) of the Consumer Affairs (Unfair Business Practices) Act, 1988 (Act No. 71 of 1988), publish the report of the Consumer Affairs Committee on the investigation conducted by the Committee pursuant to Notice 3092 as published in Government Gazette No. 21530, dated 08 September 2000, as set out in the Schedule.

M. Mpahlwa

MANDISI MPAHLWA

MINISTER OF TRADE AND INDUSTRY

SCHEDULE

CONSUMER AFFAIRS COMMITTEE

REPORT IN TERMS OF SECTION 10(1) OF THE CONSUMER AFFAIRS (UNFAIR BUSINESS PRACTICES) ACT, 1988
ACT No. 71 OF 1988

REPORT No. 120

INVESTIGATION IN TERMS OF SECTION 8(1)(b) OF THE CONSUMER AFFAIRS (UNFAIR BUSINESS PRACTICES) ACT, 1988 WITH A VIEW TO STRENGTHENING THE PROVISIONS OF NOTICE 777 PUBLISHED ON 18 AUGUST 1995 IN GOVERNMENT GAZETTE No. 16609

1. The Consumer Affairs Committee - a brief background

The Consumer Affairs Committee (the Committee) administers the Consumer Affairs (Unfair Business Practices) Act, 71 of 1988 (the Act). It is a statutory committee in the Department of Trade and Industry that reports to the Minister of Trade and .Industry (the Minister). The purpose of the Act is to provide for the prohibition or control of certain business practices.

An "unfair business practice" is defined in the Act[1] as any business practice which, directly or indirectly, has or is likely to have the effect of harming the relations between businesses and consumers, unreasonably prejudicing any consumer, deceiving any consumer or unfairly affecting any consumer.

The Committee has wide investigative powers. In broad terms the Committee is empowered to undertake investigations into:

(a) the business practices of individuals and businesses that could be involved in unfair business practices[2]
and

(b) any business practice in general which is commonly applied for the purposes of or in connection with the creation or maintenance of unfair business practices.[3]

---

(1) See section 1

(2) In terms of sections 4(1)(c) and 8(1)(a). These are commonly referred to as sections 4(1)(c) and 8(1)(a) investigations. A section 4(1)(c) investigation is an informal preliminary investigation whilst an investigation in terms of section 8 is a formal investigation and notice of the investigation is published in the *Government Gazette*. The Committee conducts section 8(1)(a) investigations when it is investigating specific businesses or individuals. Any order by the Minister would only apply to those businesses and/or individuals who are named in the notice.

(3) In terms of section 8(1)(b). The Committee conducts such an investigation when a number of businesses or individuals have adopted a particular business practice which appears to be unfair. In other words it has become a general business practice. Any order by the Minister as a result of such'. an investigation would be

Should the Committee, after the conclusion of a section 8 investigation, resolve that an unfair business practice exists, or may come into existence, it recommends corrective action to the Minister.[4] Orders of the Minister are published in the *Government Gazette.* A contravention of an order by the Minister is a criminal offence, punishable by a fine of R200 000 or five years imprisonment or both the fine and the imprisonment.

The Committee was preceded by the Business Practices Committee (BPC) which administered the Harmful Business Practices Act, 71 of 1988 (the former Act). The former Act was amended during 1999.[5] As a result, the BPC was replaced by the committee and the definition of a harmful business practice was amended and is now referred to as an unfair business practice. The investigations which could be undertaken by the Committee have remained the same.

2. Introduction

This report deals with a section 8(1)(b) investigation into strengthening of the regulations promulgated in 1995 to regulate the business practices of debt mediation and loan assistance.

3. Background

During August 1991, the BPC gave notice of its intention to conduct a general investigation into business practices involving advice to debtors and payments to or negotiations with creditors on behalf of debtors.[6] This investigation resulted in the BPC's Report on Debt

---

applicable to any individual or business who is operating a similar business or who intends to operate such a business in the future regardless of the fact that they were not specifically investigated.

(4) The powers of the Minister are set out in s 12

(5) The Act was amended by the Harmful Business Practices Amendment Act 23 of 1999

(6) Notice 750 of 1991, *Government Gazette* 13457 16 August 1991. This was a section 8 (1) (b) investigation

Mediation and Loan Assistance.") This report dealt with a range of problems which consumers, who are unable to meet their financial obligations, may encounter. These include the offering of debt counselling and advice, debt adjustment (renegotiation of debts), substitution of creditors (debt take over), debt distribution, debt refinancing and assistance in obtaining loans. These activities have the common, supposed aim, of improving the position of over-committed debtors, Notice 777 of 1995[8] was a direct result of Report 30. Notice 777 reads as follows:

"1. In this regulation "intermediary" means any director, manager or employee of, or any person who acts on behalf of, a moneylender, and any person, except the moneylender who receives an application from any person who intends to borrow money in terms of a money lending transaction or who in any manner acts on behalf of any person intending to become engaged in any negotiations relating to such loan.

2. Subject to the provisions of paragraph 6, the business practice -

(a) whereby an intermediary, directly or indirectly, in respect of a money lending transaction or an application by any person to borrow an amount of money, demands, receives or recovers any valuable consideration, excluding bank charges or lawfully permissible interest, from the borrower or from any person so applying, whether for his own account or on behalf of any person other than the moneylender, but excluding agreements in terms of which the fee of the intermediary is recovered from the loan amount; or

(b) whereby a person, directly or indirectly, undertakes the payment, for reward, of amounts to creditors on behalf of a debtor, excluding bank charges or lawfully permissible interest,

is hereby declared unlawful.

3. Subject to the provisions of paragraph 6, the advertising by an intermediary, through any medium whatsoever, of the service whereby the payment, for reward, excluding bank charges or lawfully permissible interest, of amounts to creditors on behalf of a debtor is undertaken, is hereby declared unlawful.

4. Subject to the provisions of paragraph 6, any intermediary is herewith prohibited, directly or indirectly, from entering into an agreement with a person in respect of a money lending transaction or an application by any person to borrow an amount of money, granting such intermediary the right, whether conditionally or unconditionally, to receive or to recover, on his own

---

(7) Report No 30 *Government Gazette* 15470 4 February 1994

(8) *Government Gazette* 16609 18 August 1995

account or on behalf of any person other than the moneylender, any valuable consideration, excluding bank charges or lawfully permissible interest, from the borrower or from any person so applying, but excluding agreements in terms of which the fee of the intermediary is recovered from the loan amount.

5. Subject to the provisions of paragraph 6, any person is herewith prohibited, directly or indirectly, from entering into an agreement with a debtor, involving the payment, for reward, of amounts to creditors on behalf of that debtor, excluding bank charges or lawfully permissible interest.

6. This notice does not apply to-

(a) any person who practices as an attorney on his own account or as a partner in a firm of attorneys or as a member of a professional company, as defined in section 1 of the Attorney's Act, 1979 (Act No. 53 of 1979); or

(a) any person who is registered as an accountant or auditor in terms of the Public Accountants' and Auditors' Act, 1991 (Act No. 5 of 1991); or

(b) estate agents who are holders *of* fidelity fund certificates in terms of section 16 of the Estate Agents' Act, 1976 (Act No. 112 of 1976); or

(d) a moneylender or a credit grantor or a lessor, as defined in section 1 of the Usury Act, '1968 (Act No. 73 of 1968), paying an intermediary for services rendered by him in connection with any transaction referred to in Regulation 2 (a); or

(e) a banking institution as defined in section 1 of the Banks Act, 1990 (Act No. 94 of 1990); or

(f) an employee or owner of any newspaper, magazine or other advertising medium."

4. Further complaints

Notwithstanding the order by the Minister, the Committee continues to receive a steady flow of complaints against persons and businesses acting as intermediaries for loan applications, offering debt counselling and advice through the renegotiation of debt, debt distribution and debt refinancing. In essence, persons and businesses are contracting out of the regulations contained in Notice 777.

4.1 Persons and businesses, acting as intermediaries, in respect of money lending transactions or applications to borrow money, circumvent the Minister's prohibition **by,** for example, demanding that consumers:

(a) become members of another association and pay an upfront membership fee or

(b) purchase information packages, goods or services

before a loan application will be processed or considered. Consumers who became members of the association or who purchased information packages were supposedly also entitled to a wide range of other services such as various types of loans, debt rehabilitation, credit clearance, financial planning and para-legal services.

4.2. The Banking Council brought it to the attention of the Committee that consumers, desperate for a loan, enter into agreements with intermediaries where fees exceeding 10% per annum are charged. It must be mentioned that the Usury Act, 1968 (Act No *73* of 1968), with certain exceptions, prohibits intermediaries from charging any fees and in those instances where a fee may be charged, it places a limitation on the maximum that may be charged. The Banking Council stated that the legal justification for these high charges is that Notice 777 makes provision for an agreement whereby the intermediary's fee is recovered from the loan amount.[9] It was never envisaged with the publication of Notice *777* of 1995, that consumers should be exploited "by agreement".

4.3 Various schemes came to the attention of the Committee where businesses, directly or indirectly, undertook the payment, *for* reward, of amounts to creditors on behalf of debtors (debt distributions). The Minister has declared this practice to be unlawful.[10] The businesses enter into agreements with consumers with the view to restructure the repayments of their loans to the alleged advantage of both the borrowers and the lenders. Upfront payments are also taken before the consumer's problems are investigated.

The conduct of certain debt administrators who approached consumers before the Court placed them under administration also came to the attention of the Committee. The debt administrators did not provide consumers with a proper explanation with regard to the procedure nor did they fully disclose what debt administration entailed. This was prejudicial to and unfairly affected consumers.

(9) See sections 2(a) and 4 of Notice *777*

(10) Sections 2(b), *3* and 5 of Notice *777*

4.4 It has also been brought to the attention of the Committee that businesses, specifically involved in the micro-lending industry, charge, by agreement, very high fees. Loans have been structured to remain within the maximum interest rate as prescribed by the Usury Act with an "agreement" regarding another fee to be paid to a separate entity. Instances were reported where these are not "separate" entities at all and they even operate from the same premises.

4.5 The Committee's attention was also drawn to one of the exceptions contained in Notice **777.** The Notice does not apply to an employee or owner of any newspaper, magazine or other advertising medium, The wording of the notice appears to be too wide.

5. A further investigation in terms of section 8(1)(b) into the business practices *of* debt mediation and loan assistance

The Committee, on 26 August 2000, resolved to undertake a general investigation with a view to strengthening Notice 777 of 1995. The following notice was published in the *Government Gazette:*[11])

> "In terms of the provisions of section 8(4) of the Consumer Affairs (Unfair Business Practices) Act, **1988** (Act No **71** of 1988), notice is herewith given that the Consumer Affairs Committee intends undertaking an investigation in terms of section 8(1)(b) of the said Act with a view to strengthening Government Gazette Notice 777 of 1995 published in Government Gazette No **16609** dated **18** August 1995. The investigation will include the extending of certain clauses of the abovementioned Notice No **777** of **1995** with the view to preventing the attempted circumvention of the mentioned Notice or related regulations, including for example, the contracting out of the regulation by charging membership fees for, inter alia, providing a service of arranging loans or related services."

(**11**) No 21530, Notice **3092,** 8 September 2000

The Committee also in a media release warned consumers of the business practice whereby consumers applying for loans are charged a fee by businesses (intermediaries) who allege that they will arrange loans for them or where businesses charge an "administration" fee to pay debts. Consumers were cautioned that when applying for loans via an intermediary, the payment of a membership fee or any other payment does not guarantee that the loan application will be successful. The Committee also gave notice of its intention to revisit Notice 777.

6. The practice

The attempts to circumvent and/or abuse Notice *i77* can be summarised **as** follows:

(a) the applicant must become a member of a business which requires the payment of a membership fee or must purchase goods or services before an application for a loan will be processed;

(b) intermediaries charge fees that are higher than the maximum prescribed fees in terms of the Usury Act;

(c) fees are charged (albeit by agreement) and there is an undertaking to pay, for reward, amounts to creditors on behalf of debtors; and

(d) businesses granting micro loans have been restructured to ensure that interest rates remain within the maximum interest rate which is prescribed by the Usury Act and this is coupled with another "agreement" for another fee which is paid to a separate entity.

Although there has been no evidence of possible abuses, the words that apply *to* an employee or owner of a newspaper, magazine or other advertising medium appear to be too wide and need to be reconsidered.

6.1 Membership fees or the purchasing of information packages, goods and services

The business practice of requiring consumers to become members of specific businesses and to pay a membership fee before a loan is processed, was

investigated by the Committee and found to be an unfair business practice [12]. The Committee determined that the prerequisite that consumers become members and pay membership fees, is a practice whereby an intermediary **indirectly** demands, receives or recovers valuable consideration. The committee also found that

- the advertisements/fliers claiming that the loan applications are free, are misleading. There is no evidence of any service other than that of acting as an intermediary in respect of a money lending transaction and
- the statement that the membership fee is refundable should membership not be accepted, is misleading. The criteria used to "approve" membership meant that most applicants qualified for membership but this did not mean that they would qualify for a loan. No application, even if the applicant would in all likelihood qualify for a loan, was processed before the required membership fee was paid.

The Committee also investigated the practice of purchasing information packages, goods and services. The *modus operandi* of this business practice was to require consumers, acting on advertisements, to purchase information packages. The complainants claimed that after giving their details and requirements telephonically, they were assured of an approved loan and were then told to deposit the required fee into a bank account. The Committee is unaware of any consumer who obtained a loan. The Committee determined that the prerequisite that consumers must first purchase information packages, goods or services is a practice whereby an intermediary **indirectly** demands, receives or recovers valuable consideration.

6.2 Charging of high fees

The Committee received complaints from the Banking Council and Snyman de Jager Attorneys. Both complaints dealt with what they regarded as "exorbitant fees" charged by intermediaries.

The Banking Council stated that there is an increasing number of mortgage bond

(12) Report No 100, *Government Gazette No 24860* of 23 May 2003 and Report No 101, *Government Gazette No 24861* of 23 May 2003

"switching" intermediaries who inveigle clients of the bank to switch their mortgage loans from one bank to another. In the process the intermediaries usually increase the size of the loan and then charge the client an "exorbitant fee" (sometimes as high as 8 to 10%), in addition to receiving the bond introduction commission of about 0.25% charged to the new bank. Their concerns are that the transaction represents a "same client same house" and the major beneficiary is the "switching" intermediary. The Banking Council furthermore mentioned that the high level of commission exceeds the maximum of 2.5% specified by Regulation R339 *of* 20 February 1981, issued in terms of the Usury Act. The Council stated that Notice 777 was used to justify this practice. The Banking Council is of the opinion that clauses 2(a) and 3 of the Notice, in particular the words "but excluding agreements in terms of which the fee of the intermediary is recovered from the loan amount." is shielding, what it believes, the "exorbitant fees charged by unscrupulous mortgage bond switching intermediaries".

Regulation 339, referred to above, provides for the purposes of section 2 (11)(b) of the Usury Act, that the percentage shall be one-half of one percent year of the amount *of* the principal debt of the money lending transaction but not exceeding in the aggregate a percentage of *two* and one-half of the said principal debt. In section 2(11)(b) of the Usury Act, attorneys, accountants and any person falling within such categories of persons as the Minister may designate by notice in the Gazette, are allowed to demand, receive or recover any valuable consideration. This fee is then limited by Notice R339. Notice 777 does not apply to attorneys and auditors which means that they remain subject to the Usury Act and its provisions and their fees are thus capped. Other entities, not designated by the Minister as envisaged in Usury Act, may, because of Notice 777, charge whatever fees they, by agreement, manage to negotiate with the borrower. These fees may be taken from the loan.[13]

Snyman de Jager Attorneys stated that they are extremely concerned about the highly unsatisfactorily situation resulting from the wording of clause 2(a) of Notice

---

(13) The suggestion that this is by agreement is perhaps a fallacy since desperate consumers may agree to any fee in order to obtain the loan. Evidence suggests that this is an area *of* substantial consumer abuse

777. They mentioned that clause 2(a) stipulates that subject to "certain exclusions (notably persons belonging to professional bodies i.e. attorneys, auditors and estate agents) the business practice in terms of which an intermediary receives consideration for arranging finance, is declared unlawful." They further stated that unfortunately the last part of the clause excludes "agreements in terms of which the fee of the intermediary is recovered from the loan amount." They also mentioned that they are not concerned about the conduct of intermediaries who belong to one of the categories of professional bodies as prescribed in clause 6, as the public is adequately protected. "Not only is the maximum fee for services prescribed in terms of the Usury Act (limited to 2,5%) but the professional bodies have their own disciplinary procedures which ensure adherence to strict ethical codes." Their concern is the "blatant manner in which these unethical intermediaries use the proviso of Clause 2(a) to their own advantage by charging excessive fees, not making full disclosure to the clients and in the most instances only serving their own interest. The charging of "excessive fees" is their biggest single complaint.

A further concern mentioned by them is that ethical considerations are non existent when it comes to the "agreement" applicant:; are required to sign when applying for assistance. Most of these are not properly completed and the implications are not explained to the public. The only recourse the public has is expensive legal action as the actions of the intermediaries are not regulated by any act and there is no professional body to turn to. It is said that a large number of persons applying for money through the services of intermediaries are the elderly. They are uninformed of their rights and are susceptible to influencing. The banks have the difficult task of scrutinising the instructions originating from these "doubtful" for accuracy.

Another concern raised is that because there are no rules or regulations applicable *to* these intermediaries, the practice has arisen that some of them simply start a new business advertising and contracting under a new name without disclosing the principals involved.

Both the Banking Council as well as Snyman de Jager Attorneys request that the words "but excluding agreements in terms of which the fee of the intermediary is

recovered from the loan amount" be deleted from Notice 777 of 1995.

6.3 Payment, for reward, of amounts to creditors on behalf of debtors.

A business practice has emerged whereby certain individuals or business calling themselves "debt mediators" (informal administrators) persuade consumers to restructure the repayments of their loans. This is allegedly to the advantage of both the borrower and the lender. The impression is sometimes created that it is an intermediary step to administration. A request is in some instances forwarded to the consumers' employers instructing them to cancel deductions. This happens even before any negotiations with creditors are undertaken and without certainty as to the extent of the consumer's outstanding debt The businesses obtained payment in advance as existing instalments with creditors are cancelled and are redirected to these "debt mediators". The consumers' instalments for the first 2 to 3 months are taken by the "debt mediators" as their reward for their services. Certain debt mediators use a negative consent approach when informing creditors of this debt restructuring. Creditors are told that if they do not reject the offer within a certain time period, the offer will be deemed accepted. The consumers are usually left with the impression that their debts have been frozen and that all their debt problems have been solved. Normally consumers are also expected to sign powers of attorney providing attorneys with wide powers to act. Included in these powers of attorney is a statement to the effect that consumers understand that creditors may decide to take legal action against them and that they will not hold the debt mediator responsible.

Some examples are as follows:

Example 1

"We confirm that our client has requested us to negotiate on her behalf regarding payment to her creditors. Mrs "A's" financial position is such that she is unable to meet her monthly commitments. Accordingly, we attach hereto a copy of our client's Income and Expenditure as well as a Profcrma Distribution List showing monthly payments to be made to each of Mrs "A's" creditors.

As you will see from the attached, we are proposing to pay the sum *of* R149.78 on a monthly basis in respect of liquidation *of* the amount owed to you. Kindly note that this distribution amount is subject to change should the total outstanding balance to each creditor change.

Please note that as a result of our client having numerous creditors, we are forced to wait for each creditor *to* revert back to us regarding the proposal made on our client's behalf. Thus the first distribution payment will only be made after 2(two) calender months, thereafter monthly until the debt is liquidated.

We request confirmation from you that the capital amount reflected in the attached documentation is in fact correct and whether you will be willing to accept the distribution amount reflected. We look forward *to* hearing from you within seven (7) days from the date of receipt of this letter, failing which we shall assume that you have accepted our offer and will proceed accordingly.''

Example 2

"RE: VOLUNTARY DISTRIBUTION OFFER OF CLIENT "B" REF....

NB. This is not an application for administration. Please refer this letter to the CREDIT MANAGER or responsible person.

"LETTER WITHOUT PREJUDICE"

Our client is unable to afford his normal basic monthly expenses. We are at his request implementing a voluntary distribution program to enable our client *to* meet all his financial obligations.

We know that you realise your company can only benefit from this offer, as legal action will not secure a better monthly payment.

Our client offers to tender the amount of R 375.00 p.m. from..... until his financial situation has improved *to* such a degree, that he can resume paying normal installments.

Please note that this is our client's last resort before having to apply to

administration.

Please forward us your banking details to facilitate payment as well as current outstanding balance. ....

If you wist to decline this resolve, please notify us VIA fax..... before... to avoid automatic acceptance of this offer.".

Example 3 (attorney acting on behalf of an independent financial institution)
"INFORMAL DISTRIBUTION : MS ....
We refer to the above, and confirm that we act on behalf of .... who in turn acts on behalf of Ms"C".

Our client is a financial institution assisting ordinary men who are burdened by debt. Our client attempts to strike a balance between the interests of creditors on the one hand and the debtors on the other hand. As such our client proposes an informal distribution in an attempt to achieve such a balance.

What our client envisages to achieve, operates as follows:

- that we as a firm of attorneys and agent for our client collect half *of* the debtor's current monthly payment to be distributed on a monthly basis *to* creditors;

b) that the first two instalments received from clients, will be allocated towards administration costs;

c) thereafter, on a monthly basis and after collection commission, as well as distribution costs have been deducted, payment will be made to creditors.

Our instructions are that through the aforementioned method, creditors will receive monthly payments, as well as debtors will be placed in a position to continue with their ordinary lives. The aforementioned proposal differs from administrations in the following manner;

i) no court processes are involved;

ii) no administration costs are involved

iii) no quarterly distributions, but monthly distributions will be made."

Example 4

"Herewith please find a copy *of* this letter for you to acknowledge receipt of, which acknowledgement should be returned to us at your earliest convenience.

We have been mandated to lodge this first serious and sincere approach to rehabilitate and reschedule payment of possible outstanding debt in your favour.

KINDLY FORWARD TO **US:**

1. Copies of all loan applications, loan documents, insurance and other possible contract and or legal documents signed by the mentioned debtor in obtaining possible loans from yourself as a full disclosure of documents at date hereof. The mentioned debtor has not received any written communication whatsoever from yourselves to date.
2. Disclosure statement of accounts as at this date, plus settlement balance, fully specified and analysed, setting out how the account and initial capital amount is derived at or is compounded. Further specify all commissions or costs paid on behalf of the mentioned debtor plus net amount paid out, when paid out and to which accounts.
3. Disclosure statement of interest charged, i.e the rate and stating the method of calculation as required by law.
4. Possible consent to judgement Section 58 undertakings or Garnishee orders or whatever documents signed in this regard by the mentioned debtor.
   PLEASE NOTE; any consent to judgment Section 58 undertakings or garnishee orders or whatever documents signed by the mentioned debtor ANTE legal action being instituted are withdrawn immediately. Further, any possible debit order, mentioned debtor may have signed with you is withdrawn forthwith.
5. As from date hereof, the formal address of the debtor, Domicilium Citandi ET. Executandi is to be changed to our address above mentioned.
6. Mentioned debtor is overburdened by loan repayments deducted from his/her income. Initially we must request a period of three months moratorium to

enable debtor to liquidate other area and pressing necessary accounts and to be able to re-commence payment to yourselves. ".

Example of power of attorney

"1. My financial situation is in a serious state of affairs and I am unable to meet my present monthly commitments. The rehabilitation program established by .....attorneys to whom I was referred to by..... ("debt mediator") ..... and which has been fully explained by ..... ("debt mediator") and is acceptable to me, will, if implemented substantially improve my present financial position.

2. I hereby instruct ..... ("debt mediator's") attorneys to take whatever legal steps it may deem necessary , in order to improve my present financial position, and grant to them for this purpose, full power of attorney to act in my name, and grant to them, the right:

2.1 to obtain and provide whatever information about my financial affairs, that they may deem necessary, from any of my creditors for the proper carrying out of their mandate in terms of this agreement;

2.2 to cancel any authority given by me to creditors, prior to this agreement, that they may deem necessary to improve my financial position.

3. Services *to* be rendered by ..... ("debt mediator's") attorneys on my behalf are clearly understood by me, ad I understood that .....("debt mediator") does not undertake to make payment on my behalf of any amount to my creditor, other than as provided for in terms of the scheme of arrangements concluded on my behalf, and only insofar as the relevant funds are received by .....("debt mediator's") attorneys, form me. I understand that the creditors may decide to take legal action against me, to protect their own interest, and for this I will not hold .....("debt mediator") responsible."

The practice whereby debt mediators undertake to pay debts to creditors on behalf of debtors for reward has been declared unlawful by the Minister. (14)

(14) See sections 2(b), 3 and 5 of Notice 777 of 1995

The conduct of certain debt administrators who approach consumers before the Court has placed them under administration has also come to the attention of the Committee. The Micro Finance Regulation Council (MFRC) appointed Gobodo Forensic and Investigative Accounting (Pty) Ltd (Gobodo) to investigate the use, effectiveness and abuse of administration orders in terms of section 74 of the Magistrate's Court Act. In the Gobodo report (15) it is stated that as "a result of the growth of the number of people finding themselves in trouble of debt, more and more entities have seen the opportunity to offer their services to debtors who cannot meet their obligations towards their creditors. In many of these instances, these entities appear to focus solely on placing individuals under administration ..... As more and more entities enter the market, the competition to get debtors to make use of their services has increased. This, according to witnesses interviewed, has led to widespread advertising and touting for debtors to be placed under administration. An attorney who touts for clients may be found to be contravening the Attorneys Act, 1979 (Act 53/1979). There is, however, no prohibition on a non-attorney who acts as an administrator from advertising his services or touting for clients. Evidence has been provided by Capitec Bank Limited of Stellenbosch, of a situation where their clients were approached by "agents" who informed them how easy it was to be placed under administration. These "agents" wore T-shirts depicting the name of the administrator. The administrator is allegedly an attorney.",

Also in the Gobodo report (16) it was stated that "administrators employ marketers who approach companies and market their services to low income employees. The marketing, however, does not include an educational component explaining the negative implications for the individual. .... Their experience was that most clients did not realise what the consequences of an administration order were. Some of the debtors were under the impression that their previous loans had been redeemed and applied for new loans.".

The Committee had discussions with some administrators and persons knowledgeable about some of the practices adopted by administrators. The

(15) Draft Report dated 20 September 2002, paragraph 6.6.1.1
(16) Draft Report dated 20 September 2002, paragraph 6.6.1.2

information provided to the Committee supported the view expressed in the Gobodo report that consumers, with the information made available to them, did not realise what the consequences of administration orders were or even understood that they were being placed under administration. The lack of proper explanation or full disclosure to the consumers unfairly affected consumers.

6.4 Restructuring of businesses granting micro loans

It was brought to the attention of the Committee that businesses, specifically involved in the micro-lending industry had restructured their businesses. This was done to ensure that their loans remain within the maximum interest rate as prescribed by the Usury Act. The loan agreement is coupled with another "agreement" regarding another fee to be paid to a separate entity. Instances were reported where these are not "separate" entities at all and they even operate from the same premises. These businesses used the words in paragraph 2(a) of Notice 777, i.e. "but excluding agreements in terms of which the fee of the intermediary is recovered from the loan amount" to justify the restructuring of their businesses and the request for these fees.

The restructuring of such businesses commenced after the Minister issued the Exemption Notice [17] under the Usury Act [18]. This Exemption Notice applies to loans for R10 000 and less and are repayable in 36 months or less. The exemption is conditional, the main condition being that the money lending business must be registered with a regulatory institution approved by the Minister. The main benefit for the registered money lender is that the finance charges it can demand are not limited to the rate prescribed under the Usury Act. The only regulatory institution approved by the Minister is the MFRC. In *MFRC v Southern African Lending Affairs Council* [19] Du Plessis *J* explained how these businesses have been restructured.

---

(17) Government Gazette Notice 713 *of* 1 June 1999.

(18) In terms of section 15A of the Usury Act (Act No 73 of 1968).

(19) Case No 20294/2002 in the High Court of South Africa (Transvaal Provincial Division): Judgment by Du Plessis J

Lenders are "accredited" by business "AA". When a borrower approaches a lender accredited by "AA" for a loan, the lender purports to act as an intermediary between the borrower and business "BB". The agreement with the borrower is concluded in the name of "BB" who then pays an intermediation fee to the lender. Businesses "AA" and "BB" claim that the intermediation fee is recovered from the loan amount, that it is lawful and does not form part of the finance charges as defined in the Usury Act. These businesses further claim that the businesses who charge intermediation fees do so in accordance with the Usury Act, they do not fall within the provisions of the Exemption Notice and they consequently need not register with the MFRC. They contend that if the finance charges they demand, without the intermediation fee, do not exceed the limits prescribed by the Usury Act, it is lawful. They based their contention on Notice 777.

The practice described in the affidavits prepared by persons who borrowed money from lenders accredited with "AA" appears to be the following. The borrower approaches a lender registered with "AA". The lender, not "BB" advances the required loan to the borrower. However, the lender requires the borrower to sign an acknowledgement being indebted to the "BB". The capital amount stated in the acknowledgment of debt is not the amount actually advanced but the amount plus 30% to 50%. To the inflated capital amount, interest at a rate of 12% per annum is added. From a standard loan application form that "AA" gives to lenders registered with it, it appears that provision is made therein for an intermediation fee. It appears that the acknowledgement of debt signed by the borrower in favour of "BB", is a sham. The practice is designed to allow the persons involved therein to contend that "BB" advanced the loan and that the amount added to the actual loan represents an intermediation fee. It is further designed to allow for the contention that the respondent paid the intermediation fee from the moneys advanced. Although "AA" and "BB" denied that they have devised the scheme as alleged by the borrowers, they alleged that they operate under and in terms of the Usury Act and not the Exemption Notice. They did not give any details of how they conduct their business.

Businesses "AA" and "BB" held out that a micro-loan in respect of which an intermediary's fee is charged, falls within the limits set by the Usury Act provided

that the finance charges, without the intermediary's fee do not exceed those limits. Their contention is based on Notice 777 in as far as it deals with intermediary's fees.

Judge Du Plessis stated in his judgment that with certain exceptions, Notice 777 "declares the demand, receipt or recovery of an intermediary's fee a harmful business practice. It also prohibits an intermediary from entering into an agreement granting him or her the right to receive or recover an intermediary's fee. Paragraph 2(a) of the notice deals with the harmful business. The paragraph has the following proviso: "But excluding (from the declaration as a harmful business practice) agreements in terms of which the fee of the intermediary is recovered from the loan amount". Judge Du Plessis went further stating that Notice 777 deals with money lending transactions in general, including those that are not subject to the provisions of the Usury Act (a number of money lending transactions are exempted from the provisions of the Usury Act). The provisos mean no more than that the recovery of an intermediary's fee from the loan amount is not a harmful business practice and is not prohibited in terms of Notice 777. The Notice does not purport to render lawful what is unlawful under the Usury Act. It does not in any manner affect the definition of "finance charges" in terms of the Usury Act.

In terms of section 2(10) of the Usury Act an intermediary may not demand, receive or recover an intermediary's fee on his or her own behalf or on behalf of any person other than the moneylender. Should the moneylender recover an intermediary's fee, such fee forms part of the finance charges as defined in section 1 of the **Usury** Act. In terms of Notice 777 the intermediary's fee may in any event only be recovered from the loan amount. The Usury Act and Notice 777 do not contradict each other.

6.5 Wording too wide with regard to employees or owners

The provisions of Notice 777 do not apply to an employee or owner of any newspaper, magazine or other advertising medium. The rationale for excluding employees and owners of the advertising media from the Notice relates to the fact that the employees and owners cannot be held responsible for the correctness or

legitimacy of the content of advertisements, hence their exclusion from complying with the notice. However, the wording of the notice appears to be too wide as it does not technically prohibit employees or owners from advertising in their personal capacities in which case compliance with the Notice should be an obligation. The same arguments are consequently also relevant to all the other professional persons mentioned in paragraph 6 of Notice 777 and should be addressed.

7. Consideration

The taking of up-front fees by intermediaries is a problem not limited to South Africa. In other parts of the world it is commonly referred to as " advance-fee loan scams" and such intermediaries are referred to as loan brokers or "fraudulent" loan brokers. Consumers fall victim to enticing advertisements offering financial help. Victims are "guaranteed" personal or business loans, even if they have no credit history or an unfavourable credit history. The introduction of Notice 777 in 1995 to address this problem went a long way in addressing the problems experienced by consumers in South Africa. However, it is clear from the above information that some persons are circumventing the provisions of Notice 777 by requiring that an applicant must first become a member of a club or business. It is necessary to amend Notice 777 by including in the prohibition that an intermsdiary may not require that a person becomes a member of any business and pays a membership fee before a loan is granted.

Regarding the restructuring of businesses for the purpose of circumventing the provisions of the Usury Act, the judgment by Du Plessis J has made it clear that it is unlawful. The prohibition on the marketing of those schemes should be included in the provisions of Notice 777 to ensure that no person in future misleads consumers when entering into loan agreements. Du Plessis J made it clear that the intermediary's fee in terms of Notice 777 may only be recovered from the loan amount and stated that the Usury Act and Notice 777 do not contradict each other. The same arguments can be used when analysing the concerns raised by the Banking Council and Snyman de Jager Attorneys regarding the fees charged by "switching" intermediaries. To this end Notice 777 should be strengthened by

clarifying that the intermediary fee may not be more than such fee prescribed in applicable legislation. To ensure that the consumer is aware of the cost implications, it is also necessary to amend Notice *777* to require an intermediary to make full disclosure of all cost implications in its transaction or agreement with the consumer.

From information available to the Committee, it is clear that various persons and businesses, including debt administrators, have developed innovative measures to receive their reward for payments made to creditors, directly and indirectly, on behalf of debtors. Consumers are being misled. It has consequently become necessary *to* strengthen Notice *777* to address the concerns of the committee. Money is taken from the public without any protection and in the process debtors incur further liabilities. The restructuring of the repayments of consumers, also referred to as voluntary distribution, informal distribution or rehabilitation offers before any negotiations have taken place with creditors and until formal agreements have been reached with creditors must be declared as unfair business practices. Furthermore, persons who ought to be registered or appointed in terms of appropriate legislation need to confirm in writing their registration or appointment status to the consumer.

Any instructions given to employers on behalf of an employee to cancel deductions before formal agreements with creditors have been reached must be prohibited. In addition, full disclosure must be made to clients regarding costs, the legal status of proposed arrangements and the risks involved. Any form of upfront fees or charges as a reward for these services must be declared unlawful. Money received for distribution purposes must only be deposited into an attorney's trust account, provided that account is covered by the provisions *of* the Attorneys Act **1979** (Act **No 53** of **1979)** or in the case of administrators in a separate trust account. The Committee is of the view that if money deposited in a separate trust account is not protected by legislation, that money should be deposited into an attorney's trust account where that account is covered by the provisions of the Attorneys Act **1979** (Act No 53 of **7979).** In respect of administrators appointed by the Court, an administrator may, before making a distribution, deduct the necessary expenses and remuneration in accordance with the prescribed tariff from money collected. It is of extreme importance that administrators make a full disclosure to the consumers what

the cost of the administration will be and the manner in which it will be determined before the administrator is appointed by the Court. The disclosure should also make it clear to the consumer what method of collection will be followed, i.e. the deduction of the administrator's expenses and remuneration prior to lodging the distribution account with the Court or whether the administrator's expenses will be collected through the inclusion of the administrator in the distribution account on which the names of the institutions or persons to which money must be distributed, are set out. Any money collected by the administrators without the full written disclosure should be deemed upfront fees and must be declared unlawful.

Linked to the above concerns are the approaches followed by some administrators prior to the consumer being placed under administration by the Court. The competition between administrators has increased with the effect that the soliciting of debtors to be placed under administration has also increased. It is in the public interest that all information, including advertisements, provided by administrators to debtors before lodging applications to Court, disclose fully the implications and consequences of being placed under administration. Notice 777 should be strengthened to address this concern.

To address the concern of the Committee regarding the wording being too wide in respect of the exclusion of an employee or owner of any newspaper, magazine or other advertising medium from complying with Notice 777, an amendment to the effect that the exclusion is only valid in respect of their official capacity as employees or owners of any newspaper, magazine or other advertising medium should be made. With reference to attorneys, accountants and estate agents, their exclusion from the provisions of Notice 777, needs to be limited to their actions undertaken in terms of their relevant legislation provided they have the necessary fidelity fund cover.

8. Recommendation

The attempts to circumvent the provisions in Notice 777 outlined in section 6 (page

7) above constitute unfair business practices . There are no grounds for justifying these practices in the public interest.

It is therefore recommended that the Minister declare these unfair business practices unlawful in terms of section 12(1)(b) of the Act by amending the provisions of Notice 777 as follows:

1. In this regulation "intermediary" means

(a) any director, manager or employee of, or any person who acts on behalf of, a moneylender or credit provider, and any person, except the moneylender or credit provider who receives an application from any person who intends to borrow money in terms of a money lending or credit transaction or who in any manner acts on behalf *of* any person intending to become engaged in any negotiations relating to such loan or credit; and

(b) any person who purports to act as an intermediary between a consumer and a business entity.

2. Subject to the provisions of paragraph 14, the business practices -

(a) whereby an intermediary, directly or indirectly, in respect of an agreement purporting to be a money lending transaction, credit facility, credit transaction, credit guarantee or any combination thereof or an application by any person to borrow an amount of money in terms whereof the applicant's obligation to repay the money is deferred in terms of an agreement in respect whereof any charge, fee or interest is payable, demands, receives or recovers any valuable consideration, or requires the payments of any valuable consideration of any kind to become a member of any institution, association, business or entity for the right to use services offered where the services offered include an application for any money lending transaction, credit facility, credit transaction, credit guarantee or any combination thereof, from the

borrower or from any person so applying, whether for his own account or on behalf of any person other than the moneylender or credit provider, but excluding agreernents in terms of which the fee of the intermediary is recovered directly from the consumer once the loan or credit application has resulted in the establishment of a loan or credit agreement with a loan or credit provider and in terms whereof the agreement between the intermediary and the consumer must *at least:*

(aa) specify the exact service to be rendered by the intermediary,

(bb) inform the consumer of the cost the loan or credit provider is entitled to recover from the applicant,

(cc) disclose the intermediary fee to be charged in addition to the costs in (bb) including the basis for calculating the fee, and

(dd) specify the fee charged which may not be more than such fee prescribed in applicable legislation;

(b) whereby a person, directly or indirectly, undertakes the payment, for reward, of amounts to creditors on behalf of a debtor, excluding bank charges or lawfully permissible interest;

(c) whereby a person, who has to confirm in writing his or her registration or appointment status, where applicable in terms of appropriate legislation, directly or indirectly, for a reward, undertakes to negotiate on behalf of a consumer the restructuring of payments, also referred to as voluntary distribution, informal distribution or rehabilitation offers, before negotiations have been successfully performed and written contracts have been concluded with creditors which contract must *inter alia* specify the following:

(aa) name of debtor,

(bb) name of creditor,

(cc) name of debt mediator,

(dd) amount outstanding on date of contract,

(ee) new monthly repayment amount,

(ff) new repayment period,

(gg) total cost, including interest, of amount debtor will finally pay to creditor, and

(hh) a clause in which the debtor acknowledges that his or her debt is being restructured arid that he or she is aware that the full sum including additional interest will be paid to the creditor over an extended period of time;

(d) whereby a person, directly or indirectly, for a reward, gives an instruction on behalf of an employee to an employer to cancel deductions from an employee before a written contract with creditors of the employee has been concluded;

(e) whereby a person, directly or indirectly, for a reward, does not make a full written disclosure to clients regarding costs, the legal status of any proposed arrangements or the risks involved;

(f) whereby a person, directly or indirectly, for a reward, receives payment for distribution purposes unless such payment has been deposited into an attorney's trust account, provided such account is covered by the Fidelity Fund provided for under the Attorneys Act 1979 (Act No 53 of 1979) or a separate trust account, providing the trust account is protected by legislation;

(g) whereby an administrator before appointment by the Court, directly or indirectly, receives any payment for his or her services before full written disclosure of the following:

(aa) what the cost of administration will be,

(bb) the manner in which the cost will be determined,

(cc) the method of collection, specifying whether the deduction of the administrator's expenses and remuneration will be effected prior to lodging the distribution account with the Court or whether it will be collected through the inclusion of the administrator in the distribution account,

failing which any money collected by the administrators without the full written disclosure should be deemed upfront fees;

(h) whereby a person, including an administrator appointed by the Court, directly or indirectly, does not reveal in writing the full implications and consequences of being placed under administration to a person before lodging such an application with Court;

(i) whereby a person, directly or indirectly, markets a scheme for the restructuring of any business for the purpose of circumventing the provision of legislation applicable to such business; and

(j) whereby a person, directly or indirectly, markets a scheme for the switching of any account from one financial institution to another without full written disclosure of all cost implications, provided any fee charged may not be more than such fee prescribed by applicable legislation

are hereby declared unlawful.

3. Subject to the provisions *of* paragraph **14,** the advertising by an intermediary, through any medium whatsoever -

(a) of the service whereby the oayment, for reward, excluding bank charges or lawfully permissible interest, of amounts to creditors on behalf of a debtor is undertaken;

(b) whereby a person, directly or indirectly, for a reward, undertakes to negotiate the restructuring of payments. also referred to as voluntary distribution, informal distribution or rehabilitation offers, before negotiations have been successfully performed and formal agreements have been reached with creditors;

(c) whereby a person, directly or indirectly, for a reward, does not make a full disclosure to clients regarding costs, the legal status of any proposed arrangements or the risks involved;

(d) whereby a person, including an administrator appointed by the Court, directly or indirectly, does not reveal the full implications and consequences of being placed under administration to a person before lodging such an application to *Court;*

(e) whereby a person, directly or indirectly, markets a scheme for the restructuring of any business for the purpose of circumventing the provision of legislation applicable to such business; and

(f) whereby a person, directly or indirectly, markets a scheme for the switching of any account from one financial institution to another without full disclosure of all cost implications

is hereby declared unlawful.

4. Subject to the provisions of paragraph 14, any intermediary is herewith prohibited, directly or indirectly, from entering into an agreement with a person in respect of a money lending transaction, credit facility, credit transaction, credit guarantee or any combination thereof or an application **by** any person to borrow an amount of money in terms whereof the applicant's obligation to repay the money is deferred in terms of an agreement in respect whereof any charge, fee or interest is payable, or requiring the payments of any valuable consideration of any kind to become **a** member of any institution, association, business or entity for the right to use services offered where the services offered include an application for any money lending transaction, credit facility, credit transaction, credit guarantee or any combination thereof, granting such intermediary the right, whether conditionally or unconditionally, to receive or to recover, on his own account or on behalf of any person other than the moneylender or credit provider, any valuable consideration, from the

borrower or from any person so applying, but excluding agreements in terms of which the fee of the intermediary is recovered directly from the consumer once the loan or credit application has resulted in the establishment of a loan or credit agreement with a loan or credit provider and in terms whereof the agreement between the intermediary and the consumer must *at least:*

(a) specify the exact service to be rendered by the intermediary,

(b) inform the consumer of the cost the loan or credit provider is entitled to recover from the applicant,

(c) disclose the intermediary fee to be charged in addition to the costs in (b) including the basis for calculating the fee, and

(d) specify the fee charged which may riot be more than such fee prescribed in applicable legislation; or

5. Subject to the provisions of paragraph **14,** any person is herewith prohibited, directly or indirectly, from entering into an agreement with a debtor, involving the payment, for reward, of amounts to creditors on behalf of that debtor, excluding bank charges or lawfully permissible interest.

6. Subject to the provisions of paragraph **14,** any person, including a person who has to be registered or appointed in terms of appropriate legislation, is herewith prohibited, directly or indirestly, from undertaking negotiations on behalf of a consumer for the restructuring of payments, also referred to as voluntary distribution, informal distribution or rehabilitation offers, for a reward, before negotiations have been successfully performed and written contracts have been concluded with creditors.

7. Subject to the provisions of paragraph **14,** any person is herewith prohibited, directly or indirectly, for a reward, from giving an instruction on behalf of an employee to an employer *to* cancel deductions from an employee before a written contract with creditors of the employee has been concluded. .

8. Subject to the provisions of paragraph 14, any person is herewith prohibited, directly or indirectly, for a reward, from undertaking any negotiations on behalf

of a consumer unless a full disclosure has been made to clients regarding costs, the legal status of any proposed arrangements or the risks involved.

9. Subject to the provisions of paragraph 14, any person is herewith prohibited, directly or indirectly, for a reward, from receiving payment for distribution purposes unless such payment has been deposited into an attorney's trust account, provided such account is covered by the Fidelity Fund provided for under the Attorneys Act 1979 (Act No 53 of 1979) or a separate trust account in terms whereof the trust account is protected by legislation.

10. Subject to the provisions of paragraph 14, any administrator before being appointed by the Court is herewith prohibited, directly or indirectly, from receiving any payment for his or her own account for services rendered before full written disclosure of:

(a) what the cost of administration will be,

(b) the manner in which the cost will be determined, and

(c) the method of collection, specifying whether the deduction of the administrator's expenses and remuneration will be effected prior to lodging the distribution account with the Court or whether it will be collected through the inclusion of the administrator in the distribution account.

11. Subject to the provisions of paragraph 14, any person, including an administrator appointed by the Court, is herewith prohibited, directly or indirectly, from negotiating with a consumer the placing of a person under administration unless the full implications and consequences of being placed under administration has been explained to a person before lodging such an application to Court.

12. Subject to the provisions of paragraph 14, any person is herewith prohibited directly or indirectly, from marketing a scheme for the restructuring of any business for the purpose of circumventing the provision of legislation applicable to such business,

13. Subject to the provisions of paragraph 14, any person is herewith prohibited, directly or indirectly, from marketing a scheme *for* the switching *of* any account from one financial institution to another without full disclosure of all cost implications.

14. This notice does not apply to-

(a) any person who practices as an attorney for his own account or as a partner in a firm of attorneys or as a member of a professional company, as defined in section 1 of the Attorneys Act, 1979 (Act No. 53 of 1979), provided the actions undertaken by such person are covered by the Fidelity Fund *as* provided for under the Attorneys Act (Act No. 53 of 1979); or

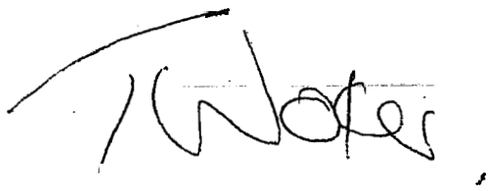
(a) any person who is registered as an accountant or auditor in terms of the Public Accountants' and Auditors' Act, 1991 (Act No. 5 *of* 1991), provided the actions undertaken by such person are covered in terms of the Fidelity Fund as provide for under the Public Accountants' and Auditors' Act, 1991 (Act No. 5 of 1991); or

(b) estate agents who are holders of fidelity fund certificates in terms of section 16 of the Estate Agencies Affairs Act, 1976 (Act No. 112 of 1976), provided the actions undertaken by such persons are covered in terms *of* the Fidelity Fund as provided for under Estate Agencies Affairs Act, 1976 (Act No. 112 of 1976); or

(d) a moneylender or a credit grantor or a lessor, as defined in section 1 of the Usury Act, 1968 (Act No. 73 of 1968), paying an intermediary for services rendered by him in connection with any transaction referred to in Regulation 2 (a); or

(e) a banking institution as defined in section 1 of the Banks Act, 1990 (Act No. 94 of 1990); or

(f) an employee or owner of any newspaper, magazine or other advertising medium provided it is in his or her official capacity as employee or owner of any newspaper, magazine or other advertising medium.



PROF T A WOKER

CHAIRPERSON: CONSUMER AFFAIRS COMMITTEE