



**Statutory set-off in terms of the National Credit Act 34 of 2005**

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## SUMMARY

It is generally accepted that set-off is a convenient manner of termination of mutual obligations that plays an important role as a method of debt settlement in modern society. This notwithstanding, many jurisdictions have regarded the common law operation of set-off as inadequate in the context of credit agreements, which is also the case in South Africa, as evinced by sections 90(2)(n) and 124 of the NCA. This dissertation aims to address the proposition that the National Credit Act (“NCA”) seems to have curtailed the rights of credit providers pertaining to set-off in relation to credit agreements regulated by the Act. The intention in this dissertation is to consider the provisions of the Act that deal with set-off, their impact on the corresponding common law right to set-off and the implications for both credit providers and consumers.

On the basis that the common law set-off method applies by the implied *ipso iure* operation of the law, the enquiry herein centres on the question whether the NCA, as it seems, has changed the entire set-off landscape for credit providers, and banks in particular, having regard to the provisions of section 90(2)(n) read with section 124. In the circumstances, the objective of this dissertation is to analyse the impact of said sections, through deliberation on the differing interpretations of these sections as currently provided for in the South African legal fraternity, focusing on considerations adopted as to whether, and if so, to what extent, the Act places a restriction on credit providers’ right to invoke set-off at common law, and whether same is desirable.

This dissertation will further explore the stance that sections 90(2)(n) and 124 of the NCA are unclear and lead to an outcome which either completely excludes a credit provider's common law right to set-off, or create an anomalous situation where a credit provider must refrain from including a provision permitting set-off in the credit agreement, in order to retain the right to apply it in terms of common law. Regard will also be had to the way in which our courts have interpreted and applied these particular provisions of the Act, taking into account their impact on the corresponding common law principle of set-off and considering the issue from a constitutional perspective.

## CHAPTER 1: GENERAL INTRODUCTION

### SUMMARY

- 1.1 Introduction and background
- 1.2 Problem statement
- 1.3 Aims and objectives of the study
- 1.4 Limitations of the study
- 1.5 Literature review
- 1.6 Research methodology
- 1.7 Chapter overview

### 1.1 Introduction and background

The National Credit Act was enacted on 15 March 2006 and became of full force and effect on 1 June 2007.<sup>1</sup> Having adopted a constitution when moving to a democratic regime in 1994,<sup>2</sup> South Africa introduced with this Act a novel post-constitutional credit landscape that aims at providing more inclusion to previously disadvantaged persons in particular, and greater protection to consumers in general.<sup>3</sup> The Act further recognises the necessity to maintain a sustainable credit market through striking a balance between the rights of consumers and credit providers to ensure a well-functioning credit market.<sup>4</sup> In this regard, the NCA lists a number of purposes or objectives in section 3 thereof. Our courts have interpreted section 3 to mean that the protection of the consumer is paramount, although a balanced approach to the rights of credit providers and consumers must be maintained in the interpretation of the Act, so as not to compromise the stability of the credit market.<sup>5</sup>

In its attempt to so strike a balance between consumers' rights and those of credit providers, the NCA has curtailed or restricted many rights previously afforded to

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<sup>1</sup> 34 of 2005 (hereinafter "National Credit Act", "NCA" or "Act"); See Proc 22, 2006 in GG 28824 of 2006-05-09. Unless indicated otherwise, all references to sections and regulations hereinafter will be in accordance with the Act.

<sup>2</sup> The Constitution of the Republic of South Africa, 1996 "Constitution", which contains a Bill of Rights in Ch 2 that entrenches several fundamental human rights.

<sup>3</sup> Van Heerden "The National Credit Act 34 of 2005 and its impact on set-off" 2017 *Annual Banking Law Update* ("ABLU") 97.

<sup>4</sup> Van Heerden 2017 *ABLU* 97, 109.

<sup>5</sup> *Nedbank Ltd v The National Credit Regulator* 2011 (3) SA 581 (SCA) ("Nedbank v NCR"); Scholtz (ed) *Guide to the National Credit Act* (2008) para 2.4; Van Heerden 2017 *ABLU* 109.

credit providers under the erstwhile credit dispensation,<sup>6</sup> which was essentially regulated in terms of the Credit Agreements Act, Usury Act,<sup>7</sup> and the common law. The statutory *in-duplum* rule provided for in section 103(5) of the Act serves as an example, insofar as this section affords consumers protection at a much earlier stage than was the case in terms of the corresponding rule as provided for at common law.<sup>8</sup> The new comprehensive debt relief mechanism/regime introduced by the Act is another instance whereby consumers are granted additional and greater protection than was previously the case, through the operation of the provisions of Part D of Chapter 4 of the Act, which provisions pertain to reckless credit and over-indebtedness.<sup>9</sup> Of significance to the discussion at hand, the NCA seems to have curtailed the rights of credit providers pertaining to set-off in relation to credit agreements regulated by the Act.<sup>10</sup>

Set-off is a common law method of debt settlement by which obligations, whether arising contractually or otherwise, can be terminated without requiring the exchange of performance by parties who are mutually (reciprocally) indebted to each other.<sup>11</sup> The common law principle of set-off has been explained as constituting a valuable commercial tool that offers simplification, convenience and efficiency, as well as the avoidance of circuity of payment.<sup>12</sup> Moreover, it also fulfills a security function from the perspective of a creditor and effects a “fair outcome”, provides a defence, facilitates debt collection and prevents default by consumers. One of the more prominent advantages of common law set-off is that it offers the creditor considerable control in that where the creditor is for instance a bank, it can decide to appropriate money from another account (for instance a savings account) held by that consumer with the bank, where the consumer fails to make payment of an instalment in terms of a credit agreement concluded with such bank.<sup>13</sup> Since common law set-off applies by the implied *ipso iure* operation of the law, the creditor bank will be able to appropriate such monies without prior

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<sup>6</sup> Van Heerden 2017 *ABLU* 97-98.

<sup>7</sup> 75 of 1980 and 73 of 1968, respectively.

<sup>8</sup> Van Heerden 2017 *ABLU* 98.

<sup>9</sup> Van Heerden 2017 *ABLU* 98, 101.

<sup>10</sup> Van Heerden 2017 *ABLU* 98.

<sup>11</sup> Van Heerden 2017 *ABLU* 99; Van der Merwe, Van Huyssteen, Reinecke and Lubbe *Contract: General principles* (2012) 469.

<sup>12</sup> Van Heerden 2017 *ABLU* 99.

<sup>13</sup> Van Heerden 2017 *ABLU* 101; Van Deventer *Set-Off in South African Law: Challenges and opportunities* (2016) LLM dissertation (“Van Deventer LLM dissertation”) 114, 123.

notification to the consumer and there are no formalities that the bank is required to comply with.<sup>14</sup>

Banks have historically done and continue to do business utilising the common law method of set-off;<sup>15</sup> they are in a *sui generis* position, as opposed to other creditors that may want to apply the common law method of set-off, given that they occupy an advantageous position as financial intermediaries of consumers and keep various accounts for them (i.e. savings, current, credit, *etcetera*) from which they are therefore able to appropriate monies through the operation of the common law method of set-off.<sup>16</sup> This advantageous position of banks in relation to the common law application of set-off has potentially been compromised by the coming into operation of the NCA.<sup>17</sup>

The National Credit Act has seemingly changed the entire set-off landscape for credit providers, and banks in particular, having regard to the provisions of section 90(2)(n) read with section 124. The former subsection deals with unlawful provisions in credit agreements and specifically provides that a credit agreement that allows a charge to be made against an account, amongst other, may not be utilised in a way that is not authorised in terms of section 124.<sup>18</sup> Stated differently, section 90(2)(n) makes unlawful a provision in a credit agreement that allows the credit provider to appropriate money from one account to cure the default in another account, unless this is done in a way that meets the requirements of section 124.<sup>19</sup> Section 124, in turn, creates quite an elaborate process in terms of which a credit provider who wants to make a charge or a series of charges, for purposes of facilitating repayment of debt by the debtor/consumer, is required to obtain prior authorisation from such consumer.<sup>20</sup>

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<sup>14</sup> Van Heerden 2017 *ABLU* 106.

<sup>15</sup> Van Heerden 2017 *ABLU* 107.

<sup>16</sup> Van Heerden 2017 *ABLU* 100; *Absa Bank Ltd v Intensive Air (Pty) Ltd* 2011 (2) SA 275 (SCA) (“*Absa Bank v Intensive Air*”).

<sup>17</sup> Van Heerden 2017 *ABLU* 98, 101.

<sup>18</sup> Van Deventer “The enforcement of credit agreements through set-off: Evaluating the impact of the National Credit Act 34 of 2005” 2017 *SALJ* 415; Van Heerden 2017 *ABLU* 102.

<sup>19</sup> Van Deventer 2017 *SALJ* 420.

<sup>20</sup> Van Heerden 2017 *ABLU* 106, 109.

## 1.2 Problem statement

In this dissertation the impact of sections 90(2)(n) and 124 of the National Credit Act on the common law right to invoke set-off will be analysed.<sup>21</sup> There will be a focus on the interpretation of these sections and consideration as to whether, and if so, to what extent, the Act places a restriction on credit providers' right to invoke set-off and whether this is desirable.<sup>22</sup> Considering that an analysis of policy documents prepared during the drafting of the NCA indicates that insufficient consideration was given to the consequences of limiting a credit provider's right to apply set-off,<sup>23</sup> this dissertation will explore the stance that sections 90(2)(n) and 124 of the NCA are unclear and lead to an outcome which either completely excludes a credit provider's common law right to set-off, or create an anomalous situation where a credit provider must refrain from including a provision permitting set-off in the credit agreement, in order to retain the right to apply it.<sup>24</sup> Regard will also be had to the way in which our courts have interpreted and applied these particular provisions of the Act, taking into account their impact on the corresponding common law principle of set-off and considering the issue from a constitutional perspective.

Accepting the proposition that it is apparent from section 3 of the Act that its objectives include the prevention of contractual default by consumers, it is arguable that the common law model of set-off is indeed in line with the objectives of the NCA.<sup>25</sup> However, the provisions of sections 90(2)(n) and 124 of the NCA seem to be at odds with this latter proposition. This ambiguous position created by the Act has posed challenges to credit providers, and banks in particular, insofar as the application of the common law method of set-off to credit agreements regulated by the NCA are concerned,<sup>26</sup> a fact attested to by case law that has dealt with this particular problem and that will also be addressed in the study.

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<sup>21</sup> Van Deventer 2017 *SALJ* 415.

<sup>22</sup> Van Deventer 2017 *SALJ* 415-416.

<sup>23</sup> Van Deventer LLM dissertation 126-135; Van Heerden 2017 *ABLU* 107.

<sup>24</sup> Van Van Deventer 2017 *SALJ* 421; Van Deventer LLM dissertation 117-118, 122; Van Heerden 2017 *ABLU* 102, 107.

<sup>25</sup> Van Heerden 2017 *ABLU* 109; Scholtz (ed) para 2.4; *National Credit Regulator v Standard Bank of South Africa Limited* 2019 (5) SA 512 (GJ).

<sup>26</sup> Van Heerden 2017 *ABLU* 109, Van Deventer 2017 *SALJ* 421.

### 1.3 Aims and objectives of the study

On the basis that the National Credit Act seems to have restricted credit providers' common law right to rely on set-off, the intention in this dissertation is to consider the provisions of the Act that deal with set-off, their impact on the common law right to set-off and the implications for both credit providers and consumers. It is generally accepted that set-off is a convenient manner of termination of mutual obligations that plays an important role as a method of debt settlement in modern society.<sup>27</sup> This notwithstanding, many jurisdictions have regarded the common law operation of set-off as inadequate in the context of credit agreements, which is also the case in South Africa as evinced by sections 90(2)(n) and 124 of the NCA.<sup>28</sup>

Having regard to the considerations that inform the objectives of credit legislation such as the NCA, it is important to ensure that the rights of consumers are not unreasonably or unjustifiably inclined towards consumers' protection at the expense of credit providers, with the effect that the sustainability of the credit market is compromised.<sup>29</sup> If this is not guarded against, the potential regulatory barriers created by the NCA will distort and/or curtail the ability of credit providers to continue the high-risk business of credit provision, which event may encourage some credit providers to exit the market, thereby leaving room for a much more concentrated market wherein access to credit will be impeded.<sup>30</sup> Furthermore, this may even result in lucrative opportunities and perverse incentives for loan sharks who are unscrupulous to operate below the regulatory radar. Also, where more regulatory compliance is required of credit providers through legislative intervention, this may have the unintended consequence of costs eventually filtering down to the consumers.<sup>31</sup> This, in turn, will be tantamount to impeding access to credit as such regulatory compliance will have eventuated in the high cost of credit and this will not be in line with the abovementioned objectives of the Act provided for in section 3.

As briefly explained above, the apparent departure of the National Credit Act from the common law principles of set-off has created uncertainty regarding the ambit

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<sup>27</sup> Van Deventer 2017 *SALJ* 415.

<sup>28</sup> Van Deventer 2017 *SALJ* 415.

<sup>29</sup> Van Heerden 2017 *ABLU* 109.

<sup>30</sup> Van Heerden 2017 *ABLU* 97.

<sup>31</sup> Van Heerden 2017 *ABLU* 97.

of the abovementioned provisions, and specifically their impact on credit providers.<sup>32</sup> Of more concern from a banking law perspective, the ability to apply common law set-off is very vital for the continued business of banks and their continued sustainability as credit providers, since they need to retain the security that the common law method of set-off avails them by allowing money grabbing from other accounts of consumers, without having to comply with the stringent notification requirements prescribed by section 90(2)(n) read with section 124.<sup>33</sup>

#### **1.4 Limitations of the study**

The study will be limited to consideration of set-off in circumstances where a bank appropriates money from a consumer's account with a positive balance to cure outstanding arrears on a credit agreement that such consumer has with the same bank.<sup>34</sup> Furthermore, and in that context, this dissertation aims to analyse the general principles of set-off at common law, as juxtaposed against those propounded in the statutory version contained in the National Credit Act. As such, this dissertation will therefore not contain any discussion of the rules pertaining to set-off in insolvency as prescribed by the Insolvency Act 24 of 1936, specifically section 46 thereof.<sup>35</sup>

#### **1.5 Literature review**

A wide array of literature is available on the general principles of the common law method of set-off, albeit that there exist somewhat competing views on its operation (insofar as whether or not same operates retrospectively or automatically).<sup>36</sup> Whilst said general principles of common law set-off have been regarded as inadequate in many legal systems in regard to its application to credit agreements,<sup>37</sup> there is somewhat of a dearth of information in relation to the question whether set-off as provided for in relevant credit legislation results in the complete ousting of the common law application thereof, as seems to be the case with sections 90(2)(n) and 124 of the National Credit Act. The latter aspect notwithstanding, there is nevertheless literature on the topics traversed above,

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<sup>32</sup> Van Heerden 2017 *ABLU* 98.

<sup>33</sup> Van Heerden 2017 *ABLU* 111.

<sup>34</sup> Van Heerden 2017 *ABLU* 98; Van Deventer 2017 *SALJ* 416.

<sup>35</sup> Van Deventer LLM dissertation 9.

<sup>36</sup> Van Deventer 2017 *SALJ* 416.

<sup>37</sup> Van Deventer 2017 *SALJ* 415.

some of which will inform the study to be conducted on the basis briefly outlined below.

The case of *National Credit Regulator v Standard Bank of South Africa Limited* may appositely be termed the current *locus classicus* in South African law on the question of what the proper construction is of the statutory set-off method when juxtaposed with the common law version of same rule, in relation to credit agreements that are regulated by the NCA. In this matter the National Credit Regulator<sup>38</sup> instituted proceedings for a declaratory order that section 124 of the Act has superseded the common law method of set-off and the court considered at length the opposing interpretations proffered on behalf of both credit providers (banks in this instance) and consumers. This judgment is seminal to ventilating the extent of the contending viewpoints regarding the correct interpretation to be attributed to the effect of sections 90(2)(n) and 124 of the NCA on the common law right to set-off and it conclusively pronounces on the proper construction to be afforded same provisions.

Scholtz (ed) explains how the National Credit Act should generally be interpreted, according to our courts, premised on the basis that interpretation of the Act has become increasingly contentious particularly in relation to balancing the respective rights and obligations of consumers and credit providers. The text is useful as it includes a focused discussion on the interpretational problem presented by sections 90(2)(n) and 124, both in the ordinary course and as through a constitutional prism, as was deliberated on in the relevant judgment to be addressed in this study.

Van Der Merwe, Van Huyssteen, Reinecke and Lubbe (2012) dedicates a section on a discussion of the general principles of the common law method of set-off and informs this study insofar as it provides background to the analysis of whether sections 90(2)(n) and 124 of the NCA prohibit a credit provider from relying on common law set-off.

Van Deventer LLM dissertation provides a detailed and critical overview of the development of set-off within the South African law. Of importance to the study to be undertaken, this text discusses at length the wildly divergent interpretations of

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<sup>38</sup> Hereinafter “the NCR”.

sections 90(2)(n) and 124 that exist and also provides a brief discussion of how credit legislation in other jurisdictions deals with the common law method of set-off, as well as looks extensively at the draft papers informing the introduction of the NCA to determine what may have been the considerations that resulted in the enactment of sections 90(2)(n) and 124 in particular, with the impact that they potentially have on the common law method of set-off.

Van Deventer 2017 *SALJ*: this journal contribution is largely based on the discussion in her above dissertation on common law set-off and how the NCA has impacted on common law set-off. In addition, this text briefly discusses the one case in South Africa that has dealt with the interpretation of sections 90(2)(n) and 124 in light of the common law method of set-off, as at the time of her LLM dissertation the judgment had yet to be delivered.

Van Heerden 2017 *ABLU* dedicates the entire contribution to the impact of sections 90(2)(n) and 124 on the common law principle of set-off, with specific focus on the context of banks as credit providers. This contribution is useful as a source given the very limitation to an examination of the said impact on banks as credit providers, particularly as the aim in this dissertation is to limit the study in the very same way. In the circumstances, the text explores the challenges as they pertain exclusively on banks and even broadens the potential problems of these sections in the NCA in ways that have yet to be addressed by our courts and academic commentators alike.

## **1.6 Research methodology**

The general principles and functions of set-off will first be outlined to provide the necessary background to the analysis of whether sections 90(2)(n) and 124 of the National Credit Act prohibit a credit provider from relying on the common law right to set-off,<sup>39</sup> after which a brief investigation of these provisions regarding set-off contained in the NCA will be explained and juxtaposed as against consumer legislation of other jurisdictions, which may have influenced or informed the drafting of the NCA.<sup>40</sup> This will be followed by a brief exposition of how same provisions have been deliberated on by academic commentators and our courts,

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<sup>39</sup> Van Deventer 2017 *SALJ* 416.

<sup>40</sup> Van Deventer 2017 *SALJ* 416, 422.

having regard to the common law method and their general impact on both consumers and credit providers. A brief discussion on the impact of this matter from a constitutional perspective will also be included.

The analysis will be concluded with recommendations of a potential way forward to cure the apparent impasse that has been created, which will essentially amount to the conclusion that although the limitation of credit providers' right to invoke set-off may be justified, the conditions set by the NCA may be too stringent.<sup>41</sup> In the circumstances, legislative reform will be suggested for purposes of clarifying and improving the protection granted by the NCA,<sup>42</sup> insofar as set-off is concerned.

## **1.7 Chapter overview**

The first chapter will serve as the general introduction to the dissertation, where the research title, problems and question will be addressed. The literature review, motivation for and significance of the study, as well as the research methodology will also be contained in this chapter, which chapter shall conclude with a chapter overview.

The second chapter will be an overview of the general principles of set-off as at common law, encompassing a brief discussion of the origin thereof, the way in which it operates, and a limited consideration of opposing views that prevail in the legal fraternity as regards the aspect relating to the operation of the common law set-off.

Chapter three will address the ambit and scope of sections 90(2)(n) and 124 of the National Credit Act, consider their impact on the common law right to set-off, investigate varying considerations that have been addressed in the attempt to construct the appropriate interpretation to be attributed to those sections, and assess similar provisions in jurisdictions with similar credit legislation to ascertain the origins of the provisions in question, with particular focus on this matter from a banking sector perspective. Policy considerations informing these provisions, as well as the origin and purpose thereof will be examined to determine the ambit and

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<sup>41</sup> Van Deventer 2017 *SALJ* 415.

<sup>42</sup> Van Deventer 2017 *SALJ* 415.

desirability of the limitation presented by these sections on a credit provider's right to common law set-off.

The fourth chapter will in conclusion be dedicated to considerations and arguments presented on behalf of both consumers and credit providers in relation to whether the statutory set-off method indeed abrogates the common law version thereof, as was ventilated and deliberated in the matter of *National Credit Regulator v Standard Bank of South Africa Limited*. This chapter will also conclude the dissertation with further deliberations and recommendations, from both a general and a constitutional perspective on the matter at hand.

## CHAPTER 2: COMMON LAW RIGHT TO SET-OFF

### SUMMARY

- 2.1 Legal nature of set-off
- 2.2 General requirements of set-off
- 2.3 Operation of set-off
  - 2.3.1 Brief historical development of set-off
  - 2.3.2 Theoretical approaches to operation of set-off in modern law
  - 2.3.3 Operation of set-off in South Africa
- 2.4 Conclusion

#### 2.1 Legal nature of set-off

In terms of general principles of contract law, obligations are terminated by operation of law or by a juristic act.<sup>43</sup> Although there is some uncertainty in this regard, set-off leads to the extinction of obligations by operation of law where persons are reciprocally indebted to one another.<sup>44</sup> Stated differently, set-off entails the extinguishing of obligations between two people who are indebted to each other, due to distinct obligations that exist between them, without requiring the exchange of performance.<sup>45</sup> Where the debts are equal in extent, complete mutual extinction will take place through the operation of set-off; whilst on the other hand, a larger debt will be extinguished *pro tanto* by a smaller debt.<sup>46</sup>

There further exists uncertainty as regards the theoretical nature of set-off, insofar as it has been regarded as involving the “reciprocal cancellation” of respective claims or deemed to be a form of payment.<sup>47</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe reject both these constructions of the nature of set-off, on the basis that the former view (“reciprocal cancellation”) is misleading given that set-off does not require agreement between the parties. They further assert it cannot

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<sup>43</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe *Contract: General principles* (2007) 511.

<sup>44</sup> Van der Merwe Van Huyssteen, Reinecke and Lubbe (2007) 511-512; *Schierhout v Union Government (Minister of Justice)* 1926 AD 286 (“*Schierhout*”); *Standard Bank of South Africa Ltd v SA Fire Equipment (Pty) Ltd* 1984 (2) SA 693 (C) (“*SA Fire Equipment*”).

<sup>45</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 546; Van Deventer LLM dissertation 1.

<sup>46</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 546; Van Deventer LLM dissertation 1.

<sup>47</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 546; *Treasurer-General v Van Vuuren* 1905 TS 588, (“*Treasurer-General*”); *Joint Municipal Pension Fund (Transvaal) v Pretoria Municipal Pension Fund* 1969 (2) SA 78 (T) 86A (set-off is “a payment effected *brevi manu*”).

be a form of payment as propounded in terms of the second view, since “[a]lthough similar in effect to payment in that the debts are substantively satisfied, set-off differs from payment in that no extinguishing agreement is required”.<sup>48</sup>

As alluded to above, it is uncertain whether set-off amounts to the automatic discharge of debts through the operation of law based on policy; or whether it is a function of a unilateral juristic act through which one party effects the discharge of the debts: either stance depends on the construction attributed to the operation of set-off.<sup>49</sup> Notwithstanding these supposedly opposing constructions, set-off remains a termination of obligations method that is efficient, given that it promotes prompt debt settlement and avoids costly and cumbersome duplication of performance.<sup>50</sup> Moreover, it serves a security function to the extent that it allows a party to enforce the fulfilment of obligations even where fulfilment may be difficult or impossible to enforce.<sup>51</sup> The benefit of this security function is particularly evident in the context of insolvency, as a party who was able to invoke set-off prior to *concursum creditorum* will be allowed to rely thereon,<sup>52</sup> should such set-off conform to the requirements stipulated in section 46 of the Insolvency Act 24 of 1936.<sup>53</sup>

It has further been said that set-off results in the “highest equity”, on the basis that it ensures fairness of outcome: firstly because it provides a defence against a claim where a counterclaim exists; secondly because it allows for the enforcement of a due obligation where there may be an inability or unwillingness to fulfil same; and lastly because it caters for circumstances where there may be lack of financial resources, yet the obligation in question will nevertheless be discharged.<sup>54</sup>

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<sup>48</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 546.

<sup>49</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 546.

<sup>50</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 546.

<sup>51</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 547; Van Deventer LLM dissertation 6.

<sup>52</sup> *Concursum creditorum* being the coming together of the creditors in the context of insolvency.

<sup>53</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 547; Van Deventer LLM dissertation 6.

<sup>54</sup> Van Deventer LLM dissertation 7.

## 2.2 General requirements of set-off

South African law adopted set-off requirements from Roman-Dutch law, which requirements have remained largely unchanged and are mostly settled, as well as uncontroversial.<sup>55</sup> First of the requirements is mutuality of obligations, which requires that there exist obligations between persons in their personal capacities.<sup>56</sup> This means that where a claim is brought in a representative capacity, set-off may not be raised against such claim;<sup>57</sup> nor can set-off be raised against a counterparty for a debt owed by the latter to a third party.<sup>58</sup>

Set-off becomes more complicated where there is a multiplicity of parties involved, such as where there is common or collective joint liability: set-off may not be invoked where the claim brought pertains only to some of those who are liable.<sup>59</sup> The view popularly espoused in relation to joint and several liability,<sup>60</sup> is that set-off will only operate where the claim in question is brought as against the party with whom a mutuality of obligations exists, such that the other parties will therefore not be able to so invoke set-off for the claim in relation to which they are jointly and severally liable for, notwithstanding that the benefit of the set-off invoked by the first mentioned party will apply in respect of all the solidarity parties.<sup>61</sup> The only instances where set-off may be invoked absent the presence of mutuality of obligations, is in the case of a surety and in certain instances of cession.<sup>62</sup> The surety may rely on set-off pursuant to a claim against the principal, given that the

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<sup>55</sup> Van Deventer LLM dissertation 35.

<sup>56</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 547; Van Deventer LLM dissertation 35; *Schierhout, Treasurer-General; Motani Lounge (Pty) Ltd v Standard Bank of South Africa Ltd* 1995 (2) SA 498 (W) 516; *AA Brick Co (Pty) Ltd v Coetzee* 1996 (3) SA 578 (BSC), (“*AA Brick Co (Pty) Ltd*”).

<sup>57</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 547; Van Deventer LLM dissertation 35; *De Beer v Kotze* 1913 CPD 252; *Strachan v The Master* 1963 (2) SA 620 (N).

<sup>58</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 547; Van Deventer LLM dissertation 35; *Liquidators of the Cape Good Hope Bank v Forde & Co* (1980) 8 SC 30; *SA Fire Equipment (Pty) Ltd*.

<sup>59</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 547; Van Deventer LLM dissertation 35; *Strydom v Protea Eiendomsagente* 1979 (2) SA 206 (T).

<sup>60</sup> Where two or more wrong-doers are *jointly and severally liable*, each such party is independently liable for the full extent of the damage stemming from the wrong-doing. Thus, if a plaintiff is granted damages against said parties collectively, the plaintiff may collect the full value of the judgment from any one of the wrong-doers.

<sup>61</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 547; Van Deventer LLM dissertation 35; *Bain v Barclays Bank (DC & O)* 1973 SR 191; *SA Fire equipment (Pty) Ltd*.

<sup>62</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 548; Van Deventer LLM dissertation 36.

ancillary nature of the liability of the surety does not conflict with the mutuality requirement.<sup>63</sup> The claim of a cessionary will also be able to be defeated through the invocation of set-off, on the basis that prior to the cession there existed mutual obligations with the cedent, which obligations satisfied the requirements of set-off.<sup>64</sup>

It is secondly required that the debts in question must be capable of set-off, which essentially means that the debts must be of the same kind or *eiusdem generis*: this allows for the subject-matter of the obligations to be compared in a balanced manner.<sup>65</sup> In the circumstances, monetary obligations are ordinarily susceptible to set-off, but so too are non-monetary goods such as fungibles of the same class, for example mealies of the same type and grade.<sup>66</sup> That said, set-off may not be applied where the obligations concerned involve the delivery of a thing from a class of things, as against delivery of a specific thing from that same class.<sup>67</sup> A bank cannot, for example, set-off a claim against a client for non-payment of an overdraft facility against the client's claim for the return of valuables deposited with that bank.<sup>68</sup> Further, set-off will not be permitted in the following instances:<sup>69</sup> where its application will be contrary to public policy; it is in respect of illegal debts, claims due to a person (such as those for maintenance or wages), or taxes;<sup>70</sup> and where goods are obtained consequent of a delict or are left with another in accordance with a contract of *depositum*.<sup>71</sup>

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<sup>63</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 548; Van Deventer LLM dissertation 36; *JR & M Moffet (Pty) Ltd v Kolbe Eiendoms Beleggings (Edsm) Bpk* 1974 (2) SA 426 (O); *Miller v Muller* 1965 (4) SA 458 (C); *SA Fire Equipment (Pty) Ltd*.

<sup>64</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 548; Van Deventer LLM dissertation 37; *Walker v Syfert* 1911 AD 141; *SA Fire Equipment (Pty) Ltd*.

<sup>65</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 548; Van Deventer LLM dissertation 37.

<sup>66</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 548; Van Deventer LLM dissertation 37; *Van der Vyver v Gee* (1980) 25 SC 632; *Langsdell v Sam* 1912 CPD 335.

<sup>67</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 548; Van Deventer LLM dissertation 37.

<sup>68</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 549; *Ngangelizwe Kama v Yates & Murry* (1902) 17 EDC 60 ("*Ngangelizwe Kama*").

<sup>69</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 549; *Ngangelizwe Kama*; *Lawson v Stevens* 1906 TS 481; *Whelan v Oosthuizen* 1937 TPD 304 ("*Whelan*").

<sup>70</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 549; Van Deventer LLM dissertation 38; *Schierhout, Tregoning v Tregoning* 1914 WLD 95; *Luttig v Luttig* 1994 (1) SA 524 (O); *Commissioner of Taxes v First Merchant Bank of Zimbabwe Ltd* 1998 (1) SA 27 (ZS).

<sup>71</sup> According to our courts: "A contract of depositum comes into existence when one person (the *depositor*) entrusts a movable thing to another person (the *depositarius*) who undertakes to care for it gratuitously and to return it at the request of the *depositor*".

The operation of set-off thirdly requires that both debts be due and payable, thus enforceable.<sup>72</sup> As such, in cases of debts that are subject to time clauses,<sup>73</sup> or are contingent on suspensive conditions,<sup>74</sup> or where a claim can be defeated by a valid defence (for instance through the invocation of the *exceptio non adimpleti contractus*),<sup>75</sup> set-off may not be applied.<sup>76</sup> This notwithstanding and based on the construction that “set-off involves the payment of the principal claim with money owed to the person raising set-off”, De Wet and Van Wyk argue that the only claim that needs be due and enforceable is the claim sought to be raised in set-off.<sup>77</sup>

The fourth requirement of set-off is that the debts involved must be liquidated, thus capable of speedy and easy proof.<sup>78</sup> The rationale for this requirement is said to be that where the main claimant is able to easily prove or has proven his claim, the outcome of the court proceedings should not be unduly delayed by reason of complicated counter claims.<sup>79</sup> On that premise, where there exists an unliquidated counterclaim reliance on set-off will not be possible, but the benefits of set-off may nevertheless be obtained through instituting a claim in reconvention pursuant to institution of the main claim.<sup>80</sup> In such an instance, the rules of court dictate that judgment on the respective claims is to be given simultaneously and, if successful,

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<sup>72</sup> Van der Merwe Van Huyssteen, Reinecke and Lubbe (2007) 549; Van Deventer LLM dissertation 38; *Schierhout, Treasurer-General* 589-590; *Roman Catholic Church (Klerksdorp Diocese) v Southern Life Association Ltd* 1992 (2) SA 807 (A) 814-815; *Siltek Holdings (Pty) Ltd (in liquidation) t/a Workgroup v Business Connexion* 2009 1 All SA 571 (SCA) (“*Siltek Holdings (Pty) Ltd (in liquidation) t/a Workgroup*”).

<sup>73</sup> A time clause is a contractual provision that makes the existence of an obligation dependent on an event or time that will arise in future as stipulated.

<sup>74</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 550; Van Deventer LLM dissertation 38; *Siltek Holdings (Pty) Ltd (in liquidation) t/a Workgroup*; *Schnehage v Bezuidenhout* 1977 (1) SA 362 (O) 365, (“*Schnehage*”); *Asco Carbon Dioxide Ltd v Lahner* 2005 (3) SA 213 (N).

<sup>75</sup> *Exceptio non adimpleti contractus* is a defence in South African law that allows a party to withhold its own performance and permits such party the right to ward off a claim for such performance pending due performance by the other party of its obligations in terms of the governing contract.

<sup>76</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 550; Van Deventer LLM dissertation 38; *Schnehage* 366.

<sup>77</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 550; Van Deventer LLM dissertation 39.

<sup>78</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 550; Van Deventer LLM dissertation 40; *Treasurer-General* 588; *Whelan; Lester Investments (Pty) Ltd v Narshi* 1951 (2) SA 464 (C); *AA Brick Co (Pty) Ltd*.

<sup>79</sup> Van Deventer LLM dissertation 40; *Trotman v Edwick* 1950 (1) SA 376 (C).

<sup>80</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 550; Van Deventer LLM dissertation 40.

the claim in reconvention will become liquidated and therefore susceptible to set-off.<sup>81</sup>

Parties may exclude the operation of set-off by agreement.<sup>82</sup> Van Deventer aptly argues that notwithstanding that the requirements of set-off are fairly settled, it is apparent that the manner in which these requirements will be applied will be impacted by the approach adopted in relation to the operation of set-off;<sup>83</sup> a topic to be addressed next.

### **2.3 Operation of set-off**

Rules in South African law that pertain to the operation of set-off derive from Roman and Roman-Dutch law, as is the case in other legal systems that share the same legal historical foundations, which rules in themselves lack clarity, apparently due to what Zimmerman describes as “Justinian’s somewhat halfhearted attempts to consolidate the rules of classical Roman jurisprudence”.<sup>84</sup> Therefore, to gain an appreciation of the uncertainty that seems to prevail in modern legal systems in relation to the operation of set-off, it is instructive to briefly examine its origins and development.<sup>85</sup> A summary overview of the development of set-off from its Roman law origins through to its application in Roman-Dutch law is particularly apposite as the principles then developed and applied were eventually adopted in South African law.<sup>86</sup> Further, said principles inform the understanding of the operation of set-off as currently applicable in South African law.<sup>87</sup>

#### **2.3.1 Brief historical development of set-off**

*Compensatio* or set-off in classical Roman law only operated in the context of judicial proceedings, as it was purely a procedural mechanism.<sup>88</sup> With the

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<sup>81</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 550; Van Deventer LLM dissertation 40; *SA Fire Equipment (Pty) Ltd Consol Ltd t/a Consol Glass v Twee Jongegezellen* 2002 (2) SA 580 (C).

<sup>82</sup> Van der Merwe Van Huyssteen, Reinecke and Lubbe (2007) 550; *Herrigel NO v Bon Roads Construction Co (Pty) Ltd* 1980 (4) SA 669 (SWA) (“*Herrigel NO*”); *Altech Data (Pty) Ltd v MB Technologies (Pty) Ltd* 1998 (3) SA 748 (W).

<sup>83</sup> Van Deventer LLM dissertation 41.

<sup>84</sup> Van Deventer LLM dissertation 11, 42.

<sup>85</sup> Van Deventer LLM dissertation 11.

<sup>86</sup> Van Deventer LLM dissertation 11.

<sup>87</sup> Van Deventer LLM dissertation 11.

<sup>88</sup> Van Deventer LLM dissertation 11.

exception of where parties reached agreement regarding set-off, it was only recognised in three specific instances being *bonae fidei* actions, actions by bankers and actions by the purchasers of insolvent estates (*bonorum emptor*).<sup>89</sup> These actions all required that the claims in question existed between the same parties, but they all had separate requirements.<sup>90</sup>

A trend towards generalisation of set-off gained traction in post classical Roman law and the distinction between different forms of *compensatio* gradually disappeared.<sup>91</sup> In response to this change, Justinian embarked on an attempt to formulate a rule, by decree, that permitted set-off to apply by operation of law in all circumstances where claims were capable of immediate assessment.<sup>92</sup> Of importance to the discussion under hand, is that in his attempt to standardise and generalise the fragmented approach to set-off in Roman law, Justinian failed to clarify the meaning of his decrees that set-off takes place “*ipso iure*”, which in turn caused different views to develop about the operation of set-off.<sup>93</sup>

From a perspective of the ordinary meaning of the phrase “*ipso iure*”, this entails that set-off would take place automatically, without the intervention of neither the judge nor the parties, such that both claims would be regarded as extinguished due to the mere fact that they co-existed. However, the above referenced uncertainty prevailed and caused the formation of divergent views as to the operation of set-off.<sup>94</sup> To that end, the Glossators found themselves on different ends of the spectrum regarding the question whether set-off operated completely automatically, or subject to a declaration in court – albeit automatic in principle.<sup>95</sup>

Recognising the impracticality of attributing a complete automatic effect to set-off, the Roman-Dutch jurists and Pandectists determined a declaration was necessary, yet they failed to meet minds on the question of whether such declaration has a substantive effect or merely served as notification of the automatic extinguishing of the debts in question.<sup>96</sup> Van Deventer deliberates that the ill-fated use of the

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<sup>89</sup> Van Deventer LLM dissertation 11.

<sup>90</sup> Van Deventer LLM dissertation 11.

<sup>91</sup> Van Deventer LLM dissertation 20.

<sup>92</sup> Van Deventer LLM dissertation 20.

<sup>93</sup> Van Deventer LLM dissertation 20, 32-33.

<sup>94</sup> Van Deventer LLM dissertation 32-33.

<sup>95</sup> Van Deventer LLM dissertation 32-33.

<sup>96</sup> Van Deventer LLM dissertation 32-33.

phrase “*ipso iure*” in Justinian’s decrees, coupled with the loss of context of certain texts over time, may well have attributed to the different groups of jurists having been misled as regards the operation of set-off, resulting in varying and oft opposing approaches to the operation of set-off.<sup>97</sup>

### **2.3.2 Theoretical approaches to the operation of set-off in modern law**

The debate regarding whether set-off takes place automatically or requires a declaration to take effect persists and remains unsettled in modern law,<sup>98</sup> with the consequence that although a historical overview is useful in delineating the development of set-off, it does not show a preferred approach to be adopted, nor does it answer conclusively the question of how set-off should operate.<sup>99</sup> As different approaches to set-off evolved pursuant to what Zimmerman refers to as “the heritage of Justinian’s dark pronouncements”, so too are different approaches to be found in modern law regarding the operation of set-off, which approaches/models Zimmerman contends there are potentially five of (briefly discussed below).<sup>100</sup>

In the first instance there is the view that set-off takes place *ipso iure*, with the effect that the debts are extinguished automatically, immediately on their co-existence, and no declaration or other action by either party is necessary for set-off to operate.<sup>101</sup> Therefore, where the requirements of set-off are met, the claims will be extinguished to the relevant extent, interest will no longer run and all sureties and security will be released.<sup>102</sup> Should a debtor not perform after set-off could operate there can be no question of default and any payments made after set-off could operate may be reclaimed as undue payment.<sup>103</sup> Since debts are extinguished at the earliest possible moment without any intervention by the parties, this view champions the stance that the payment function of set-off is a convenient mechanism to promote speedy discharge of debts and to avoid duplication of performance.<sup>104</sup>

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<sup>97</sup> Van Deventer LLM dissertation 32-33.

<sup>98</sup> Van Deventer LLM dissertation 28-29.

<sup>99</sup> Van Deventer LLM dissertation 32-33.

<sup>100</sup> Van Deventer LLM dissertation 42.

<sup>101</sup> Van Deventer LLM dissertation 42.

<sup>102</sup> Van Deventer LLM dissertation 42.

<sup>103</sup> Van Deventer LLM dissertation 42.

<sup>104</sup> Van Deventer LLM dissertation 42.

The second model entails that set-off operates *ipso iure*, but is contingent on being pleaded in court proceedings, on the premise that so pleading it merely serves to notify the court that the extinction of mutual debts has occurred automatically.<sup>105</sup> Practically, this approach has the same effect as the first approach, with the only difference being that the operation of set-off is suspended pending the pleading thereof at court.<sup>106</sup> The third approach also requires set-off to be pleaded in court, but unlike the second model, it further requires that the set-off be sustained in judgment in order for it to be rendered operative and, once so sustained, it will operate retrospectively.<sup>107</sup> Van Deventer maintains that the fact that the sustained set-off operates retrospectively renders this third model tantamount to the first model.<sup>108</sup>

The fourth approach requires the “extrajudicial, informal and unilateral declaration to the other party [of the set-off], whereupon it works retrospectively”.<sup>109</sup> In the ordinary course, it is a prerequisite that all requirements of set-off be met prior to it being relied on, such that it may not be relied on in instances where some of the requirements ceased to exist by the time it is declared; the reason being that the retrospective effect is only attributed to the effect of set-off.<sup>110</sup> That said, the retrospective effect in some legal systems is attributed to the declaration itself, with the result that set-off will be allowed notwithstanding that some requirements of set-off only existed sometime in the past and not necessarily at the time the declaration was made.<sup>111</sup>

In the fifth potential model, set-off has no effect until a unilateral declaration is made by either of the parties (whether formally or informally/extrajudicially), whereupon interest will cease to run and sureties and security will be released; the so-called *ex nunc* approach, where the question of retrospectivity does not arise.<sup>112</sup>

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<sup>105</sup> Van Deventer LLM dissertation 43.

<sup>106</sup> Van Deventer LLM dissertation 43.

<sup>107</sup> Van Deventer LLM dissertation 43.

<sup>108</sup> Van Deventer LLM dissertation 43.

<sup>109</sup> Van Deventer LLM dissertation 43.

<sup>110</sup> Van Deventer LLM dissertation 43.

<sup>111</sup> Van Deventer LLM dissertation 43-44.

<sup>112</sup> Van Deventer LLM dissertation 44.

The South African approach to the operation of set-off will now be briefly considered, having regard to the above possible approaches.<sup>113</sup>

### **2.3.3 Operation of set-off in South Africa**

South African law inherited the uncertainty that prevailed in Roman-Dutch law as regards the operation of set-off, hence the question of which approach should be adopted remains unsettled.<sup>114</sup> As such, there are diverging opinions as to whether set-off operates automatically once all its requirements have been met, or whether it requires that a party declare it, in addition to its requirements having been met.<sup>115</sup> Van Deventer explains in this regard that South African law arguably follows the second and fourth models of the theoretical approaches to the operation of set-off discussed above.<sup>116</sup>

Van der Merwe, Van Huyssteen, Reinecke and Lubbe assert that although the bulk of authority in case law seemingly maintain that set-off operates automatically, *ipso iure*, without the need for either party to invoke it, academic literature does not conclusively support any standpoint and the Supreme Court of Appeal has yet to authoritatively pronounce on the matter.<sup>117</sup> They further explain that because the automatic operation of set-off establishes the precise moment when set-off takes effect, it is said to bring about more certainty and is regarded as efficient and as serving public policy, insofar as it firstly ensures that debts are settled at the earliest possible date and also because it is said to avoid a multiplicity of claims.<sup>118</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe then criticise these arguments as ones that cannot decide the issue, on the basis that requiring the parties to declare in order for set-off to operate will not necessarily result in uncertainty or a multiplicity of claims, nor is it patent that the public interest sought to be served through extinguishing debts as early as possible outweighs the necessity to recognise the autonomy of the parties in this regard.<sup>119</sup>

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<sup>113</sup> Van Deventer LLM dissertation 44.

<sup>114</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 551; Van Deventer LLM dissertation 45.

<sup>115</sup> Van der Merwe Van Huyssteen, Reinecke and Lubbe (2007) 551.

<sup>116</sup> Van Deventer LLM dissertation 45.

<sup>117</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 551.

<sup>118</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 551.

<sup>119</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 552.

Another critique Van der Merwe, Van Huyssteen, Reinecke and Lubbe level against the automatic operation of set-off is that it includes qualifications that seem to undermine its very operation, such as the need for parties to plead and prove set-off for it to be rendered operational.<sup>120</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe find unconvincing the explanation that the requirement to plead and prove set-off serves merely to inform the court of its existence, rather than to trigger its operation.<sup>121</sup> As the argument goes, the fact that the parties are permitted to elect not to invoke set-off exacerbates the situation (that qualifications to the automatic operation of set-off undermine it) and lends credence to the conclusion that the automatic operation of set-off actually recognises as an indispensable element for the operation of set-off a party's election whether or not to invoke it, which in turn reduces the notion of automatic operation of set-off to no more than an artificial theoretical construction.<sup>122</sup>

According to Van der Merwe, Van Huyssteen, Reinecke and Lubbe, the theoretical and practical significance of the supposedly opposing automatic operation and declaration approaches should not be over-emphasised, particularly because parties may by agreement exclude the operation of set-off in any event.<sup>123</sup> They contend in relation to the view that set-off operates only when either of the parties declares it,<sup>124</sup> that this approach has garnered support by reason of it allowing the parties to keep their claims alive and to pursue them by way of action, whilst it maintains that the set-off must operate retrospectively so that the debts are regarded as having been extinguished from the moment they became capable of set-off.<sup>125</sup> Although Van der Merwe, Van Huyssteen, Reinecke and Lubbe concede that this declaration approach is also subject to a qualification, being retrospectivity, they nevertheless maintain that this qualification does not contradict the very basis of the declaration approach, as is the case with the qualifications that apply to the automatic operation approach.<sup>126</sup>

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<sup>120</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 552.

<sup>121</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 552.

<sup>122</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 552.

<sup>123</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 552.

<sup>124</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 551; *Southern Cape Liquors (Pty) Ltd v Delipcus Beleggings BK* 1998 (4) SA 494 (C).

<sup>125</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 551.

<sup>126</sup> Van der Merwe, Van Huyssteen, Reinecke and Lubbe (2007) 552.

## 2.4 Conclusion

What is immediately apparent from the stances adopted in relation to the operation of set-off in South African law, is that those who ponder on the matter seem to select a preferred approach based on the consequences that will follow that they deem appropriate in a particular situation,<sup>127</sup> as opposed to selecting a generalised approach that ought to apply to all circumstances of a particular and/or similar nature. This results in insurmountable inconsistencies in the approach taken to the operation of set-off in South African law, which inconsistencies, even if overlooked, Van Deventer submits are not as of moment as the biggest shortcoming presented by either approach to the operation of set-off in the South African context, being that neither approach “regulate modern business and banking relationships in a manner which corresponds with normal commercial practices”.<sup>128</sup> As example for the shortcoming referenced, Van Deventer points to “the effect set-off has both on the charging of interest and a party’s default ... [aspects which are] so problematic in practice that banks are compelled to regulate the operation of set-off contractually”.<sup>129</sup>

The next chapter shall address the statutory form of set-off as provided for in terms of sections 90(2) and 124 of the NCA.

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<sup>127</sup> Van Deventer LLM dissertation 81-82.

<sup>128</sup> Van Deventer LLM dissertation 82.

<sup>129</sup> Van Deventer LLM dissertation 82.

## CHAPTER 3: SET-OFF IN TERMS OF THE NATIONAL CREDIT ACT

### SUMMARY

#### 3.1 Introduction

#### 3.2 Overview of sections 90(2)(n) and 124 of the National Credit Act

#### 3.3 Initial interpretation sections 90(2)(n) and 124 of the National Credit Act

##### 3.3.1 General statutory interpretation rules

##### 3.3.2 Deliberation relating to the spirit and purpose of the National Credit Act

##### 3.3.3 Foundational policy documents: origins of sections 90(2)(n) and 124

##### 3.3.4 Similar provisions in comparable jurisdictions

##### 3.3.5 Code of Banking Practice

#### 3.4 Conclusion

### 3.1 Introduction

In recognising that set-off is a useful commercial and yet a powerful tool in the hands of creditors, Van Heerden aptly points out that banks, in particular, have readily utilised set-off given the unique and advantageous position they hold, as opposed to other credit providers, as a result of the mutual debtor-creditor relationship that essentially allows them to appropriate funds from an account of a client with a credit balance to settle or reduce a debt that same client may have in another account with the bank.<sup>130</sup> Van Heerden further submits that when banks so apply set-off, they generally do not inquire as to the purpose why funds were deposited into the client's account, with the effect that the bank in question may not consider that the client needs to utilise the money in question for his subsistence.<sup>131</sup> Van Deventer explains in this regard that banks will often insert in loan agreements what is referred to as a "cross-default clause", which entails that a bank may utilise funds held in one account of the client with the bank to satisfy outstanding loan re-payments in circumstances of default of the loan agreement by such client.<sup>132</sup>

Notwithstanding that set-off is a tremendously useful mechanism of debt settlement, many legal systems have found its general operation inadequate in the context of the applicable consumer credit regime and have sought to regulate it

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<sup>130</sup> Van Heerden 2017 *ABLU* 100-101; Van Deventer LLM dissertation 112.

<sup>131</sup> Van Heerden 2017 *ABLU* 101.

<sup>132</sup> Van Heerden 2017 *ABLU* 101; Van Deventer LLM dissertation 114.

statutorily; a *status quo* that currently prevails in South Africa.<sup>133</sup> It would seem the National Credit Act, as provided for in terms of section 90(2)(n) read with section 124, has changed a credit provider's right to apply common law set-off, which takes place without notification nor meeting certain prescribed formalities.<sup>134</sup> Prior to the case of *National Credit Regulator v Standard Bank of South Africa Limited* (to be discussed in the next chapter), the general consensus was that there existed uncertainty as to the ambit of sections 90(2)(n) and 124, as well as in respect of the impact same sections would have on a credit provider's right to apply common law set-off.<sup>135</sup>

In the circumstances, this chapter will therefore explore the varying constructions attributed to said sections and the basis proffered for the competing interpretations then argued, once the actual provisions of sections 90(2)(n) and 124 have been analysed and deliberated upon. The examination will include an analysis of whether these sections meant to oust the operation of the common law right to set-off, having regard to policy documents developed during the drafting of the NCA; consumer legislation of other comparable jurisdictions; the objectives of the NCA; impact of other provisions of the NCA that may shed light in relation to whether or not a particular interpretation of sections 90(2)(n) and 124 may amount to contravention of the first mentioned provisions of the NCA; and consideration of whether the provisions of the Code of Banking Practice at all impacts the question of whether sections 90(2)(n) and 124 takes away a credit provider's right to apply common law set-off to a credit agreement regulated by the NCA.<sup>136</sup>

### 3.2 Overview of sections 90(2)(n) and 124 of the National Credit Act

As is apparent from the above, section 90(2)(n) and section 124 provide for set-off. Section 90(2)(n) deals with provisions that would be unlawful if included in a credit agreement governed by the Act and specifically states that such a provision in a credit agreement would be unlawful if:<sup>137</sup>

- “(n) it purports to authorise or permit the credit provider to satisfy an obligation of the consumer by making a charge against an asset, account, or amount deposited by

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<sup>133</sup> Van Deventer LLM dissertation 112; Van Heerden 2017 *ABLU* 100.

<sup>134</sup> Van Deventer LLM dissertation 112; Van Heerden 2017 *ABLU* 100.

<sup>135</sup> Van Deventer LLM dissertation 112.

<sup>136</sup> Van Deventer LLM dissertation 112.

<sup>137</sup> Van Heerden 2017 *ABLU* 101; Van Deventer LLM dissertation 113.

or for the benefit of the consumer and held by the credit provider or a third party, except by way of a standing debt arrangement, or to the extent permitted by section 124;”

Section 124, in turn, is styled “Charges to other accounts” and provides as follows:<sup>138</sup>

- “(1) It is lawful for a consumer to provide, a credit provider to request or a credit agreement to include an authorisation to the credit provider to make a charge or series of charges contemplated in section 90(2)(n), if such authorisation meets all the following conditions-
- (a) the charge or series of charges may be made only against an asset, account, or amount that has been-
    - (i) deposited by or for the benefit of the consumer and held by that credit provider or that third party; and
    - (ii) specifically named by the consumer in the authorisation;
  - (b) the charge or series of charges may be made only to satisfy-
    - (i) a single obligation under the credit agreement; or
    - (ii) a series of recurring obligations under the credit agreement, specifically set out in the authorisation;
  - (c) the charge or series of charges may be made only for an amount that is-
    - (i) calculated by reference to the obligation it is intended to satisfy under the credit agreement, and
    - (ii) specifically set out in the authorisation;
  - (d) the charge or series of charges may be made only on or after a specified date, or series of specified dates-
    - (i) corresponding to the date on which an obligation arises, or the dates on which a series of recurring obligations arise, under the credit agreement; and
    - (ii) specifically set out in the authorisation; and
  - (e) any authorisation not given in writing, must be recorded electromagnetically and subsequently reduced to writing.
- (2) Before making a single charge, or the initial charge of a series of charges, to be made under a particular authorisation, the credit provider must give the consumer notice in the prescribed manner and form, setting out the particulars as required by this subsection, of the charge or charges to be made under that authorisation.”

As mentioned above,<sup>139</sup> banks are wont to include cross-default clauses in credit agreements that allow them to appropriate funds from one account of a client to discharge or reduce the debt in another account of same client held with the bank, upon default of the relevant credit agreement.<sup>140</sup> This notwithstanding, section 90(2)(n) now prohibits the insertion of a blanket provision, such as the so-called cross-default clause, authorising the appropriation of funds on default as explained above, without notification nor having met certain prescribed formalities.<sup>141</sup> The

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<sup>138</sup> Van Heerden 2017 *ABLU* 101; Van Deventer LLM dissertation 113-114.

<sup>139</sup> Par 3.1.

<sup>140</sup> Van Deventer LLM dissertation 114; Van Heerden 2017 *ABLU* 102.

<sup>141</sup> Van Deventer LLM dissertation 114.

valid inclusion of a clause authorising the appropriation of funds in a credit agreement governed by the National Credit Act can only be achieved through compliance with the formalities or prescribed conditions provided for in section 124 of the NCA.<sup>142</sup> To that end, section 124 requires the credit provider bank to obtain prior authorisation from its client that addresses the specific account from which funds may be appropriated;<sup>143</sup> the specific obligation to be satisfied with the funds so appropriated;<sup>144</sup> the precise amount to be appropriated;<sup>145</sup> and the exact date on which said appropriation of funds is to occur.<sup>146</sup> Section 124 further stipulates that the authorisation may be given on conclusion of the credit agreement, on the credit provider's request or through the client's/consumer's own initiative.<sup>147</sup> It is also a requirement of section 124 that the client/consumer be notified before the appropriation authorised actually takes place.<sup>148</sup>

Van Deventer points out that for an understanding of how these two provisions potentially limit the application of set-off by banks in relation to credit agreements, it is required that there first be an appreciation of the nature of the relationship between a bank and its client, as well as what constitutes a "charge" for purposes of the NCA.<sup>149</sup> She then explains in relation to the relationship aspect, that the bank is a debtor to the client in respect of monies deposited with it (i.e. the client retains a claim or personal right against the bank for the return of same, since ownership of the monies vests with the bank once deposited), whilst it is a creditor in respect of any loans or facilities it may have granted the client.<sup>150</sup> As the argument goes and absent contractual provisions to the contrary, where both accounts become due and payable the bank could potentially apply set-off and appropriate money from the account with a positive balance to settle or reduce the

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<sup>142</sup> Van Deventer LLM dissertation 114.

<sup>143</sup> S 124(1)(a); Van Deventer LLM dissertation 114.

<sup>144</sup> S 124(1)(b); Form 27 of the Regulations to the NCA sets out the prescribed form for the notice; Van Deventer LLM dissertation 114.

<sup>145</sup> S 124(1)(c); Van Deventer LLM dissertation 114.

<sup>146</sup> S 124(1)(d); Van Deventer LLM dissertation 115.

<sup>147</sup> S 124(1); Van Deventer LLM dissertation 115.

<sup>148</sup> S 124(2); Van Deventer LLM dissertation 115.

<sup>149</sup> Van Deventer LLM dissertation 115; Van Heerden 2017 *ABLU* 102.

<sup>150</sup> Van Deventer LLM dissertation 115-116; *Ormerod v Deputy Sheriff, Durban* 1965 4 All SA 330 (D) 334, with reference to *White v Standard Bank* 1883 4 N.L.R. 88 91-92; *Herrigel NO 674B-C*; *Dantex Investment Holdings (Pty) Ltd v National Explosives (Pty) Ltd (In Liquidation)* 1990 (1) SA 736 (A) 478F-G; *Standard Bank of South Africa Ltd v Echo Petroleum CC* 2012 (5) SA 283 (SCA) 287-288; *Gainsford NNO v Gulliver's Travel (Bruma) (Pty) Ltd* (07/ 5121) [2009] ZAGPJHC 20 (7 April 2009) paras 99-100.

indebtedness in the account with a negative balance.<sup>151</sup> Seen from this perspective, the question arises whether said appropriation of funds from one account of the client to another constitutes a “charge” within the meaning contemplated in terms of sections 90(2)(n) and 124 of the NCA.<sup>152</sup>

Insofar as the “charge” aspect is concerned, Van Deventer notes that the NCA does not contain a definition of the concept “charge”, but nevertheless maintains that the concept should be afforded a wide interpretation given that it is largely used as the equivalent of costs or fees, such that “charge” as per sections 90(2)(n) and 124 therefore refers to the withdrawal or appropriation of funds from an account – as is the case when set-off is applied.<sup>153</sup> She further agrees with the statement by Otto and Otto that “[w]hat is clearly prohibited is a clause in a contract which generally authorises the credit provider to satisfy a debt out of any account that the consumer has with it” and, on that basis, comes to the conclusion that by so appropriating funds from one account of a client to cure the indebtedness in another account of the same client, such bank’s actions fall squarely within the parameters of the conduct sought to be regulated by sections 90(2)(n) and 124 – a view the National Credit Regulator (“NCR”) is said to have been in agreement with.<sup>154</sup>

The NCR having accepted that the appropriation under discussion falls within the ambit of sections 90(2)(n) and 124 of the NCA, the pertinent question arose of whether this in effect translates into the right of credit providers to invoke common law set-off in respect of credit agreements regulated by the NCA having been replaced by implication or whether said sections were limited in application to express provisions contained in credit agreements so regulated.<sup>155</sup> This aspect will be discussed in the sections to follow and further extrapolated on in chapter 4.

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<sup>151</sup> Van Deventer LLM dissertation 115-116.

<sup>152</sup> Van Deventer LLM dissertation 116.

<sup>153</sup> Van Deventer LLM dissertation 116-117; *Evans v Smith* 2011 (4) SA 472 (WCC) para 16, where Binns-Ward J stated that “[t]he terms ‘charge’, ‘fee’ and ‘interest’ are not defined in the NCA. They therefore fall to be construed in accordance with the ordinary meaning of the words as they would be understood in the context in which they have been employed in the statute.”

<sup>154</sup> Van Deventer LLM dissertation 117.

<sup>155</sup> Van Deventer LLM dissertation 117.

### 3.3 Initial interpretation of sections 90(2)(n) and 124 of the National Credit Act

The conundrum in relation the proper construction to be attributed/ascribed to sections 90(2)(n) and 124 of the National Credit Act presented itself in the form of divergent views as to whether these provisions lend themselves to an interpretation that the National Credit Act has effectively, by implication, abrogated the right of banks to apply common law set-off in respect of credit agreements governed by the NCA. On the one hand, the creditor banks had obtained legal opinions from advisors maintaining that the NCA does not prohibit credit providers from relying on the common law right to set-off, considering that neither provision expressly refers to the application of common law set-off.<sup>156</sup> As such, it was argued, the provisions were limited in application to provisions actually contained in credit agreements, as juxtaposed to rendering unlawful the common law application of set-off by implication in all instances where the NCA governs a credit agreement, consequently the common law right to set-off could validly be applied where the credit agreement contained no provision authorising such appropriation of funds.<sup>157</sup> Van Deventer points out that accepting that this interpretation is correct would result in the rather strange, if not downright bizarre, situation that credit providers may retain the right to common law set-off by simply refraining from including any references to set-off in their credit agreements.<sup>158</sup>

The NCR disagreed with the interpretation adopted by the banks, on grounds that are presumed to be that such interpretation is contrary to the spirit and purposes of the NCA.<sup>159</sup> In amplification of the NCR's disagreement, Van Heerden opines that notwithstanding that the provisions in question make no express mention to the common law right of set-off and having regard to the canon of interpretation that the legislature does not intend meaningless legislation, it is necessarily implied that sections 90(2)(n) and 124 were intended to provide a statutory form of set-off to apply to credit agreements governed by the NCA and which would supersede the application of common law set-off in respect of such agreements.<sup>160</sup> Van Heerden maintains that despite the fact that these provisions are crafted in a rather confusing manner, any other interpretation attributed to them would be

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<sup>156</sup> Van Deventer LLM dissertation 117.

<sup>157</sup> Van Deventer LLM dissertation 117-118.

<sup>158</sup> Van Deventer LLM dissertation 118.

<sup>159</sup> Van Deventer LLM dissertation 118.

<sup>160</sup> Van Heerden 2017 *ABLU* 102.

unsustainable as it would beg the question why the legislature went to such extent to draft the elaborate provision, complete with regulation and form, if credit providers could avoid same by simply making no reference to set-off in their credit agreements.<sup>161</sup>

This state of uncertainty was further aggravated by two other factors: firstly, the fact that the Department of Trade Industry had unfortunately failed to recognise as one of the challenges presented by the NCA the uncertainty in relation to the application of the common law right to set-off, with the result that the apparent issue was not addressed nor clarified in the National Credit Amendment Act 19 of 2014.<sup>162</sup> Further, the Ombudsman for Banking Services took the stance that the dispute regarding the appropriate interpretation to be adopted in relation to the provisions in question is a matter best left for resolution through legislative amendment or by court judgment.<sup>163</sup>

As neither legislative amendment nor judicial pronouncement in relation to the issue had occurred at the time, it remained uncertain whether sections 90(2)(n) and 124 merely prohibited the inclusion in a credit agreement of a provision authorising set-off or whether a credit provider's common law right to set-off was thereby also excluded.<sup>164</sup> The significance of the debate surrounding this uncertainty is borne out by the fact that the authorisation provided for by section 124 limits the exercise of set-off by a creditor bank to that which is contained in said authorisation, as explained above, and it further exposes the creditor to the risk that the client may nominate one account for purposes of the section 124 authorisation but then later move all available funds to another account, which would frustrate any effort by the bank to apply set-off as that would require that another section 124 authorisation be obtained in respect of the latter account prior to any set-off being applied.<sup>165</sup> Van Deventer aptly points out in this regard that the bank would in the circumstances much rather retain their more flexible common law right to set-off, particularly as it requires no authorisation nor any other

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<sup>161</sup> Van Heerden 2017 *ABLU* 102-103.

<sup>162</sup> Van Deventer LLM dissertation 118; Department of Trade and Industry "Document in respect of project re policy review of the National Credit Act 34 of 2005" GN 559 in *GG* 36504 of 2013-05-29.

<sup>163</sup> Van Deventer LLM dissertation 118; Ombudsman for Banking Services "Consumer Information Note 5: Set-Off" Ombudsman for Banking Services 3.

<sup>164</sup> Van Deventer LLM dissertation 118.

<sup>165</sup> Van Deventer LLM dissertation 119.

prerequisites, such as specific amount to be appropriated, the date on which it is to take place, the account from which it may take place and prior notification before the actual appropriation.<sup>166</sup>

With the uncertainty remaining unresolved, various factors had to be considered in order to determine the appropriate construction to be attributed to sections 90(2)(n) and 124 of the NCA.<sup>167</sup> Van Deventer succinctly summarises these factors to include the consideration of the spirit and purpose of the NCA, having regard to section 2 thereof; the determination of the origins of the provisions in question, to ascertain the intention behind their inclusion in the NCA; and an examination of consumer protection legislation of comparable jurisdictions that influenced drafting of the NCA, to determine whether they contain similar provisions.<sup>168</sup> According to Van Deventer, the purpose of such an investigation would assist in determining the correct interpretation to be employed in relation to sections 90(2)(n) and further reveal the desirability, or not, of limiting the right of banks to apply set-off.<sup>169</sup> The said investigation is contained in the sections that follow.

### **3.3.1 General statutory interpretation rules**

As mentioned above, certain rules of statutory interpretation come to the fore in the plight to ascertain the correct construction to be afforded sections 90(2)(n) and 124, which process includes the determination of what the origin and purpose of these provisions are.<sup>170</sup> According to Van Deventer, two principles of interpretation are of relevance, the first being that relating to the proper boundaries of interpretation, which essentially dictates that the purpose of interpretation is to determine the meaning of the wording of a statutory provision in a sense that “sight must not be lost of the ordinary meaning of the wording of a section; interpretation should be concerned with the meaning of words without imposing a view of what the policy or object of the legislation is or should be”.<sup>171</sup> Stated differently, interpretation may not be driven by what is deemed desirable in a particular

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<sup>166</sup> Van Deventer LLM dissertation 119.

<sup>167</sup> Van Deventer LLM dissertation 119.

<sup>168</sup> Van Deventer LLM dissertation 119.

<sup>169</sup> Van Deventer LLM dissertation 119.

<sup>170</sup> Van Deventer LLM dissertation 120.

<sup>171</sup> Van Deventer LLM dissertation 120; *Mankayi v Anglogold Ashanti Ltd* 2010 (5) SA 137 (SCA), (“*Mankayi*”), para 25.

case,<sup>172</sup> as doing so will amount to disregarding the separate roles of the legislature and the judiciary.<sup>173</sup>

The description that the object of interpretation is to focus on its wording rather than the purpose of legislation, as the latter would constitute determining the intention of the legislature, has been rejected and duped incorrect by Wallis JA, who regards legislative interpretation as an objective exercise on the basis that:<sup>174</sup>

“[i]nterpretation is the process of attributing meaning to the words used in a document, be it legislation, some other statutory instrument, or contract, having regard to the context provided by reading the particular provision or provisions in the light of the document as a whole and the circumstances attendant upon its coming into existence. Whatever the nature of the document, consideration must be given to the language used in the light of the ordinary rules of grammar and syntax; the context in which the provision appears; the apparent purpose to which it is directed and the material known to those responsible for its production.”

Van Deventer argues that what must therefore be considered is the plain meaning of a provision, in addition to its context and purpose, as well as the relevant material that brought about its production.<sup>175</sup> Applying this to the provisions of sections 90(2)(n) and 124, she notes that section 90(2)(n) merely refers to a “provision of a credit agreement”, its heading reads “Unlawful provisions of credit agreement”, and it makes no reference to the common law right to set-off.<sup>176</sup> Accordingly, she contends it could be argued that the line between interpretation and legislation would be crossed by any interpretation that in any way extends the scope of the provision beyond what may be contained in a credit agreement.<sup>177</sup> She nevertheless concedes that a court is required in terms of section 2(1) of the National Credit Act to interpret the provisions of the Act in a manner that gives effect to the purposes thereof set out in section 3.<sup>178</sup> The purposes referred to are to “promote and advance the social and economic welfare of South Africans, promote a fair, transparent, competitive, sustainable, responsible, efficient,

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<sup>172</sup> Van Deventer LLM dissertation 120; *Natal Joint Municipal Pension Fund v Endumeni Municipality* 2012 (4) SA 593 (SCA) (“*Natal Joint Municipal Pension Fund*”), para 22, with reference to Spigelman “The intolerable wrestle: Developments in statutory interpretation” 2010 84 SALJ 822 826.

<sup>173</sup> Van Deventer LLM dissertation 120; *Natal Joint Municipal Pension Fund* para 22.

<sup>174</sup> Van Deventer LLM dissertation 120; *Natal Joint Municipal Pension Fund* paras 18, 20, 23.

<sup>175</sup> Van Deventer LLM dissertation 121.

<sup>176</sup> Van Deventer LLM dissertation 121; emphasis provided.

<sup>177</sup> Van Deventer LLM dissertation 121.

<sup>178</sup> Van Deventer LLM dissertation 121; *Nedbank v NCR* para 2.

effective and accessible credit market and industry and to protect consumers”.<sup>179</sup> Van Deventer further contends that the obligation to follow a purposive interpretation as dictated by section 2(1), may well afford the courts leeway to deviate from the linguistic interpretation of a particular section of the NCA, in a bid to promote the objectives thereof.<sup>180</sup>

Another rule of interpretation that is of relevance provides that the legislature is presumed to be acquainted with the state of the law, which includes the common law.<sup>181</sup> Expounding on the ambit of this rule, Van Deventer appositely explains as follows:<sup>182</sup>

“The common law can be amended by statutory provisions, but these provisions should not be interpreted to alter the common law more than necessary. For the common law to be varied, the intention of the legislature must be plainly aimed at modifying the common law, and even in such a case the modification will only be to the extent provided for by the relevant statutory provisions (whether expressly or by necessary implication).”

On the basis that no reference to nor express variation of the common law right to set-off is contained in either section 90(2)(n) or section 124, the above rules regarding interpretation may well favour the argument presented by the banks that these sections of the NCA will not affect the common law right to set-off.<sup>183</sup> On the contrary and having regard to another rule of interpretation mentioned earlier herein,<sup>184</sup> that the legislature does not intend meaningless legislation, the NCR’s view could be supported that sections 90(2)(n) or 124 modify the common law right to set-off by necessary implication.<sup>185</sup> As at the time prior to delivery of the *National Credit Regulator v Standard Bank of South Africa Limited* judgment, these considerations remained merely speculative and a consideration of other factors that could potentially influence the interpretation of the provisions in question was necessary. These are discussed below.

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<sup>179</sup> Van Heerden 2017 *ABLU* 109.

<sup>180</sup> Van Deventer LLM dissertation 121.

<sup>181</sup> Van Deventer LLM dissertation 122; *Terblanche v South African Eagle Insurance Co Ltd* 1983 (2) SA 501 (N) 504F.

<sup>182</sup> Van Deventer LLM dissertation 122; *Nedbank v NCR* para 38; Van Heerden 2017 *ABLU* 102.

<sup>183</sup> Van Deventer LLM dissertation 122.

<sup>184</sup> See para 3.3 above; Van Heerden 2017 *ABLU* 102.

<sup>185</sup> Van Deventer LLM dissertation 122.

### **3.3.2 Deliberation relating to the spirit and purpose of the National Credit Act**

Whether the limitation of a credit provider's right to common law set-off is in line with the spirit and purposes of the National Credit Act was another important factor considered, which was done through analysing the consequences of such limitation.<sup>186</sup> Stated differently, it was necessary to consider the consequences of restricting the common law right to set-off, in order to determine which interpretation of sections 90(2)(n) and 124 would be most conducive in serving the spirit and purposes of the Act.<sup>187</sup> As a point of departure, it is instructive to deliberate on why the legislature might have deemed it necessary to so restrict a credit provider's common law right to invoke set-off or why it considered such right may have an adverse impact on consumers.<sup>188</sup>

There is no doubt that the mechanism of set-off is a powerful tool in the hands of the credit provider, particularly banks, as the latter is in a far better position than other credit providers to indulge in "money grabbing",<sup>189</sup> precisely because the bank-customer relationship is basically a debtor-creditor relationship with the bank often having unbridled access to various accounts of client from which it can appropriate monies through the invocation of set-off.<sup>190</sup> In this context, the way in which a bank decides to apply set-off may result in gross unfairness towards the client or even cause them financial harm, as would be the case where for instance the bank appropriates money from the client through set-off, leaving insufficient funds to cater for such client's subsistence needs or for servicing other debts – the latter which, in turn, could see creditors accelerating payments of other debts or the client incurring additional charges for returned debit orders or having to incur further debt to stay afloat.<sup>191</sup> There is the further problem that the client is not availed the opportunity to raise defences against the bank's claim and even where it may be possible that the client may have defences against the bank's claim (eg where the signature on the loan document was forged), it remains unlikely even in the event that the client manages to have refunded the money appropriated

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<sup>186</sup> Van Deventer LLM dissertation 122.

<sup>187</sup> Van Deventer LLM dissertation 122.

<sup>188</sup> Van Deventer LLM dissertation 123.

<sup>189</sup> Van Deventer LLM dissertation 123.

<sup>190</sup> Van Heerden 2017 *ABLU* 100; *ABSA Bank v Intensive Air*; Van Deventer LLM dissertation 115-116.

<sup>191</sup> Van Deventer LLM dissertation 123.

through set-off that such refund will compensate for the abovementioned injuries caused by the unavailability of funds.<sup>192</sup>

The above reasons for limiting a credit provider's right to invoke set-off notwithstanding, there exists adverse consequences of so limiting a credit provider's right to invoke common law set-off that may be considered, two of the most pressing being access to credit and the cost of credit.<sup>193</sup> Both these aspects are said to be closely related to the perceived risk of extending credit and are of crucial importance in consumer credit legislation.<sup>194</sup> The gist of the challenge presented by these aspects is that a bank will charge a lower interest rate where the risk attached to the loan is low; whilst the result of prohibiting banks from invoking set-off to recover amounts in default consequents in the removal of the security provided by the mechanism of set-off – a consequence which, in turn, increases the bank's risk and is detrimental to the overall cost of credit.<sup>195</sup>

Van Deventer argues that set-off amounts to an effective method of debt collection, which also carries a very low cost of implementation and the added benefit of a lower cost of credit.<sup>196</sup> One of the acknowledgements contained in policy documents and research produced when the NCA was drafted is that “[e]ffective debt recovery procedures would assist credit providers by reducing bad debt write-offs, and assist consumers by ensuring that high bad debts of a minority of consumers do not feed through into higher interest rates for the rest”.<sup>197</sup>

Bearing the above quotation in mind and having regard to section 3(a) of the NCA, which reinforces the necessity to prevent consumers from being exploited whilst improving access to credit, Van Deventer posits the stance that the security function provided by set-off will result in a wider group of people being allowed access to credit through the formal banking sector, as the willingness of credit providers to grant credit will increase where there is more security granted in relation to a loan.<sup>198</sup> Moreover, conditions to the invocation of set-off such as

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<sup>192</sup> Van Deventer LLM dissertation 123-124.

<sup>193</sup> Van Deventer LLM dissertation 124.

<sup>194</sup> Van Deventer LLM dissertation 124.

<sup>195</sup> Van Deventer LLM dissertation 124.

<sup>196</sup> Van Deventer LLM dissertation 124.

<sup>197</sup> Van Deventer LLM dissertation 124.

<sup>198</sup> Van Deventer LLM dissertation 124.

requiring prior notice to client must be considered in light of the risk posed to the credit provider that the client may well remove the funds from the account in respect of which set-off is intended to apply, with the result that the mechanism of set-off will “cease to be the swift remedy that it is today [and banks] lacking this power ... may be less reticent to call in a depositor’s loan, thereby accelerating a different kind of injury to the depositor”.<sup>199</sup> Another advantage to consider in this context is that where set-off is permitted to operate, the client cannot be in default whilst there are funds available in other accounts of such client and the client will therefore be protected from the repercussions of breach (where there are no contrary contractual provisions).<sup>200</sup>

Having regard to the preceding paragraph, it can accordingly not be said that the allowance of applying set-off by credit providers “goes against the spirit and intent of the [NCA] in all respects” and, on that basis, completely abolishing set-off would also present adverse effects.<sup>201</sup>

### **3.3.3 Foundational policy documents: origins of sections 90(2)(n) and 124**

The origins of sections 90(2)(n) and 124 of the National Credit Act is the next factor to consider as regards their interpretation; a factor best addressed through an examination of the policy documents and reports that informed drafting of the NCA.<sup>202</sup> In the ordinary course and on the presumption that the legislature is circumspect in relation to amending the common-law, it is a reasonable expectation that where a significant common law right is sought to be restricted, the problems and challenges that gave rise to such restriction would be included in the reports and policy documents that informed drafting of the legislation.<sup>203</sup> Surprisingly, however, the policy documents that provide background to drafting of

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<sup>199</sup> Van Deventer LLM dissertation 124-125; Sepinuck “The problems with setoff: A proposed legislative solution” 1988 30 *Wm. & Mary Law Review* 51, 65.

<sup>200</sup> Van Deventer LLM dissertation 125.

<sup>201</sup> Van Deventer LLM dissertation 125; University of Pretoria Law Clinic “The debt counselling process: Challenges to consumers and the credit industry” NCR 294, <http://www.ncr.org.za/ocuments/pages/research-reports/apr09/ncr.zip> (accessed 30-05-2021).

<sup>202</sup> Van Deventer LLM dissertation 125-126.

<sup>203</sup> Van Deventer LLM dissertation 126.

the NCA do not address nor even mention the subject of set-off by banks – this notwithstanding the practical import of the right of banks to rely on set-off.<sup>204</sup>

Van Deventer points out, however, that the Technical Committee (that was tasked with making recommendations in relation to the NCA) made a couple of recommendations that could lend themselves to an interpretation that they were reference to the right to invoke set-off.<sup>205</sup> The first instance is where the Technical Committee state in relation to credit legislation that it ought to “[i]ntroduce regulation on collection practices such as payroll deduction and banks’ treatment of debit orders... in order to ensure that neither competition nor consumer protection are undermined”.<sup>206</sup> Van Deventer then contends it is difficult to surmise anything conclusive from this statement about the operation of the common law right to set-off, as they do not elaborate on the statement at all – not even to indicate whether “collection practices” is wide enough to encompass collection through set-off.<sup>207</sup>

The identification of the weakness in credit legislation preceding the NCA that “[c]ertian aspects of the Banks Act and National Payment System rules undermine competition in the consumer credit markets (while creating inequitable preferences for certain credit providers)”, is said to be a second observation by the Technical Committee that may pertain to set-off.<sup>208</sup> Van Deventer notes in this regard that the specific provisions leading to said inequalities in the Banks Act 94 of 1990 are not specified, further this Act actually does not contain any provisions authorising

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<sup>204</sup> Van Deventer LLM dissertation 126. Said policy documents and reports include the following: The Department of Trade and Industry SA *Credit Law Review* Report for the credit law review, Hofmeyr Herbststein & Gihwala Inc (Willemse and Mxunyelwa) (2002); The Department of Trade and Industry SA *Credit Law Review* Credit contract disclosure and associated factors: Executive summary of research to determine public awareness of legal provisions in relation to credit and satisfaction with provisions for their benefit, Reality Research Africa (2002); Meagher *Regulation of payday lenders in the United States* (2003); Dymski *Interest rates, credit structures and usury in emerging markets* (2003); The Department of Trade and Industry SA *Credit Law Review* The cost, volume and allocation of consumer credit in South Africa, FEASibilitY (Pty) Ltd (2003); The Department of Trade and Industry SA *Credit Law Review* Summary of findings of the Technical Committee (2003), “Summary of findings *Credit Law Review* (2003)”, and The Department of Trade and Industry SA *Credit Law Review* A market research report, Rudo Research and Training (2002).

<sup>205</sup> Van Deventer LLM dissertation 126.

<sup>206</sup> Van Deventer LLM dissertation 126; Summary of findings *Credit Law Review* (2003) 25.

<sup>207</sup> Van Deventer LLM dissertation 126-127.

<sup>208</sup> Van Deventer LLM dissertation 127; Summary of findings *Credit Law Review* (2003) 7; Kelly-Louw “Introduction to the National Credit Act” 2007 15 *JBL* 147 148.

banks to invoke set-off, although regulation 15 to same Act allows the reporting of the net balance of the client's liability (i.e. after set-off has occurred) – which is said to be the mere regulation of one of the consequences where the common law right to set-off exists, as opposed to being authorisation of the common law right to apply set-off.<sup>209</sup>

Notwithstanding that the legislature clearly intended to provide a statutory mechanism of set-off that arguably supersedes the common law right version thereof, none of the reports or studies considered by the Technical Committee reveal any indication that the common law right to set-off adversely impacts consumers to the extent as to warrant legislative intervention.<sup>210</sup> In the circumstances and given that the drafters of the NCA on occasion had regard to foreign law in crafting some provisions of the Act, the next aspect to consider is whether any comparable jurisdictions have provisions similar to sections 90(2)(n) and 124 in their credit legislation, which similar provisions could have inspired their inclusion in the NCA.<sup>211</sup>

### **3.3.4 Similar provisions in comparable jurisdictions**

Section 2(2) of the National Credit Act provides that appropriate foreign and international law may be considered to assist in the interpretation of the Act, although it defines neither “international law” nor “foreign law”, a fact which poses some difficulty insofar as which jurisdiction would then be appropriate to consider.<sup>212</sup> The presumption accepted is that the jurisdictions which were considered during the drafting of the NCA are appropriate for present purposes, those being jurisdictions including New Zealand, the United Kingdom and the European Commission.<sup>213</sup>

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<sup>209</sup> Van Deventer LLM dissertation 127.

<sup>210</sup> Van Deventer LLM dissertation 127-128.

<sup>211</sup> Van Deventer LLM dissertation 128.

<sup>212</sup> Van Deventer LLM dissertation 128; *Nedbank v NCR* para 2; Kelly-Louw *Consumer Credit Regulation in South Africa* (2012) 24.

<sup>213</sup> Van Deventer LLM dissertation 129; Summary of findings *Credit Law Review* (2003) 3; Kelly-Louw “Consumer Credit” in Joubert and Faris (eds) *The Law of South Africa* (2014) para 5 n 7; Kelly-Louw “The prevention and alleviation of consumer over-indebtedness” 2008 20 *SA Merc LJ* 200 207 n 29.

In the United Kingdom, a type of set-off is recognised which is referred to as “combination of accounts” or merely “combination” and allows for a bank to set-off a debit balance in one account against funds held in another, in circumstances where there exists no contractual provision prohibiting same.<sup>214</sup> Provision of credit to consumers in the United Kingdom is regulated in terms of the Consumer Credit Act 1974 (as amended by the Consumer Credit Act 2006), which Act contains no express provisions that prohibit credit providers from invoking the right to set-off and therefore does not contain any provisions similar to sections 90(2)(n) and 124 of the NCA.<sup>215</sup> Section 55A of the Act in question however requires credit providers to provide adequate explanation of certain features of the credit agreement, which explanation is argued may include the obligation on credit providers to inform debtors on conclusion of the credit agreement of the possibility that set-off may be applied, albeit that this section prescribes no conditions to be met in order for the right to apply.<sup>216</sup>

Further, most banks in the United Kingdom ascribe to the Lending Code,<sup>217</sup> which requires by way of guidelines that clients be appraised of circumstances that will ordinarily lead to set-off being applied, at the time the application of set-off is contemplated; that banks consider all available information to establish financial difficulties clients may be experiencing and to ensure availability of sufficient funds after applying set-off to ensure clients meet subsistence needs and service priority debts; the banks are generally also required to recover only most recent debts and are further required to notify client as soon as set-off has occurred.<sup>218</sup> Moreover, guidelines issued by the Financial Ombudsman highlight the need for customers to be treated fairly and requests that clients be informed as soon as money has been appropriated through application of set-off.<sup>219</sup>

Directive 2008/48/EC regulates consumer credit in the European Union,<sup>220</sup> which Directive serves as a minimum standard with which member states are to comply

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<sup>214</sup> Van Deventer LLM dissertation 129; Derham *The law of set-off* 3 ed (2003) ch 15; Wood *English and international set-off* (1989) ch 3; Ellinger *Modern Banking Law* (1987) 139 ff.

<sup>215</sup> Van Deventer LLM dissertation 129.

<sup>216</sup> Van Deventer LLM dissertation 129-130; s 55A(2)(c) and (d) of the Consumer Credit Act 1974.

<sup>217</sup> Van Deventer LLM dissertation 130.

<sup>218</sup> Van Deventer LLM dissertation 130.

<sup>219</sup> Van Deventer LLM dissertation 130-131.

<sup>220</sup> Van Deventer LLM dissertation 132; Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC.

and which does not limit the right of credit providers to invoke set-off, hence does also not contain provisions similar to sections 90(2)(n) and 124 of the NCA.<sup>221</sup> Member states are however at liberty to set their own restrictions on the right of banks to apply set-off, hence in Europe “the view is widely held that set-off should not be allowed to deprive a person of claims (such as those for maintenance or wages) which provide him with a minimum level of subsistence.”<sup>222</sup>

The Credit Contracts and Consumer Finance Act 2003 governs consumer protection in the context of credit agreements in New Zealand.<sup>223</sup> The Act makes no mention of set-off, other than to provide credit providers with the right to set-off statutory damages and penalties against the consumer’s indebtedness.<sup>224</sup> This Act further makes provision for the netting of the balance of the client’s liability, but also does not contain any provisions similar to sections 90(2)(n) and 124 of the NCA.<sup>225</sup>

### **3.3.5 Code of Banking Practice**

A consideration of the provisions of the Code of Banking Practice (“Code”) is another aspect that came into play in the determination of what the proper interpretation of sections 90(2)(n) and 124 ought to be.<sup>226</sup> Most banks in South Africa are members of the Banking Association of South Africa (“BASA”) and, as such, they ascribe to the voluntary Code, which Code explains the rights and obligations of consumers in their varying transactions with banks.<sup>227</sup> Section 7.5 of the Code is relevant to the discussion at hand and it provides as follows:<sup>228</sup>

“When you open an account, we will provide you with information that will include clear and prominent notice of any rights of set-off that we may claim over credit and debit balances in your different accounts.

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<sup>221</sup> Van Deventer LLM dissertation 132.

<sup>222</sup> Van Deventer LLM dissertation 132.

<sup>223</sup> Van Deventer LLM dissertation 133.

<sup>224</sup> Van Deventer LLM dissertation 133; s 24(1) of the Credit Contracts and Consumer Finance Act 2003.

<sup>225</sup> Van Deventer LLM dissertation 133-134.

<sup>226</sup> Van Deventer LLM dissertation 137; Van Deventer 2017 *SALJ* 436-437; Van Heerden 2017 *ABLU* 108.

<sup>227</sup> Van Deventer LLM dissertation 137; Van Deventer 2017 *SALJ* 437; Van Heerden 2017 *ABLU* 108.

<sup>228</sup> Van Deventer LLM dissertation 137; Van Deventer 2017 *SALJ* 437; Van Heerden 2017 *ABLU* 108.

When you obtain credit from us, we may require your consent to set-off any outstanding amounts against funds available in other accounts you hold with us. Any such arrangement will be concluded in terms of the requirements of the NCA, if the credit agreement is subject to the NCA.

We will inform you promptly after we have effected set-off in respect of any of your accounts. You will receive timely statements (if statements are generally produced on the relevant account), which will reflect the setoff position.

Prior to setting off your debit and credit balances, we may elect to place any of your funds on hold pending a discussion with you on any amount owed to us.”

Van Heerden argues that the above quoted paragraphs of the Code will prove problematic in relation to credit agreements regulated by the National Credit Act, given that section 124 constitutes a *lex specialis* and will therefore regulate set-off in the context of such credit agreements, in the sense that the statement in paragraph 7.5 of the Code – that banks will indicate to their clients when set-off may be applied, will therefore be secondary to the provisions of section 124.<sup>229</sup> She further contends that the Code seems to be non-committal, if not contrary, to the provisions of section 124, notwithstanding its statement that set-off will be “concluded in terms of the provisions of the NCA”, on the basis that this statement speaks to notification to consumers that set-off has been applied after the fact, which is in stark contrast to section 124 insofar as the latter requires *prior* notification to consumers that set-off will be applied.<sup>230</sup>

To Van Deventer, the other potential issue presented by the Code is that it requires a consumer to be notified of the possibility of set-off being applied on opening an account, which may be presumed means such notification is to be contained in the credit agreement and in which event it will then have to comply with requirements stipulated in section 124, if regard is had to the provisions of section 90(2)(n).<sup>231</sup> As she explains, this would mean that “instead of merely informing the client in general that any account might be susceptible to set-off should the client be in default, a bank will now have to obtain the specific authorisation contemplated in section 124.”<sup>232</sup> She however regards as welcome the requirement in the Code that the consumer must be informed as soon as set-off has been applied, especially considering that the NCA contains no such requirement, which

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<sup>229</sup> Van Heerden 2017 *ABLU* 108.

<sup>230</sup> Van Heerden 2017 *ABLU* 108-109.

<sup>231</sup> Van Deventer 2017 *SALJ* 437.

<sup>232</sup> Van Deventer 2017 *SALJ* 437.

requirement she submits serves the dual purpose of protecting the consumer whilst not detracting from the bank's security.<sup>233</sup>

### 3.4 Conclusion

What is apparent in the exposition contained in this chapter is that none of the factors deliberated upon conclusively evince a specific interpretation to be adopted in relation to sections 90(2)(n) and 124 of the National Credit Act.<sup>234</sup> Insofar as the spirit and purpose of the NCA considerations are concerned, those are fraught with ambiguity; with there being some support for the notion that the right of credit providers to invoke set-off needs be visited with some restrictions, although not to the extent provided for by the sections under discussion as that may be too restrictive.<sup>235</sup> The position is no clearer in relation to the origins of sections 90(2)(n) and 124, because neither the reports and policy documents that informed drafting of the NCA nor the jurisdictions which may influenced said drafting explain where the provisions come from.<sup>236</sup> The Code offers no better position insofar as it contains provisions that are arguably contrary the very provisions sought to be interpreted.<sup>237</sup>

Alas, it is quite a relief that judgment has been delivered in the matter of *National Credit Regulator v Standard Bank of South Africa Limited*, which judgment definitively address the question of the proper construction to be attributed to section 90(2)(n) of the NCA – an aspect to be fully ventilated in the following chapter.

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<sup>233</sup> Van Deventer 2017 *SALJ* 437-438.

<sup>234</sup> Van Deventer LLM dissertation 134.

<sup>235</sup> Van Deventer LLM dissertation 134.

<sup>236</sup> Van Deventer LLM dissertation 134.

<sup>237</sup> Van Heerden 2017 *ABLU* 108.

## CHAPTER 4: CONCLUSION – JUDICIAL PRONOUNCEMENT ON THE PROPER CONSTRUCTION OF SECTIONS 90(2)(n) AND 124 OF THE NATIONAL CREDIT ACT

### SUMMARY

- 4.1 Background
- 4.2 Findings by the Court
- 4.3 Further considerations
- 4.4 Conclusion: Legislative reform suggestions

#### 4.1 Background

On the basis of reasons including that the unfettered application of set-off as permitted at common law may cause financial hardship to consumers especially where it results in consumers being left “with little or no money to pay other creditors or meet their living obligations”, the NCR applied for a declaratory order from the North Gauteng High Court to the effect that the common law application of set-off has been superseded by the statutory set-off mechanism provided in section 124 of the National Credit Act, read with section 90(2)(n) of same Act.<sup>238</sup> The Court was essentially called upon to determine the legal question whether credit agreements regulated by the NCA could be the subject of common law set-off, particularly having regard to the statutory scheme of set-off contained in the provisions of sections 90(2)(n) and 124 of the Act.

Two widely divergent stances were taken by the opposing parties as to the interpretational principles that ought to be applied to the provisions under discussion.<sup>239</sup> On the basis that sections 90(2)(n) and 124 of the Act have the effect of displacing the common law method of set-off in relation to credit agreements governed by it, in that it provides the only scheme of set-off permissible as regards such credit agreements,<sup>240</sup> the NCR basically submitted that what was paramount in the correct interpretation of these provisions was their context and the underlying purposes of the Act.<sup>241</sup> The NCR conceded the importance of having regard to the ordinary meaning of words used when interpreting statutory provisions, but

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<sup>238</sup> Van Heerden 2017 *ABLU* 109; Media Release by the NCR dated January 2017 entitled “The National Credit Regulator applies for a declaratory order in the North Gauteng High Court” (also reported at <http://www.fin24.com> (accessed 26 July 2021)).

<sup>239</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 25.

<sup>240</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 23.

<sup>241</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 26.

nevertheless maintained that more than the mere consideration of the ordinary grammatical meaning of words is required in terms of the general principles of interpretation as was held by the Constitutional Court in *Cool Ideas 1186 CC v Hubbard & Another*,<sup>242</sup> being essentially that in interpreting legislation the text, context and purpose must always be considered simultaneously.<sup>243</sup>

The NCR further submitted that section 124 significantly departs from the common law by providing a set-off mechanism that is subject to strict safeguards designed to protect the consumer, unlike is the case with common law set-off where no such safeguards exist and the consumer is left with having to identify any set-off that may be unlawful; a situation that is further aggravated by the fact that any remedy that may be available may only be pursued *ex post facto* and will be at the cost of the aggrieved consumer (the cost factor often being prohibitive for low income consumers).<sup>244</sup> In addition, the NCR contended that the interpretation tendered by the bank would render the provisions of section 124 nothing but meaningless dead letter, given that on that interpretation banks could avoid the application of the statutorily prescribed method of set-off through simply making no reference to set-off in their credit agreements.<sup>245</sup> On this basis, it was the NCR's submission that the only interpretation consistent with the foundational purposes of the NCA and with Constitutional values, was the purposive interpretation of sections 90(2)(n) and 124 to exclude the continued application of common law set-off to credit agreements regulated by the NCA.<sup>246</sup>

Agreeing with the NCR that the interpretation adopted by the bank undermined the debt review process provided for in terms of the Act, the South African Human Rights Commission ("SAHRC") contended that such interpretation further was not congruent with various basic constitutional rights, particularly consumers' fundamental right to dignity and their socio-economic rights.<sup>247</sup> The SAHRC was admitted as *amicus curiae* and allowed to adduce evidence in relation to the impact common law set-off application has on the debt review process provided for in the

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<sup>242</sup> *Cool Ideas 1186 CC v Hubbard & Another* 2014 (4) SA 474 (CC) para 28.

<sup>243</sup> *National Credit Regulator v Standard Bank of South Africa Limited* paras 26-27.

<sup>244</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 28.

<sup>245</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 29.

<sup>246</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 30.

<sup>247</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 30.

NCA, as well as on the Constitutional rights of marginalised consumers.<sup>248</sup> Having explained to the Court how the application of common law set-off undermines the debt review process per the Act, the SAHRC submitted that the main difference between the common law application of set-off as opposed to that statutorily provided for, is that the former affords credit providers control that, from the perspective of marginalised consumers, “takes away income upon which indigent debtors rely on for their subsistence without their consent”, thereby failing to promote consumers’ socio-economic rights and their fundamental right to dignity.<sup>249</sup>

In contradistinction and notwithstanding its acceptance that interpretation needs to be holistic such that the context and purpose of the legislation in question needs to be taken into account, the bank adopted the stance that courts cannot when interpreting “impos[e] a view of what the policy or object of legislation is or should be”.<sup>250</sup> Bolstering this line of argument, the bank further made reference to the cautionary note given in *Natal Joint Municipal Pension Fund* that:<sup>251</sup>

“judges must be alert to, and guard against, the temptation to substitute what they regard as reasonable, sensible or business like for the words actually used. To do so in regard to a statute or statutory instrument is to cross the divide between interpretation and legislation...”

The bank therefore essentially submitted that both the NCR and the SAHRC in their interpretations are contending for a view that ignores the actual and plain meaning of sections 90(2)(n) and 124 of the NCA, in preference of a substituted meaning that accords with what they regard represents a better policy outcome for consumers.<sup>252</sup>

On the grounds that the provisions in question restrict application of the set-off procedure per section 124 to credit agreements actually containing set-off provisions and having regard to the fact that neither provision makes mention of common law set-off, the bank submitted that the legislature could not have

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<sup>248</sup> Scholtz (ed) para 2.5; *National Credit Regulator v Standard Bank of South Africa Limited* para 8.

<sup>249</sup> Scholtz (ed) para 2.5.

<sup>250</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 43; *Mankayi* para 25.

<sup>251</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 43; *Natal Joint Municipal Pension Fund* para 18.

<sup>252</sup> *National Credit Regulator v Standard Bank of South Africa and South African Limited* para 44.

intended for the common law application to be ousted by these provisions, else this much would have been made clear through the provisions themselves.<sup>253</sup> In amplification of the latter submission, the bank referenced other sections of the Act where the legislature makes it clear that the continued application of a corresponding common law rule is not intended, such is the case with section 103(5) that deals with interest (statutory *in-duplum* rule) and which section appositely for comparative purposes states “[d]espite any provision of common law or a credit agreement to the contrary...”: to the bank such comparative sections provided evidence that the legislature was fully cognisant of the fact that where it is intended for a provision of the Act to have the effect of ousting the application of common law, same needed to be expressly provided in that provision.<sup>254</sup>

Having regard to the objects and purposes of the Act, the bank further argued that their interpretation of sections 90(2)(n) and 124 is compatible with said objects and purposes given that permitting common law set-off to apply as contended for would see the consumer in a favourable position insofar as the latter would be prevented from being in default of their debts, thereby avoiding instances of breach and acceleration of credit agreements the consumer is subject to.<sup>255</sup> Moreover, as was argued, prohibiting the continued application of common law set-off in the context of sections 90(2)(n) and 124 would increase the cost of credit, especially considering that the prior written notification requirement per the statutory set-off method would avail consumers the opportunity to completely avoid the application of set-off; a consequence the bank submitted is contrary and anomalous to the foundational equitable balance of interests propounded by the Act.<sup>256</sup>

## 4.2 Findings by the Court

As mentioned above, the Court was tasked with interpreting the provisions of section 90(2)(n) and 124 of the National Credit Act to determine whether their application had the effect of rendering reliance on the common law method of set-off displaced in relation to credit agreements regulated by the Act, in circumstances where neither provision expressly exclude the operation of the latter method of set-

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<sup>253</sup> *National Credit Regulator v Standard Bank of South Africa Limited* paras 44-45.

<sup>254</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 46.

<sup>255</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 47.

<sup>256</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 47.

off.<sup>257</sup> Having considered the divergent approaches to and interpretations of the provisions under discussion, the Court observed that there were common cause aspects to the opposing submissions made by the parties being that sections 90(2)(n) and 124 do not expressly exclude the operation of common law set-off; further that the Act does not prohibit the application of set-off in respect of credit agreements subject to the Act (albeit the NCR and the SAHRC contended the statutory version is the only method of set-off permissible, whilst the bank contended the parallel application of the common law set-off method is possible); that the set-off mechanism provided for in the Act presents a stark departure from the common law method of set-off; and lastly that the bank's stance that common law set-off may still apply notwithstanding sections 90(2)(n) and 124 of the NCA is based on the view that this is so only where set-off is not made reference to in a credit agreement.<sup>258</sup>

In coming to its finding, the Court made the observation that the statutory method of set-off is vastly different from its common law counterpart in that it requires the consumer's consent for set-off to be applied, in respect of accounts to be designated by such consumer, in amounts and on dates specifically indicated by the consumer – thereby giving the consumer considerable control over the process.<sup>259</sup> On the other hand, the common law set-off gives credit providers full control over the process, without requiring any input or consent of the consumer.<sup>260</sup> It is precisely on the basis of this incongruity between the different modes of set-off that the Court considered itself called upon to make the determination whether the NCA in effect displaced operation of the common law method of set-off through having enacted sections 90(2)(n) and 124.<sup>261</sup>

The Court found irrational the bank's submission that common law set-off may apply where no reference to set-off is made in a credit agreement, on the basis that this interpretation contradicts one of the general purposes of section 3 of the Act, being the promotion of a transparent credit market, since retaining operation

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<sup>257</sup> Scholtz (ed) paras 2.4 and 2.5; *National Credit Regulator v Standard Bank of South Africa Limited* para 1.

<sup>258</sup> *National Credit Regulator v Standard Bank of South Africa Limited* paras 48-51; Scholtz (ed) para 2.5.

<sup>259</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 16.

<sup>260</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 21.

<sup>261</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 21.

of common law set-off would of necessity require that the consumer be purposefully kept in the dark about the possibility that set-off could be applied.<sup>262</sup> The Court further noted, without making a finding in this regard as neither party raised the point, that general principles of our contract law recognise that agreements include implied terms and the common law right to set-off would properly fall within the meaning of an implied term, with the effect that whether or not set-off is expressly mentioned in a credit agreement, any application of set-off in relation to an agreement regulated by the NCA would nevertheless be subject to section 90(2)(n) and have to comply with the requirements stipulated in section 124.<sup>263</sup> Notwithstanding that it made no findings on this score, it nevertheless held that the bank's contention that the meaning of section 90(2)(n) is clear and plain can therefore not be sustained.<sup>264</sup>

The Court further deliberated that the bank in its contentions excessively focused on the language used in section 90(2)(n) and basically overlooked section 124 (other than merely stating that it does not expressly exclude the operation of common law set-off), which latter section the Court regarded as more significant to the enquiry given that it is actually the provision that dictates what form of set-off is lawful in relation to credit agreements regulated by the NCA and, of critical importance, it is not constrained to provisions contained in credit agreements only – as does section 90(2)(n).<sup>265</sup> That said, the Court conceded that the extended reach of section 124 to provisions outside of those contained in credit agreements nevertheless does not necessarily resolve the question whether exclusion of the common law application of set-off is thereby implied.<sup>266</sup>

The Court then considered that although the Act aims to balance the respective rights and interests of consumers and credit providers, there is no doubt that the statutory mechanism of set-off per sections 90(2)(n) and 124 was patently intended to safeguard the rights of consumers in the set-off process and it was “plainly designed to represent a complete break from the past application of the common-law principle of set-off”.<sup>267</sup> Moreover, that through this statutory mechanism of set-

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<sup>262</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 53.

<sup>263</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 55.

<sup>264</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 57.

<sup>265</sup> *National Credit Regulator v Standard Bank of South Africa Limited* paras 58-59.

<sup>266</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 61.

<sup>267</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 63.

off the Act provides a balance between the rights and responsibilities of credit providers and consumers, thereby promoting equity in the credit market, which balance is wholly missing in the common law application of set-off.<sup>268</sup> Agreeing with the NCR and the SAHRC's submissions in relation to the impact of common law set-off on debt review and consumers' socio-economic rights, the Court emphasised the insurmountable necessary implication that visits an interpretation that common law set-off may operate in tandem with the statutory version; that being that such interpretation would render section 124 dead letter.<sup>269</sup> Having rejected that bank's interpretation on the basis that the wording of the provisions in question do not plainly support such interpretation nor does such interpretation correlate with the underlying purposes of the Act, the Court came to a finding, through employing what Scholtz refers to as the "drastic" mechanism of "reading in", that the common law method of set-off has been displaced in the following words:<sup>270</sup>

"In my view the purpose of s124 was precisely to effect that break from the common-law past that was necessary in order to achieve the underlying objects of the Act. When s124 provides that "it shall be lawful for ... a charge or a series of charges contemplated in s90(2)(n)" to be made on the conditions set out thereunder, it means that these are the only conditions under which set-off may lawfully be applied in respect of credit agreements under the Act. While it does not expressly oust the continued application of common-law set-off in parallel with s124, its meaning and effect is to do so. In my view, these provisions are plainly intended to alter, and to oust the common law position as regards credit agreements regulated by the Act.[22] To hold otherwise would be to render these provisions ineffective for the purpose at which they were directed. In the circumstances, I find that this is one of those circumstances where a reading-in is permissible for interpretational purposes: unless an express exclusion of the common law is read in, effect cannot be given to s124, read with s90(2)(n). I conclude that the correct interpretation of s124 is that it excludes the operation of common-law set-off in all credit agreements that are regulated by the Act."

As is clear in the above finding of the Court, the prevailing legal position is now that set-off may only be applied in accordance with the dictates of section 124 in relation to credit agreements governed by the NCA, a *status quo* that in all probability will have wide ranging ramifications for credit providers, and banks in particular.<sup>271</sup> It is not far-fetched a notion that the onerous requirements credit

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<sup>268</sup> *National Credit Regulator v Standard Bank of South Africa Limited* para 64.

<sup>269</sup> *National Credit Regulator v Standard Bank of South Africa Limited* paras 64-69.

<sup>270</sup> Scholtz (ed) para 2.4; *National Credit Regulator v Standard Bank of South Africa Limited* para 71.

<sup>271</sup> Ameermia and Mhodi "High Court rules the common law principle of set-off is not applicable to debts arising from credit agreements regulated by the NCA" 2019 *De Rebus*

providers are expected to meet in order to comply with sections 90(2)(n) and 124, will see them introducing additional security measures which in turn will have an adverse impact on access to and cost of credit for consumers.<sup>272</sup> In the premise, it has been argued that although the statutory mechanism of set-off is welcomed insofar as it provides the consumer a number of safeguards and say in the process, the requirements stipulated in section 124 may nevertheless be too restrictive and require some reform to ensure the interests of consumers and credit providers are better balanced.<sup>273</sup> On the other hand, there may be persuasive arguments to be levelled against the very constitutionality of the provisions under question, especially those of section 124 of the NCA.<sup>274</sup> These further considerations will be addressed in the section to follow.

### 4.3 Further considerations

Van Heerden deliberates on further considerations pertaining to the subject matter at hand from a constitutional perspective. Premised on the understanding that there is no doubt that the legislature intended for common law set-off to be superseded by the statutory mechanism provided in terms of sections 90(2)(n) and 124, as has now been confirmed in *National Credit Regulator v Standard Bank of South Africa Limited*, Van Heerden posits the argument that the question that may remain unresolved is whether section 124 of the National Credit Act is constitutionally sound or, stated differently, does the possibility exist that common law set-off may be reintroduced through the back door on the basis that section 124 is constitutionally invalid and falls to be struck down.<sup>275</sup> She contends that to render such reintroduction of common law set-off possible, credit providers like banks would have to raise infringement of their constitutional rights by the section in question, on grounds such as that their constitutional right to property has been taken away by the enactment of section 124, which in aggravation also makes it possible for the consumers to take out of their reach funds to which set-off could

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<https://www.derebus.org.za/high-court-rules-that-the-common-law-principle-of-set-off-is-not-applicable-to-debts-arising-from-credit-agreements-regulated-by-the-nca/> (accessed 04-04-2021).

<sup>272</sup> Van Heerden 2017 *ABLU* 111.

<sup>273</sup> Van Deventer 2017 *SALJ* 438.

<sup>274</sup> Van Heerden 2017 *ABLU* 109.

<sup>275</sup> Van Heerden 2017 *ABLU* 110.

be applied, in ways that were not possible in the context of common law set-off, since the latter operated *ipso iure* without more required from the consumer.<sup>276</sup>

To succeed with such constitutional challenge, Van Heerden explains, would require a further enquiry as to whether such deprivation of property is also arbitrary, as the mere deprivation of property does not necessarily lead to unconstitutionality.<sup>277</sup> Noting that for section 124 to be considered unconstitutional, it would have to limit the constitutional right identified in a way that cannot be justified, as required in terms of the limitations clause in section 36 of the Constitution, which justification she considers exists in relation to section 124 given that it is aimed at addressing infringement of consumers' constitutional rights that was occasioned by the application of common law set-off (an aspect extensively addressed in *National Credit Regulator v Standard Bank of South Africa Limited*).<sup>278</sup>

Van Heerden however reaches the conclusion that the measure of determining the constitutionality of section 124 will in all probability be whether or not “the procedure prescribed in the section is disproportional to the achievement of its objective and whether there is a less restrictive means to achieve the same purpose”.<sup>279</sup> Her submission in this regard is then that the legislature “probably... went too far” with the requirements prescribed in section 124, especially if one considers that this is likely to result in the increase of cost of credit and that consumers will easily be able to frustrate the set-off process by removing funds from the relevant account before set-off occurs.<sup>280</sup>

Without necessarily having regard to the constitutional context, Van Deventer essentially agrees with Van Heerden on the basis that the requirements of sections 90(2)(n) and 124, as they presently stand, are too restrictive and are not consonant with the interpretational tenets to be employed in relation the Act as explained by the Supreme Court of Appeal in *Nedbank v NCR*,<sup>281</sup> which essentially amounts to a solution being required to better balance the interests of both the consumers and

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<sup>276</sup> Van Heerden 2017 *ABLU* 110.

<sup>277</sup> Van Heerden 2017 *ABLU* 110.

<sup>278</sup> Van Heerden 2017 *ABLU* 110-111.

<sup>279</sup> Van Heerden 2017 *ABLU* 111.

<sup>280</sup> Van Heerden 2017 *ABLU* 111.

<sup>281</sup> Van Deventer 2017 *SALJ* 424, 438; *Nedbank v NCR* para 2.

credit providers,<sup>282</sup> lest prohibiting banks from applying common law set-off, without redressing the above short-comings of the provisions under discussion, may result in adverse effects in relation to accessibility and the cost of credit for consumers on the basis that banks will have a necessity for substitute forms of security and may increase interest to cater for the consequent increased risk.<sup>283</sup>

It is on the basis of such further considerations on the application of the statutory mechanism of set-off in terms sections 90(2)(n) and 124 that there seem to be widespread acceptance within the legal fraternity that the NCA needs to be visited upon with legislative reform.<sup>284</sup> A couple of suggestions to this end are contained in the next section.

#### 4.4 Conclusion: Legislative reform suggestions

The judgment of *National Credit Regulator v Standard Bank of South Africa Limited* is to be welcomed for the certainty it has provided insofar as the correct method of set-off to be applied in relation to credit agreements governed by the National Credit Act is concerned,<sup>285</sup> which is a view that is further bolstered if the stance is accepted that:<sup>286</sup>

“[i]n a society that requires the remediation of past socio-economic injustices, courts cannot afford to underestimate the resilience of large institutions in finding ways around what they perceive as unfavourable judicial ‘interference’.”

Whilst some calls for legislative reform of sections 90(2)(n) and 124 of the NCA entail merely that the provisions be amended “to provide for an express ouster clause in the same fashion as section 103”,<sup>287</sup> other views (as is evident from the above section) are that these provisions arguably require legislative reform to cater for the above identified further considerations, so that the rights, obligations and

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<sup>282</sup> Van Deventer 2017 *SALJ* 438-439.

<sup>283</sup> Van Deventer LLM dissertation 139-140.

<sup>284</sup> Van Deventer 2017 *SALJ* 439; Van Deventer LLM dissertation 141; Van Heerden 2017 *ABLU* 111.

<sup>285</sup> Reddy “*National Credit Regulator v Standard Bank of South Africa Limited: Common-law right of set-off excluded from credit agreements under the National Credit Act*” 2019 31 *SA Merc LJ* 341, 350.

<sup>286</sup> Reddy 2019 *SA Merc LJ* 355.

<sup>287</sup> Mupangavanhu “Constitutionalisation and transformation of credit law practices such as set-off: An analysis of *National Credit Regulator v Standard Bank of South Africa Ltd*” 2019 31 *SA Merc LJ* 417, 434.

interests of both consumers and credit providers will be balanced in the context of the right to set-off, which in turn will be promoting the objects and purposes of the Act.<sup>288</sup>

As regards the latter instance, Van Heerden opines that redressing the arguable inadequacies of sections 90(2)(n) and 124 will require creative thinking and makes reference to Van Deventer's proposed solution to remove the requirement of prior notification in section 124, which it is suggested will strike a balance between the rights of credit providers and consumers, as well as eliminate the uncertainty as regards the timing such notice is to be given.<sup>289</sup> Another suggestion is that an *ex post* procedure be created, in terms of which the credit provider will be required to notify the consumer once set-off has been applied and an aggrieved consumer would then be allowed to present reasons why the effected set-off ought to be reversed (which reasons could be the financial hardships the NCR contemplated in its submissions to the Court in *National Credit Regulator v Standard Bank of South Africa Limited*).<sup>290</sup>

It is submitted that the judgment in *National Credit Regulator v Standard Bank of South Africa Limited* goes a long way in safeguarding rights of consumers in the context of the right to apply set-off, as has been correctly shown to be in line with the objects and purpose of the NCA. That said, it may nevertheless be in furtherance of same objects and purposes of the NCA that the stringent requirements of section 124 be somewhat relaxed in order that the rights and obligations of both consumers and credit providers are better balanced, which in turn may ensure that access to and cost of credit may not respectively be impeded nor exacerbated.

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<sup>288</sup> Van Heerden 2017 *ABLU* 111; Van Deventer LLM dissertation 141.

<sup>289</sup> Van Heerden 2017 *ABLU* 111-112.

<sup>290</sup> Van Heerden 2017 *ABLU* 112.

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