OVER-INDEBTEDNESS AND DISCRETION OF COURT TO REFER TO DEBT COUNSELLOR

Standard Bank of South Africa Ltd v Hales
2009 3 SA 315 (D)

1 Introduction

The National Credit Act 34 of 2005 ("the Act"), being a new piece of legislation, is alive with groundbreaking opportunities. In *Standard Bank of South Africa Ltd v Hales* the question was raised whether an over-indebted consumer can, during foreclosure proceedings, insist on judicial referral for debt counselling in terms of section 85(a) of the Act.

In this discussion the above question, together with the court's discretion in this regard and factors to be taken into account to exercise same, will be addressed after an analysis of the facts.

2 Facts

The facts, as per the agreed stated case in terms of rule 33(1) of the Uniform Rules of Court, were briefly as follows: The defendants purchased immovable property, financed by the plaintiff against a first covering mortgage bond registered over the property on 10 July 2007. In time, the defendants fell in arrears with their instalments. On 18 April 2008 the plaintiff gave the defendants notice in terms of sections 129 and 130 of the Act, which notice the defendants admitted to receiving. Action for the payment of the arrear instalments and interest thereon, together with an order declaring the immovable property executable, was instituted on 4 July 2008. Summons was served on 14 July 2008 and the defendants entered an appearance to defend on 15 September 2008. On 23 September 2008 the plaintiff applied for summary judgment, which was opposed on the ground of over-indebtedness and the subsequent engagement of a debt counsellor as contemplated in section 79 and 85(a) of the Act. The plaintiff subsequently filed a declaration. In their plea the defendants admitted to all the allegations contained in the plaintiff's claim. The only defence raised by them was the aforesaid over-indebtedness and they applied for relief from such over-indebtedness in terms of section 85.

In terms of the stated case the following was clear:

(a) The loan agreement between the parties was a credit agreement in terms of section 1 of the Act.

(b) The plaintiff duly complied with the provisions of section 129 and 130 of the Act.

(c) The defendants were over-indebted.

(d) The defendants failed to apply for debt relief and were only now, at the foreclosure hearing, asking the court to grant relief in terms of section 85 and to refer the parties to a debt counsellor for debt review.

The crux of the stated case is whether or not the court, in these circumstances, should have taken the steps referred to in section 85(a).

3 Section 85(a) and 86(7)(c) of the Act

Section 3 of the Act sets out its purposes which *inter alia* entail:

- promoting the development of an accessible credit market (s 3(a));
- promoting responsibility in the credit market by encouraging responsible borrowing, avoidance of over-indebtedness and fulfilment of financial obligations by consumers; and discouraging reckless credit granting by credit providers and contractual default by consumers (s 3(c)(i) and (ii));
- addressing and preventing over-indebtedness of consumers and providing mechanisms for resolving over-indebtedness based on the principle of satisfaction by the consumer of all responsible financial obligations (s 3(g)).

To facilitate the debt relief mechanisms provided for in section 3(g), the Act in section 85 provides the court with the power to declare and relieve over-indebtedness and also contains a procedure for debt review by a debt counsellor as set out in section 86 thereof. Section 85 which was the main focus of this case, provides as follows:

> "Despite any provision of law or agreement to the contrary, in any court proceedings in which a credit agreement is being considered, if it is alleged that the consumer under a credit agreement is over-indebted, the court may

(a) refer the matter directly to a debt counsellor with a request that the debt counsellor evaluate the consumer's circumstances and make a recommendation to the court in terms of section 86(7); or

(b) declare that the consumer is over-indebted, as determined in accordance with this Part, and make any order contemplated in section 87 to relieve the consumer's over-indebtedness."

The parties were *ad idem* that both requirements set in section 85 (eg over-indebtedness and that the agreement qualified per definition as a "credit agreement") were present. The court held (para 7) that a referral to a debt counsellor could be considered only once these two factors were on the cards. The question is whether such referral is compulsory or discretionary. Gorven J held (para 7) that the word "may" in section 85 vests the court with a discretion to refer the matter to a debt counsellor and that a court is therefore not obliged to make such referral automatically.

It is to be noted that in their plea the defendants (para 7) only requested the court to refer the matter to a debt counsellor in terms of section 85(a) (not section 85(b) as alternative) with the further request that the debt counsellor evaluate the consumer's circumstances and make a recommendation to the court in terms of section 86(7)(c). This discussion is thus limited to the scope and application of section 85(a). Section 86(7)(c) provides that if a debt counsellor reasonably concludes after an assessment in terms of section 86(6) that a consumer is over-indebted, he may recommend that a Magistrate's Court make either or both of the following orders:

(i) that one or more of the consumer's credit agreements be declared to be reckless credit (which was not raised in the present matter); and

(ii) that one or more of the consumer's credit agreement obligations be re-arranged by

(a) extending the period of the agreement and reducing the amount of each payment accordingly; or

(b) postponing the dates on which payments are due;

(c) extending the period of the agreement and postponing during a specified period the dates on which payments are due under the agreement; or

(d) recalculating the consumer's obligations because of contraventions of Part A or B or Chapter 5, of Part A of Chapter 6 of the Act.

The court remarked (para 9) that since it was common cause that the defendants were over-indebted, section 86(7)(a) and (b) did not apply. No allegations were made by the defendants that any of the credit agreements should be declared to be reckless credit, nor did the defendants claim that Part A or B of chapter 5 or Part A of Chapter 6 was contravened. Gorven J pointed out (para 9) that consequently the recommendations which could be made by a debt counsellor in terms of section 86(7)(c) *in casu* were limited to an extension of the mortgage bond and a concomitant reduction in instalments, a suspension of instalments for a specific period or a combination of these two measures.

4 Onus and scope of discretion in terms of section 85(a) of the Act

Gorven J (para 10) indicated that the first question to deal with was the basis on which the exercise of the discretion in terms of section 85(a) of the Act should be approached. He agreed with the approach taken in *Pillay v Krishna* 1946 AD 946 952 where it was decided that the party alleging the right to a specific order, and

so setting up a special defence, bears the onus of proving such entitlement (special defence). However, it was held *in casu* (para 10) that a section 85(a) debt referral request does not amount to a special defence. The court held that at most, such a request is a dilatory plea, which does not attract an onus, *vis-à-vis* a plea of confession and avoidance, which would. Therefore, once it is established that the defendant is over-indebted and the agreement in question qualifies per definition as a "credit agreement", there is no further onus to be discharged. The defendant has only to persuade the court to exercise its discretion in his or her favour.

In exercising the above discretion, the question arises as to which factors should be taken into account. As the legislator did not enumerate specific factors in this regard and the courts have refused to produce a *numerus clausus* of factors that will apply in every situation, Gorven J held (para 12) that the general purpose of the Act, as defined in section 3, had to be taken into consideration, as a backdrop in exercising its discretion which, it pointed out, had to be done judicially.

In exercising any discretion, the court, with reference to *Myburg Transport v Botha t/a SA Truck Bodies* 1991 3 SA 310 (NmS) and *First National Bank of SA Ltd v Myburg* 2002 4 SA 176 (C), confirmed (para 12) that it should not be done capriciously or upon any wrong principle or on the basis of conjecture or speculation, but for substantial reasons on the material before it. Therefore, the party seeking the referral to a debt counsellor must provide as much as possible relevant information to assist the court in exercising its discretion as the court must have regard to a conspectus of all relevant material.

In casu the paucity of evidence placed before the court by the defendants apparently caused their counsel to urge the court to find that the mere fact that over-indebtedness was admitted was decisive in the exercise of the court's discretion (para 13). However, the court held that an admission of over-indebtedness *per se* will be inadequate to convince it to exercise its discretion favourably. If such an admission of over-indebtedness constituted adequate evidence for a debt referral, the court held that section 85(a) of the Act would have been worded differently by obliging the court to take the steps in section 85(a) instead of giving it a discretion to do so. Thus, Gorven J held that the *fact*, as opposed to the *allegation*, of over-indebtedness is a factor to be taken into account in exercising the discretion in terms of section 85, but it is not decisive.

The court furthermore (para 13) rejected the submission on behalf of the defendants that the sole, or at least chief, purpose of the Act is to provide protection for consumers. It indicated that no prioritisation is provided and whilst consumer protection is a clear object, it is but one factor, albeit a very important one, in the purposes of the Act.

5 Factors in consideration

Relying on *First Rand Bank Ltd v Olivier* 2009 (3) SA 353 (SE), plaintiff's counsel urged the court (para 15) to exercise its discretion based on the following considerations (mentioned in para 15 of that case):

(a) It is relevant to the exercise of the court's discretion that the defendant did not prior to the issue of summons apply to a debt counsellor in terms of section 86(1) of the Act, to have himself declared over-indebted. In this regard the principle applies that the court generally will not entertain a proceeding

where there is another similar and less expensive, effective procedure available (*Troskie v Troskie* 1968 3 SA 369 (W));

(b) having failed to avail himself of the opportunity to approach a debt counsellor prior to the institution of the action, the defendant must explain that failure to the court;

(c) the defendant's action in awaiting legal debt enforcement by the plaintiff rather than voluntarily taking steps to have himself declared over-indebted, amounts to abuse of court in view of the following factors which dictate in favour of this approach, namely:

(i) the Act provides a simple, inexpensive and effective procedure for debt restructuring in section 86;

(ii) these provisions were obviously designed to expedite and to simplify the procedure relating to debt restructuring;

(iii) these procedures are furthermore designed to avoid the necessity of parties having to resort to the far more costly procedure of applying to the High Court for relief;

(iv) it is also undesirable that the High Court has to deal with frequent applications for debt restructuring, very much along the lines of a court sitting in terms of section 65 of the Magistrates' Courts Act 32 of 1944.

However, although the court in *Olivier* held that these considerations could well in proper circumstances influence it in the exercise of its discretion, the court in that matter was not prepared to fault the defendant for not acting timeously in terms of section 86(1) of the Act, mainly because the Act was still relatively new at the stage when action was instituted and it was unclear whether the defendant had sufficient time before receiving the section 129-notice to apply for debt review in terms of section 86 and there was also no indication of how long before service of the summons the section 129-notice was delivered to the defendant (para 16).

Gorven J pointed out (para 16) that the facts *in casu* were distinguishable from *Olivier* as a notice in terms of section 129(1) of the Act was sent to the defendant well after the section had come into effect and, unlike in *Olivier*, the Act had come into effect before the bond was registered. Section 129(1)(a) provides that if the consumer is in default the credit provider may in writing notify the consumer thereof and propose debt counselling, alternatively dispute resolution or a referral to a consumer court or ombud with jurisdiction with the intent to resolve the dispute or bringing the payments up to date. It is then further provided in section 129(1)(b) that (subject to s 130(2)), a credit provider may not commence any legal proceeding to enforce the agreement before first providing notice to the consumer in terms of section 129(1)(a) or 86(10), as the case may be, and meeting any further requirements set out in section 130. The court indicated (para 18) that it is clear that the process provided for in section 129(1) is designed to provide both impetus and a window of opportunity for a consumer, in the event of there being a dispute or a desire to bring his or her payments up to date, to make use of that section or to take other steps which may redress his or her financial embarrassment.

The court, however, held (para 19), that if a credit provider has proceeded to take the steps contemplated in section 129 to enforce the credit agreement, a consumer is prohibited to apply for debt counselling, declaring him

over-indebted (see s 86(2)). Since the defendants *in casu* purported to apply to a debt counsellor in terms of section 86(1) one month after the delivery of the application for summary judgment, it was conceded (para 19) that such application for debt review was a nullity due to the provisions of section 86(2).

In addition to the factors dealt with in *Olivier*, it was further submitted on behalf of the plaintiff (para 20) that the court's discretion should be exercised against the defendants for the following reasons:

(a) There was no explanation for the delay in their application for debt review in terms of section 86;

(b) there was no explanation for the dishonest defence (namely that they did not receive a section 129(1)-notice) which was raised in the affidavit resisting summary judgment;

(c) the defence raised was clearly designed to frustrate the plaintiff in obtaining judgment and foreclosing on the immovable property;

(d) if one deducted from the monthly expenses of the defendants that amount which would be required to service the mortgage bond, they would be living within their means and would not be over-indebted, and

(e) the defendants had not paid any instalment for 14 months.

It was submitted on behalf of the plaintiff (para 21), that since the defendants did not take the steps to apply for debt review set out in section 86(1) after receiving the section 129-notice, the invocation of section 86(1) amounted to an abuse of the process of court against which the court should be astute to protect itself. The court, however, did not agree that this failure amounted, in itself, to an abuse of process and based its opinion on the following considerations (para 21):

- It interpreted sections 86 and 129 to mean that after receipt of a section 129(1)-notice, a defendant is barred by section 86(2) to apply for debt counselling in terms of section 86(1). The referral to a debt counsellor could then only be one in terms of section 129(1) and could not result in a declaration of over-indebtedness and the other steps set out in section 86. The debt counsellor's attempts would then be limited to resolving the dispute or bringing the payments up to date, as provided for in section 129(1).
- If section 86 had been utilised, no resort could now be had to section 85, since the debt counsellor would already have made a recommendation in terms of section 86(7).
- Cogent reasons (eg the failure to reach an agreement as a result of the plaintiff being unreasonable after having referred to the matter to a debt counsellor in terms of section 129) may be present why section 85(a) is raised only at the present stage of the proceedings. In this instance, an appeal to section 85(a) would be the only opportunity to show that the debt counsellor should be accorded the machinery of section 86(7).
- There may be circumstances where, even if no referral to a debt counsellor were made in terms of section 129, one of the other steps mentioned in that section was taken which did not satisfy a genuine complaint of the consumer.

In casu however, the defendants failed to provide the court with certain minimum relevant information which one would have expected them to place before the court (para 22). They gave no indication how it came about that they defaulted under the agreement. They did not indicate whether and, if so, in what

respect, their financial circumstances changed or what steps they took to remedy or minimise their default. They did not indicate whether, before receipt of the section 129(1)(a)-notice they were aware of the provisions of section 86 and, if so, why they did not make application in terms of section 86(1) to a debt counsellor. They did not mention whether they approached the plaintiff at any stage with proposals to reschedule the debt or any other proposals. They failed to explain when their other indebtedness arose and did not indicate whether it did so after they had defaulted on their obligations to the plaintiff and thus incurred monthly expenses which further reduced their ability to service the mortgage bond. They also did not indicate how, when the excess of expenditure over income amounted to just more than the entire instalment due to the plaintiffs, it would be feasible to reschedule the debt, with or without the temporary suspension of instalments.

The defendants furthermore falsely denied (para 22) having received the section 129-notice and it was submitted on behalf of the plaintiff that the absence of a cogent explanation for this false denial supports an inference that their attempt to rely on section 85(a) was simply an attempt to delay judgment. The court, however, made no finding to this effect and simply took it into account as yet another factor in exercising its discretion. The defendants also abruptly stopped paying the instalments due to the plaintiff (para 23) and the court pointed out that there was no initial reduction in the instalment, giving an indication of an attempt to meet their obligation. In fact, it appeared from the monthly commitments of the defendants that, *even without the instalment due to the plaintiff*, they would be marginally over-indebted, thus evidencing little potential to successfully reschedule the indebtedness under the mortgage bond.

The court pointed out (para 23) that, even ignoring the other monthly amounts required to service their debt commitments, the defendants would only have an amount of R1 342.20 to pay towards the mortgage bond indebtedness to the plaintiff. This would leave a shortfall to plaintiff of R8 692.74 without taking into account their overdraft indebtedness as well as their indebtedness to the Municipality and Wesbank. It is further important to note (para 23) that no evidence was presented on behalf of the defendants of how the term of the mortgage bond would be increased if an instalment of only R1 342.20 was paid. The court, however, indicated that it was clear, taking into account compound interest, that this would not be a feasible way of rescheduling the mortgage bond. It is pointed out that the defendants had not paid a single instalment in 14 months and a further suspension of instalments was only likely to increase their indebtedness in the absence of additional income. However, the defendants had also failed to mention additional income as a possibility. Consequently the court held that if it is not feasible to extend the mortgage bond debt or for the defendant to recover financially after a further suspension of instalments, it is difficult to see how a debt counsellor could make one of the remaining recommendations in terms of section 86(7).

Gorven J further indicated (para 24) that it was clear that the main source of the defendant's over-indebtedness was their obligation to maintain the mortgage bond and that they would be relieved of a substantial burden if judgment were given in favour of the plaintiff. He further deemed it relevant that the plaintiff had scrupulously complied with the provisions of the Act and did not even proceed as soon as it was entitled to do so after delivery of the section 129(1)(a)-notice, but waited some months and thereby afforded the defendants more of a window period than it was obliged to before instituting action against them.

Gorven J also pointed out (para 25) that although an order declaring the property executable was sought by the plaintiff, the defendants have not placed any relevant material before the court as to how this would result in an infringement of their right to adequate housing. He further indicated that they cannot complain that they did not know what they should do as the summons pertinently drew their attention to the provisions of section 26 and indicated that should they claim that the order for execution would infringe their rights it was incumbent upon them to place information supporting that claim before the court.

6 Constitutional implications

It was argued on behalf of the defendants that an order declaring the property executable would infringe on the defendant's constitutional right to housing afforded in terms of section 26 of the Constitution. Section 26 provides that everyone has a right to adequate housing and no one may be evicted from their home without a court order taking into consideration all relevant circumstances.

The court pointed (para 25) that it is adequate housing based on sufficient evidence and not housing *per se* that is protected by the Constitution. In *Jaftha v Schoeman and Van Rooyen v Stoltz* 2005 2 SA 140 (CC) it was *inter alia* held that there is a need that homes may be used as security to raise capital, permitting a sale in execution if the debtor who willingly put up his house as security is in default, providing an abuse of court procedure was absent.

The court indicated (para 25) that, at the time of *Jaftha*, section 85(a) had not yet come into operation. However its potential was foreshadowed in *Jaftha* (para 59) where the Constitutional Court indicated that the concept of paying off the debt in instalments is important and the practicability of making such an order must be ever-present in the mind of the judicial officer when determining whether there is good cause to order the execution.

The court further indicated (para 25) that even though the defendants in the present matter (willingly) put up the property as security, the Act has nevertheless given them the opportunity to utilise its provisions to avoid execution in suitable circumstances. Despite this, they have not even given the minimum information as set out in *Jaftha* (para 60), namely:

(a) the circumstances in which the debt was incurred;

(b) any attempts made to pay off the debt;

(c) the financial situation of the parties;

(d) the amount of the debt;

(e) whether the debtor is employed or has a source of income to pay off the debt; and

(f) any other factor relevant to the particular facts of the specific case.

Gorven J consequently remarked (para 25) that it was clear, in addition, that the facts in the present matter were distinguishable from those in *Jaftha* as the present debt was not trifling and also the mechanisms of the Act were available to the defendants. He thus held that there was no evidence before him to show that the grant of an order declaring the property executable would undermine the rights of the defendants as accorded by section 26 of the Constitution. The court was thus not prepared to exercise its discretion in terms of section 85(a) in favour of the defendants and granted summary judgment for the plaintiff and an order declaring the immovable property specially executable as well as costs.

7 Analysis

It needs to be pointed out at the outset that Gorven J throughout referred to a section 129(1)-notice in his judgment whereas such notice should actually be referred to as a section 129(1)(a)-notice. In order to facilitate an analysis of this case it is important to distinguish between the debt relief remedies that may be accessed by a consumer who is of the opinion that he is over-indebted as provided for in section 79 of the Act. Initially and ideally, the consumer will approach a debt counsellor in terms of section 86(1) for the purpose of a debt review to determine whether the consumer is over-indebted in respect of his credit agreements. The debt counsellor is only empowered to make a determination regarding the consumer's over-indebtedness but cannot declare the consumer over-indebted, as it is only a court that can make such declaration. The debt review process spans over a limited time period and affords the consumer debt relief in the sense that his credit providers will not be able to enforce their credit agreements by litigation whilst the review is pending (s 88(3)). However, the debt relief afforded by such debt review is temporary and is merely a means devised to access the actual debt relief that the Act provides for, namely, voluntary debt rearrangement (s 86(8)) or a court-ordered debt restructuring in those instances where the debt counsellor has referred the matter to court with a recommendation and the court declared the consumer over-indebted (s 86(7)(c)).

There are a number of ways in which a consumer may access the debt review process in the hope of eventually reaching a voluntary debt rearrangement agreement or being declared over-indebted by a court and entitled to having his debt restructured. As such, a consumer might on own initiative decide to approach a debt counsellor for debt review in terms of section 86 before any legal action is instituted against him by his credit providers. In many instances, however, the consumer will be in default and his credit provider will deliver a section 129(1)(a)-notice to him as a mandatory step prior to litigation in respect of the enforcement of the credit agreement. On receipt of the section 129(1)(a)-notice the consumer may then decide to approach a debt counsellor for debt review in terms of section 86. There are differing viewpoints as to the nature of the assistance for which a debt counsellor may be approached after receipt of a section 129(1)(a)-notice (Scholtz *et al Guide to the National Credit Act* (2008) para 12) but it appears that in practice many consumers apply for debt review in terms of section 86 after having received a notice in terms of section 129(1)(a). Finally, in certain instances, a consumer might refrain from voluntarily approaching a debt counsellor for purposes of debt review or pursuant to a section 129(1)(a)-notice, with the intent that only once legal action is instituted against him, he will raise the issue of over-indebtedness and require the court to invoke its powers in terms of section 85.

As was correctly pointed out in *Hales*, all that a consumer has to do in order to *invoke* the application of section 85 is to meet the requirements that the court proceedings must be proceedings in which a credit agreement is being considered and that there must be an allegation that the consumer is over-indebted. One should, however, distinguish between the *invoking* of section 85 and the actual *exercising* of the discretion in terms thereof. Unfortunately it appears that many consumers and their legal representatives are under the impression that once a consumer who has not yet gone for debt review merely alleges the issue of over-indebtedness in court proceedings he automatically becomes entitled to be referred for debt review which will enable him to have his credit-agreement debt

rescheduled or that the court itself will then review and rearrange his credit-agreement debt. This false sense of entitlement was exposed in *Olivier* where Erasmus J pointed out that section 85 confers a discretion upon the court which must be exercised judicially (para 14).

In the exercise of such discretion, certain considerations will necessarily have to be taken into account in order for the discretion not to be exercised arbitrarily. However, section 85 is silent on the factors to be considered in this regard. It is therefore submitted that one should commence this exercise by referring to the Act as a whole in order to deduce the factors that may be relevant in the exercise of the section 85 discretion. Section 2(1) of the Act obliges a purposive approach by requiring that the Act be interpreted in a way which gives effect to the purposes thereof as stated in section 3.

The court in *Hales* was thus correct in holding that section 3 and other relevant provisions are intended to provide a backdrop against which the discretion must be exercised (para 12). The court in this respect duly addressed the misconception held by many that the sole or main purpose of the Act is to protect the consumer. It is submitted that to this effect Gorven J correctly pointed out that the *fact*, as opposed to the *allegation*, of over-indebtedness, is not decisive in the exercise of the court's discretion in terms of section 85 but is merely a factor to be taken into account. Thus, even where the consumer's over-indebtedness is admitted by the credit provider, the consumer who has chosen to raise the issue of over-indebtedness after institution of legal proceedings will not necessarily be entitled to be referred for debt review with the objective of obtaining court-ordered debt restructuring.

Although the protection of the consumer is not the sole or main purpose of the Act, it attempts to provide for the protection of the consumer in a manner that strives to limit costs. To this effect it contains a statutory *in duplum* rule (s 103(5)) as well as other provisions aimed at limiting or discouraging legal costs. With regard to the latter, one may argue that the option available to a consumer to voluntarily approach a debt counsellor prior to litigation serves the purpose of discouraging litigation and the costs incurred thereby, which will add to the burden of the already over-burdened consumer. The section 129(1)(a)-notice also serves the purpose of attempting to find a solution to the consumer's credit agreement debt predicament that might obviate subsequent litigation. In this regard Erasmus J in *Olivier* held that the Act would encourage a consumer to approach a debt counsellor before the credit provider approaches the court as it is desirable, *inter alia*, that a debt counsellor be approached before the court is burdened with debt-enforcement proceedings and unnecessary costs are incurred (para 18). Erasmus J held that it is the duty of the court to discourage conduct where the consumer wants rescheduling of payment and waits, despite the section 129(1)(a)-notice, until enforcement steps are taken and then raises section 85 (para 19). He further held that it is therefore relevant to the exercise of the court's discretion in terms of section 85 that the defendant failed to act upon receipt of the section 129(1)(a)-notice and that the consumer has failed to explain or ask for condonation of his failure (para 19).

It is interesting to note that *in casu* the court interpreted section 86(2) read together with section 129(1)(a) as barring a consumer who received a section 129(1)(a)-notice from applying for debt review in terms of section 86(1). It is submitted that this limited approach in terms of which a consumer who receives a section 129(1)(a)-notice can only approach a debt counsellor for two restricted

purposes, namely, to attempt to resolve a dispute under a credit agreement or to agree on a plan to bring payments up to date, militates against the objective of the Act to address over-indebtedness. Practically it would leave a consumer with only one option, namely, to approach a debt counsellor for debt review prior to receipt of a section 129(1)(a)-notice as the fact that he only attempted to access the debt review process via section 85 after institution of court proceedings may be held against him in certain instances. Where the consumer is unaware of his right to approach a debt counsellor in terms of section 86 or where he does not have sufficient time to approach a debt counsellor due to a vigilant credit provider having delivered a section 129(1)(a)-notice to him immediately upon his default, his efforts at obtaining debt review and being eligible for debt restructuring might be thwarted, leaving him no other option than to raise his over-indebtedness during costly court proceedings in the hope of achieving eventual debt restructuring by a court following a section 85-referral. It is submitted that by the time such a consumer invokes the provisions of section 85 his over-indebtedness might have increased, leaving him even worse off. Further, he also faces the possibility that the fact that he requests to be referred to debt review at such a late stage might be viewed negatively by the court absent an acceptable explanation.

It is submitted that the interpretation given in *Hales* to section 86(2) actually limits the discretion the court has in terms of section 85 to take into account the fact that the consumer failed to apply for debt review prior to court proceedings and only made the request once court proceedings were instituted. If the receipt of a section 129(1)(a)-notice does not provide the consumer an opportunity to access debt review, then the question can obviously not be asked why the consumer did not apply for debt review after receiving the section 129(1)(a)-notice. In such instance the court will then only be able to consider whether, given the circumstances of the particular matter, the consumer had the opportunity to apply for debt review voluntarily prior to receipt of the section 129(1)(a)-notice. However, one finds it difficult to perceive how the legislature could have intended that a consumer who receives a section 129(1)(a)-notice would be able to consult with a debt counsellor for purpose of attempting to agree on a plan to bring payments up to date without the debt counsellor conducting at least a limited debt review. A further problem with this specific construction is that the Act contains no specific process to facilitate it. Whereas it is clear from section 129(1)(a) read together with section 130, that the consumer has 10 business days after receipt of the section 129(1)(a)-notice to consult the debt counsellor, there are no provisions detailing the period within which the debt counsellor must then come up with a solution to the dispute or a repayment plan. The only provision in the Act that sets out exactly what a debt counsellor must do and the time frames within which he must do so, is section 86 and its accompanying regulations.

It is therefore submitted that the legislature also intended section 129(1)(a) to provide the consumer an opportunity to access debt review. This construction is not improbable, given the fact that many consumers remain uneducated about the debt relief measures in the Act. It is quite likely that the legislature intended that no consumer who has credit agreement debt to which the Act applies will be able to state that he was unaware that he could go to a debt counsellor to have his debt reviewed and so avoid costly litigation. In such an instance then, where the consumer has received a section 129(1)(a)-notice and fails to approach a debt counsellor for debt review, his failure becomes relevant for purposes of deciding

whether he should be allowed to do so in terms of section 85 and, in the absence of a proper explanation may justify a conclusion that he elected at his peril not to apply for debt review subsequent to receipt of the section 129(1)(a)-notice.

The limited approach in *Hales* to section 86(2) read together with section 129(1)(a) basically has the effect that, in the context of the section 85 discretion, the fact that the consumer received a section 129(1)(a)-notice is significant in the sense that, although it bars the consumer from applying for debt review, it at least affords him the opportunity to approach a debt counsellor only for the purposes stated in the said section and might at least point towards an intention by the consumer to address his over-indebtedness. However, it is submitted that the viewpoint that section 129(1)(a) was introduced as a measure to ensure that the consumer is explicitly informed that he may approach a debt counsellor, and that the conduct of a debt review is inherently implied this provision, serves the debt-relief objectives of the Act better than the aforementioned limited approach.

Despite the above criticism, it should be pointed out that the judgment in *Hales* has added value by extending the list of factors that have to be taken into account by a court when exercising its discretion in terms of section 85. What becomes abundantly clear is that a consumer who wishes the court to exercise its section-85 discretion will have to favour the court with sufficient detailed information, first to decide whether it should exercise its discretion at all by *invoking* the provisions of section 85 and secondly to decide whether it should *exercise* its discretion in the consumer's favour. As such the exercise of the discretion will entail a two-stage approach, namely, to determine whether the discretion should be *invoked* and if affirmative, to *exercise* the discretion judicially in accordance with certain factors.

It is submitted that as a result of *Hales* there is now more clarity that the following factors must be considered by a court called upon to exercise its discretion in terms of section 85, namely:

(a) Factors to be considered in deciding whether the discretion should be *invoked*:

  (i) Are the proceedings court proceedings in which a credit agreement is being considered? (para 7);

  (ii) Is there an allegation that the consumer is over-indebted? (para 7).

  If the answer to any or both of the above questions is in the negative, the court should refrain from exercising its section 85 discretion. If the answer to both the above questions is affirmative, the court should then exercise its discretion in terms of section 85 with reference to the following:

(b) Factors to be considered in deciding whether the court should exercise its discretion in favour of or against the consumer:

  (i) Is the consumer indeed over-indebted?

  (ii) Did the consumer give a sufficient explanation of how his default arose? (para 22).

  (iii) Did the consumer receive a section 129(1)(a)-notice? (para 22).

  (iv) If so, was the consumer prior to receiving a section 129(1)(a)-notice, aware that he could voluntarily apply for debt review in terms of section 86(1)? (para 22).

(v) If so, did the consumer furnish an explanation as to why he failed to voluntarily apply for debt review in terms of section 86(1) and did he request condonation of his failure? (para 22).

(vi) Did the consumer at any stage, prior to or after receipt of a section 129(1)(a)-notice approach the credit provider with proposals to re-schedule the debt or any other proposals? (para 22).

(vii) Did the consumer disclose to the court the nature and extent of his other indebtedness? (para 22).

(viii) Where applicable, did the consumer falsely deny receipt of a section 129(1)(a)-notice or make any other material false denial? (para 22).

(ix) Did the consumer attempt to make some payment towards the debt or did he abruptly stop payment? (para 23).

(x) Given the consumer's income or means to service the debt, and the nature and extent of the debt, is there any potential to successfully re-schedule his indebtedness? (para 23).

(xi) Did the credit receiver comply with the requirements of the Act? (para 24).

It is submitted that having regard to the latter category of factors, *Hales* illustrates that the possibility of successfully rescheduling the debt plays the more decisive role. It may thus happen that a consumer is able to satisfy a court that he is over-indebted with regard to credit agreement debt, offers a reasonable explanation why he did not go for debt review prior to court proceedings and sets out his financial predicament with great detail but that his over-indebtedness is so substantial that it cannot be cured by debt review followed by subsequent debt rearrangement (eg where it will take an unreasonably long time to reschedule the debt). In such an instance a court, exercising its discretion judicially, will then be obliged to refuse the consumer the opportunity to go for debt review in terms of section 85 as the debt review in such a case would serve no due purpose and may even amount to an abuse of process.

8 The constitutional issue

Before *Jaftha* it was possible, where there were insufficient movables to satisfy a judgment debt or if the court so ordered on good cause shown, to have a warrant against immovable property issued by the clerk of the court (s 66(1)(a) of the Magistrates' Courts Act). No provision was made for judicial oversight by a magistrate before issuing such warrant and the court held that section 66(1)(a) was overbroad and violated section 26(1) of the Constitution to the extent that it allowed sales in execution of the homes of indigent debtors, causing them to lose their security of tenure (paras 41–44). Consequently by means of a method of reading in of the words "a court after consideration of all the relevant circumstances", it was provided that judicial oversight is henceforth required in the Magistrate's Court before issuing of a warrant of execution against immovable property (paras 61–64).

The court in *Jaftha* (paras 56–60) summarised the following factors which a Magistrate's Court might consider in providing the necessary judicial oversight, namely:

(a) the circumstances under which the debt had been incurred;

(b) any attempts made by the debtor to pay off the debt;

(c) the financial situation of the parties;

(d) the amount of the debt;

(e) whether the debtor was employed or had a source of income, to pay off the debt; and

(f) any other factor relevant to the particular facts of the case before the court.

Although *Jaftha* dealt with trifling debt, it is important to note that the court held (para 41) that there were factors, apart from the debt being trifling, that could militate against a finding that execution was unjustifiable, such as the fact that the debtor had incurred debts despite the knowledge of his inability to repay them and had been reckless in regard to the consequences of incurring the debt. *Jaftha inter alia* triggered the question as to the interaction between a creditor's right to execution against specially hypothecated immovable property which was subject to a mortgage bond and the debtor's right to security of tenure and adequate housing as provided for in section 26 of the Constitution. In *Jaftha*, Mokgoro J indicated (para 56) that if a judgment debtor willingly put up his or her house as security for debt, a sale in execution should ordinarily be permitted where there has not been an abuse of court procedure. Subsequent to *Jaftha*, this issue was pertinently addressed in a number of other cases and it appears to be settled law that our courts recognise that a debtor who mortgaged his or her home participated in a commercial transaction and willingly utilised such property as security and thus put it at risk of being executed against, with the effect that such property may be declared specially executable (*Nedbank Ltd v Debbie-Ann Mortinson* 2005 6 SA 462 (W); *Standard Bank of South Africa Ltd v Saunderson* 2006 2 SA 264 (SCA)).

In the context of property specially hypothecated by means of a mortgage bond it was also held that the purpose for which the property was acquired, namely, residential or commercial, is important, the argument being that in the case of commercial property there is no possibility of infringing upon the right to adequate housing in terms of section 26 of the Constitution (*Mortinson* para 22). It should, however, be pointed out that although it was held that the sole fact that specially hypothecated immovable property is residential in character did not necessarily imply that an infringement of section 26(1) of the Constitution will occur, the court also did not rule out the possibility that there may be instances where execution against specially hypothecated immovable property may infringe on such rights (*Saunderson* paras 18–19).

One may consequently ask what the interaction between section 85 of the Act and section 26 of the Constitution is when it comes to property specially hypothecated by means of a mortgage bond. As correctly pointed out by Gorven J in *Hales* (para 25), section 26 protects the right to adequate housing and not housing *per se*. Thus if it appears that a debtor whose house is sold in execution still has the means to obtain alternative housing, his section 26 rights will not be held to have been violated.

Where a natural-person consumer allows a mortgage bond to be registered over his property, such transaction will usually fall within the ambit of the Act. If the consumer consequently becomes over-indebted and cannot continue with his payments he has the option to apply for debt review in terms of section 86 and the opportunity to eventually obtain rearrangement of the mortgage bond payments in terms of section 86(7)(c) or 86(8)(b). Alternatively, in accordance with *Hales*, he can at the least approach a debt counsellor in order to propose a plan to

bring his payments up to date once he has received a section 129(1)(a)-notice. If, for whatever reason, he has not made use of any of the two aforementioned options, he would still be able to invoke section 85 and require to be referred to a debt counsellor for debt review or for the court to declare him over-indebted and grant him debt relief. In exercising the discretion afforded by section 85 the court will inevitably take into account certain of the factors as mentioned in *Jaftha* as part of the factors it will consider over-all to decide how to exercise its discretion. However, the court is not during and for purposes of its section-85 enquiry obliged to take into consideration the possibility that the debtor's rights in terms of section 26 of the Constitution may be infringed. The infringement of the latter right is irrelevant within the context of the exercise of the section 85-discretion.

It should be remembered that when a court is requested to exercise its discretion in terms of section 85 the main issue will usually be whether a debtor should be afforded the opportunity of debt review eventually culminating in debt rearrangement or whether judgment should be granted against such debtor. Where section 26 of the Constitution is relied upon in this context, it will usually imply that judgment has already been granted and the only question that remains is whether, as alleged by the debtor, an order that the immovable property may be executed against will render the debtor homeless and unable to find alternative adequate housing.

Where a court exercises its discretion in terms of section 85(a) favourably the consumer is referred to debt review and his debt may be rescheduled, allowing him to keep his house. Where, however, a court exercises the discretion in terms of section 85(a) against a debtor in respect of mortgage bond debt, the effect will normally be that judgment will be granted against the debtor and the immovable property will be declared immediately executable. In the first scenario section 26 of the Constitution will not come into play as there is no violation of the debtor's right to security of tenure. In the latter instance, the mere fact that the immovable property has been declared executable does not *per se* imply a violation of the debtor's right of security of tenure. Only in those rare instances where the property is used for residential purposes and such execution will leave the debtor destitute, will section 26 be in issue. In such instances, the interplay between section 85(a) of the Act and section 26 of the Constitution becomes evident, namely, that even though the court might have considered certain of the *Jaftha* factors during the exercise of it section 85(a)-discretion and decided against exercising its discretion in the debtor's favour, those very same factors may lead the court to conclude that the debtor's section-26 rights have been infringed. Thus, the significance of an allegation of violation of the debtor's rights in terms of section 26 of the Constitution is that even if a court has held that a debtor's debt cannot be restructured in accordance with the provisions of the Act the consumer who will be rendered homeless and unable to find adequate housing might have one last chance of retaining his house – if he can furnish sufficient evidence to justify a determination that his right to security of tenure will be violated by the sale in execution of the immovable property.

9 Conclusion

Insofar as the section 85(a)-discretion and its invocation and exercise are concerned, it is submitted that the court in *Hales* came to the correct finding. However, one cannot help but wonder whether dealing with this matter on the basis that reckless credit (as per s 80(1)(b)(ii)) was granted by the plaintiff would not

have aided the defendants who appeared to have been granted credit that they could not afford at all – given the fact that by the time of the summary judgment proceedings they were already not paying their bond for 14 months. Thus, one can infer that, bearing in mind that the bond was only registered in July 2007 and the summary judgment application was brought in September 2008, it appears that either they made very few payments or no payments at all. It is submitted that the shocking disproportion between their incomes and the bond repayments (para 3) should have at least prompted the court to *invoke* its powers in terms of section 83 of the Act to have looked into the possibility of reckless credit granting as this appears to be an issue that the court can raise *suo motu* (*Ex parte Ford and two similar cases* 2009 3 SA 376 (WCC)). It is submitted that whereas over-indebtedness *per se* does not constitute a defence on the merits to an application for summary judgment, reckless credit indeed constitutes a defence on the merits. However, given the fact that the defendants *in casu* were not truthful about having received the section 129(1)(a)-notice, it is not unlikely that during the compulsory credit assessment (s 81(2)) they failed to answer fully and truthfully to the requests for information and by so doing materially influenced the credit provider's ability make a proper assessment, thus providing the credit provider with a complete defence against reckless credit (s 81(1) read with 81(4) of the Act).

C VAN HEERDEN
DJ LÖTZ
University of Pretoria