

12 JUNE 2019

# CORPORATE & COMMERCIAL ALERT

## IN THIS ISSUE >

### Developmental credit agreements and the obligation to conduct affordability assessments

This alert discusses developmental credit agreements and the obligation of credit providers to conduct affordability assessments.

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CLIFFE DEKKER HOFMEYR

## Developmental credit agreements and the obligation to conduct affordability assessments

Having regard to the definition of developmental credit agreements, it appears that developmental credit focuses on providing more vulnerable consumers with greater access to credit in order to improve their access to housing, education and business opportunities.

**This alert discusses developmental credit agreements and the obligation of credit providers to conduct affordability assessments.**

Developmental credit agreements are defined in s10(1) of the National Credit Act, No 34 of 2005 (NCA) as follows:

- (1) A credit agreement, irrespective of its form, type or category, is a developmental credit agreement if:
  - (a) at the time the agreement is entered into, the credit provider holds a supplementary registration certificate issued in terms of an application contemplated in s41; and
  - (b) the credit agreement is:
    - (i) between a credit co-operative as credit provider, and a member of that credit co-operative as consumer, if profit is not the dominant purpose for entering into the agreement, and the principal debt under that agreement does not exceed the prescribed maximum amount;
    - (ii) an educational loan; or
    - (iii) entered into for any of the following purposes:
      - (aa) development of a small business;
      - (bb) the acquisition, rehabilitation, building or expansion of low income housing; or

- (cc) any other purpose prescribed in terms of subsection (2)(a).

Having regard to the definition of developmental credit agreements, it appears that developmental credit focuses on providing more vulnerable consumers with greater access to credit in order to improve their access to housing, education and business opportunities. The aforementioned purposes are of course critical to ensuring economic growth in the country and also assists in improving the accessibility of the credit market for those who may not otherwise be able to afford credit.

Credit providers who advance developmental credit are incentivised to provide this form of credit in that the maximum prescribed interest and initiation fees that can be levied by credit providers in terms of the NCA for these types of agreements are generally higher than those for other categories of credit agreements. These higher rates of interest and fees are also presumably catered for as a means to compensate credit providers for advancing credit to potentially "high risk" consumers.

Notably, developmental credit agreements are not exempt from the application of s81 to s84 of the NCA as they relate to the affordability requirements and provision of reckless credit by credit providers. In particular, s81 of the NCA places an obligation on the credit provider to assess the financial position of the consumer prior to entering into a credit agreement with the consumer, which includes an assessment of the "financial means, prospects and obligations of a consumer".

## Developmental credit agreements and the obligation to conduct affordability assessments...*continued*

This apparent inconsistency raises the question as to whether, given that regulation 23A explicitly excludes developmental credit agreements from the ambit of the affordability assessment regulations, there remains an obligation on a credit provider to conduct affordability assessments where credit is of a developmental nature.

Section 82(2) of the NCA empowers the Minister, on the recommendation of the NCR, to make affordability assessment regulations. These were introduced on 13 March 2015, and are contained in regulation 23A to the NCA. The affordability assessment regulations set out specific criteria to be considered in assessing the financial position of the consumer. Importantly for our purposes, is that regulation 23A(2)(a) exempts development credit agreements from the application of the affordability assessment regulations. This is seemingly inconsistent with s78 of the NCA which does not provide for the same blanket exclusion for developmental credit agreements, and only expressly excludes developmental credit agreements from affordability assessments insofar as they are school loans or student loans, the aforementioned being sub-categories of educational loans, which fall within the definition of developmental credit agreements.

It is also worth mentioning that the regulations are subordinate regulations, and it is trite in our law that subordinate legislation cannot go further than the primary legislation, being in this case, the NCA.

This apparent inconsistency raises the question as to whether, given that

regulation 23A explicitly excludes developmental credit agreements from the ambit of the affordability assessment regulations, there remains an obligation on a credit provider to conduct affordability assessments where credit is of a developmental nature. Furthermore, given that, inter alia, (i) the failure to conduct an affordability assessment; or (ii) where an affordability assessment is undertaken and credit is advanced notwithstanding such assessment indicating that the consumer cannot afford the credit, are the key factors in determining whether credit was advanced recklessly, it is open to question whether the provisions of the NCA in relation to reckless credit apply to developmental credit agreements.

It is our view that one way to approach these issues is for credit providers, in the case of developmental credit agreements, to nevertheless undertake some form of affordability assessment. It is seemingly not necessary for this affordability assessment to be in strict compliance with regulation 23A, but it is in any event prudent for credit providers to conduct an enquiry into the consumer's financial affairs akin to this affordability assessment in order to mitigate its own risk and because the NCA has not specifically exempted credit providers from doing so.

*Chloe Brockman and Allan Hannie*

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