LENDING TO A FRIEND OR SELLING PROPERTY ON CREDIT - MUST YOU REGISTER AS A CREDIT PROVIDER?

“Neither a borrower nor a lender be, for loan oft loses both itself and friend” (Shakespeare)

It seems logical that the very strong consumer protections in the NCA (National Credit Act) are designed for commercial situations in which credit is advanced by “credit provider” businesses to “credit consumers”.

But does the NCA also apply to non-commercial, once-off loans? Like a loan to a friend or relative? And what about property sales?

Why should you be worried?

If you aren’t in the business of providing credit it seems counter-intuitive that you should have to worry about NCA registration when making a single loan or giving credit on a once-off basis. And in fact until now our various High Courts have been split over the question.

But that has all changed with a recent Supreme Court of Appeal (SCA) decision, and your danger is this – if you should have registered as a credit provider but didn’t, your agreement is unlawful and could be declared void. You might have to write off your whole loan.

A “family” fall out and a R2m “time to pay” share purchase deal

A couple brought into their business a businessman who was “like a son” to them. The idea was that eventually he would take over the business and over time he became a substantial shareholder. Alas however some 12 years down the line there was a falling-out and a mutual decision to part ways.

It was agreed that the businessman would sell his interest in the business to the couple for R2m, to be paid by way of a R500,000 deposit and monthly instalments of R30,000 p.m. Interest was payable on the deferred amount and a mortgage bond registered over the couple’s house as security.

The businessman (as seller) registered as a credit provider (in order to get the mortgage bond registered in his favour) but only after the credit agreement was signed.

When the business ran into trouble the couple couldn’t continue paying and the seller sued them for the outstanding balance of R1.13m. The couples’ defence was that the agreements were null and void due to non-compliance with the NCA.

The SCA held that the seller should have registered as a credit provider before the credit agreement was entered into. He didn’t, the agreement was thus unlawful, and he loses his R1.13m.

What is excluded from the registration requirement?

So are you at risk? Firstly, the NCA has many general exclusions and situations of limited application, such as to “incidental” credit agreements, interest-free loans, larger corporates and agreements (thresholds apply - take advice for details).

Secondly, the NCA only applies if you are “dealing at arm’s length”. What does that mean in practice?

To start with, there are specified exclusions for certain shareholder loans and for loans between family members who are “co-dependent” or “dependent” on each other. Think for example of parents supporting a student daughter or the daughter supporting her parents.

Then there’s the much wider provision excluding “any other arrangement … in which each party is not independent of the other and consequently does not necessarily strive to obtain the utmost possible advantage out of the transaction”. That might suggest that loans to close friends are also excluded, but it’s not nearly as simple as that.

The lender in this case couldn’t of course claim to be an actual family member of the couple. But he did argue that because of his “almost familial relationship” with them, he didn’t try to get the “utmost possible advantage” out of the deal and therefore the NCA didn’t apply. On the facts however the SCA disagreed, the relationship between the parties having become hostile and threatening prior to signature of the agreement. The point is that if there is an element of “independence” between you and the debtor, you are at risk.

Outside those specific exclusions, deciding whether or not a court will consider you to be “at arm’s length” is always going to involve grey areas.

Sale of property with deferred payments

There’s particular danger here for the increasing number of property sellers who, in order to attract cash-strapped buyers in these tough times, are agreeing to sell their properties on a deferred payment or instalment sale basis rather than the standard “pay in full against transfer” basis. Watch out also for a normal “pay in full” deal morphing into a “pay me the rest later” sale when the buyer can only get a bank loan for part of the total price.

If either of those scenarios apply, your sale may have to comply with both the NCA’s obligation to register as a credit provider and with the strict requirements of the Alienation of Land Act. Specific legal advice is essential before you agree to any form of “deferred payment” property sale.

The bottom line

Unless and until the NCA is amended to make it clearer, less confusing and more pragmatic, tread very carefully in lending money or giving credit – in relation to a property sale or otherwise - to anyone. Even family and friends.

Ask your lawyer for advice on your specific circumstances – do you fall into one of the exceptions or must you register as a credit provider? If you do need to register, prepare for lots of red tape and delay!