

Consumer Note 5

Set-Off





Please note that the information provided does not constitute expert legal or financial advice. You should consult a professional legal or financial adviser for expert advice.

We have only mentioned sections of the National Credit Act (NCA) where they are applicable to the complaints we receive. The Act however contains many other sections and details that may not have been mentioned. There may be other legislation that is also applicable. For more information and detail on other legislation and the Act, you should consult a legal professional.

The purpose of the document is to provide you with practical information based on our experience. Each case we investigate is however assessed on its merits.

Background

The bank's practice of deducting money from a client's account to pay another account that is in arrears affects many banking customers. This process is based on an old legal principle known as set-off. In summary, the legal principle is that if A owes B R100 and B owes A R50 then A can deduct the R50 owed to him by B and only pay R50 to B in settlement of the debt. A has thus set-off R50 from the debt he owes to B. There are several legal requirements, exceptions etc. for this principle but this is the essence of it.

The banks use this legal principle to deduct money from a customer's account that is in credit and using it to settle or pay an account for the same customer that is in arrears. For example, they may deduct money from a savings or current account to pay a credit card account that is in arrears and due and payable.

The Code of Banking Practice

The Code of Banking Practice (the Code) contains the following clause relating to set-off:

7.5 Set-off

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.

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 set-off 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.

The Code only requires the bank to advise you that it has applied set-off to an account after the fact. The argument is that if any prior notice had to be given then the customer would simply withdraw the money from the account before the bank can apply set-off.

Loan contracts entered into before the National Credit Act

The National Credit Act (NCA) came into operation on 1 June 2007. Before the National Credit Act came into operation the banks inserted a clause into most of their credit contracts (credit card accounts in particular) allowing them to apply this principle.

The banks therefore continue to apply set-off on any loan contracts entered into before 1 June 2007.

Loans entered into after the National Credit Act

For loans entered into after 1 June 2007 the NCA now prohibits a bank from inserting a set-off clause in their contracts [Section 90 (2) (n)]. The NCA further prohibits the bank from debiting an account for a loan repayment unless the customer has agreed beforehand that the account may be debited [Section 124].

The banks complied with the NCA in this regard and no longer insert set-off clauses in any contracts as from 1 June 2007.

The banks however continue to apply set-off on all accounts despite the provisions in the National Credit Act - even on accounts where there is no clause providing for set-off.

Current Legal debate

The banks obtained legal opinions on this aspect. The legal opinions submitted that the NCA did not in any way prohibit the bank from using the common law principle of set-off. This meant that although the set-off clause is not in the contract, the law still permits the bank to use the common law principle for all contracts entered into after 1 June



2007. The NCA does not specifically refer to the common law principle of set-off and does not specifically prohibit it.

The National Credit Regulator does not agree with the legal opinions that the banks obtained and remains of the view that the banks may not apply set-off on any loan contracts entered into after 1 June 2007 unless this is done in accordance with the provisions of the NCA – Section 124.

The current position however is that the banks are applying the common law principle of set-off despite the views of the National Credit Regulator, and this position will remain until the issue is resolved through new legislation or in a court of law.

Ombudsman's approach

As the issue is subject to an ongoing legal dispute that needs to be settled by legislation or in a court of law we are not able to make recommendations against the bank in this regard.

We have however requested the banks to apply the principle as fairly as possible. We have proposed to the banks that they do not attach a customer's entire salary as this can cause a snowball effect whereby numerous other existing loans are not paid and therefore fall into arrears.

We have urged the banks to only attach a "*reasonable portion*" of a salary to enable the customer to still pay other ongoing debts.

What constitutes a reasonable amount is however subject to debate. Each case depends on its merits and facts.

Where the bank has applied set-off to an account by attaching the entire salary or most of it, we advise that the customer to lodge a formal written complaint with the bank. In the complaint, we suggest that the consumer sets out a detailed list of their income and expenditure. The consumer also needs to make it clear how much he/she is prepared to repay on the debt every month. The bank may then agree and refund a portion of the attached amount in return for the consumer signing an acknowledgment of the debt (AOD) and an undertaking to pay an agreed amount every month.



Also, where an entire salary has been attached and the bank refuses to accept a reasonable repayment offer, a consumer can lodge a complaint with us and we will assess the matter. Please remember that we cannot negotiate repayment offers on your behalf. Consumers can refer to our Consumer Information Note 1 – Financial Problems for more information.

The Ombudsman for Banking Services

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